FIFTEEN YEARS OF INDIAN PLANNING

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"People must come to accept private enterprise not as a necessary evil, but as an affirmative good."

Eugene Black

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By

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I. National Income and Mass Well-being

For assessing economic progress, we must first define the term. By economic progress we shall mean, first, a continued rise in the standard of living of the masses of the people. Since the masses of the Indian people are close to the margin of subsistence, for quite some time, the measure of economic progress will lie in the consumption of food, the average of which is below the nutritional norm, and the consumption of cloth, the average of which is substandard.

In democracies, the expectation would be that, while the level of living of the masses rose fast enough, the affluence of no sector should go up significantly faster than the national average. If the incomes of the more prosperous groups galloped ahead, whilst the economic condition of the masses remained comparatively stagnant, there will be complaints of social injustice. Therefore, the second test of economic development is in a reduction of income

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contrasts between the more affluent sectors of the community and the masses.

With these two criteria of economic progress in our mind, it is easy to say what does not constitute economic progress. First, if the standard of living of the people as a whole did not rise, or lagged far behind the accelerating opulence of some groups, we do not have economic progress. Such a state of affairs may be described as economic development of the classes; it is not Indian economic development. Secondly, spectacular progress in nuclear science, the science of rocketry and space sicence, and the stock-piling of missiles and other nuclear weapons, in the context of shortages of food, clothing, house-room and the like, is not economic progress either. These developments may add enormously to the striking power of the nation and may be termed military development. Thirdly, heavy engineering and heavy chemicals, mammoth river valley projects, idle production capacities and indiscriminate industrialisation, when the masses of the people are ill-clad and under-fed, do not constitute economic development. We may call it show-window economic activity and at best sectoral development.

Ordinarily, in free societies, production would get adjusted to meet the changing needs of consumers, this adjustment being effected by the pricing system. Prices of commodities in larger demand would rise and entrepreneurs would increase the output of such commodities under the inducement of higher returns on the capital invested, which higher prices would bring. Under such conditions, the increase in the national product may provide a dependable measure of the trend in consumption, i.e., the standard of living of the people in general.

Under the policies which we have pursued during the past one and a half decade, and which are generally described as planning, there is, on the other

hand, a divorce between production and consumer needs. Production is directed, or indirectly controlled, by the Planning Commission, the instruments of control being import restrictions and exchange controls, controls over the distribution of domestic supplies, capital issues controls, and price controls of essential goods. Being constrained by these controls, entrepreneurs have not been free to orient production to satisfy consumer demands. Production has been governed more by the policy measures laid down by the Planning Commission. During the Third Plan, about 70 per cent of the investment resources are drawn into the so-called "infrastructure" undertakings in the Public Sector; and a considerable part of the rest of the resources are used up in industrialisation, including import substitution. This has involved comparative neglect of the production of food, agriculture generally and basic consumer goods industries such as cotton textiles.

These policies have caused two damaging consequences. First, they have retarded the expansion of the national product. This retardation is the direct outcome of the shift of resources from sectors where the output on the capital invested is high, namely, agriculture and cotton textiles, into sectors where such output is low, namely, "infrastructure" industries and industries brought into existence under policy pressures for substituting import goods. It has been estimated that Rs. 1 crore worth of additional resources invested in agriculture may add to the national product about Rs. 57 to Rs. 69 lakhs of output. The same amount of resources may add to the national product about Rs. 36 lakhs, if invested in cotton textiles, and about Rs. 19 lakhs if invested in iron ,and steel. Our policy preferences for "infrastructure" industries and for import substitution, regardless of costs, to the neglect of agriculture and of cotton textiles thus has involved producing less in place of producing more for the same quantum

of resources. This, in large part, explains the slow pace of growth of the Indian national product during the past 15 years, despite a more than three-fold increase in investment.

Secondly, these policies have led to a pattern of production diverging from the pattern of consumer needs. In place of more food and cloth, the economy has been producing more of other things — iron and steel, cement, chemicals, machinery and other industrial output. This divergence has meant that we can no longer depend on the statistics of the national product for a measure of overall economic progress, defining the latter term, as we have done, to mean a rise in the level of living of the masses. For the statistician whatever is produced — whether rice, butter, guns, chemicals or machinery — adds to the national product. When there is a heavy armaments programme, as in Communist countries, or when economic policies foster programmes of expansion of heavy engineering and heavy chemicals and other "basic" industries, as in India, the curve of the national product present a misleading picture of mass well-being. For an assessment of mass well-being, we have then to take a look, not at national income statistics, but at the consumer goods content of the national product.

During the past ten years, Indian national income rose at an annual rate of 4.6 per cent and the population at an annual rate of about 2.5 per cent. This yields a per capita annual rise of about 1.8 per cent The provisional estimate for 1964-65 shows an impressive jump of 7.7 per cent in the national income and of 5.3 per cent in **per capita** income. The **Economic Survey 1965-66**, fears that during the current year, because of a decline in agricultural output, national income may be less than in 1964-65. At this low pace of growth in **per capita** income, seeing that economic development in the more affluent countries of Europe and America

is much faster, we may be never able to catch up the order of economic well-being in these countries. The gap between our level of living and theirs may continually widen. It is not a welcome idea that this widening gap may have a chance of being reduced only in the event of catastrophies such as wars in which these other countries may be engaged and we may keep out.

Unsatisfactory as these statistical averages are, the actual well-being of the masses may be less than semi-stagnant. First, as pointed out by Mr. Narottam Shah,[1] of **The Economic Times,** through an old-standing and inexplicably unrectified error, incomes from Commerce, Transport and other "Services" sectors of the national income are considerably exaggerated in the statistics. Incomes at current prices are converted into incomes at constant prices by deflating the former to allow for the inflationary rise in prices. Though prices have risen by 38 per cent from 1955-56 to 1963-64, incomes at current prices have been deflated only nominally, by 2.4 per cent. If we make full allowance for the inflationary price rise with respect to these sectors, the increase in national income during the past decade may be at the lower annual rate of 3.5 per cent, and of **per capita** income at the lower annual rate of 1.2 per cent.

Secondly, for a proper assessment of mass well-being, due allowances must be made from the statistics of **per capita** income for the considerable income shifts from the masses to the upper-income groups. Though this takes us to a subject which does not make welcome discussion in public its exclusion may detract from full appraisal of the basic forces now operating

[1] Narottam Shah, "Deflation of Income Originating in Non-Commodity Sectors of the Indian Economy", a paper read before the Fifth Indian Conference on Research in National Income, April 1966, Ahmedabad.

in the Indian economy a comprehension of which is essential to a correct diagnosis of the maladies confronting us. These income shifts have resulted from three factors: (1) from inflation, which has corroded the incomes of the fixed and the sticky money income groups, who comprise the masses, wage earners and salaried people, and has added correspondingly to the incomes of a fraction of the community, traders, businessmen and industrialists; (2) from controls, in particular, import controls, which have transferred incomes as monopoly gains, or illicit earnings, through corrupt practices, which controls give rise to, from the general body of consumers to the privileged upper-income groups, who include entrepreneurs, intermediaries, and the corrupt functionaries of the State; and (3) from the phenomenal expansion of the Public Sector, which have added enormously to the illicit gains of the contractors and other participants in this expansion.

In recent years, aggregate income transfers due to inflation, controls and the expansion of the Public Sector may not be far lower than the annual increases in national income, the bulk of this being due to import licensing and exchange restrictions. If we may assume, that the whole of the values in respect to import licences issued to Public Sector undertakings accrue to the Public Sector we may regard them as a species of taxation. But the values of the import licences issued to the Private Sector accrue to private parties, to which they have neither an economic nor moral title. Currently, the premia on these licences are reported to vary from 500 to 700 per cent in respect to 10 per cent of the licences and to be below 200 per cent in respect to the rest.[1] Assuming an average premium of 75 per cent on all Private Sector licences — on which my computations elsewhere, too, have been based — the income shifts on account of import licences on Private

1. *The Economic Times,* 31st March 1966, P. 1.

Sector imports — which averaged Rs. 625 crores annually during 1961-62 to 1964-65 — may be of an annual order of Rs. 470 crores.

If so, the benefit of the largest part of the annual expansion of the national income has accrued to a thin upper crust of the privileged sections of the people, leaving the condition of the masses unchanged or worse than before. With the rich becoming richer and the poor remaining poor, or becoming poorer, income contrasts between the rich and the poor have become sharper. Though this is an unwelcome phenomenon, much cannot be gained by ignoring it as any prolonged persistence of it may not be conducive to continued social and political stability, which is so essential not only for rapid economic progress but also for the preservation of the higher values which we cherish.

Thirdly, to get a clear picture of the trends in mass well-being, statistics of **per capita** income have to be adjusted for (a) the unduly large output of non-consumer goods and the creation of excess production capacities; and (b) for the undue build-up of inventories, which attends rising prices. Productive activity which ends up in idle production capacities and idle stocks would no doubt drive up the curve of national income in the same way as productive activity which ends up in effective capital formation and increased consumption. But the former does not add to the well-being of the people, which the latter does. Excess capacities exist both in the capital goods and consumer goods industries and in the public as well as the Private Sector. They are estimated at about one-third of the total capacity in the major and minor irrigation works, at somewhat less in the power projects and at an average of 45 to 50 per cent in 40 industries. Additions to inventories are inevitable under inflation, though it is not possible to assess their precise magnitudes.

II. Consumption of Food and Cloth :

Corroborative evidence in support of the view that mass well-being may be less than semi-stagnant is provided by statistics of the consumption of cloth and food. **Per capita** "availability" of cotton cloth, already sub-standard, fell from 14.7 metres in 1956 to 13.4 metres in 1959; after some fluctuation, it was 14.63 metres in 1963 and improved somewhat over the base year to 15.11 metres in 1964.

Per capita "availability" or foodgrains (i.e., cereals and pulses) tells a similar story. Even without adjustments being made for the additions to stocks by traders and farmers, **per capita** availability of foodgrains fell from 16.4 ozs. in 1961 to 15.4 ozs. in 1963 and was 15.8 in 1964. With record imports of 7.45 million tonnes, the **per capita** availability rose to 16.6 ozs. in 1965. The downward fluctuation of food supplies is distressing evidence, seeing that the nutritional norms for the lower income groups, who consume little of other foods, may be 18-19 ozs., army rations 19 ozs., and jail rations 16 ozs.

How does this picture compare with the position before World War II? We have the benefit of a Reserve Bank study on the subject for the period, 1931-32 to 1944-45. From the figures reproduced from this study in Table I, we find that for the seven years ending 1937-38, the **per capita** availability of cereals averaged 14.2 ozs., per day, The corresponding figure for the seven years ending 1964-65, was 13.9 ozs. per day. Imports of cereals, during the two periods of comparison, aggregated 9.5 milion metric tonnes before the war and 34.4 million metric tonnes after the war. It would appear, therefore, that despite phenomenal imports, the masses of the Indian people are more hungry today than before the war.

TABLE I

Per Capita Availability of Cereals Before World War II and in Recent Years

(million tonnes)

Year	Net Production (1)	Net Imports	Per Capita net availability (2) (ozs. per day)	Year	Net Production (1)	Net Imports	Per Capita net availability (ozs. per day)
1	2	3	4	5	6	7	8
1931-32	53.44	0.99	15.3	1958-59	57.30	3.86	13.8
1932-33	51.77	0.83	14.6	1959-60	56.77	5.13	13.5
1933-34	50.72	1.65	14.3	1960-61	60.65	3.49	14.0
1934-35	50.71	2.33	14.3	1961-62	62.08	3.64	14.1
1935-36	48.17	1.82	13.3	1962-63	58.63	4.55	13.1
1936-37	52.97	1.27	14.2	1963-64	61.41	6.26	14.0
1937-38	52.22	0.64	13.7	1964-65	66.52	7.45	14.5
Total :	360.00	9.53	—		425.36	34.38	—
Annual Average	51.43	1.36	14.2		60.48	4.91	13.9

(1) Net of seed requirements, placed at $12\frac{1}{2}$ per cent of production.
(2) Per "adult" figures, based on the assumption of adults being 80 per cent of the total population, have been converted into per capita figures.

Source :— Reserve Bank of India Bulletin, October 1948, p. 611, for pre-war years, and Economic Survey 1965-66, Table 1.4, for post-war years.

III. Investment and Foreign Aid:

This disappointing state of affairs is not owing to any slackening of investment activity, nor of the flow of foreign aid. Total investment in the Second Plan was more than double that in the First Plan. The Third Plan was over three times as large as the First and the Fourth may be about six times as large. Foreign aid. valued at the official exchange rate, rose steeply from an annual average of Rs. 40 crores in the First Plan to Rs. 720 crores in 1964-65. Budget receipts from aid amounted to Rs. 680 crores in 1965-66 and are placed at Rs. 810 crores, in the budget for 1966-67.

Large as these figures of foreign aid are, they understate the actual magnitude of aid. If aid is valued at the Indian market prices of the import goods acquired against aid funds, instead of at their landed costs which is, in effect, the budget practice, aid in 1964-65 may be Rs. 1,025 crores. This represented about 5 per cent of Indian national income; nearly two-thirds of national savings, assuming savings to be at 8 per cent of national income; and was equal in value to about four-fifths of our foreign exchange receipts from exports. On the same reckoning, budget support from foreign aid in 1964-65 amounted to 45 per cent of the capital outlay and one-fourth of total budget disbursements. Except for a year or so in the case of one or two countries, at no time of the post-war reconstruction phase did any of the Marshall aid countries receive aid on so massive a proportion.

IV. Inflation:

Notwithstanding phenomenal foreign aid, we have been harassed by inflation. So recently as 1960-61, the **Economic Survey,** issued with the Central Budget. observed that, "up to a point", because of the national upward "pull of demand", a price rise was

not only inevitable but was "the very condition of economic advance". This dangerous and misleading doctrine dominated official thinking long enough to cause considerable damage; it still holds sway with some, though the defenders of inflation are today happily, less vocal. When investment is financed from savings, investment outlays represent saved incomes. Such outlays merely replace private consumption expenditures and cannot add to the monetary circulation. Nor can inflation result from investments financed by foreign aid. Aid financed investments do not involve the issue of inflationary moneys into circulation; they add to the domectic supply of capital goods, intermediate products and other imports financed from aid.

Inflation results when investments exceed the sum of domestic savings and foreign aid. In underdeveloped economies, inflation is generally initiated by over-investment in the Public Sector. It then spreads to the Private Sector by inducing over-investment through the expansion of commercial bank credit. such credit expansion being made possible by the increase in commercial bank reserves, which must necessarily follow deficit financing of the Public Sector.

Recent experience of a number of countries, Canada, West Germany, Italy and Japan among them, demonstrates that the official thesis has no empirical support whatsoever. From 1953 to 1964, West German national income rose at an annual rate of over 16.8 per cent. And yet, prices in Germany rose only by about 1 per cent, per year, during the same period. The Japanese record is even more striking. During the period, the Japanese national Income rose at an annual rate of 22.3 per cent, probably a world record for a sustained rise at this high rate. But the Japanese price index showed a rise of only 1 per cent over the whole period. The Italian experience is no less impressive. Though the

Italian national income over the 11-year period went up by 14.4 per cent per year, prices rose by 1 per cent, per year. So far from economic progress generating inflation, in the post-war world generally. rapidity of development has been in proportion to the achievement of monetary and fiscal stability.

Economic development. even like the growth of an infant into manhood, is not a disease to cause an inflationary upset. Development must be a weird phenomenon, indeed, if, as it progresses, the fixed and sticky money income groups — the masses of the people — must suffer a continued fall in their real incomes for the benefit of the upper-income groups, traders, businessmen. and industrialists a fraction of the community. And yet, this is what would happen if prices must rise with development.

Latterly, official thinking on this subject seems to have changed somewhat. The budget speech of February 1965 referred to the "imperative" necessity of "financial stability" and of the need, with this end in view, to "eliminate" altogether long-term borrowing from the Reserve Bank. The budget speech of February 1966. repeating this sentiment, speaks of "the immediate need to restore a greater measure of monetary and price stability". But there is a contrast between precept and practice; inflation continues unabated.

The current phase of inflation began in 1955-56. when budget deficits more than doubled lo Rs. 225 crores, money supply went up by Ks. 203 crores (10.3 per cent) and prices rose by 10.7 per cent. During the past decade, 1955-56 to 1964-65, large budget deficits having persisted year after year, money supply rose by Rs. 2.160 crores and prices by 70 per cent. Since then, as at the close of February 1966, prices went up further by 12 per cent.

V. Foreign Exchange Difficulties:

The economic condition of the masses — semi-stagnant or worse — and continuing inflation are, so to speak, the primary ailments of the Indian economy. Most of the other major economic difficulties confronting us — including acute foreign exchange scarcities, mounting food deficits, undue reliance on foreign aid, paralysis of the capital market and aggravated income contrasts — have their origin, or are materially influenced by, over-investment and inflation.

The foreign exchange crisis, which has survived all attempts to solve it, is a direct outcome of deficit budgets. Ordinarily, individual money incomes are the monetary counter-part of our respective contributions to the national product. When we expend these money incomes, or invest savings from them, we claim from the stream of the national product our choice of an assortment of goods, the result of other people's efforts. What we produce others take; what others produce, we take. So long as all money incomes represent the sweat of our brows, being the equivalent of individual outputs, aggregate money demand will be balanced by aggregate output.

When budget deficits appear and moneys are created to cover them, the government acquires from the stream of the national product output equivalent to the created moneys without adding anything at all to the stream. As the consumption and investment of the people would continue as before, this reduces the goods available for exports, which constitute. so to speak, the residual or unpledged sector of the national product, on which the excess money demand may feed. Inevitably, the Public Sector projects may acquire import goods as well. This may cause imports to increase. Lesser exports would reduce the available supplies of foreign exchange; and larger imports would add to the

demand for foreign exchange. Consequently, foreign exchange difficulties would intensify as deficit financing persisted, the gap between the demand for the and the supply of foreign exchange becoming wider by the amounts of the created moneys.

We find that recalcitrant balance of payments difficulties, subject to a time lag, proceed **pari passu** with the continuance of inflation. With the commencement of inflation in 1955-56, there ensued a rapid running out of currency reserves from April 1956, the total drafts on reserves amounting to Rs. 645 crores in the decade, which followed. Currency reserves having fallen to rock bottom, the impact of inflation on balance of payments, in recent years, has produced crisis conditions in the foreign exchange market. The freeze on foreign aid with the Indo-Pakistan war in September 1965 has deepened the crisis.

VI. Mounting Food Shortages:

The mounting food shortages may be traced to the incredibly large appropriations of investment resources in Public Sector undertakings since 1955-56. Currently, valuing foreign aid at the Indian market prices of the import goods financed by it — not at their landed costs — such resource appropriations may be about 70 per cent of the total. In 1955, we had almost reached self-sufficiency in food, the foodgrains imports of the year being a meagre 600,000 metric tonnes. Imports have since fluctuated upward, the deficit in 1966 being placed at 10 million metric tonnes. U.S. experts estimate the deficit at double this figure. To attribute this deterioration to the backwardness of agriculture alone is to subscribe to a misleading and dangerous half-truth; the more important other half of the truth is the acute shortage of agricultural credit, which is reflected in the fantastic interest rates of the order of 30 to 50 per cent or more ruling in the rural sector.

When the bulk of the capital resources is drawn into Public Sector undertakings, some one in the economy must go short of capital. In the Indian context, that someone includes the cultivator, the weakest part of the economy, though he receives much lip sympathy. Capital being scarce, we cannot pursue the prevailing investment policies and have more credit for the cultivator, too.

No one doubts that, if agriculture received more investment attention, we could easily make good our food shortages, which have been of the order of 6 per cent or less of the domestic output. Per acre production of foodgrains in India is among the lowest in the world. It is higher only than the average for the African countries. In 1961-62, the Indian per acre yield of wheat was little better than one-half of the U.S. yield; and of rice about two-fifths. For both cereals, the Indian yields were less than one-third of the Japanese averages. Even simple innovations are known to bring ample returns. A recent survey in Mysore showed that better seeds alone added to the output of rice 7 to 15 per cent; transplanting, in place of broadcasting, 20 to 50 per cent; rotatinp paddy after gram, 15 to 50 per cent; and pest and disease control 10 per cent."[2] Better ploughing, more fertilisers and better irrigation should lift up the yields much higher. In all cases, the ampler returns may appear in the first crop year.

VII. Social Injustice:

Anti-social income shifts have resulted from inflation, controls and undue expansion of Public Sector investments, to which reference has been made above. We saw, too, that perhaps the bulk of the annual increases in national income accrued to a thin layer of the more affluent income sectors, corro-

2. *The Agricultural Situation in India,* January *1964.*

borative evidence of this being in the sub-standard and semi-stagnant consumplion of food and' cloth by the ,masses.

The social injustice of this arrangement is also reflected in the trend of our pattern of production. During the 14 years ending 1964-65, the output of capital goods rose from 4.3 times (commercial vehicles) to 8.3 times (railway wagons); and the output of intermediate products, from 2 rimes (coal) to 16 times (caustic soda). By contrast, the output of consumer goods used by the masses and the middle classes rose by much smaller multiples, from 1.4 times (matches) to 2.0 times (soap). The output of cotton cloth in universal use rose 1.8 times. On the olher hand, the needs of the comparatively well-to-do people, a fraction of the population, have been very well looked after. The output of goods entering into their consumption, which are mostly curios to the masses, generally rose steeply — electric lamps to 3.9 times, electric fans to 6.4 times, radios to 9.5 times, sewing machines to 10 times, and rayon yarn to 34 times.

Social injustice is reflected, too, in the price structure. The output of consumer goods in common use being unduly restricted through the forced transfer of resources into non-consumer goods industries, the prices of food articles during the past 61 years rose by 48 per cent, cereals by 53 per cent and textiles by 23 per cent. The prices of luxuries and semi-luxuries generally, on the other hand, remained comparatively steady until recently, rising only latterly and by a much lesser percentage.

VIII. Malaise of the Capital Market :

The malaise of the capital market, the heart of a modern economy, calls for urgent and serious attenlion. The failure of the stock market to respond with enthusiasm to the specific corporation tax reliefs

in the last budget proposals is evidence that stock market sentiment rests on more basic factors than individual tax measures. Share values reflect the yields on them, current and prospective; the latter depend on the volume of output and its acceleration; output is a function of thoughtful and effective investment; and investment varies with the availability of savings. The flow of national savings, therefore, is the ultimate and root determinant of share prices and stock market activity. Latterly, with the phenomenal rise in the inflow of foreign aid, interest rates and capital market activity have depended on the magnitude of foreign aid as well.

When Private Sector savings steadily rose from Ks. 670 crores in 1954-55 to 1,335 crores in 1960-61, the share prices index kept rising, too, though subject to a certain time lag. It galloped from 48.5 in 1953-54 to 100 in 1961-62, a climb of somewhat above 100 per cent in 8 years. With the sharp drop of Rs. 115 crores in Private Sector's savings in 1961-62 and their downward fluctuation thereafter, equity prices slipped downward, reaching an all-time low of 71.5 in December 1965 (1961-62 : 100), a drop of 28.5 per cent. With the failure of savings to recover, the stock market has failed to register any significant recovery apart from the attention which scrips with bonus possibilities have received since budget day.

The repressed flow of Private Sector savings is related to the steep rise in revenue colleclion and in public consumption. The link between the two is easily seen. Revenues shift incomes from the pockets of the people into government treasuries. Virtually, the whole of Revenue receipts are burnt up in public consumption, the amounts saved through Revenue surpluses for capital formation in the Public Sector being, since 1960-61, a meagre 3.8 per cent of the revenue. In the hands of

the public, the same incomes might have added to savings vastly more, perhaps about 25 per cent, as the marginal rate of saving of the more significant groups of the tax-paying public may contrast with the rates of saving of the rest of the community.

On this basis, every increase of Rs. 100 crores in Revenue collections may deprive the Private Sector of Rs. 25 crores of savings, while it may add Rs. 3.8 crores to Public Sector capital formation; and the net result may be a decline in national savings by about Rs. 21 crores. The converse may also hold true. With every scaling down of Revenues by Rs. 100 crores, private savings may go up by Rs. 25 crores, Public Sector savings may fall by Rs. 3.8 crores, and national savings may show a net increase of about Rs. 21 crores.

IX. Need for Policy Shifts

From the foregoing review, it would seem that the more usual description of India being a developing economy is rather deceptive. The masses of the people remaining poor, under-fed, and as ill-clad as ever, it may take a lot of argumentation to try to maintain that we are forging ahead. As may be seen from Table II, what has developed most rapidly during the past decade is the industrial sector, which accounts for but 19.7 per cent of the national product, the development of agriculture, which accounts for nearly one-half of the national product, lagging far behind. As the prevailing policies of centralised planning began in earnestness in 1955-56, an assessment of plan achievements should be appropriately related to the position obtaining in 1954-55. With this as the base year, we find that, as at 1964-65, industrial production rose by 111 per cent or 11 per cent, per year; agricultural production by 35 per cent. or 3.4 per cent, per year; and the national product by 46 per cent, on 4.6 per cent per year. Simultaneously, the output of foodgrains rose by 30 per cent,

or 3 per cent, per year; the output of cotton cloth by 28 per cent., or 2.8 per cent, per year; art silk yarn by 167 per cent, or 16.7 per cent, per year; motor cars by 392 per cent, or 39.2 per cent per year; and refrigerators by 3,533 per cent, or 353.3 per cent, per year.

On a socio-economic audit, the record of our achievements of the past decade or more of interventionist policies is far from pleasing. If this is their outcome despite a jump of over three times in total investments, clearly, these policies need to be changed.

X. Maximisation of National Income

It will be agreed that, as economic and social well-being are necessarily linked up with the income curve the aim of all economic policies must be the maximisation of the national product. To achieve this, the available resources — aprt from limited amounts appropriated for certain social benefits, whose market consideration cannot prevail — must be distributed such that, first the sectors where returns are high receive investment priority; and, secondly—as may be mathematically demonstrated — the last unit of resources in all production plants yield the same returns. In proportion as we may not succeed in fulfilling this doctrine of equimarginal output, the yields on marginal investments in some places may be less rhan in marginal investments in other places, and the aggregate national product may suffer.

It follows that, in the context of changing demand for end products, changing factor prices, and technological improvements, the maximisation of the national product would call for continual adjustments in the flow, or shift, of resources among the several sectors and production plants. An essential precondition of these resources adjustments and shifts is full entrepreneurial freedom over resource appro-

priations and their disposal; and no less freedom to individuals to invest their savings in accordance with their own schedule of choices.

XI. Centralised Planning

These general considerations rule out centralised planning, as administrative control over, and allocations of, investment resources are integral parts of it. Red-tape procedures and rigidities will not permit the necessary flexibiiities in resource flows and transfers, and as centralised planning continued, we may have, in place of maximum development, as Indian experience has illustrated, show-window sectoral achievements, with overall economic chaos or decay.

Centralised planning is necessarily apt to yield chaos in the prevailing Indian economic background. Nearly one-half of the Indian national income ensues from agriculture and 70 'per cent of the population draws its living from it. Peasant farming dominates agriculture, the number of farm families being 67 million and the average holding per family 5.5 acres. Tens of inillions of independent production units exist in the rest of the economy, too. Cotton textiles, the oldest and largest industry, which accounts for one-third of industrial production, comprise 2 million handlooms, scattered round the country, 80,000 to 90,000 powerlooms, and 478 large-scale mills. In such a production pattern, which cannot change overnight, it is not possible to organise centrally resource allocations, and hope to satisfy the law of equimarginal output.

XII. Rdiance on Free Market Forces and the Free Pricing System

It follows that, if we are earnest in aiming at true socialist progress — i.e., lifting up the precarious level of living of the common man — as rapidly as may be, we must reverse and abandon the policies of economic interventionism of the past $1\frac{1}{2}$ decades and

permit resource allocations, and the course and pattern of production, to be determined and directed by free market forces and the pricing mechanism, the consumer, through the shopping referendum, which he exercises daily, being in supreme charge of affairs, replacing the Planning Commission. In an effort to maximise their earnings, entrepreneurs would, then, continually shift resources to sectors and production units which bring the highest yields and help fulfil the doctrine of equimarginal output. The end of all economic activity being consumer satisfaction. this is but the most natural order of institutional arrangements we should resort to, as, consumer satisfaction being subjective, the consumer knows best what he needs and how much of the numerous things he wishes to purchase against his income. Under such an arrangement, we cannot possibly have, in peace-time, queer bundle of economic oddities of rising incomes, food shortages and declining **per capita** availability of cloth: mounting foreign aid and mounting investments; shift of resources from sectors where the output is phenomenal to sectors where it is meagre; mounting unemployment; continued mass poverty and growing opulence of the few; and intractable balance of payments deficits with inability to meet the amortisation payments on external debt. It takes a Planning Commission to produce these oddities from so hopeful a background which, under the policy reform we have indicated may very well have had continued prosperity, not continued and deepening crises.

As Professor Milton Friedman points out, the potentialities of the free market and the free pricing mechanism as an engine of truly socialist procress — i.e. progress for the common man — has been, time and again, demonstrated under all climatic, historical and social conditions.

"This is true in the broad survey of history -- of ancient Athens and Rome as well as of Britain,

Scandinavia, Western Europe and the United States in the Nineteenth and Twentieth centuries. It is true around the world today: contrast West Germany with East Germany; Malaysia and Singapore with India and Indonesia: Thailand with Burma; Hong Kong. Formosa and Japan with Red China: pre-Castro and post-Castro Cuba.

"I do not know of a single example of a predominantly collectivist and centrally planned society in which the ordinary citizen has achieved a major and sustained improvement in the conditions of his everyday life, or a real hope for the future of himself or his children — though many such societies have produced impressive monuments, ranging from the Pyramids of ancient Egypt to the steel mills and international airline of modern Egypt, which demonstrate the power of centralised authority to wrest resources from the populace for purposes of its choosing."

Referring to South-East Asia, Professor Friedman observes :

"Malaya and Singapore are islands of prosperity in a sea of misery. On the one side is India. on the other side. Indonesia. Both have relied on the techniques of central planning as the primary instrument to achieve economic growth. Both have failed. In Indonesia. there has been an absolute deterioration in the condition of the people since independence; in India, at best. minuscule growth if not stagnation. The ordinary people in Malaya and Singapore have a level of living four or more times as high as the level in India or Indonesia. And this high level has been produced entirely through free market arrangements. Singapore is a free port, and owes its prosperity to that fact. Malaya's main industries are tin and rubber. The tin mines were developed entirely by private enterprise.

The rubber tree is not even native to Malaya and none grew there 70 years ago; rubber trees were imported into Malaya from South America and their cultivation developed entirely by private enterprise."

A decisive shift from interventionism — miscalled "planning" — to the free market and the free pricing system is the first basic reform which the Indian economic situation urgently calls for. It is good to read press reports that the technicians of the World Bank, and possibly also of the I.M.F. have veered round to this line of thinking. This is a hopeful development in view of the age-old influence on policy which those who have control over purse strings may wield.

Given this basic reform. we may hopefully look for a prolonged rate of increase in **per capita** income of 8-10 per cent per year, or more, in place of the meagre increase of 1.8 per cent of the past decade. Without this basic reform, there is little chance of any lasting exit from the multiple economic crises confronting us: and, except for show-window pieces of achievement here and there, we may slip down the inclined plane of economic chaos and decay, with growing risks of social and political instabilities.

While this policy change involves abandonment of interventionism as an instrument for development, in view of its incapacity to deliver the goods, it does not amount to abandonment of all planning. In the Private Sector, planning will be done by the millions of production units; in the Public Sector, by the State; the free market and the free pricing system, conditioned by the Rule of Law, helping both. Planning by the State should be confined to its natural sphere — the maintenance or provision of the Rule of Law, of defence from external aggression, of monetary and basic communication and of agricultural extension services.

Beyond this it is not safe to go, as to do so may be to impede progress. The fatal error of policy-makers in India in common with their counterparls in many under-developed countries. has been to identify basic industries wrongly. The true basic industries are those which yield the highest output and maximum employment at current wage rates. They are not the same set of industries for all time and in all countries. Nor are they meant to be run by the Slate. In U.S.A., basic industries shifted with time from agriculture to consumer goods industries and later to heavy industries. Currently, citrus fruit and diamond polishing are among the basic industries in Israel, whose national income has been increasing at phenomenal speed during the past decade. Nor has this interfered with Israel's progress of industrialisation: as incomes and savings grew. industries developed. and Israel's industrial output has already doubled in less than a decade.

XIII. Monetary Reforms

Adoption of this basic reform must be accompanied by measures to clear the chaos which has resulted from the prevailing policies and to remove the hindrances to the full and free functioning of the market mechanism. Monetary reforms must precede other measures. The first essential step is to put a stop to inflation. P.L. 480 funds are created moneys. How can expenditure5 from these funds be anything but expansionary? Since 1956-57, drafts on P.L. 480 funds have been playing a growing role in the forces making for inflationary pressures. In recent years. about two-thirds or more of the total deficit spending in the Indian economy has come from the use of P.L. 480 counterpart funds by the Government of India and the U.S. Embassy. The most appropriate course to adopt with regard to those funds would be to freeze them, or, replace them by non-negotiable long-term debt. To use $ 300 million worth of these funds to finance an Indo-U.S. Educational

Foundalion, as proposed by President Johnson at his meeting with the Indian Prime Minister on 29th March 1966, may amount to the latter, if disbursements from the Foundation are limited to interest earnings on the Capital.

The stop on inflation must be followed by an adjustment of the exchange rate of the rupee to its equilibrium level. As it is difficult to identify the equilibrium rate otherwise than through the computer of the free market, a floating rupee may precede stabilisation, though, with risks of monetary instability ever present, merit may lie in adopting the flexible exchange arrangement until we are ready for the monetary and fiscal disciplines, which a fixed exchange rate calls for.

Press reports of World Bank and I.M.F. support to devaluation is most welcome. Public discussion on this subject shows a heavy bias against devaluation in full, to the equilibrium level. Much of the resistance to devaluation rests on the assumption that it may, first, drive up the rupee costs of imports to consumers and, secondly, that it may, reduce the dollars receipts against our exports.

Both assumptions are misconceived. Devaluation would raise the landed cost of imports. not their Indian market prices. In the prevailing context, the latter are determined by forces which are independent of the exchange value of the rupee. The impact of devaluation would be on the gaps between the landed costs and market prices of import goods, which may disappear with devaluation; this impact will be, therefore, on the market values of tho import licences, which may drop to zero. Devaluation cannot reduce the foreign exchange receipts from our exports, as the international prices of the export commodities are determined by World forces of demand and supply, which are independent of the exchange value of the

rupee. The impact of devaluation would be on the rupee prices of our exports, which may go up; and this is desirable to help restore export production to parity with the expansion of the national product and thereby to restore balance of payments viability. Foreign exchange is the cheapest economic good in the Indian market today, sterling being rated at the same value as in April 1925, and the U.S. dollar at the same value as in September 1949. It is strange logic to argue, as the opponents of devalution do, in effect, that this is an economic necessity.

XIV. Relaxation and Removal of Controls

Thirdly, import controls and exchange restrictions, which are among the worst forms of economic controls, need to be relaxed and removed. The first two reforms — zero inflation and an equilibrium exchange rate — through improving the balance of payments position, may prepare the ground and facilitate the relaxation and removal of import controls and exchange restrictions.

Fourthly, price controls, allocation controls, controls over the internal movements of goods, gold controls, and the other hurdles of licences, permits and quotas must go, too.

XV. Cuts in Public Sector Activity

Fifthly, Public Sector activity has to be scaled down drastically — in recent years Public Sector undertakings have appropriated 70 per cent of domestic savings and foreign aid, though they contribute less than 10 per cent of the national income — to permit agriculture in particular, its due share of investment resources. This must be accompanied by repeal or reform of legislative and administrative measures which, though intended to ameliorate the status and economic conditions of cultivators, have, in reality, on the one hand, undermined their creditworthiness

and, on the other, retarded the flow of credit from the capital market into farm finance.

This change in investment policy is essential not only because increased production at grass roots may increase production fastest but also because this will at the same time, ensure that the masses become co-sharers of these increases. The face of the economic landscape cannot change sufficiently fast, as Indian planners still seem to fancy, through a few units of monumental and "strategic" projects, though they may absorb colossal amounts of capital, talent and enterprise. The face of the landscape has a much better chance of changing rapidly if the 67 million farm families could get better seed; more fertilisers; more efficient implements; more irrigation; better storage and transport facilities; a nationally integrated market for their outputs; and less extortionate marketing arrangements to enable them keep a larger share of the, product of their toils than is the case presently.

What is needed is not a so-called "agricultural bias" to "planning", if by this is meant mammoth projects in rural sectors in place of more such projects in urban sectors, though this is the direction in which policy-makers seem to be moving. Mammoth projects in rural sectors may do no more than shift the geographical location of resource misdirection, extravagance and wastages; and the damage of this to the economy may continue. What the situation calls for is a free and larger flow of credit and capital to the tens of millions of cultivators and other entrepreneurs to permit increased grassroot investment.

Finally, public consumption, which, in the past decade, has risen 33 times, to 18 per cent of the national income, needs to be axed no less drastically than Public Sector investments, so as to step up national savings and economic development. In a poverty-ridden economy, overharassed by taxation, there is no practical device of achieving significant

increases in national savings otherwise than through reduced revenue collections, which the cuts in public consumption would permit. Incrased national savings would ensue from revenue reductions because of the contrast between rate of saving by the State from revenues (3.8 per cent) and the marginal rate of saving by the tax-paying public (about *25* per cent).

Many Public Sector projects, though run at a loss or at nominal profits, are capable of being worked on sound commercial principles. There is little hope of achieving this result speedily or in full when these projects are run by the State. **A** reversal of the upswing in Public Sector activity and a drastic scaling down of Public Sector investments may be helpfully accompanied, therefore, by **a** progressive denationalisation of such projects, at appropriate stages in this policy reversal. As a first step to this changeover to the Private Sector, the share capital of the Public Sector undertakings concerned may be listed for quotation on the stock exchanges. This may help to tone up their inefficient management, as share prices would necessarily reflect the degree of soundness of the enterprises concerned. The State may continue to retain ownership and control over the management of such undertakings as may not attract sufficient entrepreneurial attention from the Private Sector. To this category may belong projects of basic communication and transport, irrigation and educational or research institutions. Considering the inefficiency, colossal wastages and enormous over-capitalisation of many Public Sector projects, such denationalisation may involve, in most cases, considerable accounting losses to the national exchequer. But in the long-run public interest, in may be much wiser to write off these losses than to carry forward the budgetary and social costs and incidences of maintaining these projects as part of state activity.

The hurdles in the way of these supporting measures of reform are not economic, though doctrinaire

predilections may hinder the acceptability by some of the need to scale down Public Sector outlays; and to repeal or liberalise the land reform and money-lenders' legislation. Ideological considerations need not interfere in the same measure with the acceptability of the rest of the reforms, in particular, the monetary reforms. Even the adoption of these latter reforms alone may help to clear the economic mess sufficiently and yield handsome dividends.

CONCLUSIONS

The following conclusions emerge from the foregoing discussion:

1. The slow pace of increase in *per* capita income (1.8 per cent annually), despite mounting investments and foreign aid, is mainly attributable to the colossal misdirection of resources into the so-called infrastructure industries, where the returns are low, and for indiscriminate import substitution, where the costs are unconscionably high.

2. The actual well-being of the masses continues to be semi-stagnant or worse as evidenced by the fluctuation in the consumption of foodgrains at below the nutritional norm; and the continued sub-standard consumption of cloth. The *per capita* consumption of food in recent years is less than the *per capita* consumption in the pre-war period.

3. Notwithstanding heavy budget support from foreign aid—budget receipts from aid were as high as Rs. 680 crores in 1965-66—budget disbursements have exceeded domestic resources and foreign aid, giving rise to inflationary expansion of money. During the past decade or so money supply rose 3 times and prices by 70 per cent.

4. Neither logic nor empirical evidence support the view that inflation is a necessary accompaniment of economic development. Though official pronounce-

ments now recognise the need for non-inflationary policies, inflation is continuing unabated.

5. Most of our major economic difficulties—recurring foreign exchange scarcities, mounting food deficits, undue reliance on foreign aid, the continued paralysis of the capital market and deteriorating income contrasts — stem from, or are aggravated by, over-investment and inflation.

6. As all economic and social progress hangs on the income curve, the aim of all economic policies must be maximisation of the national product. There is little hope of achieving this without basic policy shifts.

7. The first major reform should be change over from policies of interventionism to increasing reliance on the free market and the free pricing system. The adoption of this basic reform must be accompanied by measures to clear the prevailing economic chaos and to remove the hindrances to the free functioning of the market mechanism.

8. Monetary reform must precede other measures. Inflationary finance must cease and the hurdle of currency over-valuation must be remedied by floating the rupee.

9. The major source of inflation currently being from drafts on P.L. 480 funds, these funds should be frozen or replaced by non-negotiable long-term government debt.

10. All legislative and administrative measures, which clog the springs of production and obstruct the flow of output, including import restrictions and exchange controls, should be relaxed and removed.

11. Public sector investment activity must be scaled down drastically. to permit larger availability of credit and capital to agriculture and the basic consumer goods industries. The existing public sector

undertakings, which may be easily run on sound business principles, should be denationalised: as a preliminary step to de-nationalisation, the shares of the projects concerned may be listed for quotation on the stock exchanges.

12, Public consumption, too, must be axed drastically, revenue collections being reduced to match, in order to step up national savings.

13. Given these reforms, per cnpitu national income might rise by 8 to 10 per cent or more, per year, in place of the meagre 1.8 per cent under the prevailing policies; and within a reasonable time we may have a truly socialist order of society with the income and consumption of the common man doubling every ten years or so. If, on the other hand, we persisted in the prevailing policies, we would continue to slip down the inclined plane of economic chaos and social distress, with recurring and deepening crises, which must be attended by increasing risks of social and political instabilities.

14. The difficulties in the way of adopting these reforms are mainly political. In comparison with the prevailing policies, the power content of the new policies will be less to nil. Some of these difficulties may be doctrinaire and ideological They are not economic or technological.

The views expressed in this booklet are not necessarily the views of the Forum of Free Enterprise.

TABLE II

PATTERN OF PRODUCTION, 1954-55 to 1964-65

(1954-55 — 100)

		1955-56	'56-57	'57-58	'58-59	'59-60	'60-61	'61-62	'62-63	'63-64	'64-65
1.	Investment in the Public Sector	129.0	133.4	187.0	213.9	212.6	234.7	245.8	281.8	351.8	438.3
2.	Industrial Production (1)	110.8	120.5	125.3	130.1	141.0	156.6	167.5	181.9	197.6	210.8
3.	Agricultural Production (2)	99.8	106.2	99.1	114.1	111.4	121.5	123.8	117.5	121.9	134.7
4.	National Income at constant prices	101.9	107.0	105.9	113.3	115.4	123.8	127.0	129.4	135.9	146.4
5.	Population (3)	101.9	104.0	106.2	108.5	110.9	113.5	116.2	119.0	121.9	124.8
6.	Foodgrain	100.3	105.0	95.0	113.6	111.2	119.2	122.0	113.4	118.2	129.7
7.	Cotton Cloth	103.1	107.3	109.9	106.7	108.3	111.0	117.2	115.3	122.0	127.6
8.	Art Silk Fabrics	105.4	138.5	135.1	127.5	157.6	173.2	181.5	190.8	220.1	267.2
9.	Motor Cars	223.2	259.4	207.2	185.5	272.5	385.5	423.2	410.1	394.2	492.8
10.	Refrigerators	87.2	60.2	145.1	447.9	679.8	1404.1	1169.7	1566.8	2550.2	3633.2

(1) Calendar Years; (2) Crop Years; (3) Mid = Year estimates

"Free Enterprise was born with man and shall survive as long as man survives."

—A. D. Shroff

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