THE UNION BUDGET 1974-75

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By

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Will Durant, the most philosophical of modern historians, observed, "The world situation is fouled up. It has always been fouled up. I see no reason for change". Currencies fluctuate wildly; the stock market whirls up and down in a frenzy of its own; and most nations seem to be on the escalator of inflation, with their experts totally confounded by the seemingly insoluble crisis.

Professor Galbraith admitted openly at the Fourth European Management Symposium held recently in Davos that "economics as it is taught and practised, seems again to have lost touch with the problems it is meant to mitigate and solve". Professor Fritz Machlup of Princeton University, an eminent authority on pricing theory, confessed sadly that he had no formulae for solving the problem of inflation. Peter Bernstein, the famous consultant, said, "What we are asking ourselves is not 'what is your forecast?', but rather 'can we forecast?' ". Knowledge of such a world situation must engender sympathy for our Finance Minister and an understanding of the tremendous problems facing him.

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The highlight of this year's Budget is undoubtedly the reduction in the rates of personal taxation at all levels, the highest rate being brought down from 97.75% to 77%. The only two years since independence in 1947 when the rates of income-tax on individuals were so slashed, were 1957 when the highest rate was reduced to 77% and 1965 when Mr. T. T. Krishnamachari dropped it to 74.75%. The political atmosphere in the country is so little conducive to dispassionate economic thinking that the reduction in personal taxation, which merely represents a re-entry after nine years into the realm of rationality, must be regarded as evidence of great political courage. It is an act of faith on the part of the Finance Minister; and it is now up to the citizens to show by their response that the faith was justified. The change should result in less concealment of income and larger open investment in productive enterprises.

It is our public duty to justify the conviction of the Finance Minister that the loss of Rs. 60 crores involved in the reduction of the rates of personal taxation would be more than made up by more honest returns of income.

Unfortunately, the reduction in personal taxation is the only streak of light, the only ray of mercy, that gilds the darkness of the night. The rest of the Budget is as pedestrian in its outlook as its predecessors in our last eight years of stagnation. Some other countries have doubled in eight years their gross national product at constant prices!

India has to solve five major problems—poverty, unemployment, stagnation in production, inadequacy of savings and investment, and double-figure inflation. These portentous problems can be solved not by the Budget alone, but only if all the major instruments of economic control are operated in harmony and with imaginative vision by the Government.

The utter irrelevance to these problems of the Union Government's fiscal proposals and economic policies can best be appreciated in the light of some staggering figures.

The problem in India is not that of relative poverty but of absolute poverty. In the words of McNamara, absolute poverty is a condition of life so degraded by disease, illiteracy, malnutrition and squalor as to deny its victims basic human necessities, a condition of life so limited as to prevent realisation of the potential of the genes with which one is born, a condition of life so appalling as to insult human dignity. 40% of the Indian people live in such misery which no statistics can adequately describe.

The income *per capita* in real terms (i.e. after making allowance for the factor of inflation) rose at the annual average rate of 1.7% during the 1950s; but in the 1960s the rate of growth dropped precipitously to 0.8%. The painful truth is that, after 1970, there has actually been a drop in *per capita* income at constant prices. In real terms and at 1960-61 prices, the *per capita* income which was Rs. 348.6 in 1970-71 declined to Rs. 346 in 1971-72, and further declined to Rs. 333 in 1972-73. This means that the real income *per capita* was lower in 1972-73 than it was in 1964-65 for which the corresponding figure was Rs. 335.

The Planning Commission stated last year that, on the basis of the findings of the Bhagwati Committee, there were 18.7 million people unemployed in 1971; today the number is estimated at more than 25 million. The number of the unemployed is increasing, at a conservative estimate, at the rate of 10,000 a day.

When the West Bengal Government recently advertised 17 vacancies for poorly paid unattractive jobs in rural areas, the number of applications received was nearly one lakh. When the Haryana State Electricity Board invited applications for 300 assorted jobs, including 150 jobs of lower division clerks, nearly 60,000 candidates applied. The Electricity Board earned Rs. 60,000 as the price of application forms and a further sum of Rs. 4.5 lakhs as application fees! Some months ago a local bank at Moga, Punjab, received 4,000 applications for five posts of clerks, and among the applicants were a large number of post-graduates with first division; and the New Delhi Branch of the Bank of Baroda received about 1,25,000 applications for 2,000 posts. In the Fifth Plan period alone, new jobs will have to be created for an additional labour force of 25 million.

Agricultural production has not been expanding as fast as the population. In quantitative terms, the common man today has less of foodgrains, edible oils and other necessities of life than he had a decade ago. It is well known that pulses are virtually the only source of protein for the common man in India; the consumption of this vital item of food in 1972 was 32% below the figure of consumption (*per capita*) of 2.43 ozs. per day in 1961.

Industrial production, which grew at the annual average rate of 9.2% between 1960 and 1966, has registered a rate of growth of only 4.5% after 1966. The increase in industrial production in 1973-74 has been nil. Half the targets in the Fourth Plan have not been achieved. While India comes second in population, it takes the 103rd place in gross national product *per capita.*

As a result of inflation, unrealistic price controls and top-heavy taxation, new investment in the private sector remains woefully inadequate and is far lower than what it used to be in the early sixties. The annual average of risk-bearing capital raised by existing and new private sector companies during the last three years has been only Rs. 75 crores, as against Rs. 89 crores in 1961, even without taking into account the erosion in the value of the Rupee during the intervening period. With an existing investment in assets around Rs. 10,000 crores, the private sector industry is barely able to instal additional net assets worth Rs. 150 to 180 crores each year.

To expect the Budget to reverse these frightening trends is almost as reasonable as trimming a lawn with nail-scissors.

There is nothing in the Budget which can abate poverty by generating national wealth, tackle unemployment by creating jobs, procure the necessities of life for the masses by giving a fillip to production, or generate savings and investment by leaving substantial amounts in the hands of individuals and the corporate sector. The reduction in personal taxation is undoubtedly a factor which would leave larger savings for investment in the hands of private individuals; but inflation would eat, to a very large extent, into the savings, and the unchanged tax burden on the corporate sector would rule out the possibility of increased corporate investment.

In countries like West Germany, Sweden, Japan, Canada and U.S.A., Finance Ministers wisely reduced corporate taxation at the same time that they reduced taxes on individuals,—and their Exchequers benefited largely from the resulting buoyancy. Mr. Y. B. Chavan would have been well advised to reduce our rates of corporate taxation which are, by and large, higher than those in any progressive country.

The late Mr. T. T. Krishnamachari had wisely provided various tax incentives, but his successors have been far less pragmatic.

The tax concessions which would encourage expansion and development of the corporate sector have all been withdrawn one by one. The last casualty will be development rebate which is scheduled to depart on 31st May 1974. The Finance Bill proposes an extension of only one more year for development rebate, and that too only in cases where the plant or machinery has been ordered, or its fabrication has commenced, before 1st December 1973. In place of development rebate, the recent Income-tax (Amendment) Bill proposes to grant initial depreciation. It is obvious that initial depreciation can never be a substitute for development rebate. The whole point of development rebate is to enable the industrial unit to meet the ever increasing costs of renovation and replacement. Development rebate provides a deduction over and above the full cost of the assets. On the other hand, initial depreciation merely means accelerated depreciation or a larger depreciation in the first year which is, however, taken into account for determining the total depreciation (available over a period of years) that can in no event exceed the actual cost. In other words, unlike development rebate which means a reduction in tax, initial depreciation only means postponement of tax. The trend in many progressive countries, including the U.K., is now to let the taxpayer choose the amount of depreciation he will claim in any year—he can claim even 100% of the cost as depreciation in the very first year. Thus initial depreciation is a highly antiquated technique and is hardly used as an incentive in any progressive country. Further, even this initial depreciation is proposed to be made available only to a few selected industries.

Since almost the entire tax revenues of the Government of India are derived from the non-agricultural sector, it is clear beyond doubt that it is only by enlarging the industrial base that the Union Government can generate sufficient tax resources to finance laudable plans for social justice like the provision of water, education and medical facilities. 12% annual increase in industrial output would generate additional revenue of over Rs. 1,000 crores per year for the Central Government alone, apart from the large increases in sales tax and other revenues for the State Governments.

The single gravest danger facing India today is that of inflation. While it took prices 65 years—1873 to 1938—to rise 32%, in just four years from the end of 1969 to the beginning of 1974 wholesale prices rose 60%, and food prices 62%. During the same period the supply of paper money increased by 70%; while the real output of the necessities of life increased by only 12%. During 1973-74 wholesale prices shot up 29% and money supply 17%.

Inflation is not self-correcting but self-accelerating; it rises with compound vengeance. Of all economic phenomena, it is the most ruthless, relentless and remorseless.

As against our current inflation rate of 27-29% the dangers of inflation even at the yearly rate of 15% can be brought home by simple arithmetic. With 15% inflation *per annum*, prices would double in five years, multiply sixteen times in twenty years, and multiply nearly 18,000 times in a normal life-span of 70 years. At this rate of inflation, a capital of Rs. 15,000 would only be worth 85 paise at the end of the life-span.

J. M. Keynes said: "There is no subtler, nor surer, means of overturning the existing basis of society than to debauch the currency. The process engages all the hidden forces of economic law on the side of destruction, and does it in a manner which not one man in a million is able to diagnose".

Inflation devours democracy. It is the favourite food of that demon. No country which has suffered over 20% inflation for long has ever survived as a democracy. In South Korea and the Philippines, which experienced inflation in the 10-20% band for a few years between 1960 and 1972, freedom has been very largely eroded.

India has already entered the danger zone. The primary defect of the Budget is that instead of acting as a nutrient, it will only continue the pathetic tradition of being a parasite on the national economy. It cannot increase production; it will not stem the tide of inflation. So far from helping to roll back prices, it will, at a reasonable estimate, increase prices by at least 20% during the next twelve months. The estimated deficit of Rs. 125 crores for the next year will need 5 as the minimum multiplier to make it approximate closer to reality.

The total tax revenues of the Central Government in 1965-66 were Rs. 2,061 crores; while they were estimated to be Rs. 5,052 crores, i.e. two and a half times higher, in 1973-74. This means that our Budgets merely keep on raising in money terms more resources, without raising in real terms the rate of national savings or growth.

It is, however, but fair to add that the cost-pull and wage-push inflationary spiral cannot be brought under control by mere governmental policy alone. The imperative need is for the people to observe self-restraint and self-discipline and to put the national interest above group selfishness. The ineluctable rule of economics is that you cannot divide more than you produce. Hence a demand by militant Trade Unions for higher wages without increased productivity can only serve to aggravate the problem. As Lord Keynes observed, "A demand on the part of the Trade Unions for an increase in money rates of wages to compensate for every increase in the cost of living is futile, and greatly to the disadvantage of the working class. Like the dog in the fable, they lose the substance in gaping at the shadow. It is true that the better organised sections might benefit at the expense of other consumers. But except as an effort at group selfishness, as a means of hustling someone else out of the queue, it is a mug's game to play".

One of the more endearing characteristics of our Finance Ministers has been their readiness to make brave assertions which are taken by the credulous as factual but which are in reality delightfully fanciful. This year's Budget is described in the concluding paragraph of the Budget Speech as one more step in the direction of "a rapidly expanding economy with socialist objectives". In truth, the last eight years have been years of tragic stagnation and the socialist objectives remain as unfulfilled as the desire of the moth for the star.

Nothing short of a U-turn in our fiscal policy and economic ideology will ever enable our democracy to tackle these problems.

The Budget must take a long-term view of the entire nation's future, instead of being only concerned with raising tax revenues for twelve months. What is needed is a Budget conceived in a large, far-seeing spirit and dedicated to the task of harnessing the enterprise and skills, the energy and endeavour of tens of millions of citizens in an atmosphere of trust and freedom.

The present exercise by the Planning Commission in the field of policy-making will also have to undergo a sea change. The fatuousness of its present efforts at formulating the policy can best be brought home by the fable which recently appeared in "The Financial Times" (London). Walking through the jungle, a lion spied a mouse sitting sadly by a bush; and he asked the mouse what was wrong. "I am so small," the mouse replied, "and all the other animals look down upon me". "Then", said the lion, "I can help you. Just stop being a mouse and be a lion instead". The mouse was very grateful. "I shall certainly do what you suggest," he said, "but how do I stop being a mouse?" "That,' said the lion, as he walked imperiously away, "is for you to decide. I formulate the policy".

It would be easier to under-estimate than to exaggerate the gravity of the economic crisis facing the country. We must not be lulled into complacency by the fact that the nation still somehow manages to stumble along. History affords ample evidence that down the centuries during periods marked by chaos most people go on living as before.

While formerly we used to suffer from social evils, we now suffer from the remedies for them. We suffer from such a pathological obsession about our favourite and fatal brand of socialism that we are prepared to let the nation sink deeper into the quagmire of misery rather than adopt pragmatic policies.

"We would rather be ruined than changed
We would rather die in our dread
Than climb the cross of the moment
And let our illusions die".

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