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RECENT ECONOMIC TRENDS IN INDIA AND PROSPECTIVE CHANGES IN DEVELOPMENT STRATEGY

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RECENT ECONOMIC TRENDS IN INDIA AND PROSPECTIVE CHANGES IN DEVELOPMENT STRATEGY*

by

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Though agriculture accounts for only about two-fifths of India's national income it is still dominant enough to set the pace for everything else. So when relatively bountiful harvests follow a succession of lean years the entire economy gets a boost for some time. This happened very clearly a decade ago when, after the severe droughts of 1965-66 and 1966-67, agricultural production picked up rapidly (partly in response to new high-yielding varieties) and national income grew at a rate of over 5 per cent per annum on the average in the following four years. It has happened again, from 1975-76 to 1978-79, when the economy recorded an average rate of growth of nearly 5½ per cent per annum. But in between was a lean period — which also lasted four years — when there was hardly any increase in agricultural production over the levels reached earlier and national income could grow at only about 1½ per cent per annum. Another fairly serious drought appears to be taking shape in 1979-80. One cannot therefore be sure whether the latter half of the 1970s has made a difference to the long-run growth rate of the economy or it still remains around 3½ per cent per annum.

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* This paper will appear in the December 1979 issue of the Seminar (Post Box 338, New Delhi 110 001). No reproductions of any part of it are to be made till after this publication, or without the permission of the Editor of the journal and the author. A longer and somewhat more technical version of the paper, with all the supporting statistical material presented in appendices is expected to be ready within a few weeks, in any case before the end of December. Those who wish to get a copy of it — which will be initially in the form of a Working Paper of the Centre for Development Studies, Trivandrum — are requested to write to me. Meanwhile all comments, questions, and outbursts on the present shorter version will be most gratefully received, and explicitly acknowledged if made use of in the preparation of the longer version.

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It seems highly probable however that a process of acceleration has got initiated during this period. All the elements that could have gone into it are certainly by no means clear. But there is more than circumstantial evidence to suggest that some important changes have been taking place in the economy, and that they may make a perceptible difference over the next few years. At any rate these changes need to be noted.

The potentially most significant of them, and also the hardest to explain, is a rather dramatic improvement in the rate of saving. According to the estimates published by the Central Statistical Organisation (which are now regarded as the official estimates), this rate has gone up from a little less than 12 per cent of the net national product in 1966-67 to about 14½ per cent in 1974-75 and nearly 18 3/4 per cent in 1976-77 (all at current market prices). A tentative estimate for 1978-79, offered recently by the Reserve Bank of India, places it at no less than 20 per cent of the nnp.

One of the long-term targets set in the First Five Year Plan was of course to raise the rate of capital formation and saving in the economy to this level by 1967-68. But it was revised later, and the Third Plan had made it clear that this was not to be expected till after 1975-76. The draft of the Fifth Plan had pushed it back still further, mentioning it as something to be achieved only by the middle of the 1980s. The apparent realization of the target by 1978-79 comes therefore as a surprise, and requires explanation.

A first reaction is to doubt whether it could really have happened. This is an area in which statistics are rather slippery and changes in concepts or methods of estimation could make a difference. Moreover, in the "household" sector — which in this context covers all unincorporated business enterprises as well — it is extremely difficult to estimate changes in commodity stocks and investments of various other kinds such as in agricultural farms, small-scale industries and residential housing, and one must allow for a large margin of error. With what confidence can it then be claimed that increases in rates of saving (and investment) of the order indicated have really taken place and that they are not just the outcome of some statistical manipulations?

It is clear however from a close examination of the estimates that increase in saving in the household sector, corresponding to investments of the kind mentioned above, can at most account for only one percentage point or so of the much larger increase (of 8 percentage points) in the overall rate of saving between 1966-67 and 1978-79 that has been reported. What is more, the margin of error in tracking down the precise sources of this overall increase need be only very small, as part of the higher saving has been in the public sector (for which accounts should be available) and the rest has evidently come from the household sector through accumulation of financial claims (which can also be concretely identified) against savings transferred to other sectors.

In other words, the estimated increase in the overall rate of saving in the economy — from about 12 per cent of the net national product in 1966-67 to around 20 per cent in 1978-79 —

can be accounted for fairly convincingly and does not appear to be a statistical mirage. Saving in the public sector has gone up during this period from about 1 1/2 per cent of the net national product to about 4 per cent, and in the household sector from about 10 per cent to nearly 15 3/4 per cent of the nnp, with almost all of the increase in the latter taking the form of additions to financial claims. (The contribution of the private corporate sector to net saving has been throughout less than 1 per cent of the net national product, and variations in it are therefore of no great importance in this context).

A further fact of considerable significance is that, since 1974-75, over five-sixths of the increase in the financial asset holdings of the household sector have taken the form of either bank deposits and insurance and provident funds or claims of various kinds on government. (Bank deposits, alone accounted for more than half of the increases). It should therefore be possible to identify, through more detailed scrutiny of the data relating to such assets, the broad categories of "households" from which most of the increase in saving within the economy has emerged over the last decade.

Unfortunately such data in the necessary detail are not readily available. Even in regard to bank deposits the latest published data on the pattern of ownership are only for March 1976 — since when the total deposits have doubled. However, unless there has been a sharp change in the pattern of ownership in the last three years compared to the period 1972-76, it would appear that not more than about one-third of the annual growth in bank deposits could be from households in rural and semi-urban areas (that is, from centres with population of less than 100,000). And there is no reason to believe that their share in other financial assets, except possibly in currency holdings, would be any higher. The annual growth in currency holdings has seldom exceeded 1½ per cent of the net national product during the last decade. It seems therefore reasonable to conclude that the contribution of households in rural and semi-urban areas to the increase in the rate of saving in the household sector in 1977-78 (compared to 1966-67) is unlikely to have been more than about 2½ per cent of the net national product in that year. Indeed this could be an over-estimate, particularly when full allowance is made for the reverse flow of funds to such households through cooperative credit institutions.

Actually it was not expected at any earlier stage in Indian Planning that saving in the household sector, from either the rural or the urban segment of it, would grow at the rate it has over the decade since 1966-67. In the Fourth Plan as well as in the Fifth, the marginal rate of saving in this sector was assumed to be only about 12½ per cent (i.e. of the "personal disposable income" accruing to it). A close analysis of the available data shows that it has been on the average well over 25 per cent between 1967-68 and 1976-77; and that it has exceeded 40 per cent since 1973-74.

The other side of the coin is of course that the rate of saving in the public sector was always assumed to rise very much faster. Despite the rise in this rate to about 4 per cent of the net national product in 1977-78, it is however still below the target set for 1973-74 in the Fourth Plan and much lower compared to the target for 1978-79 in the Fifth Plan draft.

The consequent reversal in the relative importance of private and public sector saving in the growth process poses naturally some problems. To the extent that the investment programme in the public sector is planned on the assumption of a higher rate of saving within the sector, either this has to be adjusted downward or a larger quantum of saving has to be transferred from the household sector to support it, perhaps both in some degree. There may also be required some rise in investment in the private sector to absorb the excess saving and, if adequately profitable opportunities are not readily available, some of it could go into unproductive channels such as in speculative holdings of land, commodities and bullion.

The broad lines along which the adjustment has taken place in India in the last few years can be inferred from the available data (though, for this purpose, the available estimates of investment do leave a great deal to be desired). Thus it is clear that, though the rate of saving in the public sector in 1966-67 was only 1½ per cent of the net national product in that year, and investment in the sector was a little over 7 per cent of the nnp, the net transfer of saving from the household sector required to support this investment was only around 2½ per cent of the nnp, since inflow of foreign saving was at that time as high as 3 per cent of the nnp. By 1976-77 the saving within the public sector had gone up to a little over 4 per cent of the nnp but, since investment in the sector had also risen to the same extent, and inflow of saving from abroad had been replaced meanwhile by a sizable outflow (reflected in a net addition to foreign assets in that year to the extent of nearly

2 per cent of the nnp), the transfer of saving from the household sector that was in effect required to support this investment was about 7 per cent of the nnp. Though data are not available yet for offering similar estimates relating to 1978-79 there is no reason to believe that there has been any decline in the order of the saving transfer required from the household sector.

It is also clear that, though the rate of investment in the public sector rose from about 7 per cent to 9½ per cent of the nnp, most of the increase was on account of additions to inventories (particularly of foodgrains). There has been therefore no significant increase in the rate of investment on fixed capital. Moreover, the available price indices (derived from national accounts) show that the prices of machinery, equipment and construction materials have risen much more since 1972-73 than prices of goods and services in general. When allowance is made for this change in relative prices it is evident that, over this period, there has been in real terms a significant decline in the rate of investment in this sector and transfer of a much larger quantum of saving than before from the household sector to support such investment.

Large transfers of saving from the household sector, particularly when effected through financial institutions and instruments such as bank deposits, have naturally the effect of increasing the liquidity within the system. It is of course true that well over a half of the banks deposits now held are in the form of fixed deposits which cannot be so easily withdrawn, but even current and savings deposits have together grown at an average rate of well over 20 percent per annum since 1975-76. Since most of the savings deposits have been getting classified as "demand deposits (according to some rules of the thumb laid down by the Reserve Bank of India) this has been also reflected in phenomenal increases in money supply during this period.

Actually such increase in liquidity need not by itself cause much concern, particularly when the rate of saving in the economy has been exceeding the rate of domestic investment and large stocks of foodgrain and foreign exchange are available (as has been the case in India since 1975-76) for taking care of possible imbalances from time to time in the supply of essential commodities. Even the growth in money supply has to be viewed in this broader framework more so since a significant part of this growth has taken the form of savings deposits whose rate of turnover is known to be hardly one-fifteenth of that of current deposits.

Nevertheless, the conventional "quantity theory", which associates growth in money supply with more or less proportionate changes in prices, is still very deeply ingrained in the thinking on this question in India. And even economists with greater sophistication are inclined to play safe and support this kind of reasoning when there is a suspicion of price rise.

Prices have in fact risen in Indian since early 1979, and quite sharply. But the reasons are quite different. In part the price rises reflect the inflationary movement abroad which has been gaining momentum; in the case of products such as petroleum and steel, and some commodities consumed in urban areas which received the attention of the Finance Minister in the last budget, prices have been pushed up by the deliberate policy of levying higher indirect taxes on them; and similarly, in the case of some agricultural products also, the minimum support prices have been raised as a matter of conscious policy. The rest of the price increases recorded over the year, particularly those which have raised the general index number of wholesale prices in the last six months, appear to be largely the result of temporary shortages such as in vegetable oils, gur, and vegetables and fruits, all of which it should be possible to rectify in a short period without much difficulty.

No doubt such prices increases have also created expectations of further price rise and promoted speculative holdings of a wide range of commodities, thereby raising prices even more. A tight control over credit would have certainly helped to curb them. But this is not achieved by merely reducing the rate of growth of money supply.

Such reduction can of course be effected nominally by just changing the procedure for determining the 'demand' and 'time' portions of the savings deposits, and showing a higher percentage of the increase under the latter category (as in fact the Reserve Bank of India confesses to have done in 1978-79). But nothing will have really changed. Even if a genuine shift is brought about from savings to fixed deposits, it would not prevent the holders from drawing on them when speculative trading in commodities offers the prospect of high rates of profit; all they would lose in the process is a part of the interest that would otherwise have accrued, and this loss need not also be very much if they have been careful enough to hold a fair proportion in the form of short-maturing deposits. It is therefore worth reminding ourselves that savings and fixed deposits together add up now to over Rs.20,000 crores, and that a substantial part of them do represent liquid assets available (over and above currency holdings and current deposits) for financing speculative activity if it should appear attractive enough.

So the answer lies not so much in restricting more severely the rate of growth of money supply (which can at best make only a small difference to the available fuel for feeding inflation) as in preventing such speculation becoming attractive. For this there is no more effective deterrent than large reserves of foreign exchange and of essential commodities such as foodgrain, supported by an administrative machinery that could really make speedy and effective use of them for counter-speculative operations when needed.

Within the narrower sphere of credit control it is perhaps the widely used system of cash credits and overdrafts on which attention requires to be focussed for checking speculative activity in commodity markets. Such facilities are given by banks not only to joint stock limited companies (to the extent of as much as 10 times their current deposit balances) but to proprietory concerns, partnerships, etc which (as is well known in business circles) function as buying and selling agents on the periphery of the private corporate sector and make all the large trading profits that are thereby shielded from the public eye (and of course from taxation as well to varying degrees).

However, even if action is taken along these lines (which is not always the case), a period of price rise promotes the growth of fairly strong lobbies (in the political as well as in the administrative sphere) favouring restraints on government spending. Since cuts on items of recurring expenditure meet usually with considerable resistance it is the projected increases in public investment outlay that really get axed. There is already ample evidence of such cuts in investment this year.

At the same time, over a longer period, the prospects of any significant increase being achieved in the rate of saving in the public sector (compared to the level of about 4 per cent of the nnp attained in 1978-79) are not very bright. The political climate does not favour higher rates of either direct or indirect taxation; the appetite for subsidies seems insatiable; and there are pressure groups only for distributing the profits of public enterprises, none for raising them. In the circumstances there can be no further rise in the rate of public investment without much larger transfers of saving from the household sector.

The case for promoting such savings transfers will be of course recognised if higher rates of public investment seem essential to keep the economy going; and if there is such a clear perception (as there has been in the last few years), one can expect the rate of public investment to be raised despite ideological considerations. On the other hand, when investment in this sector has touched as high a level as 9 to 10 per cent of the net national product (as it had by even 1976-77), and at least a part of it is on projects of questionnable economic value, there could be valid doubts about the wisdom of raising it any further. Public sector investment in 1976-77 had included (as indicated earlier) a large component of investment in inventories, for which the necessary bank credit was made available to the concerned state corporations without any reservations. But would such credit be extended for fixed capital investment without questions being raised?

Moreover, in an economy in which the marginal rate of saving in the "household" sector has risen to over 25 per cent (we shall ignore the higher rate that appears to have been realized since 1973-74, as it could have been due to large migrant remittances from the Middle East which may not last very long at that level), new ideas can also develop on the uses to which such savings are put. One has only to look around the urban and the more prosperous semi-urban areas to notice the channels into which such savings go; they include investment not only in residential houses, theatres, and semi-luxury hotels but in a fairly wide range of "small-scale" industries catering in various ways to demand from the relatively high income groups. Enterprises have also been emerging for meeting export demands in new lines, such as garment manufacture and fabrication of jewelry from precious stones, though they too are largely confined to the "small-scale" sector in which labour laws, power cuts, and taxes are easier to escape. Once such avenues of alternative private investment are found on an adequate scale the concerned interests are bound to find political expression in demands of various kinds.

How soon this kind of private investment will grow, and whether it will be large enough to absorb a high proportion of the growing savings of the "household" sector, is likely to depend to a considerable extent on the rate of growth of agricultural output and incomes in the coming years. As mentioned earlier, there is no firm indication so far of any acceleration in the long-run growth rate of the economy, whether in the agricultural or in the industrial sector; and yet it is not improbable that a process of acceleration has been initiated in the last few years. Apart from the high rates of "household" saving that have been achieved during this period there are some other reasons for expressing this judgement.

The most important of them is the accelerated pace of development of irrigation. Though the gross irrigated area in the country had been increased by more than a third between 1950-51 and 1965-66, the average rate of increase during this period was only about 0.5 million hectare per year. Between 1965-66 and 1970-71 it was stepped up at the rate of nearly 1½ million hectares per year, and it continued to grow at this rate till 1975-76. Since then gross irrigated area appears to have been growing at the rate of 2 million hectares per year, and currently the targets set are still higher, though it remains to be seen whether such further acceleration is realizable in the near future in view of the obvious organisational problems involved. All the available evidence shows that it is irrigation that is the critical factor in agricultural growth.

This has been naturally getting reflected in higher proportions of increases in agricultural output being realised in a small number of States where area under irrigation has been extended most. For instance, nearly three-fifth of the increase in foodgrain output between 1967-68 and 1977-78 (from 95 to over 125½ million tonnes) was in the six States of Punjab, Haryana, Tamil Nadu, Uttar Pradesh, Andhra Pradesh and West Bengal. This suggests that the fluctuations in agricultural output are also likely to be less severe in the future than in the past, unless of course the droughts which take place affect the sources of irrigation on an extended scale. For this reason, though a setback to agricultural output in 1979-80 is inevitable on account of drought conditions over large parts of the country, and there could be a recurrence of it even next year, the prospects of a relatively high growth rate being maintained in agriculture over a period seem to be clearly better now than a decade ago.

One other promising development in agriculture remains to be mentioned. In the period before 1964-65 the output of non-foodgrain crops (referred to conventionally as "commercial" crops) had grown faster than of foodgrains, but the position was sharply reversed between 1964-65 and 1970-71 when non-foodgrain output grew at only about one-third the rate of foodgrain crops. This had serious consequences not only for exports but for agro-based manufacturing industries and the relative price structure within the country. Between 1970-71 and 1977-78, however, the rate of growth of non-foodgrain crops has not only picked up but slightly exceeded the rate of growth of foodgrains.

These developments in agriculture have apparently had already some impact on industrial growth. The rate of increase of industrial production, which had fallen from the average rate of about 8 per cent per annum (realized over the period 1951 to 1965) to less than 3½ per cent per annum between 1965 and 1974, exceeded 6½ per cent per annum in the following four years. The rate of growth of output in agro-based industries between 1975 and 1978 was over 4½ per cent per annum, compared to a little under $1\frac{3}{4}$ per cent per annum in the period 1965-70. Though it is too early to say that it clearly represents a reversal of the downward trend which had set in earlier, it may well prove to be the case for the reasons already mentioned.

All in all it seems highly probable that the rate of growth of agricultural utput will rise somewhat above the level established over the level established in the course of the last quarter of a century, carry along with it the rate of industrial growth as well, and thus help the economy to achieve an average rate of growth of about 4 to 4¼ per cent per annum. The higher rate of saving that has already been realized should be able to maintain this rate, and even help to raise it a little further, without any net foreign aid.

This does not of course mean that the problems of mass poverty and of unemployment in the country are likely to find a solution in the forseeable future. A higher rate of growth of foodgrain output would of course help at least to maintain, if not slightly improve, levels of nutrition. However, the pattern of income distribution is likely to get no better. Less than 10 per cent of rural households operate well over one-half of the total area; agricultural growth may tend to be more heavily concentrated in large, irrigated farms; and there are strong pressures for introducing labour-displacing mechanization in such farms. The top decile of agricultural holdings it should be noted, has also received the bulk of the agricultural credit extended by cooperatives. Indeed, for these reasons, disparities must be expected to grow both within each region and as between different regions within the country.

Above all, the higher rate of growth realized can benefit only peripherally the large and growing class of workers in the countryside who depend primarily on wage employment for their living. The proportion they form of the total rural labour force varies widely from State to State. The number of such workers has however grown very rapidly in most of the States over the last decade, and in the country as a whole from about 35 million in 1964-65 to over 54½ million in 1974-75. The pressures of grinding poverty on this class have been getting reflected in the percentage increase in the number of women workers being much higher (over 60 per cent during this period) than in the number of men workers (in whose case it has been a little under 50 per cent), and in the number of child workers (which has grown by nearly 80 per cent over this decade) exceeding both by a large margin. Since the core of rural poverty in India is in this class, and not much can be done to increase the employment opportunities for them in the areas in which their highest concentrations are to be found, one can safely predict that, within the pattern of development that has been emerging in the country, there is little hope of their conditions improving in the forseeable future except in some areas where the rate of growth of agricultural output is high enough to absorb them in productive employment.

This is not a very cheerful conclusion, however cheering may be the prospect of a higher rate of growth in the economy as a whole. It also raises some very important questions about the politics of development in the future (not to mention politics of socialism). These questions have a direct bearing on the tragic-comic operas that are being enacted now by the organised political forces in the country. But they should have no reason to complain about the emerging pattern of development, because this is the best most of them can hope for given the kind of politics that has been played hitherto, irrespective of ideology and apparent commitment, by even the well-meaning among them.

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