THE PROBLEM OF RISING PRICES

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

—Eugene Black

INTRODUCTION

The problem of rising prices has been in the forefront of public discussion in recent months. This is a question which vitally affects, every citizen and, therefore, a careful consideration of the causes of price rise is necessary in order to tackle it suitably. This booklet, which brings together relevant excerpts from the statements issued by various commercial and industrial organisations as also from the speeches of their presidents, gives an insight into the problem. We hope this booklet will be useful for all students of economics in the country.

Since considerable controversy is raging round the cost of living index, an appendix on the subject is **also** given.

Readers interested in further readings on the subject can read with profit the following two books.

1. "Inflation & Society"
by
Graham Hutton
(Pub: Allen & Unwin)

2. "Inflation—Causes and Consequences"
by
Milton Friedman
(Pub. Asia Publishing House)

THE PROBLEM OF RISING PRICES

FACTORS INFLUENCING PRICE MOVEMENTS*

While fundamentally the rise in prices has been due to a maladjustment between demand and supply, and while also basic imbalances in the economy of West Benqal have distorted the price structure in the State, there are at the same time certain factors of all-India character of which due notice has to be taken. In fact, economically, India is a one indivisible unit. The factors governing the price situation in different regions of this 'country are basically the same. The factors are stated below:

(1) Increasing purchasing power of the public sequent on larger and larger investments under the successive plans:

Investments under the First and Second Plans were of the order of Rs. **3,360** crores and Rs. **6,750** crores, while Third Plan envisages an investment of about Rs. **10,400** crores. Of the investments during the First and Second Plans, foreign aid accounted for **6%** and **19%** only, while, in the Third Plan, foreign aid is expected to be about **26%** of the investment. Besides, the amount of deficit finance during the First and Second Plans was Rs. **333** crores and Rs. **948** crores. Provision has also been made for deficit finance under the Third Five Year Plan, although on a reduced scale. **All** these have resulted in increased money income in the hands of the people which has been given a further upward swing on account of the Emergency and the consequent rise in the Defence Expenditure. Apart from the aid from friendly countries, about Rs. **400** crores would have to be raised annually to meet our Defence Expenditure alone. It is interesting to note that the total money supply with the public has already increased from Rs. **1,804** crores in **1951** to Rs. **3,406** crores in April **1963,** recording a rise of **88.8%.**

(2) The population of India has increased from **361** millions in **1951** to **439** millions in **1960.** Since then the rate of growth has been more sharp, the latest estimate being more than 2% per annum.

(3) Variations in agricultural output have affected the prices of foodstuff and industrial raw materials. Agriculture is the king-pin of prices in the Indian economy. It contributes about **50%** of the National output and any rise or fall in the output greatly affects prices all-round and the economy of the country.

(4) Slower rate of increase in industrial production due to shortage of power, local raw materials as also of imported raw materials as a result of foreign exchange difficulties.

(5) Time lag involved between investments made for an industrial project and its fructification or the gestation period in the fructification of a project.

(6) Investments in basic social overheads and other capital goods industries which bring in benefits to the consumers only after a long period.

(7) Increase **in** the manufacturing cost on account of rise in the prices of raw materials and in wages and social security legislation.

(8) Taxation Policy of the Government: There has been a gradual increase in the number of items brought within the purview of excise duty, the rates of which have been progressively increased.

The total excise revenue has increased from Rs. **67.54** crores in **1950-51** to Rs. **145.25** crores in **1955-56,** and to Rs. **489.31** crores in **1961-62.** The revenue for the current year after taking into account the additional duties imposed under the last Finance Act has been estimated at Rs. **700.17** crores. The figures for **1961-62** and the current year also include the yield from additional excise duties imposed in lieu of sales tax. Undoubtedly, during the intervening periods, production of different commodities has

* *This is an extract from the Memorandum submitted to the Price Inquiry Committee set up by the West Bengal Government by the Bengal National Chamber of Commerce & Industry in July 1963.*

also increased, but it will be evident from the following tabla that the revenue from excise duties from particular duties has been very much more proportionate to the increase in production:

	Production		Excise Revenue	
	1951	1961	1951-52	1963-64
	(Monthly average Production in thousand yards)		(Rupees *in Crores*)	
Mill Made cloth ...	339,682	420,695	16.36	56.50
	1951-52	1960-61		
	(Monthly average production in thousand tons)			
Sugar ...	124.5	248.6	8.43	63.80
	1951 (Monthly average production in millions lbs.)	1961 (Monthly average production in thousand kg)		
Tea ...	52.4	28,984	4.31	15.98
	1953	1961	1953-54	1963-64
	(Monthly average of production in tons in the organised sector)			
soap ...	6,850	11,900	0.16	4.98

Apart from the specific commodities (only soma of which have been mentioned above by way of illustration),

on which the incidence of taxation has borne very heavily, due account should also be taken of the indirect effect on the prices of commodities caused by the imposition of, or increase in the rates of, excise duties on such articles as packaging materials and containers and also on parts and components of motor cars and trucks and petrol and diesel.

, Similarly, the increase in the coverage and the rates of sales tax, both State and Central, have caused a rise in the prices both of finished and also of raw materials.

In West Bengal alone, sales tax revenue has increased from Rs. 6.15 crores in 1950-51 to Rs. 19.73 crores in 1960-61 (Reports of the Finance Commission).

These fiscal measures have been taken avowedly with two-fold objects of increasing the revenue of the Government and also of curbing consumption by forcing an indirect rise in the prices of commodities.

(9) Increase in railway **freight and road transport** cost: The basic rate of railway freight was last revised upwards in 1958 on the recommendation of the Railway Freight Structure Committee. The rise at that time was to the extent of 4%. Since then, further additions have been made in 1960, 1962 and 1963. The additions have been to the extent indicated below:

1st April 1960—Additional Surcharge of 5%.
1st July 1962—50 nP. per ton up to 40 Kilometres.
1st July 1963—Further Surcharge of 5% on goods freight and 10% on parcel traffic.

These rises have been uniformly applied to both raw materials and finished goods as well as on coal. Certain concessions which have been given in the case of goods exported from the country do not, however, affect internal prices, except perhaps indirectly in so far as in enhancing the freight charges on all other commodities, the Government has taken into account the loss of revenue that would be entailed in giving these concessions.

(10) The financial burden imposed by the Emergency Risks Insurance Schemes has also increased the cost of production. Though the rates of premium under both the Schemes have been progressively reduced since

they were first introduced, the fact remains that the amounts paid on these two accounts have added to the cost of, production.

(11) Credit Control of the Reserve **Bank**: It is doubtful how far the Selective Credit Squeeze Policy of the Reserve Bank of India has been successful in curbing speculative hoarding. It has, in fact, been complained that at least in the case of rice and paddy, the policy has actually caused some rise in the price of paddy by preventing rice mill-owners from acquiring stocks at a time when prices ruled at a comparatively lower level in the market.

There is a wrong impression harboured in certain quarters that one of the main causes for the rise in prices is the undue margin of profit retained by trade and industry. The fact is, however, otherwise, though there may be individual cases of profiteering. By and large, trade and industry in general are retaining lesser margin of profit than in other countries or is generally believed. In so far as companies are concerned, a survey made by the Department of Statistics and the Division of Monetary Economics of the Economic Department of the Reserve Bank of India shows that their profits after tax as percentage of net worth are generally very low. In cases of certain industries like coal, cement, steel and textiles, the selling prices of their products or their margin of profit is controlled by either the Government|Tariff Commission or by the industries themselves. Further, companies have to pay income-tax at a high rate. As a result, the amount of profit retained by companies is generally too low. Regarding trade, the wholesalers are generally retaining a gross margin of not more than 2 to 3% on sale of commodities such as foodgrains, sugar, etc., while the retailers' gross margin would not exceed 5 to 10%. If account is taken of the cost incurred by the trade in procuring and storing the goods and then selling the same, net profit margin would indeed be negligible. It is also to be remembered that there is always a competition in the trade which generally helps in maintaining prices at a reasonable level.

On the other hand, complaints have been received

about the unduly high profit made by the S.T.C. in selling certain essential goods imported by it. **Some instances** are given below:

Name of commodity	c.i.f. price	Custom's duty	S.T.C's Margin	Trade's margin	Total price
Betel Nuts per bag of 100 kg.	37.20	300.00	@ 187.50% on c.i.f. price = 69.50	@ 2.5% on landed cost = 8.10	414.80
Camphor per kg.	Landed cost 2.50 to 2.75		10.10		
Clove	4.25	18.15	6.60	......	31
Coconut Oil (from imported Copra on the basis 60% recovery)	1300.00	135.00	340.00	......	1,775.00

IMPACT OF TAXES ON THE PRICE LEVEL NEEDS TO BE STUDIED*

G. D. SOMANI,
President, Indian Merchants' Chamber, Bombay

One of the main conditions for the successful implementation of the development programmes and for maintaining the civilian morale in the period of the emergency is the holding of the price line. The commercial community has given its utmost co-operation and has taken all steps to ensure that the prices did not rise on account of factors within their control. This is also recognised by the Government and Mr. Nanda was of the view that the prices had stabilised at a reasonable level and the price changes were of small magnitude. But since the announcement of the budget proposals, the satisfaction of the prices being stable has proved to be short-lived. The index of prices has continuously looked up and was placed at 130.2 for the week ended April 20, 1963, indicating a rise of 6.3 points or 5.1% over the corresponding week last year. The largest increase at 31.3% was noted by sugar and gur followed by tobacco at 16.2% and fuel, power, light and lubricants at 13.1%, pulsesrose by 11.1%.

Whenever there is an upward trend in prices, the commercial community, particularly the industrialists, are held to be responsible, and it is often suggested that if the prices are not brought down by the commercial community, price controls and physical controls will have to be clamped down as the necessary remedy! We have today reached a situation in price level when the real factors which have contributed to the price rise require to be examined objectively so that both Government and the public should know very clearly where the responsibility for this rise lay. As is well known, the steep rise in indirect taxation in the Budget for 1963-64 had given an immediate push to prices and a measurement of the impact would really yield revealing results. It is not possible for industries to pass on at once the fresh imposts of excises and import duties to the consumers.

* *An extract from the Presidential speech at the first quarterly general meeting in June, 1963.*

The present price rise is also the result of a multiplicity of factors. The stagnation in the output of food and industrial consumer goods, deficit financing, enhanced development expenditure, doubling of the defence expenditure and increase in indirect taxation have all exercised their pull and when the volume of effective monetary demand is higher than the supply of goods and services, the prices must inevitably rise.

The industrial sector, though it has shown a modest improvement, has not been dynamic in respect of consumer goods. The rise in the output of producer goods was 14% compared to a rise of only 2% in consumer goods. The consumer goods both in the agricultural and industrial sector have failed to rise so as to match the effective demand which has been increasing both because of the rising money incomes and population. The shortage is particularly felt in food supply and in sugar among the a@-cultural commodities. The food front has almost failed to relieve the supply position. Even in sugar the adequate supplies of the last two years have been succeeded by acute shortage because of a sudden fall in production. The latest estimates show that the sugar output is not likely to rise beyond 21.5 lakh tons compared to 27.14 lakh tons in 1961-62 and.30.29 lakh tons in 1960-61. The price rise is obviously the result of inadequate production. But the traders have been held responsible for the situation.

Besides, the steep rise in the volume of Government expenditure—development and non-development—is also a determining factor in stimulating additional purchasing power which in turn cannot but impinge on the price level. The sharp rise in the size of the Union Budgets with similar increase in the budgets of State Governments has led to an inflationary impact on prices. The budget deficits have imparted an additional push to the price level. In the first three years of the Third Plan, the overall deficit is likely to be around Rs. 585 crores. Without the cushion of additional supplies of consumer goods, which have not increased, the pressure on prices arising from budget deficits has not been restrained. The rise in defence expenditure is another factor also strengthening the inflationary potential. The fiscal policy of the Government is also to be examined in relation to the developing pressure on prices. While credit curbs are necessary to prevent speculative transactions, the pipe-line of credit should be open to industry and trade for genuine demands, To an extent, it is recognised that the credit policy of the Government has been a factor in preventing the growth of industry. Further, the rise in prices has set up a vicious circle in relation to industrial wages. The increase in prices is reflected in the cost of living indices and the dearness allowance of industrial labour being linked to the movement of cost of living indices the wages of labour get inflated and exert additional pressures on the prices of consumer goods. Wage inflation has thus been an additional factor for increasing buoyancy in prices at the present moment. These are the various factors, external to the industry and to the trade, and over which they have no control, which largely explain the spiralling of prices. In this national emergency the commercial community have assured their fullest support to the Government in holding the priceline and they will abide by it. But if factors entirely beyond their control give a push to the priceline, it is not fair to hold them responsible for it.

Controls on prices and distribution are of doubtful utility. If the present situation where prices threaten to break the reasonable level is the result of the shortfalls, of failures and waste in the p-duction line, the controls on prices and distribution would only accentuate further the scarcities and thereby lead again to the most unhealthy spiralling of prices in the future. It is a moot point whether present spell of inflation can be checked by tinkering with the problem either through price controls or through opening more consumer co-operatives or acquiring the entire stocks of the scarce commodities. Even the very announcement of such threatening steps may lead to unhealthy hoarding and excess demand on the part of consuers which the existing supplies cannot meet. The price rise should be clearly understood to be due to overall shortages and to the price regulation policy of the Government. It has to be very seriously considered whether the industry bas any scope for inflating the prices of the product

in the present scheme of regulation, that is already existing. Many of the basic commodities, such as iron and steel, cement, coal, paper, soda ash, are under the rigid control of the Government in relation to prices. Similarly, in regard to rice and sugar and certain other consumer goods there is regulation. If there is any upward movement in the prices of these goods, obviously it must be mostly due to the factors beyond the control of the industry and trade; either it must be the result of the Government policy of regulation itself with lack of proper co-ordination, duplication of work and red-tapism or it must be due to basic economic deficiencies. Therefore, a great responsibility rests on the business community in educating the public on the policy of the Government in regard to price fixation and also on the real factors which impinge on the price level. It is necessary to have a special study of the impact of taxation, especially of indirect taxation on certain primary consumer goods and intermediary industrial goods. The indirect taxes, the bulk of which are on wage goods and producer goods, have great inflationary potential in so far as they affect substantially the wage and cost structure of the various industrial and consumer products. They affect not only the final product but the cost of the entire range of intermediate goods. Such a study would bring to light the cause behind the persisting inflationary rising prices.

AGRICULTURAL PRODUCTION DESERVES MORE ATTENTION*

At a Press Conference, the Union Planning Minister is reported to have stated that the principal cause of the recent rise in prices was the exploitation of marginal shortages by the trade despite the business community's assurance at the time of the Chinese aggression to hold the price line. While any unscrupulous elements in the trade who may have exploited the situation resulting from the scarcity of goods in certain areas are to be condemned, it is high time that the Government also realises its

* *This is a statement* issued *by* the Indian *Chamber of* Commerce in *Calcutta in July 1963.*

own responsibility in enabling the price line to be maintained. After the emergency, the demand for goods and services has continued to increase, but the overall production apparatus has remained stagnant, and it has not been possible to achieve a higher rate of production either in the agricultural or industrial sectors. The national income in the agricultural sector has declined during the last year, and the availability of cereals per capita has been reduced instead of increasing.

It seems less attention is being paid to fundamental issues concerning production and instead there is more emphasis on regulation and control of distribution. Unless agricultural production increases substantially and adequate attention is paid to the factors which impede a higher rate of production, it will hardly be possible to maintain sufficient supplies for distribution. While the agricultural production is not going up, the country continues to be deficient in fertilisers and there seems little possibility of the targets being achieved in the Third Plan. Our agricultural output will continue to be stagnant without adequate availability of fertilisers and other essential requirements of the agriculturists. If as a result of lower production there is less left to go round, it will be wrong to blame the trade for not delivering the goods.

In the case of the sugar industry, the cost of sugar production is largely dependent on the length of the season. If there is less production, the industry suffers, as also the consumers. At one time, the industry had huge accumulated stocks of sugar as there was no demand. It was then decided by the Government to limit production temporarily though it was no solution to the problems of the industry. The industry could thrive only with larger production, more consumption, and larger exports. But the statement of the Union Planning Minister creates an impression as if the industry was interested in reducing production, which is not the case. In fact the statement of the Minister to the effect that the Government was pushed into imposing imprudent curbs on production by the agitation of the industry is not justified. On the other hand, the industry was actually pressing the Government to maintain buffer stocks of sugar just as had been done in the case of certain other commodities like wheat. If the Government had accepted the suggestion of the industry, the present shortage would not have occurred.

It is well known that rice production in the country has fallen, and there is not enough rice to go round in certain parts of the country, while there are surpluses in certain other parts. The cultivators had been reluctant to release paddy in the expectation of higher prices, and the rice mills have not been able to obtain sufficient supplies to meet their requirements. For want of paddy, most of the rice mills in West Bengal had been working only up to 30 to 40% of their capacity and some of them had even to close down. No positive action was taken by the Union Government either to remove the zonal restrictions on the distribution of rice, or make available more paddy to the rice mills,

The business community is at one with the Government in its anxiety to maintain the price line. Ever since the emergency was declared, responsible organisations of trade and industry have been straining every nerve to keep prices down, and have succeeded to a large extent, which is indicated by the fact that the index of wholesale prices went down after the emergency was declared. Wherever they have not succeeded, it has been due to factors beyond their control, such as progressively rising fiscal levies, inadequate supplies, higher transport costs, inadequacy of transport and such other reasons. Somehow these factors are overlooked while assessing the responsibility for any rise in prices. It is necessary that the factors which have led to rising prices should be realistically examined by Government and measures devised to help increase production which alone will help to maintain the price level.

THE GOVERNMENT SHOULD ADOPT A PRICE POLTCY BASED ON PRODUCTION CONSIDERATIONS*

LALCHAND HIRACHAND

President, Maharashtra Chamber of Commerce, Bombay

The Government of India has all along been expressing concern at the rising tempo of prices, but has also been increasing the rates and basis of Union taxes. We have been noticing an almost continuous rise in prices, and side by side, a trend of rising taxation. It is claimed that taxation is intended to mop up excess funds put into circulation through deficit financing and Government spending. In that case, the wholesale prices should have shown some restraint. But the contrary is the case. The "Report on Currency and Finance" of the Reserve Bank of India admits the rise in prices during March that year, which reflected the impact, to some extent, of the new levies on several commodities in the Budget for 1963-64. In the six months period, i.e., April-September, 1962, the index number of commodity prices (base 1952-53=100) had gone up by over 7 points from 122.9 to 130. This year as compared to March 1962, the index number has gone up from 122.9 to 127.3. Between April 1963 and 22nd June, 1963, the period following the new taxation, in a comparatively smaller period, the index number has gone up by 7.4 points. The consumer price of steel has already been increased. Textiles are straining against the price barriers, and the position in many other industries is not more secure. It appears that in India taxation has already gone beyond the saturation point when it can be absorbed without affecting the price level. Every further rise is bound to raise the prices. It is, therefore, high time, that the Government should take account of this factor in the economy, lest the injury to the economy of the country may go beyond repair.

It is becoming increasingly clear and painfully evident that the Government lacks a well-knit price policy.

* *Excerpts front the Presidential address at the Third Quarterly General Meeting of the Chamber in July, 1963.*

In respect of commodities now in short supply—sugar, vanaspati, rice, steel and cement—the Government has often tended to move by fits and starts, tinkering with control and decontrol alternatively, achieving hardly anything except disappointment and frustration.

It would be well if the Government recognised that the control of prices is essentially an economic, rather than an administrative problem. So long as prices cover production costs, the administration of price controls is simple. If the costs go up, as they have done in cement and paper, the Government should be prepared to revise prices. But it is not always prompt in conceding the industry's demand. The Government should not develop a blind spot to the realities of production costs. An adequate price policy based on such considerations could help in bringing down prices through increased production.

PRODUCTION OF ESSENTIAL COMMODITIES SHOULD BE INCREASED*

The country has embarked upon an ambitious programme of planned development and, in that context, it is considered necessary that prices of essential commodities are maintained at a reasonable level and inflationary trends do not distort the expanding economy. The recent rise in prices of foodgrains and other essential commodities has been a matter of concern to the Central and State Governments. With a view to arresting the rising spiral of prices of foodgrains, sugar etc., the Government of India has given a directive to State Governments to enforce the Defence of India Rules, tighten the machinery of Inspectorate and take drastic measures against erring traders.

The committee of the Gujarat Vepari Mahamandal shares the anxiety of the Government to hold the price line, regulate prices of essential commodities and ensure equitable distribution thereof. Interests of consumers is a matter of great importance and trade and other interests should extend all possible co-operation to the Government

* *This is a statement issued by the Gujarat Chamber of Commerce in Ahmedabad in July 1963.*

to achieve the objective. Although, the business community is in accord with the Government as to the need for bringing the prices under check, taking action against anti-social elements and safeguarding interests of consumers, in its enthusiasm and anxiety to hold the price line, the Government conveniently ignores a very patent fact that the price sructure is a very delicate and complex mechanism and price level of commodities depends upon a number of factors apart from the profit motive of the distributive trade alone which is so loudly talked about. The most vital factor is the supply position of commodities. Whenever an acute shortage of a commodity is found, the holding of price line becomes well nigh impossible. The magnitude of Government spending, fiscal levies and other burdens, increased purchasing power of the people, growth in the rate of consumption, and in population, failure or continuously irregular and insufficient monsoon, shortfalls in production, inadequacy of transport etc. are also factors which contribute to the rise of prices.

There may be a few anti-social elements in business, as in every sphere of life, who might be exploiting the situation to their own interests; however, it would be a travesty of truth to single out traders and business men alone and hold them solely responsible for the present rise in prices and charge them with speculation, hoarding and profiteering. It would be highly unfair to trade to malign the business community as a whole and treat them in a manner as if they are devoid of patriotism, civic conscience and a sense of duty towards the Country.

With a view to checking the rising prices of foodgrains and prevent malpractices, the Government of India has recently sent a directive to the State Governments to take stern measures against erring traders, strongly enforce Defence of India Rules and put in motion the machinery of the Inspectorate. However, these measures by themselves cannot achieve the purpose in view, in a vast country like India. What is needed to ensure proper distribution is utilisation of the experience and skill of the established trade channels.

After the Communist Chinese aggression on our northern border, when the Government made a call to the

Nation to keep the enemy at bay, consolidate our forces and be prepared for greater sacrifices, it was the business community along with other classes that had come forward, evolved a code of ethics and made every effort to see that the prices did not rise. Patriotism and the Keen sense of duty that were shown by trade in subsequent months were openly recognised by Government spokesmen at that time.

It is highly unfortunate and regrettable that whenever there is a rise in prices, it has become the practice with Government spokesmen to hold traders solely responsible for the situation. While one may not object to the policy of the Government in enlisting the support of Co-operative Societies for distribution of essential commodities, the Government's approach of diverting commodities to Co-operative Societies on the plea that trade has misbehaved cannot be accepted.

CONTROLS HAMPER BUSINESS AND JNDUSTRY*

JAYANTILAL P. SANGHRAJKA,

President, Andhra Chamber of Commerce

The Government, the politician, the planner, the businessman and the common man are all quite in agreement that prices should be brought down or at least kept under check, if a reduction is not possible. A rise in prices takes place often due to causes beyond the control of the businessman. But, he being the person who passes on the product to the consumer becomes the scapegoat.

Suggestions are made that industry and trade should be nationalised or drastic steps should be taken against the businessman. Threats of replacing the normal trade channels by co-opeartive and other agencies are also given. While I am not holding any brief for anti-social elements who may be exploiting the situation here and there, I am of the view that the generality of businessmen are not

* *This is based on a speech delivered at the Regional Conference of Chambers of Commerce in Hyderabad in June 1963.*

only honest but they have also been playing their part very well. They have been, in their own way, contributing towards arresting the rise in the price level.

It is common knowledge that consequent on the restrictions on imports there has been a shortage of many commodities. There is shortage even of food articles. When demand exceeds supply, prices naturally tend to go up. The Government is interested in assuring the farmer a minimum economic price for his produce. It is, at the same time, interested in assuring the consumer of his requirements at a low price. The businessman invests his money, takes all the risks and incurs expenditure by way of transport, storage, marketing, taxation, insurance, and the like besides salaries and amenities to his employees. The; difficulties of the manufacturer are all the more greater since he has to meet many more problems such as the procuring of raw materials, power and fuel besides meeting increasing labour costs. Little is spoken of the cost of these items when referring to the profit the businessman or industrialist would ultimately earn after meeting all these charges. In fairness, the Government should assure a minimum net return to the trade also. It is little realised that taxation measures, direct and indirect, State and Central, coupled with the inflationary trends, have contributed to the present price phenomenon. It, therefore, becomes incumbent on the Government to tell the public at large that they have to put up with the rises consequent on such measures.

The businessman is today completely lost in a maze of controls and regulations and procedural tangles. He has to maintain innumerable records and registers and submit a large number of returns under various taxation and legislative measures. In spite of all these things, he does not receive the appreciation that is his due.

While businessmen have pledged themselves to contribute their part and appreciate that no hardship, sacrifice and self-restraint is too great for strengthening national freedom and economy, it is not too much to ask the Government and the public to realise the role played by the bceinessmen.

FAULTY PLANNING AND FALSE PRIORITIES SHOULD BE CORRECTED*

P. U. Patel

Despite its best efforts, the Government has found it impossible to exercise any effective control over a rise in the price level of articles of daily necessity—such as food, clothing etc. Constant pumping of additional currency into circulation on the one hand and the levying of additional Excise Duties on a substantial scale, year after year, cannot but result in higher prices. Instead of straightway admitting that the rise in prices has been the direct consequence of the fiscal and monetary policies it has been pursuing, the Government has adopted the unusual alternative of blaming the-business community for what has been happening. While it may not perhaps be altogether correct to exonerate businessmen or traders from their share of the blame, it must be clear to any fair-minded person that a major portion of the blame for prices shooting upwards attaches to the Government and to no one else. To the extent that the levying of additional excise duties would result in reduced consumption, a rise in prices would be prevented. But it is only in an era of plenty that this would happen. We, in India, are living in a world of "scarcity all-round" and as such, a rise in prices is inevitable. Increased production on all fronts is the only answer to the situation facing us today. And it is high time it is realised that mere sanctimonious sermonising by Ministers will not and cannot lead to increased production either in the fields or in the factories.

Faulty planning and false priorities have been responsible for the mess in which we find ourselves today. There has been too much of gloating over imaginary achievements in the past and too much of wishful thinking so far as the future is concerned. If we are really to gel anywhere, a reorientation of outlook is desiderated.

* *Extracts from Mr. Patel's address at the annual meeting of the Indian Insurance Companies Association as the outgoing Chairman, in July 1963.*

APPENDIX

THE COST OF LIVING INDEX*

The retail prices of consumer goods are a matter of concern to all as they determine the level of the standard of living that one can afford out of one's income. A general rise in the prices of consumer goods may increase, what is called, the "cost of living" of all persons; and, unless there is a corresponding rise in their income, it may even compel them to reduce their standard of living. But such situations have a relatively more serious effect on the well-being of those whose income is comparatively low, as a price increase that may cause the comparatively rich to go without a few articles of luxury and comfort may require the comparatively poor to curtail their consumption of necessaries. There is, therefore, in most countries some provision to compensate industrial workers, salaried clerks, and the like, whose income is both fixed as well as low, for the changes in their cost of living due to the changes in the retail prices of goods they are accustomed to consume. The device to measure such changes in the cost of living is still called in India the "cost of living index", although in the U.K., and the U.S.A. it is called, more appropriately, as explained below, the "retail price index" and the "consumers' price index" respectively.

Although most people would like to see their "standard of living" rise and their "cost of living" fall, they might differ about the meaning of the two terms. Some may regard the tangible things—such as foodstuffs, clothing, houses, entertainment and means of transport—that they consume as their standard of living. Others may regard the "satisfaction" or "utility" they derive out of the tangible things they consume as their standard of living.[1] For the purpose of analysis, it might be helpful to define "standard of living" in terms of abstract and subjective elements such as "economic satisfaction" or "utility"; but, as these elements are incapable of being measured, such definitions are unsuitable for a practical purpose like the construction of a price index. A widely accepted definition is given below.

In general, standard of living may be defined as such a sum of commodities and services of all sorts as is habitually consumed in a given length of time—say a year—by a person or a family group of given size and given social stratus. It is not itself a sum of money but a sum of goods. Its money cost will necessarily vary at different times and places and must therefore be recalculated periodically.[2]

The above definition, which has been adopted for this study, gives a concrete meaning to the term "standard of living." The content of the standard of living is a "sum of goods and services," which may be determined by conducting a "family budget inquiry" or a "family living study." A systematic inquiry may help determine the average composition, income, and the consumption pattern of families belonging to a particular socio-economic group during a particular period. The average "sum of goods and services" so determined may be regarded as the **standard of living** of the class, and it may be described, for the sake of simplicity, as the **market basket** of the family belonging to that class. All items of expenditure, such as foodstuff, clothing, housing, medical services and transport, during a particular period, may be imagined as packed in the family's market basket, which may be regarded as the physical embodiment of the standard of living of that family during that period.

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1. An international authority defines standard of living as "the sum of the economic satisfactions or utilities which an individual (or *a family) derives from the consumption of the goods and services which he is able to obtain with his income available during a certain period of time." International Labour Office: A Contribution to the Study of the International Comparisons of Costs of Living, p. 7.*

2. Bowley: The Nature and Purpose of the Measurement of Social Phenomena, 2nd Edition, London, *1923, p. 164.*

Before proceeding further, it is necessary to be clear about two other points. Firstly, according to the definition given above, the market basket or the standard of living of a specified family that is relevant to the index is the one that the family **actually consumed** during the period of inquiry, and not the one that the family itself or others relying on scientific data may regard as ideal. It is obvious that the problem of the ideal standard of living, though of great human interest, is irrelevant to the construction of a price index. Secondly, the "free or social income" of the family, such as, for example, free education, medical attention, entertainment and also the benefit of working conditions obtaining at the place of work, for which no payment is made out of the income of the family, is excluded from the market basket of the family for the purpose of the index, as there is no satisfactory method of taking such items into account.

For the purpose of the index, the stantard of living of a person or a family belonging to a particular socio-economic group during a certain period is, as explained above, the sum of goods and services actually bought for consumption by the family out of its own income within that period. This sum of goods and services has been described above, for the sake of simplicity, as its market basket. The money cost of buying the market basket or of maintaining the standard of living of a **particular** family during a particular period is the cost of living of that family during that period.

The cost of living of a family may change from period to period owing to two causes: firstly, changes in the retail prices of the, constituent items of the family's market basket; and, secondly, changes in the composition of the market basket itself. It would he easy to obtain the retail prices of the constituent items of the market basket from month to month and to compute a series of index numbers that reflects the monthly changes in the cost of living due only to changes in prices; but it would not be feasible to obtain every month the huge mass of data that is necessary to ascertain the changes in the composition of the market basket of the family in the corresponding months, and, as such, it is not practicable to construct

an index that reflects changes through time in the cost of living due to changes in the composition of the market basket. Because of this difficulty, an index has to be constructed on the assumption of a **fixed market** basket, that is, on the basis of a constant standard of living. The standard of living determined in accordance with a family budget inquiry is regarded as constant for one or more years, until such time as it is revised on the basis of another comprehensive inquiry or a sample survey and the **fixed** market basket is revalued monthly at current prices to compute a series of monthly indices.

The assumption that the market basket of a family does not change from month to month is not true to facts. Certain changes in the composition of the market basket of the family occur only over long periods and it would be reasonable, therefore, to ignore their effects on the cost of living, at least during short periods. But the effect of those changes in the market basket that take place during short periods cannot be reasonably ignored. The changes that take place over long periods in the family's market basket may be due to changes in the composition of the family, which may occur, for instance, owing to the birth of a new child; or due to changes in the family's income or tastes (consumption habits); or due to the unavailability of the particular goods and services habitually consumed by the families; or due to rationing and other governmental controls that limit the free choice of consumers. Normally, such changes in the market basket are not frequent; and when they occur suitable adjustments may be made in the index and during the period between such adjustments the market basket may be reasonably assumed as fixed. But it would not be reasonable to ignore the short-term changes in the standard of living that are due to price-induced substitutions as they take place almost every month. A family may find that a part or the whole of a certain amount of money that it used to spend on buying a certain quantity of a particular item—say tea—may be better spent in buying instead more of another item—say coffee, when in a different price situation, the **former** item becomes, in the judgement of the family, relatively dear and the latter item relatively cheap. Every family exploits the scope for such substitution till it finds that further substitution is not worthwhile. Such substitutions alter the composition of the market basket of the family from month to month and, as such, they must be taken into account when calculating its cost of living from time to time. But, as it would not be feasible to obtain every month the huge mass of data that is necessary to ascertain such substitutions, it is not practicable to construct an index that reflects changes in the cost of living due to price-induced substitutions in the market basket.

As the term "cost of living index" often leads laymen to believe that it reflects changes in the cost of living due to price changes as well as due to other causes, and also that it measures the total current expenditure on consumption, the authorities in the U.K. and the U.S.A. have replaced the term by the more appropriate terms "retail prices index" and "consumers' price index", respectively.

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—A. D. Shroff

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