FRESH THINKING ON PLANNING AND PRICES

FORUM OF FREE ENTERPRISE
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"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

INTRODUCTION

In a situation of rising prices and disillusionment with old methods of planning, two important documents were placed before the public in the second half of April 1977. One was "People's Plan II", by the Indian Renaissance Institute. It was a sequel to People's Plan, prepared by a committee set up by the Indian Federation of Labour, under the inspiration of a great thinker, the late M. N. Roy. It was placed before the country in 1944. The committee, which was assisted by a number of economists, comprised Mr. V.M. Tarkunde, Prof. B.M. Banerjee and Prof. G.D. Parikh.

A Planning Committee with Mr. V.M. Tarkunde, Prof. Amlan Datta, Dr. G.R. Dalvi, Prof. G.D. Parikh and Dr. Amrutananda Das was set up by the Indian Renaissance Institute, a society founded by the late M.N. Roy, to prepare People's Plan II.

In February 1974, led by the doyen of Indian economists, Prof. C.N. Vakil, and Prof. P.R. Brahmananda, of Bombay University, 140 economists submitted a Memorandum to the Prime Minister outlining a package of measures to contain inflation. Three months later, a supplement called SEMIBOMBLA (Scheme of Economists for Monetary Immobilisation through Bond Medallions and Blocked Assets) was issued. These documents greatly influenced Government policy measures, and the fall in prices witnessed from September 1974 during the subsequent 18 months may be attributed to these two documents.

In April 1977, Prof. C. N. Vakil and Prof. P. R. Brahmananda submitted to the Prime Minister a follow-in scheme to reduce prices. The document is called FULLMANGAL (Five per cent Upper Linear Limit on Money's Annual Growth rate As per Law).

Extracts from "People's Plan II" and 'FULLMANGAL' are given in this publication, with a recommendation that every serious students of economics—nay, all citizens—interested in economic growth with social justice should read the original texts.

Fresh Thinking on Planning & Prices

I

Planning of a Different Type

The Basic Objectives: We believe that planning in India during the coming twenty years or so should be guided by the following basic objectives:—

(i) that the minimum primary consumption needs of India's growing population should be satisfied (Primary needs)

(ii) that the productive involvement of the people in the process of economic development should be ensured by generating adequate employment opportunities. (Employment)

(iii) that economic growth on which the above two objectives are directly dependent should simultaneously reduce inequalities of incomes and wealth. (Distributive Justice), and

(iv) that the poverty, prevailing among bottom 40 per cent of the population should be eliminated. (Elimination of poverty).

Satisfaction of Minimum Primary Needs: The primary needs of the people are food, clothing, shelter, education and medical care. We recognise that satisfaction of the primary needs even at minimum leavels is unlikely to be attained in the **short** run. Nor will it be attainable **simultaneously** at some specific date. Rather, the attempt must be to attain the minimum levels of primary needs of each type at the earliest possible date. Evidently, given an assumed pattern of dates for reaching the minimum targets of primary needs and the size of population at those dates, a certain set of physical growth targets independently emerge and these become relatively rigid inputs for the planning process. Indian planners so far have hesitated to incorporate such consideration into development planning. For one thing, this would come into immediate and **drastic**

conflict with the pattern of developmental priorities to which they have become accustomed. Given the resources constraints and the postulated growth rate, the planners found that any attempt to introduce such targets would have lowered the growth rates of most of the sectors of the economy. In other words, the heavy-industry sectors virtually represented to the planners ends in themselves and not the requirements emanating from the pattern and growth rate in the demand for primary consumption needs. Rather, it was the pattern of final consumption demand, including that for essential commodities, which was to be adjusted to the requirements of an adequately high rate of growth of the heavy industry sectors. Since we do not look upon industrialisation or capital goods production as ends in themselves, we belive that development priorities should include specific commitment to reach minimum primary needs targets by specified dates. We realise, of course, that the introduction of such physical target attainments may not always be easy to harmonise even with an agriculture-wage-goods services strategy. The "shelter, water supply, sanitation" group of needs which involves heavy investment will pose difficult problems. Yet, the fact that we treat industrialisation and capital goods production as tools rather than as ends provides scope for harmonising the compulsions of growth and employment with those of supplying minimum primary needs of the people.

Maximising Employment Opportunities: We consider that development plans should embody a clearly stated employment plan and manpower utilisation programme. The most important part of such a programme would be concerned with the utilisation of idle and partially idle manpower. There should be definite and distinct progress in every plan towards a better balance of job-seekers and job-opportunities (in terms of employment and self-employment) in the economy.

Effective participation of people in the process of economic development is one of the central objectives of the People's Plan. Unless this fundamental aim is seriously and consistently pursed, we see no prospect for any significant improvement in mass welfare standards. Neither the provision of social welfare benefits to poor households, nor the establishment, at public cost, of community utility services in poor neighbourhoods or settlements, has a perceptible long-term impact on the welfare of the recepients. It is, therefore, necessary to ensure growing productive involvement of people in the expanding sectors of economic activity. Consequently, so long as the productive involvement of the Indian "people" in the expanding sectors of economic activity remains at its present low level, standards of mass welfare cannot possibly improve. Neither an acceleration of the rate of growth of the economy, nor the strengthening of "redistributive measures" nor finally, the expansion of social welfare activities of the State, will make a significant difference.

The statement made above is not meant to deprecate the usefulness of efforts currently being made to provide social welfare benefits and to develop "minimum essential community services" for the poor. Our intention is to emphasise the crucial importance of **productive** involvement of the people as an **instrument** of raising mass welfare standards. By "productive involvement" of the people we mean their becoming "engaged in worthwhile economic activity" (either as wage workers or as self-employed) in sectors where opportunities are likely to expand as a result of economic development.

However, in order that opportunities for employment/self-employment being created by the process of economic development are effectively utilised by the people of a poor country, such opportunities need to be of an appropriate type. This means in effect that (a) the opportunities should be suitable for unskilled/semi-skilled workers and should require only "minimal" training or retraining and (b) the self-employment opportunities must be viable at low levels of techno-entrepreneurial know-how and based on moderate amounts of investible capital.

The problem with modern economic growth in a less developed country is precisely that most of the new employment opportunities being created are of a very different type. Typically they require effective orientation in favour of a techno-industrial civilisation, emphasise technical skills and managerial sophistication and usually involve fairly heavy investment of capital. This mismatch of the type of opportunities being created and the type of opportunities which can be effectively utilised by the people accounts for two features of the growth process in a less-developed country: (a) the under-utilisation of investment and (b) the confining of the major benefits of economic growth to a small section of the population which alone is in a position to exploit the new opportunities.

Planning of a different type, operating at several levels is necesary in order to offer a reasonable chance for correcting this basic mismatch. The central purpose of such planning is to secure a faster rate of expansion of economic opportunities that the people can quickly utilise and to do this in a manner which does not prejudice the long-term capacity of the economy to grow and modernise itself.

Distributive Justice: While a well-defined strategy of economic development may ensure the supplies of essential goods and also generate adequate employment, it would not, however, automatically guarantee that the proceeds of growth are distributed in a just manner among the partners in the process. The growth mechanism itself may possess in-built factors through which the gains would accrue mainly to the asset holders, particularly in the short term. Indian planning has during the past 25 years created a situation in which the beneficiaries seem to be the rentiers, the traders and the middlemen. The process has been reinforced by the kind of strategy and policies adopted by the planners. The consequence is also quite clear. The efforts at enhancing the average living standards of the Indian people have suffered a serious set-back. Income accruals among the vested sections went on unabated, considerations of equality in income distribution between the factors of production got relegated to the background and hence disparities in their personal distribution of incomes and wealth got, in effect, accentuated. It appears that inequity in distribution of incomes and wealth has become a queer characteristic feature of Indian growth process. This trend has to be reversed and this needs to be accomplished as early as possible. We, therefore, emphasise the importance of ensuring an increasing measure of distributive justice and indicate practical ways of doing so.

Poverty Elimination: A reference has already been made to the extent of prevailing poverty in India despite the long and strenuous efforts of Indian planning over the past 25 years. Leaving apart the nature of data regarding the size of population in the poverty bracket and the unsettled debate on the temporal pattern of this poverty margin, the appalling living standards of the bottom 40 per cent of India's population remains an economic reality to be reckoned within any effort to plan for future development. While the above mentioned objectives and the consequent strategies may prevent the economy from any further deterioration, we believe that consciously chosen policies are immediately called for in order to recover the huge population already caught up within the poverty trap. We recognise that achieving the objective of poverty elimination is not as easy a task as one would like it to be, but we also recognise that this is, above all, a human problem which requires priority attention in the coming two decades.

Investment Priorities: A major internal contradiction in the Indian pattern of development has been the combination of a heavy-industry-oriented pattern of allocations and an investment rate too low to validate such a pattern of allocations. This contradiction has emerged primarily because the ratio of domestic investment to national income has continued to remain low. We, therefore, approach the issue of investment priorities from the standpoint of removing this internal contradiction. The investment priorities which would be most appropriate according to us are:

(i) Since India's development performance both in terms of **per capita** product and the growth rate of employment will depend predominantly on what happens in the agricultural sector, the pattern of investment allocations in the People's Plan should be governed, above everything else, by the need for providing an adequate "inputs-infrastructure-institutional" base for a sufficiently rapid rise in (a) the incomes of the agricultural sector, and (b) rural employment opportunities. The People's Plan aims at a comprehensive reconstruction of the rural economy through the development of agriculture, agro-based industries and cottage/household industries. We also regard that building of the necessary infrastructural facilities (both physical and social) is of equal importance.

(ii) Since the supplies of primary consumption goods have been lagging behind their effective demand during the past two decades, economic growth has not generated the required improvements in the standard of living of the masses. Therefore, sectors engaged in producing goods of primary needs (agricultural as well as non-agricultural) should receive priority attention in the matter of investment allocations.

(iii) Since improvements in the general welfare significantly depend on services like health, education and other community development services including those to the under-privileged and the rural masses, outlays on these services/sectors, should be stepped up substantially. Apart from satisfying the known socio-political requirements, this order of investment priorities would directly enhance employment potential because of the low capital-output ratio in this sector.

However it needs to be noted that these priorities are not necessarily sequential or chronological. They are interdependent and complimentary in character. We deliberately opt for this group of investment priorities in preference to any other group, in any case, for the 10 year plan period.

Guidelines for Planning

Population Target: The first important guideline is that the planning process should be based on a specific reasonable population estimate and that the plans themselves should visualise the outlays and programme necessary to implement a population policy based on such estimates. At the same time, an all-out effort needs to be made to bring down the rate of growth of population.

Primacy to Agriculture, Small Industry & Social Services: The investment pattern should also accord primacy to expansion in agriculture, small industry and social service activities. The logic behind this has been already indicated. These are the three sectors (along with basic wage-goods-industries) which determine the economic opportunities and standards of living enjoyed by the poor. The meaning of "primacy" in the context of investment planning is that reasonably high growth rates for these sectors should be introduced as exogeneous inputs into planning and; the investments and growth requirements for all other sectors be derived on the basis of intersectoral balances within this framework.

Supply and Marketing of Basic Wage Goods: A high degree of importance should also be attached to rapid expansion of supplies and effective marketing of basic wage goods. Here the choice of investments should be guided into the lines which promise the fastest output increase per unit of direct and indirect investments. Small-scale technologies may be inappropriate for some of the basic wage goods on the ground of investment-effectiveness and total factor productivity considerations. Confusion should not be allowed between the targets of rapid growth in basic wage goods production and the promotion of small-scale industries. The effective marketing of basic wage goods and their supplies to the poor at reasonable prices will involve not only production, but proper arrangements for stocking and off-take, and elimination of speculative irregularities. A system of state trading, distribution through co-operatives and effective buffer stock operations will have to be instituted in order to progressively reduce dependence on private traders and suppliers/agents of various types.

Non-Inflationary Economy: We envisage an essentially non-inflationary process of economic development. This does not imply that all price should be rigidly fixed or controlled. This implies that the planned investments should match actual savings and public outlays should match the quantum of resources that can be reasonably expected to be mobilised. The size of investments and outlays should be determined on the basis of realistic estimates of mobilizable savings. Such an approach will rule out recourse to inflationary and deficit financing as a means of mobilising plan resources.

Relative Independence from Aid: Another basic guideline on which the Peoples' Plan II is based is that economic development should become relatively independent of foreign aid in any essential or critical manner. This will call for rational planning of exports and imports to maximise the net gain in foreign exchange to be utilised for developmental imports. We believe that such rational forward planning would lead to a more dynamic approach towards export promotion and a more liberal import regime than the one currently prevailing. We do not favour an autarchic system based on the concept of exclusive self-sufficiency. We would, therefore, like to encourage development of India's foreign trade on the basis of comparative cost advantage.

Approach to Capital Goods Investments: An attempt should be made to allow investments in capital goods production to the necessary minimum for attainment of the growth pattern visualised. This does not mean an anti-capital-goods bias, but suggests the rational principle that (in a country with limited resources for investment) the less the resources are locked up in costly long-term investments, the better. An attempt should be made also to structure the growth in such a manner and to employ such technical options as would regulate the growth rate of the capital goods sector, subject to the maintenance of intersectoral balances.

Restricted Growth of Heavy Infrastructure: Similarly, subject to intersectoral balance requirements, there must be an attempt to restrict the investments in heavy (high-per-unit-investment-cost) physical infrastructure. Throughout an attempt must be made to substitute low-invesment-cost and labour-intensive methods for infrastructure construction and to devise interim stop gap measures which allow heavier forms of infrastructure investments to be deferred to a later date when the economy will be better able to afford such investments. The application of this and the previous principle of investment planning will involve accurate estimation of real factor scarcities and consistent application of shadow-pricing techniques in investment planning and project evaluation.

Minimum Necessary Controls: Plan implementation should be based on minimum essential controls. While such controls should be carefully determined and pursued with the utmost vigour, the multiplicity of (mostly unnecessary) controls and regulations which are now hampering activities at every turn should be quickly scrapped. Besides foreign exchange control, rationing and distribution of basic wage goods and restrictive controls on luxury consumption of durables and housing, there does not seem to be any other control implied in the type of planning we visualise. The resources of administration are now tied-up in non-essential and counterproductive controls described above and towards more effective enforcement of land reform legislation.

Managerial Autonomy and Productivity Orientation: Plan implementation should emphasise managerial autonomy of organised-sector units (both public and private sector) and the development of productivity orientation. A decentralised indicative planning procedure, coupled with the introduction of productivity planning at enterprise and sector levels and a stress on professionalisation of management will go a long way towards meeting these aims. The same set-up will provide a chance for effective introduction of industrial democracy and workers' participation in equity capital and management of large-scale public and private sector units. The plan implementation set-up should also emphasise parallel treatment of public and private sector enterprises in credit and resource allocations and the awarding of government contracts. Small-scale sector deserves special consideration with respect to credit facilities and also in respect of awarding government contracts.

Regional Development and Decentralisation: Another important aspect of plan implementation is the emphasis on balanced regional development and effective decentralisation of planning of regional/sub-regional units. There is a need for evolving a multi-level indicative planning set-up which allows the central planner to retain control of macro-aggregates of the national economy, while delegating detailed planning and implementation responsibilities down the line. (An extract from "People's Plan V"—A Plan for India's Economic Development" published by the Indian Renaissance Institute, 13 Mohini Road, Dehra Dun, in April 1977. Full text available from the Institute at Rs. 15, inclusive postage and packing.)

II

Reversing Trend of Rising Prices

The following is a summary of the suggested short-term plan of Action to halt the rising trend in prices and to reverse it.

1. The Government must announce a target-norm of a reduction in the price level from the current figure of 182 in end March 1987, by about 10 per cent or by about 18 points, over the next two financial years.

2. Over the current year, 1977-78, the stock of money should be reduced by about 5 per cent in the light of the feasible growth-rate of output of about 3 per cent during the current year; this would enable prices to be brought down by about 4 to 5 per cent over the year. The contraction is to be achieved through (a) a reduction in net bank-credit to the Government sector by Rs. 750 crores, (b) Limitation of credit expansion, over the fiscal year 1977-78, to Industrial-Commercial sector to about Rs. 1,000 crores, (c) Limiting monetized new exchange-reserves over 1977-78 to about Rs. 500 crores, (d) an expansion in time-deposits by about Rs. 1,500-1,750 crores, (e) an increase in net impounded deposits by about Rs. 250 crores. For 1978-79, the growth

rate in money supply should be targetted at 2 to 3 per cent less than the expected feasible growth-rate in real output, as perceivable around end of 1977-78.

3. The fiscal-operations of the Public Sector must make a sizeable contribution to the goal of a reduction in money supply by a budgetary surplus. We must achieve an **ex-ante** budgetary **surplus** on the combined operations of Central and State Governments, as reflected in the reduction in the net bank credit to the Government sector, by about Rs. 500 crores, or as reflected in the conventional figure of overall balance, by a surplus to Rs. 750 crores.

4. A 5 per cent across-the-board-cut in all disbursement of Central and State Governments during 1977-78 amounting perhaps to about Rs. 22,000 crores, would yield a saving of Rs. 1,000 crores. A 10 per cent cut in non-essential items, including curtailment, or postponement pending reconsideration of the large outlays earmarked for the heavy industry sector, would yield an extra saving of about Rs. 250 crores.

5. A reduction in the subsidies currently amounting to about Rs. 1,000 crores, with a 50 per cent cut in export subsidies.

6. Fresh tax efforts of about Rs. 500 crores by both Central and the State Governments, no reduction in minimum income-tax exemption limits, no reduction in tax-rates on higher income. Henceforth, all reliefs should be conditional upon reinvestment of released amounts for savings in specific channels.

8. Net market-borrowings of the governments should be reduced by Rs. 250 crores.

9. The continuance of the CDS with some reductions in rates of compulsory collection for groups with annual emoluments below Rs. 3,000 and groups between Rs. 3,000 to Rs. 5,000; the temporary withholding of further repayments; the continuance of the CDS for income-tax payers, with, again, temporary withholding of repayments; 25 per cent of the dividends to be funded during 1977-78 in the form of compulsory deposits.

10. A ceiling of about 6 per cent on the expansion of bank credit to the Industrial-commercial sector over the 1977-78 fiscal year; thus not more than Rs. 1,000 crores would be the incremental funds available to this sector during 1977-78.

11. Financing of additional stock-purchases by the Food Corporation through surcharges, on Central excises and a levy on sales-tax revenues of State Governments.

12. A 8-point interest-policy consisting of, (1) abolition of ceiling on lending rates, on dividend rates and on interest on company deposits, (2) a hike in the Bank Rate by 2 percentage points, (3) upward movement of deposits rates and (4) the rates on small savings, and also of (5) prime-lending rates by 1½ to 2 percentage points, (6) A drag-up of yields on government securities by 3 to 5 percentage points, to reach a level of between 9 to 10 per cent, (7) treasury bill rate to move up and to be made equal to the average of the call money rate of the last 3 months, and (8) abolition of all interest subsidies; the drawbacks to be considered by a separate National-Interest-Subsidy Commission.

13. Following six Macro-guidelines in regard to Credit-Management: (1) Medium-term, revolving and long-term credit, and investment in Government securities be reduced to the proportion of time-deposits to monetary resources; (ii) Short-term borrowing by industrial-commercial sector should not exceed 30 per cent of the ratio of inventories to value-added; (iii) Discouragement, by penal rates, of revolving loans; (iv) Government borrowing not to be undertaken during busy season; (v) Term-lending financial institutionns should be prohibited from access to the RBI; (vi) Non-bank financial institutions should not enter the call market, and commercial banks should not enter into the market for treasury bills.

14. Firm-by-firm credit scrutiny by the RBI should be done with; the RBI to confine itself to overall policy matters in regard to credit.

15. Following measures to boost savings: (i) Additional tax-relief for household-savings in prescribed forms; (ii) Tax-relief to retained profits of business concerns; (iii) Flotation of 10-year tax-free principal-and-interest-index-linked loans from the rural areas through gold-plated bond-medallions. The interest will be 12½ per cent. Rs. 300-500 crores can be mobilised per annum through this source; (iv) Complete tax-relief to savings in the form of increments in provident funds and increments in special categories of deposits, and in savings in the form of bond-medallions and in contractual-savings categories, (v) 50 per cent of the bonus of all categories of workers, above prescribed minimum amount, to be lodged with respective companies, or enterprises, as a contribution to the special deposits of the concern. These deposits should be insured and both the amounts and the interest amount should be freed from tax liability; (vi) 50 per cent of the emoluments of employees drawing a salary of more than Rs. 3,000 be treated as deposits (also insured) for the enterprises in which they are saving.

16. Exchange-dealers converting exchange into Rupees should lodge 50 per cent of exchange-remittances in blocked deposits, carrying a special interest rate; both amounts and the interest being index-linked and tax-free; a higher rate of conversion ratio for those portions of exchange which are held in the form of blocked amounts.

17. Four guidelines on trade policy; continuation of export quotas, which are flexible, continuation of import quotas, again flexible; free imports of gold, no free floating rupee; managed floating as of now, with some discretion to fix official exchange-rates.

18. Embargo on export of food articles and other necessary wage goods.

19. Rs. 500 to Rs. 600 crores exchange reserves to be used for forward-purchases of oil and grains and for serving as a cushion for some borrowings in the international market and for investment in well-chosen international portfolios. The formation of an International Investment Corporation through consortium of financial institutions, to look

after the investment portfolios; the rest of the reserves to be kept for normal purposes.

20. The use of 4-6 million tonnes of gains out of the existing stock for promoting employment through a Food-for-work scheme; the scheme being integrated with the new Plan to be recast since it involves need of about Rs. 1,200 crores of matching extra-savings.

21. Preparation work on a New Wage-goods model Plan to begin from 1978-79, with drastic alterations in structure of plan priorities; about 45 per cent of the net investments to be allocated to Agricultural and related lines so as to ensure a minimum of 5 per cent to 6 per cent rate of growth in Agricultural output.

22. Immediate steps to initiate a constitutional amendment placing on upper limit of 5 per cent on the annual rate of expansion in money supply. [Reproduced from "Memorandum on Inflation Reversal and Guaranteed Price Stability", titled FULLMANGAL (Five per cent Upper Linear Limit on Money's Annual Growth rate As per Law), by Prof. C. N. Vakil and Prof. P. R. Brahmananda. The full text published in book form is available from Vora & Co. Pvt. Ltd., 3 Round Building, Princess Street, Bombay-400 002. Price: Rs. 12/-, plus Rs. 3 for postage and packing.]

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

—**Eugene Black**

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