

# ECONOMIC GROWTH WITH SOCIAL JUSTICE

PROF. B. R. SHENOY



**FORUM OF FREE ENTERPRISE**

PIRAMAL MANSION, 235 DR. D. N. ROAD,  
BOMBAY 400 001.

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

—EUGENE BLACK

# ECONOMIC GROWTH WITH SOCIAL JUSTICE

BY

PROF. B. R. SHENOY\*

A free society is so called because its citizens are free individuals, free in the sense of "independence of the arbitrary will of another". Individuals in a free society function, in the economic sphere, under the guidelines of the doctrine of pragmatism, pursuing the line of success and discarding the path of failures, success and failure being assessed by their own subjective criteria. Viewed functionally, a free society may also be termed, therefore, as a pragmatic society. As the terminal aim of the individual's activity is the maximum satisfaction of his consumption needs, and he is unfettered in this as in other matters, a free society is described, too, as a society of consumer sovereignty.

The principal economic constituents of a free society may be briefly stated :

- (i) First and foremost the economic affairs of a free society are controlled, directed and governed by truly sovereign consumers. Therefore, by definition as it were, all economic activity other than those delegated by consumers to the government — which they do in their capacity as sovereign voters — have, for their end objective, maximum consumer satisfaction.

---

\* The late Prof. B. R. Shenoy was an eminent economist. This paper, written in August 1977, a few months prior to his death, is of relevance today when there is considerable rethinking on need for a new economic policy.

- (ii) Consumer control and direction of the economy is effected through a price-regulated market mechanism. Consumers register, in the shopping centres or other markets, their votes regarding their requirements continually, and their preferences get reflected in commodity price changes and in turnovers.
- (iii) Traders interpret these price and turn-over signals, and direct producers to adjust their production programmes to match the consumer needs, thus recorded.
- (iv) Available investment resources, i.e. domestic savings and inflows of foreign savings, get shifted, through such activity of traders and producers, and via the capital market — which is an integral part of the overall price-regulated market mechanism — or otherwise, into production channels which meet consumer-preferences.
- (v) In a modern society — whether it is free, communist or socialist — production involves time, and the production process has, for technological reasons, to commence in anticipation and in advance of demand. The forward market, which is another integral part of the overall price-regulated market mechanism, helps such anticipatory production. The forward market may reduce to a minimum, or eliminate, resource wastages from production errors, by projecting the changing market situations.

Operationally, the first link in this chain of consumer-directed economic system is, it will be noted, trade which interprets and transmits to producers consumer decisions. That trade is the spearhead of all economic development emerges graphically when we imagine a community cut off from the rest of the country, of which it had been traditionally an integral part. Production for the national market will then soon be replaced by production to meet the limited

needs of a small community; and its people are consequently destined to slip down into poverty and, possibly, into more or less primitive way of life, depending on the size of the isolated community's market. A pre-condition for the full and efficient functioning of a free society is, therefore, the absence of barriers to internal and external trade. Logic and experience have shown that this freedom will permit continued prosperity for the economy — the result of the use to capacity of its specialised talents through integration of the national economy with the world markets, the demands of which — unlike the demands of the limited national markets — may not be easily satiated.

Secondly, the full and efficient functioning of a free society demands recognition of the institution of private property, not only in respect of a family house, the durable consumer goods in it and a car, but also in respect of capital assets, the means of production. In a free society, because of the discipline of a most ruthless consumer, the management, under the duress of survival, has to keep a continual watch over cost, quality and turnover. This calls for perpetual flexibility of decisions. Consumer discipline operates, in the case of the larger corporations, through its impact on the stock-market quotations for the scrips of the corporations. It is just not practical to achieve the requisite decision flexibilities under social ownership — i.e. the ownership of no one in particular! — of the means of production. Experience has shown that the magic of ownership is among the most powerful forces making for progress. Ludwig von Mises observes in his book **The Free and Prosperous Commonwealth**: “The foundation of any and every civilization, including our own, is private ownership of the means of production. Whoever wishes to criticize modern civilization, therefore, begins with private property. It is blamed for everything that does not please the critic, especially those evils that have their origin in the fact that private

property has been hampered and restrained in various respects so that its full social potentialities cannot be realized."

The power of the magic of ownership of the means of production is nowhere more convincingly demonstrated and highlighted than in Soviet agriculture. In 1964, the output of 3% of the land under collective farms, the private plots allotted to their workers, accounted for no less than 1/3 of the gross farm output of USSR and 1/2 of the Soviet livestock production. (W. N. Loucks, **Comparative Economic Systems**, See Chap. 25, on "Soviet Agriculture"). Russia's dependence on the capitalist world for its food and other agricultural needs — this dependence is, incidentally, rather amazing as about 1/3 of the Soviet labour force is engaged in, and an equal proportion of the total population lives on, agriculture — would have assumed disastrous dimensions, if Communist ideologues were to prevail and abolish completely private ownership of the means of production in Soviet agriculture.

The third pre-condition for the full success of the consumer directed economic system is the economic freedom of the individual, particularly in respect of:

- (a) the distribution of his income between consumption and saving;
- (b) the choice of consumption and the power to direct entrepreneurs, through a price-regulated market mechanism, to import, or to fabricate at home, the commodities of his choice;
- (c) the distribution of his savings among the several alternatives;

and

- (d) the choice of his occupation.

These four freedoms constitute fundamental economic freedoms of free citizens. When these freedoms are infringed, the charms of mundane life correspondingly diminish.

Quite obviously, a consumer controlled system cannot come into being, nor function, without freedoms (a) and (b). Freedoms (c) and (d) are essential to ensure that the material and the human resources of production get drawn into channels where their output is the highest. These latter freedoms will, through continual resource shifts, minimise or eliminate less effective resource deployments and thus make for the maximisation of the national product from a given quantum of resources.

Under consumer sovereignty, four desiderata are integral to the functioning of the system. First, to seek consumer patronage, entrepreneurs would strive to reduce costs and improve quality. With consumer approval and appreciation of such effort, high-cost and low-quality products would continually tend to be replaced, through resource shifts and technological progress, by low-cost and high-quality products; and this will continually tend to lift up production, and hence employment, income and the level of living.

Secondly, rapid expansion of employment is built into the economic system where everybody's concern is to meet the demands — which, it may be noted, are most exacting, in addition to being ruthless — of the consumer. The expansion of employment at current, or rising, wage rates is a function, not of investment, as Indian experience has shown; nor of stepping down the technology of production, which is currently in use. It is solely a function of the expansion of overall production. Since consumer sovereignty makes for rapidity of growth of the national product, it may, therefore, liquidate unemployment with corresponding rapidity.

To illustrate the working of this built-in urge to expand employment: in Japan, low wages, the heavy pressure of population on land, 291 persons per square kilometer, — the average land holding in the country, as a result of this population pressure, is but 1.01 hectares — the scarcity and high cost of capital, induced farmers to adopt labour-intensive methods of cultivation in agriculture. Japanese agricultural output is well above the world average. The Japanese output of paddy, per hectare, in 1974 was 5.84 tonnes, as against the world average of 2.36 tonnes. Japanese agriculture employs 2,031 workers per 1,000 hectares of cultivated land. In USA, on the other hand, capital is less scarce, the average holding is 157.6 hectares, population density is but 22 per square kilometer; and the country adopted capital-intensive methods of cultivation, the labour employed per 1,000 hectares of cultivated land being a mere 17. These differing systems of cultivation were adopted, not under the direction of a planning commission, but by independent farmers in free economies, the course and destinies of which are, on the whole, determined by sovereign consumers. By contrast, the Russian Gosplan copied the American method of capital-intensive cultivation, notwithstanding low wages; with none too complimentary results.

Thirdly, under full consumer sovereignty, there is no need, nor room for monopolies in production, distribution, imports or exports; and incomes of all individuals — wages, interest, rent and profits — would correspond to their respective contributions to the national product. Such a situation permits no windfalls. Hence, none can appropriate someone else's earnings, i.e., there can be no social injustice. Social injustice, on the other hand, is inevitable under socialist economic systems, which abound in monopolies, privileges and subsidies; and hence bring to privileged individuals and groups unearned and also unmerited incomes, at the expense of the rest of the community.



Fourthly, income contrasts tend to decline as economic development progresses, under consumer sovereignty. This is so not merely because of the absence of social injustice, but also as a consequence of, on the one hand, a natural decline in interest, rent and profits, the earnings of the economic elite, and a natural increase, on the other, of wages and salaries. As a free economy progresses, the proportion of wages and salaries to the national product tends to increase and the proportion of interest, rent and profits tends to decline.

In Japan, wages and salaries rose continually from 41.3% of GDP, in 1960, to 50.8%, in 1974. In West Germany, this percentage rose from 46.9 to 54.7. By contrast, in Socialist India, this percentage fluctuated within a narrow range and was, in 1974-75, 28.2 or lower than in 1960-61, 29.9.

The growing prosperity of the masses of the people in free societies is evidenced by the overwhelming proportion of economic activity being directed to the turning out of articles of mass consumption and by the vast multiplicity of departmental stores, safeways, shopping centres and the endless series of retail shops which purvey these products. Many of these products would be, if then available, matters for envy among the noblemen and the elite of the 18th century. The shoppers that crowd these places are not plutocrats but farm and factory workers and salaried people. Except in Communist countries, cars are no longer a luxury transport, accessible only to the favoured top crust of the community.

In a communist society, none of the economic constituents of a free economy hold true. The state determines the needs of consumers, arranges the distribution of goods and services and allocates resources among alternative uses. Individuals do not enjoy fundamental economic rights; and forward markets do not exist.

It is much more relevant to review socialism as we have been practising it during the past three decades. Under our socialist policies, consumer control and direction of the economy is hindered, among other ways, by exchange control; by import and export restrictions; by the control of capital issues; by the industrial policy resolution, 1956; by the allocation of investment resources, including capital inflows from abroad, by a planning commission; by nationalisation of numerous undertakings; by state trading; by state financial agencies; by Reserve Bank control of credit; by a multiplicity of economic legislation both by the Centre and the States; by the creation of a series of monopolies of varying degrees; by numerous subsidies and privileges; and, until last April, by internal barriers to the movements of rabi foodgrains.

As a result of the working of these measures, we may identify four sectors in the economy, a public sector, which receives priority attention, an industrial sector, which is policy favoured, an agricultural sector, which is harassed and neglected, though it receives much lip sympathy, and a corrupt sector. The industrial sector is inherently unviable, viability being assessed by reference to cost-quality standards of the output, its competitive ability in world markets, and this sector's contribution to employment and income. Exceptions, if any, apart, there is not a single major industrial product which is not subsidised — more generally, this subsidy may be exceedingly heavy — by the consumer in the home market, and the export of which is not subsidised by the state in the markets abroad. And yet, this sector has galloped ahead, through deliberate policy inducements and by preferential allocation of resources. Its contribution to employment has been most disappointing, in relation to the resources employed. Industrial production (manufacturing) accounted for but 16.3% of the national product, in 1975-76, having risen from 12.9% two decades ago, in 1955-56.

The public sector is the most pampered sector. Taking an overall view, objectively and realistically — leaving alone doctrinaire dogma — public sector undertakings in India have, by no means, been a striking success. This is but inevitable when management and stakes are divorced. Even without including the gaps between landed costs and market prices of the import goods acquired against foreign aid, the public sector absorbs, from the data in the National Accounts Statistics, about 55% of the total available investment resources, though the contribution of this sector to NNP, was, in 1975-76, but 17%. Save and except when a powerful and selfless individual may be at the helm of affairs, is assisted by a team of like mettle, and this body of rare people is free from interference by interested parties, operating with the aid of politicians, public sector undertakings may be more or less milch-cows of those who may gain control over them. The illicit, though not always illegal, gains which they may gather are — being cases of resource wastages — a drag on the performance of these undertakings and a heavy debit, because of the magnitudes involved, on the national product. The nature of the operation of these factors in the nationalised coal industry is well brought out by Mr. B. P. Pai in his book, **Save Coal India**, Vol. I, published in 1977.

The agricultural sector is as inherently viable as the industrial sector is unviable, this viability being assessed by the same yardsticks cited above. No agricultural product receives any subsidy from the consumer in the home market, nor any subsidy from the state on exports. Agricultural exports, which are able to **stand on their own in world markets**, account for about 40% of total exports. The **Rupee prices** of many agricultural items, e.g. rice, coffee, and Bengal desi cotton, are way lower than international prices, and their exports are banned, restricted or are subjected to penalty export duties. In desperation, some agricultural produce,

like rice, is smuggled out! For all its viability, agriculture, however, is the least cared for of the three sectors. With the public sector and the industrial sector appropriating the lion's share of the resources, agriculture is starved of capital, though it accounts for about one-half of the national product and 72% of the population lives on it.

The corrupt sector is fed by the public sector, by exchange control, by import restrictions, by licensing policies, and by the complex network of economic legislation and administrative measures, which, as noted earlier, have created numerous monopolies and other privileges, that yield windfalls and hence give rise to corrupt payments. Until April 1977, rabi food zones, across which foodgrain movements were not permissible except under permits, were among the major sources of corruption and the generation of black money. Mr. Y. B. Chavan, when he was Finance Minister, stated that black-market transactions were probably as large, in the aggregate, as those in white money. Black incomes being, generally, cases of investment funds converted into private incomes, through corrupt payments, they turn back the hand of development.

The National Accounts Statistics, issued by Central Statistical Organisation, help to present the ultimate end product of these measures. The **per capita** income of the agricultural population, which constitutes 72% of the total, declined from a near-peak of Rs. 219.20 in 1960-61 to Rs. 195.50 in 1976-77, or Rs. 2.30 below its level in 1950-51, on the eve of the adoption of socialist policy measures. During the census decade, 1961-71, agricultural workers, the lowest rung of the economic ladder, rose by 75%; the number of cultivators fell by 16%, and the population below the poverty-line moved up from 39% to 45% of the total population. The income of the rest of the population, mostly the urban people, on the other hand,

more than doubled from Rs. 400 in 1950-51 to Rs. 813 in 1976-77. In these statistics is writ large the neglect of agriculture and of the interests of the masses, the pampering of industry and of the urban elite, and the fostering of corruption.

There is no remedy to these consequences other than to extinguish the corrupt sector, and divert resources, in a big way, from the public sector and the industrial sector into the agricultural sector. Our analysis demonstrates that the most effective and the most appropriate method of achieving this is to make a right-about turn and move rapidly in the direction of the Gandhian concept of the role of the state in economic affairs. This involves the release of the consumer from the socialist chains and taking the other consequential policy U-turns, more particularly :

- (i) channelising more funds into the agricultural sector, both under public and private investments;
- (ii) removing the barriers to internal and external trade;
- (iii) revising the industrial policy resolution, 1956;
- (iv) abolishing industrial licensing and the system of subsidies;
- (v) scaling down drastically overall public sector outlays, even withdrawing part of public sector investments;
- (vi) limiting state activity to its natural and proper duties;
- (vii) removing exchange control, and adopting a fully floating Rupee;
- (viii) reducing taxation, and balancing the budget at a vastly lower level of expenditure and investment than now; and

- (ix) reviewing all economic legislation and administrative measures with a view to their abandonment or for restructuring them to match the needs of a free economy.

Experience has shown, again and again, that no country which has been directed, in its economic affairs, by the collective counsel of sovereign consumers, has come to grief. The dividends harvested have invariably been of the "miracle" order, both in respect of growth and social justice. In the contemporary world, West Germany (under Professor Ludwig Erhard), Spain, Japan and the several mini-Japans in Asia are outstanding examples. On the other hand, no country which has fallen victim to any significant policy-mix of socialism, — which has generally been under the guidance of self-seeking businessmen, industrialists and administrators, and aided by deluded ideologues — has escaped chaos and overall semi-stagnation or decay. India, Burma, Sri Lanka, Pakistan and Bangladesh are classic examples.

The sovereignty of the consumer, on which hinges rapid economic growth with social justice, and the sovereignty of the voter, the foundation of all democratic institutions, are but different aspects of a free citizen. We may have an ideally free society when the two sovereignties go together.

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

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

—A. D. SHROFF  
(1899-1965)

Founder-President,  
Forum of Free Enterprise.

# HAVE YOU JOINED THE FORUM?

400

The Forum of Free Enterprise is a non-political and non-partisan organisation, started in 1956, to educate public opinion in India on free enterprise and its close relationship with the democratic way of life. The Forum seeks to stimulate public thinking on vital economic problems of the day through booklets and leaflets, meetings, essay competitions, and other means as befit a democratic society.

Membership is open to all who agree with the Manifesto of the Forum. Annual membership fee is Rs. 15/- (entrance fee Rs. 10/-) and Associate membership fee Rs. 7/- only (entrance fee Rs. 5/-). Graduate course students can get our booklets and leaflets by becoming Student Associates on payment of Rs. 3/- only. (No entrance fee).

Write for further particulars (state whether Membership or Student Associateship) to the Secretary, Forum of Free Enterprise, 235 Dr. Dadabhai Naoroji Road, Post Box No. 48-A, Bombay-400 001.



Published by M. R. PAI for the Forum of Free Enterprise,  
235 Dr. Dadabhai Naoroji Road, Bombay-400 001, and  
Printed by H. NARAYAN RAO at H. R. Mohan & Co.,  
9-B Cawasji Patel Street, Bombay-400 001.