

# USE OF SHADOW PRICES IN A DEVELOPING ECONOMY\*

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## I. *Introduction*

1. A detailed plan for economic growth requires the use of a detailed input-output table as well as detailed capital coefficient matrices. Once the technological matrices and the initial data about the economy are available, it is possible to plan for detailed resource allocation for a few years during which technological data are not supposed to undergo any significant changes. Various methods for such planning are available.

2. However, while detailed planning requires resource allocation among a 1000 or 2000 sectors, the biggest input-output table available so far does not extend beyond a few hundred classifications. Those available in developing countries like India, are of much smaller size. The table prepared by the I.S.I. distinguishes only 30 sectors while that prepared by the Planning Commission distinguishes 29 sectors only. In such circumstances, the construction of a detailed plan becomes more or less approximate and depends upon judgement circumscribed by overall considerations. There is nothing theoretical to guide these judgements and sometimes they become at the most compromises between the claims of various contending interests. All calculations which are helpful to taking such a judgement are based on current price structure. This, as will be shown below, is a very questionable guide. To guide evaluation of various programmes for the purpose of their being incorporated in a plan, it is necessary to have estimation of shadow prices that will help the calculation of cost benefit ratios for individual plants. Then the planner will automatically choose programmes having the least cost benefit ratios. In a big country like India there are so many economic decisions to be made that each and every problem cannot be transmitted to some central office for being solved. For planning to be

\* The calculations for this paper were carried out by Shri P. D. Parkhi.