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UNIVERSITY OF NORTH BENGAL

MASTER OF ARTS - HISTORY

SEMESTER-IV

ECONOMIC HISTORY OF INDIA

(1757 A.D.-1947 A.D.)

ELECTIVE 405

BLOCK–2

UNIVERSITY OF NORTH BENGAL

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FOREWORD

The Self-Learning Material (SLM) is written with the aim of providing simple and organized study content to all the learners. The SLMs are prepared on the framework of being mutually cohesive, internally consistent and structured as per the university's syllabi. It is a humble attempt to give glimpses of the various approaches and dimensions to the topic of study and to kindle the learner's interest to the subject

We have tried to put together information from various sources into this book that has been written in an engaging style with interesting and relevant examples. It introduces you to the insights of subject concepts and theories and presents them in a way that is easy to understand and comprehend.

We always believe in continuous improvement and would periodically update the content in the very interest of the learners. It may be added that despite enormous efforts and coordination, there is every possibility for some omission or inadequacy in few areas or topics, which would definitely be rectified in future.

We hope you enjoy learning from this book and the experience truly enrich your learning and help you to advance in your career and future endeavours.

ECONOMIC HISTORY OF INDIA (1757 A.D.-1947 A.D.)

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Unit 2 The Early Drain Of Wealth And Its Mechanism, Magnitude And Effects

Unit 3 - Indian Manufactures For External Market-Internal Commerce

Unit 4 - Agrarian Conditions-Regional Variations – Permanent Settlement

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BLOCK-2 ECONOMIC HISTORY OF INDIA (1757 A.D.-1947 A.D.)

Introduction to block

UNIT 8 focuses on conditions of Indian industries before Industrial revolution in 19th century

UNIT 9 focuses on long term investments by capitalists whether Indians or British

UNIT 10 focuses on the Modern industry in pre-1914 phase-nature-main industry;cotton, jute, iron and steel and others. Impediments to growth,nationalist critique, industry and the First World War phasewith special reference to economic depression.

UNIT 11 focuses on Colonial state and industrial growth, Rise of industrial labour, labour force in large scale industry,type of labour movements, changing social composition ofindustrial labour.

UNIT 12 focuses on the fiscal policies especially shift from direct to indirect taxes

UNIT 13 focuses on the tariff and excise details of the British Government

UNIT 14 focuses on the monetary and credit policies under British Govt.

UNIT 8 - CONDITIONS BEFORE THE EMERGENCE OF MODERN INDUSTRY

STRUCTURE

8.0 Objective

8.1 Introduction

8.2 Conditions Before The Emergence Of Modern Industry

8.3 Lets Sum Up

8.4 Keywords

8.5 Questions For Review

8.6 Suggested Readings

8.7 Answers to Check Your Progress

8.0 OBJECTIVE

The four major sectors will be examined in order. The paper will focus on how they developed throughout history through production rates and statistics until independence in 1947. Considering the special colonial history of India and its de-industrialization phenomenon, this paper also seeks to answer whether British colonialism harmful or beneficial to the modernization of India's economy.

8.1 INTRODUCTION

In 1750, India produced nearly 25 % of the world's manufacturing output and was only outdone by China, which constituted 32.8 %. By 1880 however, India only took up 2.8 % of world exports, and after its independence from British colonization in 1947, it was one of the most poverty-stricken regions in the world. India's economic deterioration is particularly ironic, considering the industrial boom that Britain

experienced during the same era. Nevertheless, from 1750 to 1947 India experienced modernization of its economy in various areas including agriculture, factory production, finance, and even film production. Though India did lose its edge in the textile trade and did in fact experience de-industrialization, its thriving "Bollywood" cinema market and automobile production in Hindustan are some notable examples of economic modernization.

8.2 CONDITIONS BEFORE THE EMERGENCE OF MODERN INDUSTRY

Ancient Period:

In the ancient or primitive period of industry are included those works which were performed by man when he was neither literate nor civilized. In this period no systematic industry had developed. This main concern of man dusting these days was merely too provide for food and physical protection. The means, which were adopted by him to meet these ends, were symbolic of his industrial effort. For food the primitive man used to hunt animals andgather wild vegetables and fruits. For hunting he employed bow and arrow and certain instruments made by sharpening stone. All primitive weapons were made either of wood or stone. These weapons were symbolic of industrial development of that period. Besides, making fire by friction of stone or bamboos was industrial miracle of that time. For a pretty long time this state of affairs persisted.

Medieval Period:

In medieval period there was sufficient development in industry. In this period the signs of industry become quite visible in the efforts of man. A number of manfully operated machines were fabricated. Man also began using animal power to meet his ends. The signs of industrialization, production of goods in excess of consumption and stocking of these came in evidence at this time. The exchange of goods and division of labour also came into vogue. As a consequence of this, different industries started operating separately. For example, blacksmith,

carpenter and weaver set up independent units. Thus, began the specialization of jobs. The artistic spirit of the artisans was awakened. The medieval industrial age in the west wan be divided into three distinct industrial systems. This division of based on the nature of the industrial system. These industrial systems area) Feudal System) Guild Systemic) Domestic System.

Feudal System: Under this system, the primary industry was agriculture. Few persons controlled vast tracts of lands each and they engaged and employed hundreds of workers to do the farming. This system was in vogue in Europe between 9thand 12thcenturies. Under this system the owner of the land was called feudal lord and persons engaged by him were called serfs, the serfs were virtual slaves of the feudal lord. Besides agriculture, other important professions were dependent upon feudal lords. Under the feudal system, the serfs were required to give all kinds of services to their respective lords. In case required, they had to wage war against the enemies of their lord. From 11thcentury onward, urban towns started coming up in Europe with urbanization feudal system got a setback. The labor or the working class now had an alternative to working as serfs. They could migrate to towns and find work there. As a result of urbanization, Guild system came into vogue.

Guild System: The urbanization in Europe emancipated the serfs from their traditional slavery. Having emancipated themselves from serfdom under feudal lords, the worker started learning new trades and skills, as a result of specialization and proficiency in trades acquired by workers, centers of trade came up. Gradually this process gave rise to Guild system. In guild system, trade associations representing various trades came into being. These trade associations worked for the promotion and development of their respective trades. This association supervised the quality and quantity of goods being produced by the member of their association. They also fixed and regulated the prices of goods. Under guild system there used to be two kinds of guild: the Merchant Guilds and Craft Guilds. The main task of the Merchant Guilds was to look after the interests of businessmen. They used to demand justice from government in a manner in which chambers of

Commerce of today function. The Craft Guilds were association formed by craftsmen carrying on a particular craft. The Craft guilds worked for the promotion of the crafts and protection of the interests of craftsmen. The craft guilds used to arrange e weekly markets where craftsmen could sell their products. In Craft guilds, master craftsmen played crucial role, though less skilful Craftsmen were also given due share. They were helped to acquire proficiency in their skill. The master craftsmen used to belong to families of master craftsmen. The craftsmanship was supposed to be hereditary. In these days, the Craft guilds of Blacksmiths, Carpenters and Weavers were particularly prominent. The guild system occupies a place of pride in the history of Industrial development. This system was important in maintaining social harmony and unity. Remarking about the merits of this system Raj Kohli says, "The builders of the great cathedrals of Europe (at the period) had achieved a untie of feeling and thought which the modern world has apparently lost" The guild system lasted for a pretty long time, but gradually it declined. From 16thCentury there was a gradual decline and deterioration in this system. There were two chief causes for the decline of this system. The first cause was internal and the second was external. The first internal cause of the decline of the guild system was that its functions and the rights of its officials were not well defined. This gave rise to myriad conflicts. For example, the guild of goldsmiths was always warring with the guild of silversmiths. Moreover, there was gradual fragmentation of the guilds.

Originally, there was only one guild of cloth merchant. But soon many sub-guilds like association of weavers, tailors, embroiderers etc., were formed. The second cause of the decline of the guild system was external. Under this system there was one group of traders who were manufacturers and the other was on group of traders who were manufacturers and the other was that of middlemen. This group of middle mean later began exploitation of the manufacturers. It acted in the manner and style of modern capitalist. The middlemen took over the control of all levers of production and arbitrarily used them for their own selfish ends. Generally they took over the control of raw material. The arbitrary acts of theses middlemen gave severe setback to

the guild system. Besides these two reasons, there were certain local and immediate caused of this decline. At this time America was discovered. The way to commerce and trade with east also opened. Due to this the trade and commerce was deeply affected. In the production sect of Christianity had greater dominance at this juncture. The rise of protestant religion factor also contributed its share in the decline of guilds. The rise of protestant religion spelt the rise of individualism and this, too, proved inimical to guild system, which was based on a sense of cooperation. In these days another factor which gave deathblow to guild system was the invention and use of big machine and introduction of sophisticated techniques of production.

Domestic System

After the decline of guild system, domestic system came into vogue. This system was a kind of capitalism. As far as the method of production was concerned, it was not much different form that of guild system. However, under domestic system there was no place and no role for various guilds and trade associations. Under domestic system a head of family who normally was a master craftsman controlled the entire production and everything was under his personal ownership. The head of the family used to provide for the raw material and also the manufactured goods. All processes or stages of production were under his individual control and subversion. Under this system the craftsmen had not much freedom. The system is to be seen today in the form of cottage industries. It was again the role of middleman and the moneylender, which ruined the domestic system. The head of a trade in domestic system required from time to time extra funds for the purchase of the raw material. This extra amount came from the moneylender and he usually exploited the opportunity to the fullest. Besides, mechanization of industry rendered this system obsolete and economically non-viable. The capitalistic by investing huge amount into industry and mechanizing it to the hilt completely ruined the domestic system. Thus, the domestic system came to an end and modern industry came into being.

Modern Industry: Modern industry in India did not develops a continuation of the previous domestic or guild system as it did in the west and other social not had it much to do directly with the 'Caste Panchayats' country to what some writers has contended, modern industry in India represents in general as it does in other eastern countries a break with the traditional social economic institute of the paste, which hand they remained would have undoubtedly retarded its development. Modern industry in this country began about the 1850-60 decade when the first cotton and jute mills were opened and a railway line was inaugurated of Bihar and Bengal railway and road transportations experienced subsequently a considerable growth which greatly influences the economic and social life of the country5. The advent of railways was decisive for Indian economic development the chronic transport bottle need of Indian industry was broken, the way was they proved for the development of large-scale industries. It was no accident that the development of the jute and cotton the coal and iron and plantation industrial progressed slowly before 1850 and occurred in quick succession therefore, transport in the life blood of industry and without railways it lacked the arteries through which to flow6.During this period the British power had become consolidated in India and thereby attracted large number of foreign entrepreneurs, particularly from England and Scotland who had discover in India a source of cheap labour and raw materials. Cotton mills were opened during this period in Bombay and Ahmadabad, jutes mills proliferated on the Hooghly banks while woolen and lather factories become prominent in Kanpur. Mr. Justice Ranade said that, 'it was at this period and during the first decade of the present century(or 20thcentury), that there was general tendency to make a greatly increased use of mechanical appliances everywhere7. The two world wars also accelerated the advance of Indian Industries. Iron and steels works started during the First World War while an industrial growth took place during the Second World War. The numbers of industries during the war increased by 3.475 and the paid up capital by Rs 100 cores8.In spite of this advance, the traditional policy of the British rulers was to use delaying tactics with regard to Indian

industrial development. Some industries were fostered, especially jute manufacturers and railways, but on the whole, it was a sluggish growth. By 1900 the total mileage of railway tracks in India was 25,000, which by1928 was increased to 40,000. But even this moderate accomplishment was due to military and strategic considerations especially in the northern and eastern frontiers. The idea behind this resistance to the industrial development of India was to prevent Indian goods from competing with British goods, though most of the new Indian industries were in British hands and run by British management and capital9.Nevertheless, due to the efforts of Jamshedji Tata and his successors, the pioneers of modern industrial development in India, in 1911 the Tata Iron and Steel Works were completed in what is now Jamshedpur, giving thereby an added impetus to Industry. But this was not accomplished without great difficulties and was also too short of what the country needed10.But it was during the First World War, that Britain realized how dearly it had to pay for this policy, when the Germans and their allies preventing British goods and resources from reaching India, and Indian raw materials from being sent to the metropolis cut the normal trade routes. The outcome of this was that the Indian continent was left to itself without the possibility of utilizing its own means with the consequent hardships to the population, danger to the commonwealth, and difficulties to the imperial army then operating in India. The reaction after the war against this state of affairs brought about spell of freedom and a comparative relaxation of controls. But the irony of the situation was that while the growth of industry, which between the two World Wars was taking place everywhere, could not be halted in 32India, the policy of restriction adhered to by the British Raj only succeeded in unnaturally retarding this development. Had better counsels prevailed and had Britain accepted India as a partner in industry, and not as a competitor, not only the history of India but that of Britain also, and probably of the whole world, would have been quite different from what it was especially for the developing countries of the East11.Yet another World War seemed to have been needed in order to make the ruling powers see things in their proper perspective; but the vision came

too late. “It was not until the Second World War that were factories started in India for the manufacture of spinning ring frames and looms or even such simple items as pickers, bobbins, and starch, all of which are required by an industry which had been in operation since 1855.

Industry and Independence:

Whatever encouragement was given industry during the war periods, the then ruling power had to contend with the difficulties created by the war itself, especially in the East. The result was that two years after the war, on 15 august 1947, the Indian tricolor, the symbol of freedom and independence, was a prelude to the only genuine industrial revolution which India has so far experienced and which was to leave its mark on the nation for many years to come, not only in economic and social fields, but also in the political and cultural spheres. Without going into a description of the industrial growth during this period it may only be mentioned here that while the capacity of the traditional industries increased about 25 per cent in a period of five years ending in 1953, that of modern industries like motor, diesel engines, batteries, transformers, radios, etc, experienced a growth of over 100 per cent in the same period. Since then, other capacity and output have been increasing at a proportionate pace. Furthermore, the general indoor of industrial output in 1951 rose to 117.4 as compared with 100 in 1946; and in 1960-61 it experienced a further rise up to 194 taking the index for 1950-51as 100. During this period a number of institutions and agencies like the Industrial Finance Corporation and the State Finance Corporation were established in order to help the growth of industry

Why Industrialisation? What are the ultimate objectives of economic development?

Different governments may have different objectives in mind. Generally, however, they will include a faster growth of national income, alleviation of poverty, and reduction of income inequalities. But how is industrialisation expected to contribute to these goals? The experience of industrial economies shows a close association between development and industrial expansion. But industry is also

thought to provide certain spill overs which would benefit other activities: enhancement of skills, training of managers, dispersion of technology, etc. Moreover, pessimism about the prospects of food and raw materials made the substitution of domestic for imported manufactured goods seem the most promising route to development for many countries. Industrialisation and foreign trade Economists and policymakers in the developing countries have long agreed on the role of government in providing infrastructure and maintaining stable macroeconomic policies. But they have disagreed on policies toward trade and industry. The form of government intervention in this area is the distinguishing feature of alternative development strategies. A convenient and instructive way to approach the complex issues of appropriate trade policies for development is to set these specific policies in the context of a broader Less Developed Countries strategy of looking outward or inward.

Outward-looking development policies encourage not only free trade but also the free movement of capital, workers, enterprises, the multinational enterprise, and an open system of communications. By contrast, inward-looking development policies stress the need for LDCs to evolve their own styles of development and to control their own destiny. Within these two broad philosophical approaches to development, a lively debate has been carried out between the free traders, who advocate outward-looking export promotion strategies of industrialisation, and the protectionists, who are proponents of inward-looking import substitution strategies .The advocates of import substitution (IS) – the protectionists – believe that LDCs should substitute domestic production of previously imported simple consumer goods and extend this later to a wider range of more sophisticated manufactured items – all behind the protection of high tariffs and quotas on imports. In the long run, IS advocates cite the benefits of greater domestic industrial diversification and the ultimate ability to export previously protected manufactured goods, as economies of scale, low labour costs, and the positive externalities of learning by doing cause domestic prices to become more competitive with world prices. By contrast, advocates of export promotion (EP) of both

primary and manufactured goods cite the efficiency and growth benefits of free trade and competition, the importance of substituting large world markets for narrow domestic markets, the distorting price and cost effects of protection, and the tremendous success of the East Asian export-oriented economies of South Korea, Singapore, and Hong Kong. The balance of the debate has swung back and forth, with the protectionists predominating in the 1950s and 1960s, and the export promoters gaining the upperhand in the late 1970s and in the 1980s and 1990s, especially among Western and World Bank economists. Indicators for measuring economic development

Of course, any development policy has to be assessed by measuring the economic development it effects. India's first Prime Minister Jawaharlal Nehru declared on the eve of the departure of the British, on 14 August 1947, that India's task in the future included "the ending of poverty and ignorance and disease and inequality of opportunity". These measures will be used to determine the success of the inward-looking policies he initiated, as well as to compare their success with the success of the reform policies. Therefore, growth of income per capita, alleviation of poverty and reduction of income inequalities are amongst the most important indicators. To measure advances regarding inequality of opportunity and ignorance, several indicators pertaining to education and health will be used. These are two important public goods to which every individual is entitled; both for their intrinsic importance and for their enhancement of instrumental personal, social and process roles, and also empowerment and distributive roles. History of Industrialisation in India This section gives a rough overview of the history of industrialisation in India. Several areas will be discussed in more detail in the following section. Colonial rule Under colonial rule, India, as with most other developing countries, followed an on-industrial model. But many Indians believed that progress was retarded by this. It was believed that true economic progress lay in industrialisation; Smith's and Ricardo's ideas of international specialisation and mutually

advantageous free trade 3 of 13were rejected, at least until India became an exporter of more sophisticated goods.

Development and History of the Primary Sector

Agriculture

Production of Main Food Crops

Compared to other countries India had from early on much more arable land reserved for main food crops, which were wheat, barley, maize, millet, sorghum, and rice. 10,900 thousand hectares were available for wheat growth in 1892, and by 1947 the land had expanded to 13,910 thousand hectares. India also had 26,556 thousand hectares of rice fields in 1890 and 34,625 by 1947. The increase in the available farmland was primarily due to the development of irrigation and canal networks in Punjab, Narmada Valley, and Andhra Pradesh. Statistics about the available arable crop land alone however, does not signify an increase or a decrease in production levels. The annual growth rate of all crop output was 0.4 percent from 1891 to 1946. The actual data concerning the output of main arable crops corroborate; in 1905 the wheat output was 116,359 thousand metric tons, but in 1947 the output had dramatically dropped to a mere 8,020 thousand. During the period between the two world wars, from 1918 to 1939, agriculture declined. (6a) For instance, the output of rice in 1918 was a dismal 38,088 thousand metric tons, compared to the 56,328 metric tons output in 1917. Bengal especially suffered, with food output declining by 0.7 percent annually from 1921 to 1946.

Production of Cotton

In 1865, India only produced 12 thousand metric tons of cotton. By 1889, the number had risen to 533, and in 1919 doubled to 1052 thousand metric tons. Note that during the post-World War I years India began to produce much more cotton that before. In 1947, however the cotton output directly after independence was 569 thousand metric tons. This meager amount gives onlookers a clue as to how Indian cotton producers were pressured by their British colonizers to increase output prior to independence.

The amounts of cotton exported throughout Indian history are more tell-tale than the production rates alone. India exported 102 thousand metric tons of cotton in 1850; 250 in 1863; 326 in 1905; 456 in 1915; and 738 in 1930. After independence in 1947, cotton exports were down to 211 thousand metric tons. These numbers may be part of a pattern of British exploitation of Indian raw materials, as cotton exports increased drastically during the 1930s when the British economy was suffering from the Great Depression. Much earlier on, at the beginning of the 19th century, India became the supplier of the raw material, cotton, for England's Lancaster cotton textile industry. Like many other colonized countries, India's cheap cotton and other raw materials were exported to Britain to help produce final goods in British factories.

Livestock, Meat, and By-Products

There was no significant change in the number of horses, cattle, pigs, sheep, goats, and camels in India from the late 1800s to 1947. From 1895 to 1947, the number of horses increased from 1,133 thousand to 1,397 thousand. In the same period, the number of cattle rose from 78,380 thousand to 133,544 thousand. Though the number of cattle doubled, this is hardly significant when considering the natural population growth of animals. As the cow is a sacred animal in the Hindu religion, a major religion in India, there would likely be an increase in the number of cattle rather than a decrease.

Meanwhile, there were no systematic records of meat and by product outputs in India until the 1950s. However, it is safe to surmise that dairy products were produced in large quantities as they are considered an essential nutritional component of most Hindi meals in India.

Mining

Coal mining was a profitable business during British colonial times. However, although the British did indeed support coal, gold, silver, iron ore and steel mining, they did not look favorably upon mining other metals such as lead. They believed that India's development of metallurgy would lead to production of weapons for the "natives," a potential threat to British rule. The British implemented the Arms Act in 1878 to outlaw Indian ownership of firearms and limited Indians from

mining and working metals that might "sustain it in future wars and rebellions." Several mines were actually closed down under British rule.

Coal Mining

Large-scale commercial coal mining in India began in 1774 under the East India Company in the Raniganj Coalfield along the Western bank of the Damodar River. The introduction of steam locomotives in 1853 made possible the effective transportation of coal from the mines to urban centers and ports. India's output of coal rose from 2,203 thousand metric tons in 1890 to 30,695 in 1947. Coal mining proliferated during and after World War I; from 1920 to 1930, national coal output increased from 18,250 to 24,185 thousand metric tons (16a). However, coal mining declined during the early 1930s, when the output dropped by more than 4,000 thousand metric tons in just three years. The facts collaborate with other sources that claim Indian industries declined along with Britain's economic stagnation during the 1930s.

Iron Ore Mining

India's output of iron ore increased significantly during British rule, though there was a small drop in production during the early 1930s. In 1912, the national output in thousand metric tons was 24. By 1947, the quantity had reached an astounding 1,625. Iron ore mining will be discussed in further detail below in the secondary sector, which deals with the iron and steel smelting industries.

Gold and Silver Mining

India's total output of gold in 1885 was only 0.2 metric tons. However, with the expansion of gold mines, output reached an all-time high in 1915 at 17.3 metric tons. The gold output quickly decreased after the 1915 peak, and in 1947 only amounted to 5.2 metric tons. As for silver, India was a major importer, not an exporter or a producer nation. According to the American Council Institute of Pacific Relations in 1933, China and India were long time importers of silver, as opposed to exporter nations like the United States, Mexico, Canada, and Australia.

Development and History of the Secondary Sector

Textile Industry

Problems then and now

The textile industry is one of the biggest components of the Indian economy today, and accounts for 21 percent of employed workers in India. Many of the advantages that sustained India's textile industry in the past still continue to influence the market. For example, India still has a huge production capacity, and still has a large pool of skilled and low-wage workers available for cheap labor. At the same time, the current weaknesses of the Indian textile industry are the same ones that plighted it in the past, during British rule. Some problems include the import of cheap textiles from other neighbors, the use of out dated manufacturing technology, and disorganization. One aspect that may have changed is the shift in competition. India had to struggle against cheap British textiles before independence, but now have to deal with cheap Chinese textiles. The textile industry has yet to undergo a dramatic modernization process.

Development during British Colonial Rule

Prior to British rule in the eighteenth century, Indians had dominated the world textile trade. However, along with the Industrial Revolution, the advent of spindles, looms, and new spinning processes made better textile producers out of the British. In India, the textile industry evolved from being a mere domestic industry to a top notch national industry far before the Industrial Revolution. Meanwhile, after the introduction of looms and spinning mills, Lancashire was the center of the cotton and fabric industry in Great Britain, out-competing India though lower production costs, greater supplies, and forced tariffs

Thus, the traditional textile industry of India went under de-industrialization during British rule. Nonetheless, modernization of India's textile industry took place during the early 19th century; the first textile mill in the country was established at Fort Gloster near Calcutta in 1818. A few years later, the first cotton textile mill of Bombay was established in 1854 by a Parsi cotton merchant. In 1861, the first cotton mill in Ahmedabad was established in the Gujarat region. By the end of the 19th century, there were 178 cotton textile mills in India.

Notes

Automobile Industry

India's automobile industry is the tenth largest in the world, producing 2 million units annually. Though India's automobile industry did not flourish until after independence, the foundations of domestic carmakers such as Tata Motors and Hindustan Motors were set up prior to 1947.

Tata Motors

In 1897, Mr. Foster of Crompton Greaves Company in Mumbai became the first person in India to own a car. A few years later in 1901, Jamshedji Tata became the first Indian to own a car in his homeland. Jamshedji Tata was a pioneer in the field of modern industry in India, being the founder of what would later be called the Tata Group of companies. One such company is today's Tata Motors. Tata Motors is part of the Tata and Sons Group, which was founded by the aforementioned Jamshetji Tata and J. Baker. Founded in 1945, just two years before independence, the industry did not generate much profit until it formed a joint venture with Daimler-Benz AG of Germany in 1954.

Hindustan Motors

Hindustan Motors is another major Indian automobile manufacturer and it is famous for the Ambassador car, a model popular among Indian taxi drivers. The company was founded before Tata Motors, in 1942, by B. M. Birla. Hindustan Motors Limited commenced its operations in a small assembly plant in Port Okha in Gujarat, until the facilities were later transferred to Uttarpara, West Bengal in 1948. Currently Hindustan has operational facilities in Chennai, Kolkata, and Indore.

Iron and Steel Industry

First step forward : Bengal Iron Works

In 1870, James Erskine founded the Bengal Iron Works, the first step towards an iron/steel smelting industry ever taken in India. He used raw coal to fire open top furnaces, using the locally available poor-grade iron ore. Operations began in earnest in 1875 at Kulti. The plant at Kulti also made steel, but could not overcome the competition from imported steel.

Though Bengal Iron Works was the first plant to produce iron and steel, more credit is given nowadays to TISCO, which was able to produce steel and make profit. The plant was not very successful, and was salvaged by Sir Rajendranath Mookerjee and Sir Acquin Martin, the founders of Martin & Co.

The two important and historic iron and steel industries of Indian colonial history that still exist today are Tata Iron and Steel Company, Ltd (TISCO) and The Indian Iron and Steel Company, Ltd. (IISCO)

Tata Steel

Tata Steel was established by Indian Parsi businessman Jamshetji Nusserwanji Tata in 1907. It was the first steel company in India, and the company also had significant labor policies that differed from the prevailing British system. For example, Tata Steel introduced an 8-hour work day in 1912 when only a 12-hour work day was the legal requirement in Britain. In its modern-day website, the company boasts that its operations since 1907 were never once disrupted by a labor strike. Tata Steel is one major component of the Tata Group, along with Tata Motors.

The Indian Iron & Steel Co. Ltd

If Tata Steel was founded by an Indian businessman, IISCO was established by Englishmen to suit the needs of the impoverished British government, which suffered from disruption of supplies of iron and steel from Europe during World War I. G. H. Fairhurst founded the IISCO plant at Burnpur, which went into operation in 1918. At first, IISCO only had iron making facilities, but in 1939 the Steel Corporation of Bengal set up a steel plant at Burnpur as well. The two merged and operated under Martin Burn's agency during the late 1940s and the early 1950s.

Underdeveloped countries are greatly handicapped by shortage of capital for industry and enterprise.

Finance is the prime maker of growth. Anyway, capital for industry and entrepreneurial zeal were severely and conspicuously scarce in India when the East India Company (1600-1874) stepped into this country.

It was very difficult to raise capital on private initiative in the days of the Company rule and, thereafter, because of damped forces of demand and supply capital remained shy.

Naturally, under the circumstance, the state is supposed to act as a godfather for promoting and financing industries. Since India was under the British rule for almost 200 years (1757-1947), the British Government, found it unprofitable and unnecessary to go for industrialization in India. However, imperialist capital came in this country as a matter of colonial policy—the policy of subordination of Indian to British capital. It was only after the First World War (1914-1918), that state patronage for industrial development was visible as Britain's supremacy all over the globe came under serious threat.

Against this backdrop, a "new" pattern was evolved to overcome the obstacles of (i) shortage of entrepreneurship; (ii) non-availability of, mainly, venture capital; and (iii) dearth of managerial skill and knowhow.

This new pattern of industrial organisation that evolved came to be known as the Managing Agency System (MAS)—a peculiar business entity in the early years of the nineteenth century. Before we embark upon this form of industrial organisation, we will make a brief review of the industrial development during the British rule.

Early Efforts of Industrialisation:

Modern industry or the large-scale industry is a mid-19th century pheno-menon. Before the British conquest, India's supremacy in the industrial field reached its high watermark—India was called 'the industrial workshop of the world' during the 17th and 18th centuries. Demand for Indian cotton goods in England during this time was unprecedented. Indian cotton cloth was considered by Englishmen as the badge of 'style and fashion' of the time.

Woollen and silk items were also in huge demand. All this development brought untold miseries in England and other parts of Europe. Firstly, import of Indian goods destroyed the prospect of woollen and silk industries. Secondly, unemployment and suffering among the weavers

mounted up. Thirdly, change in the composition of India's trade led to the export of treasure from England to India.

To counteract these unhappy developments, some measures were taken to pacify the British nationals, but with little relief. Ultimately, the way out was found through legislations. Acts were passed, first in 1700, then again in 1720, to prohibit or restrict import trade of Indian cotton good, silks, calicos, etc., by total prohibition or by imposing heavy duties. As these measures did not yield desired result, one British author commented in 1728: "two things amongst us are ungovernable: our passions and our fashions".

What was the net effect of this state of industrial development? What was 'industrialisation' to India by the standards of time was 'de-industrialisation' to Britain. India, however, had not been fortunate enough as soon as the 'ugliest' thing came on us in 1757—the loss of freedom through British conquest of India.

India had never been an industrial country in the modern sense of the term. In this sense, even England and other industrialised countries of today had not been so, until recently. What strikes most about India was that even being pre-dominantly an agrarian country large varieties of industries existed in India and some of them competed quite successfully with many other countries.

But her industrial supremacy started crumbling when the English cotton industry raised its head rapidly by the mid-18th century.

Two important developments of this were:

(i) The beginning of the era of industrial revolution in England around 1750 and

(ii) The battle of Plassey in 1757 that established the Company (foreign) rule.

As soon as the battle was won, the foreign ruler started abusing both economic and political power in an un-sympathetic and hostile way. Under pressure from the powerful rising English manufacturing interests, EIC dealt a severe blow to Indian industries that led to final extinction—

the phase of India's 'deindustrialization'. Now the cycle turned inside out. It employed the arm of political injustice on Indian products (one-way free trade) to strangulate a competitor with whom she could not contend 'on equal terms'.

The last nail in the coffin was hammered in 1813 when the trading monopoly of the EIC was withdrawn. It was the political domination and the commercial policy of Britain that threw open India to all. India now suddenly was reduced to an importing country from an exporting nation. Indian market now became flooded with machine-produced goods at a lower price and also witnessed the loss of export markets. Further tragedy was in store.

Being a colonial country, she had to pay a large sum for England's industrialization scheme. India was forced to supply raw materials for triggering industrial revolution with greater rapidity in England. India was then forcibly transformed from being a country of combined agricultures and manufactures into an agricultural colony of British manufac-turing capitalism.

A history of modern Indian large scale private industry between 1850 and 1914 is associated with the developments in mainly plantations like jute, cotton, and steel. Beginning of these modern Indian industries was the 'product of India's economic contact with Britain'.

There was also a limited development of mining, especially coal. One thing that is worth noting is that most of these industries, except textile factories, were under European control.

In the early days of the Company rule, Indian raw jute had been in great demand for the Dundee mills. World conditions after 1850 were quite propitious for the growth of jute manufacturing and the credit for jute spinning firm in Rishra, near Serampore, Bengal, went to George Acland—a Scottish. The founda-tions of cotton textile industry were laid also during the early 1850s. Though the jute industry was dominated by the foreigners the cotton industry was shaped and cared by the natives, mainly the Parsee entrepreneurs.

Some abortive attempts were made by the East India Company in the 19th century to develop iron and steel industry. However, the credit for the development of large scale manufacture of steel in India goes to Jamshedji Tata and his son Dorabji. Tata Iron and Steel Company were set up in 1907 and it started function of producing pig iron in 1911 and steel ingots in 1912.

The progress or the achievements of modern large scale industries can be visualised by considering the output produced and the employment data. Between 1880 and 1914 large scale industrial output grew at the rate of 4-5 p.c. p.a. —a rate of growth that is comparable to other contemporary countries of the world. But in the light of total economic activity in India, output produced was rather insignificant. This is also true about the employment situation; it came to less than eight-tenths of 1 p.c. of the total labour force in 1913-14.

Meanwhile India's industrial structure started diversifying. In spite of inadequacy of domestic demand and high production costs, industries like woollen mills, breweries, and paper making industries made significant march during this time. Though these industries were recorded officially as the large industries, they were small in character.

Other industries having small-scale character that operated were tanning, vegetable oil processing, glass-making, leather goods manufacturing, etc. Despite diversification, India's modern manufacturing industry could not develop on a sound footing before the outbreak of the World War I.

The three important reasons behind such industrial development were:

(i) Young in experienced entrepreneurs,

(ii) Absence of State aid towards industrialisation,

(iii) Steep uninhibited competition with developed foreign machine manufactures.

R. C. Majumder then adds: "The pattern of industrial development which had emerged in the 19th century—confined to a limited sector and concentrated in a few unevenly distributed areas—remained virtually

unchanged till the beginning of World War I, though within these narrow limits the years 1905-14 witnessed a relatively rapid growth".

Industries in the Inter-War Period (1919-38):

No country under colonial dependence could undertake any industrial transformation, if not all-round development. Up to the First World War, India experienced the classic period of imperialism of free trade and the British Government's unsympathetic, hostile policy against industry.

In addition, shortage of capital, management experience and technical expertise, as well as the absence of a growing indigenous market, and, above all, general poverty, caused slow expansion of Indian industries. Even then, one can safely conclude that during 1850-1914, the foundations of modern industries were laid in India.

Meanwhile, the outbreak of the First World War exposed the weakness of Britain's strategic position in the East as India had been deprived to develop the most elementary basis of modern industry. In order to impress upon the Indian people and the (industrial) bourgeoisie, Britain granted some political and economic concessions, particularly future industrialisation during the War and immediately after the War.

As the issue of tariff protection crept into the heads of Indians, the British Government appointed the Industrial Commission in 1916 and assured that industrialisation efforts would henceforth continue with utmost sincerity. Unfortunately, industrialisation scheme as prepared by the Industrial Commission ultimately came to nothing.

However, during the war-period, industries like cotton and jute made much headway. Steel industry also experienced substantial growth. Consumer goods industries like chemicals, cement, fertilisers, mineral acids, etc., for which India depended on foreign countries, also progressed during the War.

However, such prosperity of Indian industries was not a long-lasting one. Above all, promises made by the foreign ruler remained, however, unaddressed—as usual. On the contrary, faced by the intense foreign competition, Indian industries in the mid- 19205 demanded protection in

an unwavering manner. To this end, the Fiscal Commission was appointed in 1921 that ushered in a policy of discriminating protection.

This was indeed a belated response to repeated demand made by the Indians from at least since the 1880s. The policy definitely helped some industries to develop. But the end result was rather a haphazard development of certain industries and not general economic development as such. In 1936, 'The Economist' observed India's industrialisation effort: "Although India has begun to modernise her industries, it can hardly be said that she is as yet being industrialised".

On the whole, during the inter-war period, output of cotton piece goods, steel ingots, paper, etc., increased substantially. Many other industries also progressed even in terms of employment and the number of factories. But as far as diversification was concerned, it was indeed slow and the state of transformation of the economy was only 'marginal'.

Industries during 1939-47:

The Second World War, however, opened a new phase in India's industrial history. As the character of the World War II was different from that of the First, the latter created a far more urgent and intense demand for the rapid growth of India's basic and key industries. Against the backdrop of this favoured ambience of industrial development and the near-cessation of imports due to war operations, Indian industries somehow came to take pleasure in having a quasi- monopoly situation in the home market.

As a result, not only industrial output of large scale industries expanded significantly, but also a more widening of the industrial diversification became possible during the war-time years. During 1938-39 and 1945-46, the general index of output of all large scale manufacturing activity (at 1938-39 prices) rose from 100 to 161.6 and that of factory employment increased from 100 to 159.

Despite this headway, India's manufacturing before independence displayed many frailties. Firstly, India did not possess capital goods industries worth the name. This, therefore, hampered her potentiality to

reproduce its existing productive capacity. Secondly, import dependence of the Indian manufacturing sector was enormous.

Thirdly, possession of technical skill and institutes offering technical education were virtually negligible. Industrial development is largely conditioned by the stock of 'human capital'—the stock of scientific and technical cadre. India was still a country denied to grow by the apathetic foreign government.

However, the prospect for industrial development in India after indepen-dence must not be undermined as she had already constructed enough possibilities for industrial development.

Reasons for Low Industrial Development in India:

In this connection, it is better to point out some reasons behind the low level of industrial development in India.

It was the result of:

(i) Inadequate capital accumulation;

(ii) Mobilisation of unproductive investment; (Keynes castigated inordinate love for liquidity of Indians. Male people were desirous of seeing jewellery in the neck of their female counterparts);

(iii) Undue preference for quick-return yielding commerce and trading activities of the Indian capitalist classes; and

(iv) Concentration of entrepreneurship in the hands of a few small sections of Indians.

In addition, shortage of capital goods and absence of skilled personnel also acted as drag on India's industrial development.

Though these acted as strong depressants, colonial status seemed to be the moststrong stumbling block for India's drive for industrialisation. Above all, the contribution of the British Government towards India's industrialisation was minimal before 1916, that is, before the establishment of the Industrial Commission. The industrial policy of the imperial power could be described as 'a case of too little and too late'.

Check your progress –

1. What were karkhanas?

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2. Write about industrialization during medieval age.

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8.3 LETS SUM UP

Because it would have been difficult to reach a judgment about the effects of British colonization on India's economic modernization and development as a whole, the economy was examined sector by sector.

The primary sector included agriculture, livestock, and mining. Though statistics from the late 1800s to independence in 1947, it was easy to see that available land for food crops expanded during the colonial period. However, at the same time, it was evident that wheat and rice production faltered under colonial rule. Not only that, cotton was produced primarily to support the Lancashire textile mills in England.

On the other hand, the secondary sector developed under British rule, as coal mining boomed and later fueled the Indian iron and steel industries. Nevertheless, restrictions by the British in fear of Indian armament deterred potential business expansion.

In the tertiary sector, the cinema industry was relatively free of restrictions and contents dealt with glorification of traditional Indian culture and Hindi romance. The banking and finance services by Indians could not grow as much under European rule, but the Swadeshi movement enabled local businessmen and politicians to successfully establish their own enterprises.

Last of all, the quaternary sector failed under British administration, whose educational policies were short-lived, prejudiced, and limited, available only to the elite class.

Because the British introduced regulation, standardization, and new technologies to India, but at the same time de-industrialized India through exploitative tactics, one cannot reach a black-or-white judgment as to whether British rule benefited or deterred modernization of India's economy.

8.4 KEYWORDS

Karkhanas, pre colonial, industrialization

8.5 QUESTIONS FOR REVIEW

Discuss the conditions of industrialisation before colonial times.

Elaborate about the industrialisation from 17th century onwards.

8.6 SUGGESTED READINGS

The Cambridge Economic History of India, Vol 2 by Meghnad Desai.

Economic History of India by Tathagata Roy

8.7 ANSWERS TO CHECK YOUR PROGRESS

1. Hint – 8.2

2. Hint – 8.2

UNIT 9 - CAPITALIST INVESTMENT IN INDIA-INDIGENOUS AND BRITISH EFFECTS

STRUCTURE

9.0 Objective

9.1 Introduction

9.2 Indian Capitalist Investment

9.3 Lets Sum Up

9.4 Keywords

9.5 Questions For Review

9.6 Suggested Readings

9.7 Answer to Check Your Progress

9.0 OBJECTIVE

To learn about the capitalist investment by Indians

To learn about the capitalist investments by British

9.1 INTRODUCTION

Historically industrialization has had a strong association with capitalism and profit-oriented capitalist firms have been its important instruments in many parts of the world. Britain was the pioneer nation in this regard. Many other countries have successfully followed her to achieve an 'industrialized' status. Such success, however, has been far from universal and there have been other sides to that process.

9.2 INDIAN CAPITALIST INVESTMENT

Notes

The Indian case serves to highlight the significance of the concrete internal and external conjunctures in determining whether and to what extent does a process of capitalist development produces industrialization. IIn Europe, a period of time separated the initial emergence of capitalist relations of production and the advent of the Industrial Revolution. Capitalism emerged out of a process of transition from feudalism whereby the dominance of capital over the production process took the form of the emergence of a new kind of capital - industrial capital. The pre-condition for the emergence of this industrial capital was the availability of wage-labour which made it distinct from the historically older form of capital, namely merchant capital, which required only the existence of trade and commerce as its basis. It is the advent of capitalist production and the subordination of commerce to production rather than the other way around that provided the setting, as vividly described by Marx in Volume I of Capital, for the gradual revolutionising of production that eventually expressed itself in the transition from handicraft production to machinery-using modern industry. Capitalism's emergence in India in a colonial context, however, did not have a similarly revolutionising effect. Colonialism itself played the kind of role that in Marx's view merchant capital did in Europe when it established its sway over production – expanding commerce but preserving and maintaining the pre-existing mode of production as a precondition for a surplus appropriation process. India's agrarian sector under colonial rule provided the prominent example of this phenomenon. The surplus appropriated from that sector, a kind of primitive accumulation, in addition fed not capitalist accumulation in India but instead formed the basis for tribute transfer to Britain from its Indian colony. The destruction of India's traditional handicraft industry fostered by colonialism on the other hand had little to do with the expansion of modern industry in India, facilitating instead industrial expansion in Britain. It gave rise to a process of deindustrialization rather than industrialization – whose effects were only partially reversed by the import-substitution process that took place towards the later part of colonial rule. In addition to these was the absence of any consistent support to industrialization from a state guided by the imperatives of

maintaining India as an appendage of the British imperial system. The emergence of the capitalist class in India also reflected the lack of capitalism's revolutionary character.

Capitalist production was more or less synonymous with modern industry from the very beginning. This emergence of modern industry was initiated by pre-existing merchant capital making use of the availability of machinery in the form of imports. It was thus an extension of commercial activity rather than a process of industry coming to rule commerce. In addition was the fractured development of the industrial capitalist class, its originally dominant component being a European segment tied to and dependent on colonial rule and inhibiting the development of its native component. This reinforced the effects of the fact that it was not their mastery over production or technological innovativeness but instead accumulations through trade and commerce and their connections and skills in that sphere that had formed the basis for the emergence of India's industrial capitalist class. This combined with the colonial background to shape an attitude towards technology of long-term significance. Technology was not something to be developed but simply something to be acquired in the market and from foreign sources. India's industrial capitalist class never fully shed this attitude acquired as a result of its specific origin. The development of modern industry in the period of over nine decades preceding independence was hardly spectacular. When the process began, most of the world excluding Britain did not qualify to be called industrialized. By 1947, however, all the advanced countries and regions had experienced their industrial take-offs. In India, the modern industrial sector remained very small and narrow. The real historical significance of itsdevelopment under colonialism lay not in the great economic transformation it produced but in it creating the future ruling class and its immediate antagonist, the working class. IIThe historical background of colonialism also meant Indian independence lacked the character of a full-fledged bourgeois revolution. It meant the end of direct foreign rule and that was of critically important significance insofar as it opened up the possibility for the use of the state to promote capitalist industrialization.

Notes

However, the transfer of power associated with independence did not represent a decisive episode in the transition from one social formation to another. The end of colonialism did not mean fundamental changes in the economic and social structure created under its aegis. It brought India's capitalist class to power but only in alliance with dominant landed interests. The limits to the agrarian reform programme and the consequent persistence of an enduring agrarian constraint on industrialization stood testimony to this. Capitalist industrialization under the dirigiste regime after independence had to thus take place in a constrained internal and external context. In such circumstances, the achievement sof India's import-substituting industrialization between independence and 1991 were limited along many different dimensions. The average pace of industrial growth was far more rapid than in the colonial era but was marked by instability.

Yet an industrial sector considerably larger and more diversified than at independence came into being by the end of the 1980seven as per capita levels of industrial production remained low. The industrial sector's share in aggregate output, including the part contributed by its informal component, crept up very slowly to just over a quarter by the end of the 1980s. Industrial expansion and even services growth, however, contributed very little to the expansion of non-agricultural employment and shifts in the occupational structure. The large part of the workforce remained rural and employed in agriculture. On the foreign trade front, India ceased to be a mainly primary product exporter but did not succeed in becoming a significant exporter of manufactured products. Whatever limited exports happened were also dominated by low-tech labour-intensive products. Import-substituting industrialization did not also generate sufficiently strong incentives for Indian industry to invest in development of its own technological capacity.

Instead, the diffusion of technology from abroad formed the basis for the appearance of new products, industries and processes. The growth and diversification that India's industrial structure experienced was part of a larger story of the diffusion of industrialization to the Third World in the second half of the twentieth century. This diffusion brought the industrial structures of Third World economies

closer to that of advanced countries, though the latter continued to account for a disproportionate share of manufacturing value added. However, in comparison to some of her other Third World counterparts in Asia, India’s long-term trend of industrial growth as well as its transformative impact were more limited. Industrial development nevertheless did enable a significant development of Indian big business whose significance was to be fully revealed only after liberalization.

The private corporate share in the economy’s output remained relatively stable at around or below 15 per cent till the end of the 1980s after some initial increase in the 1950s. Capital accumulation in the corporate sector was largely ‘externally’ financed and there was a trend to shift from equity to debt and from individual to institutional financing. However, the private corporate sector’s expansion was not based on a net transfer from outside the sector as the outflows from it in the form of taxes, dividends and interest remained in excess of external funds raised. The relative stability of the private corporate share in output reflected the combined effect of two factors – the limited extent of industrialization and the redistribution of economic activity between the private corporate, public and unorganized sectors. A feature of the post-independence development was the tendency for the narrowing down of private corporate activity to the manufacturing sector, as sectors like mining, electricity, transport, communication, and the large financial sector became virtually the exclusive preserve of thepublic sector.

Even in manufacturing activities, the public sector share increased, though private corporate capital remained the dominant component in the organized manufacturing sector. However, there was a massive redistribution of the weaving segment of the textile industry from the organized mills to the unorganized power loom sector. As the corporate sector became more concentrated in a diversifying manufacturing sector even as it ceded space in what was the largest manufacturing industry at independence, the industrial spread of private corporate capital changed considerably. Associated with this were a number of other important changes. At independence, large private corporate capital was heavily concentrated in industries like the cotton and jute textile industries, mining, tea manufacture, etc. By the end of the 1980sprivate corporate

capital in these was limited or absent. Instead big businesses were often built around presence in one or more of a range of other industries that had grown over different time periods such as steel and steel products, chemicals, cement, automobiles and automobile products, industrial and other machinery and consumer electronics. These industries were also technologically more 'modern' industries. In the process of being agents of their development, private capitalist firms learnt how to to find, source, handle and adapt for profitable use technologies available internationally and gained this ability and production experience across a whole range of industries. They, however, moved away from producing for a mass market to focusing on narrower market based on higher average incomes. The change in the industrial spread also meant a retreat of private corporate capital from large direct employment and the management of large workforces. The newer industries into which corporate capital had spread by the end of the 1980s were also inherently more oligopolistic in nature than the textile industries had been. The acquiring of industrial features by the capitalist class through the process of import-substituting industrialization should of course be seen alongside its limits.

The leaders of capitalist industry achieved or sustained their status not on the basis of an ability to be technologically innovative but by their successful manoeuvring of the regime of controls and securing technology from abroad. These abilities had a generic character and fostered a tendency towards business groups expanding wherever opportunity presented itself – thus inhibiting both a widening of the class as well as the development of abilities associated with specialization. This ability to be mobile across industries, however, enabled many of the older constituents of the Indian capitalist class to survive the transition associated with industrial development. At the same time, the growth of new constituents on a similar basis meant that changes in the composition that did happen produced very little independent effect on the process of Indian capitalists shedding some of the features they acquired due to the peculiar circumstances of their origin. Notwithstanding the above, import-substituting industrialization did contribute to Indian capitalists gaining strengths they did not have at

independence, enhancing their general ability to confront international competition. At the same time it had increased the scale and frequency at which technological advances needed to be introduced, which increased technological dependence. Catching up with the structure of industries at the international level had reduced the scope for industrial expansion through a successive diffusion of industries.

Continued expansion had to be based primarily on existing industries rather than on new ones, and that too under conditions of a narrow domestic market. Such an expansion had to follow the international pattern or constitute a niche within it. Either way, the technological requirements were different from those of the past. Expansion on the basis of existing industries meant that all firms required recurrent technological advances in all industries. The strengths and weaknesses of Indian capital thus worked in tandem to move Indian capitalist opinion towards favouring a greater degree of integration with the world economy.

India's transition to liberalization and the opening up of the economy did not produce any overall growth depressing tendencies. Instead, the story of India's growth being faster than that of the rest of the world, which had emerged in the 1980s, continued and the first decade of the current century saw a further acceleration in growth. India's weight in the world economy measured in terms of its share in world GDP therefore has increased considerably. Anew trend that appeared after liberalization, however, was that of the growth of the corporate sector being more rapid than that of the rest of the economy, more so in periods of higher growth. This was accompanied by a persistent trend of redistribution of the income generated within that sector in favour of profits and other surplus incomes, which cornered the entire gain in the sector's increased share in national income. Despite the opening up, it has not been foreign capital but Indian capitalists who have been the principal beneficiaries of this unprecedented corporate expansion.

Moreover, Indian capital has also managed in this period to itself internationalize to an extent. Rapid aggregate growth and the success of Indian capitalist firms have thus provided the basis for the story of

India's 'emergence' under globalization. Industrialization has, however, not been at the heart of the post-liberalization capitalist accumulation regime in India. Industrial growth has tended to fluctuate with spells of high growth tending to be very short. The share of the industrial sector in GDP and that of manufacturing in particular have stagnated at the comparatively low levels achieved by themid-1990s. On the export front, while India's share in world exports has grown and there has been some diversification of manufactured exports, imports have grown much faster leading to a significant increase in the trade deficit.

Rather than manufacturing, it is services and construction activities that have contributed the bulk of the aggregate growth as well as that of the corporate sector. It is also in services that India has achieved its greatest export success and this has combined with large remittance inflows to compensate somewhat for the ballooning trade deficit. For Indian capitalists, therefore, profitable opportunities for expansion in services and construction have provided the principal base for expanding their share in the economy's production. These have thus displaced manufacturing as the principal sphere of private corporate activity, reversing the earlier trend. This expansion pattern has, however, been at odds with the investment behaviour of the private corporate sector in which manufacturing still plays a key role. In two bursts, one in the first half of the 1990s and the second in the high growth phase before the global crisis, significant corporate investment took place in manufacturing and these were also periods of rapid growth of aggregate corporate investment and of manufacturing output. Both these bursts ended with collapses of corporate investment.

The services and construction dominated growth pattern and the instability of industrial output and investment are inherent features of the accumulation regime under liberalization which has been based on creating a generalized wage and income depressing tendency. On the one side is the rapidly growing private corporate sector which employs only a tiny fraction of the labour-force and where employment has not grown rapidly either. The largest sector of employment, agriculture, on the other hand has suffered a deep-rooted crisis under liberalization and contributed less than 9 per cent of India's GDP growth in the last two

decades. As agriculture is unable to absorb any more of the labour force and the corporate sector having such a narrow bas of employment, non-agricultural informal employment has swelled considerably. Moreover, this has happened in a situation where the agrarian situation has held down the reservation wage in non-agricultural activities so that most employment –in agriculture, in the non-agricultural informal sector, and even in the organized sector, pays very little. Thus, even in the organized factory sector real wages have been flat or creeping downwards for two decades during which Indian per capita income has nearly tripled. Despite high aggregate growth, therefore, a large segment of the population remains caught in a low-income or low-wage situation.

The holding down of wages, along with growth that is more productivity rather than employment driven, has contributed to moving private corporate sector distribution of income in favour of surplus incomes, even after accounting for the existence of a small segment of high-salaried white-collar employment within the sector. Partly this gain has tended to be retained by companies and has underlain the rapid rise in corporate savings seen in the last two decades. Even when distributed, however, its beneficiaries are inherently few in number. The income distribution pattern of Indian growth, the parallel iniquities in access to credit, and the fiscal restrictions imposed on the state by liberalization have meant that it is the consumption and asset demand emanating from a small high-income group and from the private corporate sector which has shaped the overall pattern of movement of Indian demand. One implication of this has been that the increasing share of expenditure on services rather than on manufactured goods has characterized private consumption expenditure. While the large majority with low incomes has been kept out of the market for non-agricultural products, the increasing incomes at the top have produced a greater diversification of their demand.

Relative to industry and manufacturing, however, these services have limited capacity to absorb investment. Corporate investment, therefore, tends to still go largely into manufacturing. This has made industrial

demand more dependent on corporate investment in manufacturing and expenditure on real estate by high-income groups. Corporate manufacturing investment then faces the perpetual risk of creating capacity in excess of demand and has therefore shown great volatility and simultaneously generated instability in industrial growth. Aggravating this problem is the fact that the pattern of demand being generated makes it more biased towards relatively more import- and capital- intensive or high productivity production. The former combines with limited exports to aggravate the market constraint as well as balance of payments difficulties while the latter keeps employment growth down. Moreover, if productive investments like in manufacturing face a barrier it generates a tendency for asset demand to shift towards more unproductive and import-intensive forms like gold. The success of Indian capitalist firms in the liberalization era has not been achieved by eliminating the old weakness in the technological sphere, but despite it. Consequently, their tendency has been to expand in directions where limited ability to develop technology does not constitute a serious barrier.

This has reinforced the growth pattern because relative to many manufacturing activities in a number of services and construction activities the role of self-development of technology as a source of competitive strength tends to be limited. Increased technological sophistication in these has been facilitated by technical equipment suppliers and software service providers. This has combined with the process of privatization of many such sectors to create the tendency after liberalization for big business groups to move into an array of non-manufacturing activities like mining, power, construction (real estate and infrastructure), financial services, trade, information technology and telecom, etc. In the process, even as the technological sophistication of the production process has increased, Indian capital has in more senses than one experienced a process of losing its already limited industrial character.

Modern factory industry and a corresponding industrial capitalist class have had a consistent history in India of over one and a half centuries. Yet capitalist development in India has failed through its different phases

to produce anything more than what at best can be described as stunted industrialization and limited the industrial nature of the capitalist class. In the current phase of Indian capitalist development, the relationship between capitalist accumulation and industrialization has not only become weaker but this weakening has also become more entrenched over time. As the capitalist class has managed to grow as never before through an expansion in non-manufacturing activities, its stake in an industrialization process has tended to get eroded. At the same time that very expansion has reinforced the capitalist demand for maintenance and strengthening of the neoliberal economic policy regime that enabled it.

The economic policy regime in turn has increased the pressure exerted by this capitalist demand because of its effect of increasing the leverage of capital over the state which has reinforced the ruling class status of capitalists. Capitalist priorities press down harder on a state constrained to rely on private capital to drive the growth process and to generate revenues. Of course the current accumulation regime is not without its contradictions and has faced serious difficulties from time to time. At the current juncture in fact it faces a serious crisis that is its direct outgrowth - the combination of a large current account deficit, high rates of inflation particularly of food, and slackening growth and investment. Such a crisis alone, however, does not produce any tendency for change in course. Indeed, if anything it generates the opposite – as exemplified by the series of 'reform' measures announced in recent times. Its only, therefore, a change in the correlation of class forces that can compel any change. The basis for such a change may be created by the current accumulation regime and its crisis though of course it will never be their automatic problem.

Bombay and Calcutta, two metropolitan port cities, experienced very different patterns of industrial investment in colonial India. One was the hub of Indian mercantile activity and the other the seat of British business. The industries that relied on the export market attracted investment from British business groups in the city of Calcutta. Bombay, on the other hand, became the centre of the import substituting textile industry. Indian cotton traders from different communities moved from trade to production of cotton textiles. Few British entrepreneurs were

present. British industrial interests exercised monopoly control over various industrial activities in Calcutta and the hinterland. British firms were set up in tea, jute and coal and here the presence of Indians was minimal.

Although geographical factors determined the location of these industries, who invested and why remain questions of interest. Cotton was grown in the hinterland was Bombay and tea and jute in the hinterland of Calcutta. History could matter too. Indian merchants in Bombay had a more dominant presence in Bombay. These merchants had a strong presence in internal as well in the Indian Ocean trade. In the cotton textiles industry around Bombay, most of the investment was by Indians, who had links with the trade in raw cotton. The trade in raw jute around Calcutta was also in the hands of Indian traders, but they were not involved in the investment in jute manufacturing until the First World War. Investment in tea, jute and coal in and around Calcutta came from the British. A puzzle is why did British entrepreneurs not take advantage of these profitable opportunities open to Indian merchants. Why did British and Indian investment stay separated? Why did British capital flow into some sectors and not to others?

The literature on early industrial development in India has emphasized the role British investment and entrepreneurship. Some scholars see it as a crucial factor in the development of an economy scarce in capital, technology and entrepreneurial skills. Max Weber claimed that the negative effect of Hinduism on entrepreneurial spirit was a reason for India's economic backwardness. Morris criticized Weber, arguing that Indians did become industrial entrepreneurs when conditions were attractive. Others have emphasized the negative impact British rule in circumscribing the sphere of operation for domestic capital. This literature emphasizes the discrimination faced by Indian business and the favor received by British entrepreneurs from the colonial state. These favours included subsidized land transfers to tea planters and legislations in support of contracts with indentured workers in these plantations. While this may explain the absence of Indian business interests in Calcutta, it does not explain their dominant presence in Bombay.

More importantly in does not explain the small presence of British capital in the cotton textile industry.

The role of social networks in long distance trade in history is well researched. Less is known about its role in investment. This paper explores the role of social networks in decisions to invest in industry. Investors faced significant risks and problems of moral hazard and asymmetric information. Consequently, investment flows were influenced by the extent of knowledge that investors had of particular markets.

The information was transmitted through community networks creating separate spheres of investment. I argue that access to information about markets differed across social groups and gave an advantage to specific groups in specific markets. Conditional on the initial advantage, information flows within a network further accentuated the segregation of economic activity by social group and showed up in the different investment patterns in the cities of Calcutta and Bombay.

Informational Constraints and Capital Flows: A Simple Model of Informational Advantage

The recent literature on international capital flows provides a backdrop to my analysis of the Indian economy in colonial times. . Only a quarter of British capital went to the Empire of which only 30 percent went to the colonies under British rule with India receiving two thirds. Lucas, in his well-known paper, argued that British capital flows to India were low even during the colonial period when the threat of expropriation was low and returns were high. The low volumes of capital flows could be explained if the imperial power had exploited its monopoly position and restricted capital flows to keep returns on capital high.

This does not seem to have been the case in British India. On the contrary, large inflows of capital into the railways were encouraged by guaranteeing favorable rates of return. Bovenberg and Gordon set out a model of asymmetric information to explain why capital flows do not equalize returns across countries. They consider a situation where domestic investors are better informed about the quality of the investment project than foreign investors. Foreigners fear being

overcharged and hesitate to buy equity. Thus asymmetric information between foreign and domestic investors prevents capital from flowing to high return economies. Empirical evidence from recent cross-country equity flows support the view that information asymmetries reduce the involvement of foreign investors.

Portes et al. estimate a gravity model for capital flows and find the distance and speed of information flows, measured by telephone connections, have significant effects. The results suggest that local producers have better information about local markets and foreign firms are not willing to undertake long distance investment even when political risks are minimal. These informational barriers may be reinforced by the absence of institutions that are effective in enforcing commercial contracts.

In my framework, informational asymmetries are defined by social groups. Information flows were easier within social groups and restricted across groups. Therefore if one member of a social group invested in a particular industry, others could be persuaded to invest in it too. Members of a community made similar decisions to diversify from trade to industry in response to changing economic conditions of the 19th century. The shift from cotton trade to production of cotton textiles is a case in point. Community members also made similar decisions to migrate. There are many examples of this. Bhatia and Parsi merchants moved as groups from Surat to Bombay as the city began to grow in the 18th century. Marwari traders moved as a group from North –Western India towards the East in search of new business opportunities.

We can think of two channels of information flow through social networks. The informational constraints faced by investors were different from those faced by entrepreneurs. Potential entrepreneurs had information about investment opportunities. Potential investors were guided by the risk associated with buying shares in a foreign company. Familiarity with products could overcome this type informational constraint.

Reputational value of the entrepreneur could also be an advantage. Entrepreneurs decided which is a profitable enterprise and the investors chose whether to invest in the enterprise.

Investors' choice depended on who the entrepreneurs were and the type of industry.

An example of the first is that British savers invested in companies started by British entrepreneurs. An example for the second type of information is tea, where the product was present in the consumption basket of the average British consumer giving them an incentive to invest in this industry. I will return to this point in the next section.

For now, I focus on the informational constraints facing entrepreneurs. Potential entrepreneurs have different quality of information about investment opportunities. This information is shared with members of the community so that it influences their decisions to enter a particular industry. I put forward a simple model to illustrate the way in which informational flows within a community give rise to a herding effect so that different communities specialize in different industries.

Consider two sectors and two communities. First, any initial entrant is a pioneer, who observes only imperfectly which niche is profitable. The pioneer has the option to enter either industry and select a niche. However, in compensation, such an entrant earns monopoly profits initially. Second, entrants from the same community become informed about the profitability of a niche once successful entry takes place. By entering the same industry, they face reduced risk, and this offsets the congestion arising from additional entry. On the other hand, entrants from a different community suffer from competition and the congestion and have no informational benefits. This produces a tendency towards segregation, with different communities specializing in distinct industries.

This model is ex ante symmetric so that each social group is equally likely to enter either industry. In reality, the British had better information about the export markets in tea and jute, while the Indians had better knowledge of the domestic market in cotton textiles.

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This implies that the quality of signal, that is the value of p in the model would depend on the identity of the entrant. It is larger for the British in the export industries and larger for the Indian in the import substituting industries. Therefore ex ante the British were more likely to be the pioneer in the export industry and Indians in cotton textiles. The model implies that the herding effect would lead to persistence even if profitability was different in the two industries. To the extent the quality of the signal depended on prior knowledge of markets, there may be examples which run contrary to the simple model outlined, such as the presence of a few British firms in cotton textiles. Note that these entrepreneurs were also involved in the domestic cotton trade and therefore would have a higher p than a British firm not involved in cotton trade.

The model also assumes that the profitability of the industries is stationary over time and varies only with the number of entrants. This is a simplification and the model can be extended to allow for the profit opportunities to change over time across industries. It can be modelled by assuming that Gi (m) is determined by a Markov process, where at any date, profits could increase or decrease stochastically so that it may become unprofitable for a new follower to invest in the industry chosen by a member of his social group even if perfectly informed. He may prefer to invest in the other industry even if he is less informed. Similarly rising profitability of an industry may induce members of the other community to enter even in the absence of full information. High dividends could encourage “outsiders” to buy shares even if they were not socially connected to the entrepreneur.

The size of the group of “outsiders” can increase though information flow within the social network, Once the share ownership reaches a critical minimum, it can encourage entry into the industry. The jute industry is a case in point. Jute traders belonging to the Marwari community began to acquire shares in the British firms during the First World War and entered as entrepreneurs in the 1920s. The Marwaris did not take over British firms, but set up new firms. With this framework in mind, I turn to the dynamics of industrial investment in colonial India.

Capital and Entrepreneurship: The Industrial Divide The port cities of Bombay and Calcutta also became the railway hub in the course of the 19th century, when not only raw materials, but industrial goods began to be exported out of these cities. However, there had been a difference in the interaction between British business and Indian commercial interests in the two cities. Both had seen the rise of British agency houses as the trading monopoly of the East India Company ended. While some of them ventured into new activities such as coal mining or shipping, their primary involvement was in trade and the China trade in cotton and opium was an important component. The presence of Indian merchants in the East was small. Indian partnerships with British business in joint stock companies such as Carr, Tagore and Company were short lived.

In contrast in Western India, the Indian merchants had a long history in the trading world, including overseas trade based on social networks. Their role in the illicit opium trade to China out of the ports in the West shaped their economic importance in the region. With the decline of the opium trade and shipbuilding in the middle of the 19th century, the communities involved in these activities, such as the Parsis, began to look for alternative profitable opportunities. The Indian traders in the West were guaranteed brokers for the importers of cotton goods and distributed them in the local markets. But in the internal trade in jute cloth, Indian traders were not the principal brokers and had a relatively small presence until the First World War.

It could well be the case that Indian merchants had a special position in Bombay and were able to exploit opportunities of industrial investment, which they could not in Calcutta. However, it is the case that the industries that developed in the two regions targeted separate markets. In the East, tea and jute were export commodities mainly and the British had an informational advantage in these markets mattered, In the West, cotton textiles, was an import substituting activity and the knowledge of the local markets was important. Traders involved in the cotton trade and distribution of British imports of cotton textiles had an advantage here. The long standing economic role of Indian merchants in the West gave them this advantage.

From the mid-19th century, changes in company law led to the formation of limited liability joint stock companies. Companies were set up by British entrepreneurs who could raise capital from markets in Britain as well in India. Firms were floated on the London Stock Exchange as sterling companies or in India as rupee companies. The sterling companies raised capital in Britain and traded shares in the London stock market. Some sold block shares to British expatriates in India. The rupee companies raised capital from Indians as well as British expatriates, for whom this was ideal investment opportunity. The capital for the rupee companies came from British civil servants, army personnel and traders. These firms were run by managing agents or specialist management firms that owned shares, but were not required to have a majority shareholding. The managing agents managed companies across industries through long term agency contracts. They could be either British or Indian firms, the latter typically the Indian counterpart of the British agent.

In the context of India's industrial sector, firms are classified as British or India in relation to the managing agent. We can adopt a simple criterion to classify all sterling companies as British owned and managed. The picture is less clear for rupee companies.

Capital was raised in India and did not show up as direct inflow of foreign capital. However, the managing agents were the Indian counterpart of the British agency firms and acted as an indicator of ownership. This is a reasonable assumption as all decisions were undertaken by these agents and the new issue of shares also relied on their reputation and social connections. The reputational value of the managing agency houses in raising capital in the British and Indian markets was important. If a new firm was unknown to the British investor, the managing agent associated with it had a reputation.

The managing agency

system may be seen as an institutional innovation, which addressed the problem of informational constraints in long distance investment by providing a trustworthy name to the British investor. This system was universally adopted by British business in Asia.

Table1 shows the involvement of several leading managing agents in different industries.

British investors could invest in sterling or rupee companies. They could choose to invest in tea, cotton or jute or utilities such as railways. There were two types of British investors: those resident in Britain and those resident in India. The first group invested mainly in sterling companies in railways and public utilities and in tea, while the second invested in rupee companies in tea, jute and coal. Britain was the main market for tea, and consumers were familiar with the product. In India, it was still a consumption good largely unknown. Tea attracted large volumes of sterling investment in London. When the tea companies were floated in the 1860s and 1870s, it turned into a mania. On the other hand, jute was relatively unknown to the average British consumer and jute companies in Scotland might have might have been less risky. Only a handful of jute companies were registered in London. It was a product widely used in India for centuries and most of the capital was raised locally from British residents in India looking for profitable investment.

These Rupee companies in Calcutta were the ideal investment opportunity for the british residents in India.

In the tea industry, which was the largest sector, most companies were sterling companies, while in jute and coal, the typical firm was a rupee company managed by the Indian counterpart of the British agent. Indian investors could also buy shares in the Rupee companies. While systematic quantitative evidence is difficult to come by, case study based evidence from individual managing agency houses indicate that British investors accounted for bulk of the investment. For the agency house Bird and Company, nearly 90% of the investment in rupee companies in tea and jute came from British investors. The Indian Industrial Commission of 1918 reported by Indian shareholders held just over 15 per cent of the shares of jute companies.

The second largest industrial sector was cotton textiles. Here the Indian firms were dominant. Investors in this sector were their friend and family. The Parsis in Bombay had the financial resources to subscribe as paid up capital a large part of the authorized capital of a new company

and well as the reputation to attract interest from the public. When Davar, a Parsi, floated the first cotton mill in 1854, fifty leading traders of Bombay paid up the initial capital of Rupees 500,000. Majority of the shareholders, were Parsis, the same community as the entrepreneur, but there were others from other Indian caste groups as well as two Englishmen.

Davar retained a large chunk of the shares, Parsis and Gujaratis subscribed one-third. In other towns raising capital by Indians proved difficult except when backed by community support. When Ranchhodlal set up the first cotton mill in Ahmedabad in 1858, most of the shares were bought by his friends and family after he failed to raise capital from the local traders. Examples of raising capital through the network of friends and family can be found in the case of other textile entrepreneurs in Bombay, such as Tatas and the Bhatia merchants When Tata offered shares to a member of another trading community, a Marwari trader, it was met with skepticism. Members of the Bhatia community were the main shareholders in companies floated by Thackersey, Morarjee and Khatau, all Bhatia merchant. In Buckingham Mill, one of the few British cotton textile firms, Indian shareholders held only one-tenth of the shares.

The demand for coal came from the British owned railway companies and this sector was dominated by British firms. The majority of coal firms were set up and managed by British managing agents in India and the investors were British expatriates living in India. Jardine Matheson, the managing agent, argued that it was better to issue shares in India where there was local knowledge.

The export trade in jute and tea was in the hands of British companies and this gave British entrepreneurs an informational advantage. Jute was sold both in local and foreign markets. About 25% of jute output was sold in the domestic market. This market was well known to the Indian traders buying and selling raw jute and jute products, but the local traders were reluctant to become entrepreneurs. Demand for coal came from sectors that were dominated by British capital. Railways accounted for over 30% of total demand for coal. The cost of transporting coal from

Bengal to other region remained high in comparison to the price of imports and Indian industry used substantial amounts of imported coal. After 1900, the price of imported coal increased making Bengal coal competitive in the home market as well as in the nearby export markets. Indian owned firms that were in the industry were small and produced poorer quality coal that was sold in the local market.

It was the market for cotton textiles was relatively unknown to the average British investor. Cotton textile firms in Lancashire exported to the Indian market, where the distribution was in the hands of Indian traders. These traders had knowledge of local market in cotton textiles and became entrepreneurs when the opportunity arose. The trade in raw cotton had been in the hands of these local merchants in Western India. They made large profits in the cotton famine, ready to be invested. The cotton traders came from specific communities, such as the Parsis and Bhatias, who had a long history in intraregional as well as Indian Ocean trade. One of main British firms that entered this industry had also been involved in the cotton trade and the other was set up by a British technician working in the industry.

Check your progress –

1. Discuss the Parsee investment mode.

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2. Discuss the British investment mode.

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9.3 LETS SUM UP

Industrial investment in Colonial India was segregated by the export oriented industries, such as tea and jute that relied on British firms and the import substituting cotton textile industry that was dominated by

Indian firms. The literature emphasizes discrimination against Indian capital. Instead informational factors played an important role. British entrepreneurs knew the export markets and the Indian entrepreneurs were familiar with the local markets. The divergent flows of entrepreneurship can be explained by the comparative advantage enjoyed by social groups in information and the role of social networks in determining entry and creating separate spheres of industrial investment.

9.4 KEYWORDS

Parsee, Marwari, British Raj

9.5 QUESTIONS FOR REVIEW

1. explain the native capital investment.

2. How Europeans invested in India?

9.6 SUGGESTED READINGS

The Cambridge Economic History of India, Vol 2 by Meghnad Desai

Economic History of India by Tathagata Roy

9.7 ANSWER TO CHECK YOUR PROGRESS

1. Hint – 9.2

2. Hint – 9.2

UNIT 10 – MODERN INDIAN INDUSTRIES BEFORE 1914

STRUCTURE

10.0 Objective

10.1 Introduction

10.2 Indian Industries Before 1914

10.3 Lets Sum Up

10.4 Keywords

10.5 Questions For Review

10.6 Suggested Readings

10.7 Answer to check your progress

10.0 OBJECTIVE

To learn about the modern Indian industries in pre 1914 era.

To learn about their impact in Indian economy

10.1 INTRODUCTION

A history of modern Indian large scale private industry between 1850 and 1914 is associated with the developments in mainly plantations like jute, cotton, and steel. Beginning of these modern Indian industries was the 'product of India's economic contact with Britain'.

10.2 INDIAN INDUSTRIES BEFORE 1914

Underdeveloped countries are greatly handicapped by shortage of capital for industry and enterprise.

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Finance is the prime maker of growth. Anyway, capital for industry and entrepreneurial zeal were severely and conspicuously scarce in India when the East India Company (1600-1874) stepped into this country.

It was very difficult to raise capital on private initiative in the days of the Company rule and, thereafter, because of damped forces of demand and supply capital remained shy.

Naturally, under the circumstance, the state is supposed to act as a godfather for promoting and financing industries. Since India was under the British rule for almost 200 years (1757-1947), the British Government, found it unprofitable and unnecessary to go for industrialization in India. However, imperialist capital came in this country as a matter of colonial policy—the policy of subordination of Indian to British capital. It was only after the First World War (1914-1918), that state patronage for industrial development was visible as Britain's supremacy all over the globe came under serious threat.

Against this backdrop, a "new" pattern was evolved to overcome the obstacles of (i) shortage of entrepreneurship; (ii) non-availability of, mainly, venture capital; and (iii) dearth of managerial skill and knowhow.

This new pattern of industrial organisation that evolved came to be known as the Managing Agency System (MAS)—a peculiar business entity in the early years of the nineteenth century. Before we embark upon this form of industrial organisation, we will make a brief review of the industrial development during the British rule.

Early Efforts of Industrialisation:

Modern industry or the large-scale industry is a mid-19th century pheno-menon. Before the British conquest, India's supremacy in the industrial field reached its high watermark—India was called 'the industrial workshop of the world' during the 17th and 18th centuries. Demand for Indian cotton goods in England during this time was unprecedented. Indian cotton cloth was considered by Englishmen as the badge of 'style and fashion' of the time.

Woollen and silk items were also in huge demand. All this development brought untold miseries in England and other parts of Europe. Firstly, import of Indian goods destroyed the prospect of woollen and silk industries. Secondly, unemployment and suffering among the weavers mounted up. Thirdly, change in the composition of India's trade led to the export of treasure from England to India.

To counteract these unhappy developments, some measures were taken to pacify the British nationals, but with little relief. Ultimately, the way out was found through legislations. Acts were passed, first in 1700, then again in 1720, to prohibit or restrict import trade of Indian cotton good, silks, calicos, etc., by total prohibition or by imposing heavy duties. As these measures did not yield desired result, one British author commented in 1728: "two things amongst us are ungovernable: our passions and our fashions".

What was the net effect of this state of industrial development? What was 'industrialisation' to India by the standards of time was 'de-industrialisation' to Britain. India, however, had not been fortunate enough as soon as the 'ugliest' thing came on us in 1757—the loss of freedom through British conquest of India.

Growth of Indian Industries till World War I:

India had never been an industrial country in the modern sense of the term. In this sense, even England and other industrialised countries of today had not been so, until recently. What strikes most about India was that even being pre-dominantly an agrarian country large varieties of industries existed in India and some of them competed quite successfully with many other countries.

But her industrial supremacy started crumbling when the English cotton industry raised its head rapidly by the mid-18th century.

Two important developments of this were:

(i) The beginning of the era of industrial revolution in England around 1750 and

(ii) The battle of Plassey in 1757 that established the Company (foreign) rule.

As soon as the battle was won, the foreign ruler started abusing both economic and political power in an un-sympathetic and hostile way. Under pressure from the powerful rising English manufacturing interests, EIC dealt a severe blow to Indian industries that led to final extinction—the phase of India's 'deindustrialization'. Now the cycle turned inside out. It employed the arm of political injustice on Indian products (one-way free trade) to strangulate a competitor with whom she could not contend 'on equal terms'.

The last nail in the coffin was hammered in 1813 when the trading monopoly of the EIC was withdrawn. It was the political domination and the commercial policy of Britain that threw open India to all. India now suddenly was reduced to an importing country from an exporting nation. Indian market now became flooded with machine-produced goods at a lower price and also witnessed the loss of export markets. Further tragedy was in store.

Being a colonial country, she had to pay a large sum for England's industrialization scheme. India was forced to supply raw materials for triggering industrial revolution with greater rapidity in England. India was then forcibly transformed from being a country of combined agricultures and manufactures into an agricultural colony of British manufac-turing capitalism.

A history of modern Indian large scale private industry between 1850 and 1914 is associated with the developments in mainly plantations like jute, cotton, and steel. Beginning of these modern Indian industries was the 'product of India's economic contact with Britain'.

There was also a limited development of mining, especially coal. One thing that is worth noting is that most of these industries, except textile factories, were under European control.

In the early days of the Company rule, Indian raw jute had been in great demand for the Dundee mills. World conditions after 1850 were quite propitious for the growth of jute manufacturing and the credit for jute

spinning firm in Rishra, near Serampore, Bengal, went to George Acland—a Scottish. The founda-tions of cotton textile industry were laid also during the early 1850s. Though the jute industry was dominated by the foreigners the cotton industry was shaped and cared by the natives, mainly the Parsee entrepreneurs.

Some abortive attempts were made by the East India Company in the 19th century to develop iron and steel industry. However, the credit for the development of large scale manufacture of steel in India goes to Jamshedji Tata and his son Dorabji. Tata Iron and Steel Company were set up in 1907 and it started function of producing pig iron in 1911 and steel ingots in 1912.

The progress or the achievements of modern large scale industries can be visualised by considering the output produced and the employment data. Between 1880 and 1914 large scale industrial output grew at the rate of 4-5 p.c. p.a. —a rate of growth that is comparable to other contemporary countries of the world. But in the light of total economic activity in India, output produced was rather insignificant. This is also true about the employment situation; it came to less than eight-tenths of 1 p.c. of the total labour force in 1913-14.

Meanwhile India's industrial structure started diversifying. In spite of inadequacy of domestic demand and high production costs, industries like woollen mills, breweries, and paper making industries made significant march during this time. Though these industries were recorded officially as the large industries, they were small in character.

Other industries having small-scale character that operated were tanning, vegetable oil processing, glass-making, leather goods manufacturing, etc. Despite diversification, India's modern manufacturing industry could not develop on a sound footing before the outbreak of the World War I.

The three important reasons behind such industrial development were:

(i) Young in experienced entrepreneurs,

(ii) Absence of State aid towards industrialisation,

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(iii) Steep uninhibited competition with developed foreign machine manufactures.

R. C. Majumder then adds: “The pattern of industrial development which had emerged in the 19th century—confined to a limited sector and concentrated in a few unevenly distributed areas—remained virtually unchanged till the beginning of World War I, though within these narrow limits the years 1905-14 witnessed a relatively rapid growth”.

Industries in the Inter-War Period (1919-38):

No country under colonial dependence could undertake any industrial transformation, if not all-round development. Up to the First World War, India experienced the classic period of imperialism of free trade and the British Government’s unsympathetic, hostile policy against industry.

In addition, shortage of capital, management experience and technical expertise, as well as the absence of a growing indigenous market, and, above all, general poverty, caused slow expansion of Indian industries. Even then, one can safely conclude that during 1850-1914, the foundations of modern industries were laid in India.

Meanwhile, the outbreak of the First World War exposed the weakness of Britain’s strategic position in the East as India had been deprived to develop the most elementary basis of modern industry. In order to impress upon the Indian people and the (industrial) bourgeoisie, Britain granted some political and economic concessions, particularly future industrialisation during the War and immediately after the War.

As the issue of tariff protection crept into the heads of Indians, the British Government appointed the Industrial Commission in 1916 and assured that industrialisation efforts would henceforth continue with utmost sincerity. Unfortunately, industrialisation scheme as prepared by the Industrial Commission ultimately came to nothing.

However, during the war-period, industries like cotton and jute made much headway. Steel industry also experienced substantial growth. Consumer goods industries like chemicals, cement, fertilisers, mineral acids, etc., for which India depended on foreign countries, also progressed during the War.

However, such prosperity of Indian industries was not a long-lasting one. Above all, promises made by the foreign ruler remained, however, unaddressed—as usual. On the contrary, faced by the intense foreign competition, Indian industries in the mid- 19205 demanded protection in an unwavering manner. To this end, the Fiscal Commission was appointed in 1921 that ushered in a policy of discriminating protection.

This was indeed a belated response to repeated demand made by the Indians from at least since the 1880s. The policy definitely helped some industries to develop. But the end result was rather a haphazard development of certain industries and not general economic development as such. In 1936, 'The Economist' observed India's industrialisation effort: "Although India has begun to modernise her industries, it can hardly be said that she is as yet being industrialised".

On the whole, during the inter-war period, output of cotton piece goods, steel ingots, paper, etc., increased substantially. Many other industries also progressed even in terms of employment and the number of factories. But as far as diversification was concerned, it was indeed slow and the state of transformation of the economy was only 'marginal'.

Industries during 1939-47:

The Second World War, however, opened a new phase in India's industrial history. As the character of the World War II was different from that of the First, the latter created a far more urgent and intense demand for the rapid growth of India's basic and key industries. Against the backdrop of this favoured ambience of industrial development and the near-cessation of imports due to war operations, Indian industries somehow came to take pleasure in having a quasi- monopoly situation in the home market.

As a result, not only industrial output of large scale industries expanded significantly, but also a more widening of the industrial diversification became possible during the war-time years. During 1938-39 and 1945-46, the general index of output of all large scale manufacturing activity (at 1938-39 prices) rose from 100 to 161.6 and that of factory employment increased from 100 to 159.

Despite this headway, India's manufacturing before independence displayed many frailties. Firstly, India did not possess capital goods industries worth the name. This, therefore, hampered her potentiality to reproduce its existing productive capacity. Secondly, import dependence of the Indian manufacturing sector was enormous.

Thirdly, possession of technical skill and institutes offering technical education were virtually negligible. Industrial development is largely conditioned by the stock of 'human capital'—the stock of scientific and technical cadre. India was still a country denied to grow by the apathetic foreign government.

However, the prospect for industrial development in India after indepen-dence must not be undermined as she had already constructed enough possibilities for industrial development.

Reasons for Low Industrial Development in India:

In this connection, it is better to point out some reasons behind the low level of industrial development in India.

It was the result of:

(i) Inadequate capital accumulation;

(ii) Mobilisation of unproductive investment; (Keynes castigated inordinate love for liquidity of Indians. Male people were desirous of seeing jewellery in the neck of their female counterparts);

(iii) Undue preference for quick-return yielding commerce and trading activities of the Indian capitalist classes; and

(iv) Concentration of entrepreneurship in the hands of a few small sections of Indians.

In addition, shortage of capital goods and absence of skilled personnel also acted as drag on India's industrial development.

Though these acted as strong depressants, colonial status seemed to be the most strong stumbling block for India's drive for industrialisation. Above all, the contribution of the British Government towards India's industrialisation was minimal before 1916, that is, before the

establishment of the Industrial Commission. The industrial policy of the imperial power could be described as 'a case of too little and too late'.

These questions have long guided the study of the economic history of India. The imperialist, or "orientalist," belief was that the empire heralded modernity in India.

For example,

Karl Marx shared that belief with many of his contemporaries, although he also observed that modernity came with a cost. In contrast, twentieth-century writers on imperialism and development believed in an enduring link between colonialism and underdevelopment.

The view that impediments to development were inherited from the damages of colonial rule, and not home grown, became a key premise of Indian nationalist thought articulated by, among others, Jawaharlal Nehru himself. In 1947, this diagnosis of Indian poverty held that it was a product of "laissez-faire," exploitation by foreign capital and the noninterventionist stance of the Indian government under the British raj.

In turn, these ideas supported the two key planks of India's development strategy: strong sentiment against foreign trade and investment and statism. Indian big business at 1947, the principal backers of the Indian National Congress, eagerly embraced the former and, somewhat uneasily, the latter.

These policy stances now have few takers in the nations of south Asia. Since 1990, if not earlier, the worldview that habitually warns against globalization has been in decline. Faith in statism has diminished, too. The study of India's economic history has been affected by this shift. Scholarship continues along the imperialism-underdevelopment axis, albeit on a smaller scale than in earlier years. But this stance looks increasingly dated and disoriented, especially at a time when economic liberalization in India is drawing upon the tenets of classical political economy on which British policy in India was founded. Another reaction is simply to sidestep India's economic history and to focus instead on recent decades. Indeed, the study of the economy history of India is at risk of losing wider relevance, audience and funding. In fact, market-

oriented British imperial policies did initiate a process of economic growth based on the production of goods intensive in labor and natural resources. However, productive capacity per worker was constrained by low rates of private and public investment in infrastructure, excessively low rates of schooling, social inequalities based on caste and gender and a delayed demographic transition to lower birth- rates and the resultant heavy demographic burden placed on physical capital and natural resources.

The end of colonialism did not see a dramatic break in these conditions.

Economic policy between 1950 and 1990 attempted much harder than had the British to raise the quality of labor and rates of investment, but India's economic growth continued to focus on semiskilled labor. On the other hand, whereas British policy believed in exploitation of comparative advantage in trade, independent India turned firmly away from participation in the world economy, precisely at a time that the world economy experienced a boom. When economic reforms in the 1990s reintegrated India in the world economy, the major beneficiaries were manufactures that were intensive in semiskilled labor, in a late but welcome reversion to the colonial pattern of growth.

It was a century from 1757, when the English East India Company established its supremacy in Bengal, and 1858, when the Crown took over administration of India. British Crown rule over India lasted 90 years, from 1858 to 1947.

The period of British colonial rule was long enough to defy any simple summary. However, in discussing this period, it is useful to focus on three features.

Structural features include the overwhelming importance of natural resources and labor to economic growth, fluctuations and welfare. Agriculture and labor-intensive I The descriptive sections draw on Roy (2000), which contains a detailed list of readings on specific industry and services were the main livelihoods throughout this period and beyond.

Global features focus on the fact that India's economy was more open during this period compared with periods before and after colonialism.

India participated in a global revolution in transport and communication, which for India includes especially the Suez Canal, the railways and the telegraph. The third set of features can be called colonial features.

For example, India's status as a colony imposed certain peculiarities on its balance of payments, like large remittances paid by the government to Britain. However, the ratio of investment to government expenditure was apparently much higher in British India than in earlier Mughal India.

The structural features of India's economy changed slowly. For example, India's economy was primarily agrarian before, during and since colonialization.

However, the global and the colonial features shifted dramatically after 1947.

Industry in colonial India had strong global ties, whereas after 1947, the policy of "self-reliance" involved a deliberate and drastic reduction in the influence of global factors on the domestic economy.

Setting the Stage: The Century Before British Control

An orientalist cliché, with adherents as great as Karl Marx and Max Weber, held precolonial south Asia to be stagnant and backward in political-economic terms. A corollary of this cliché was that economic modernity in south Asia began with European involvement in the region. Later research has shown that cliché to be a myth. South Asia was already a major player in world commerce and possessed a well-developed trading and financial world when Europeans discovered it. How- ever, radical claims in world history scholarship, such as the one made recently by Frank (1998), that the center of early modern world economy was Asia rather than Europe, are not reliable. Such claims usually involve rather exaggerated assumptions about the share of regional commercial blocs in world trade and also about the size of the trading economy relative to the primarily subsistence-oriented economy within these regions.

By 1757, the English East India Company commanded political power in Bengal. The transition from trade to direct rule can be explained partly by the needs of trade itself. British mercantilists criticized Britain's

payment of bullion for Indian textiles, the most important item in this trade. Local political circumstances that enabled the British to command land revenues of Bengal came as a less controversial means of payment. The local circumstances included the support of the elite disaffected by the local rulers. When the company's monopoly in trade ended in the early nineteenth century, it was committed to building an empire. By 1857, the boundaries of colonial India, which were the basis on which nations were carved out in 1947, had been defined.

A more or less uniform administrative system came into place in this time span.

In the economic sphere, there were several major changes. Agrarian "settlements," which were contracts between the state and the cultivators on property rights and revenue commitments, were drawn. The British wanted to create a class of cultivators with secure property rights who would yield more revenue to them by pursuing profit-oriented cultivation. However, property rights often went to non cultivating

classes due to mistaken identity, imperfect information or political compulsions.

The legal recognition of a property right, conditional on payment of land revenue, went along with the erosion of many customary rights over usage of land or what it produced. These customary rights were poorly understood, oversimplified or irreconcilable with private property rights; for example, tenancy rights and rights to the use of common lands were victims of this confusion. Ultimately, these settlements transformed rural institutions and restructured classes. Also, one universal effect of introducing secure property rights was the extension of markets in land.

Another set of changes had their origin in foreign trade in an increasingly integrated world. Trade expanded quickly. Indian exports had been dominated by textile manufactures in the eighteenth century. The composition of exports changed toward no manufactured goods and that of import toward manufactures, notably British textiles.

The early nineteenth century saw the rise of new commodities in trade, such as indigo, opium and cotton. Profits of these trades sustained new commercial-cum-port towns, such as Calcutta, Bombay and Madras.

It is not easy to read in this period a general trend. We do not have the basic data to make an assessment of growth, stagnation or decline in the early nineteenth century. Nevertheless, there is a widely shared belief that the consolidation of British power in the economic sphere saw a violent and uncompensated economic disturbance. The fact of a decline, the period, the regions and the causes remain imprecise.

One thing we do know is that India's traditional cotton textile industry declined between 1820 and 1860. At first, an export market for Indian cloth disappeared. Later, hand spun cotton yarn and hand woven cloth suffered due to import of yarn and cloth from the mills in England. The decline seems dramatic if seen against India's earlier dominance in world textile trade. This single example of decay appears to have generated the "deindustrialization" thesis, which at its narrowest holds that early British rule introduced a violent shock to India's economy, and at its broadest holds that colonialism caused underdevelopment. Both the narrow and broad inferences, however, are deeply questionable for a number of reasons.

First, the industrial decline was apparently restricted to cotton textiles. Second, the decline of the textile industry did not continue through the rest of the nineteenth century and on into the twentieth century as British colonial rule strengthened, which calls into question whether the fundamental cause was the rise of colonial rule in the first place. Third, a decline in cotton textiles was not capable of causing economy-wide distress. The proportion of textile export in total textile production was very small, at its peak not more than 1 to 2 percent. Fourth, losses for the Indian textile producers were largely balanced by gains for the consumer, which were large. By 1850, prices of ordinary cloth were about 20 percent of what they were by 1800. Finally, many of the jobs lost due to competition with mechanized textiles consisted of poorly paid domestic workers with low opportunity costs.

A second and more plausible source of an economic regress in some areas was taxation, mainly because India's government of the time collected taxes more The main occupations were transport and communication, commerce, public administration, professions and liberal arts.

The Central Role of Agriculture in India's Economic History Agriculture has been the predominant sector for India's workers for the last two centuries, right up to the present.

By the start of the twenty-first century, after 50 years of statebacked struggle to industrialize, the share of the primary sector in GDP has fallen from over one-half at the time of independence to about one-quarter at present.

Nonetheless, the majority of workers continued to be engaged in the primary sector. Thus, conditions for agriculture have been a primary determinant of India's economic progress and the well-being of most of its people.

The typical weather pattern in most of India is nine months of dry weather and three months of monsoon season, which refers to the seasonal shift in wind direction between June and September that brings 90 percent of total rainfall in the region. Rainfall during the monsoon season is usually adequate to raise one or two food crops in the months following the monsoon. But rainfall is rarely adequate for winter crops and marginally adequate in some of the drier regions even for the main food crop.

High risk was a constant feature of economic life in most parts of India throughout history. If the monsoon rains failed even slightly, starvation was wide-spread and sudden. In the short run, famines affected all parts of the economy via violent shifts in consumption and labor force. For example, in Madras Presidency, the great famine of 1876—1877 took between 5 and 8 million lives, or about a quarter of the population of that region. In the long run, two observed tendencies seem attributable to endemic risks.

First, rates of private investment in India have generally been low. Instead, Indians who held assets displayed a marked preference for precious metals, which tended to be more stable in value, but generated smaller return than productive investment. Second, the high risk of famine mortality was possibly a reason why birth rates also tended to be high. Due in large part to high mortality from recurrent famines, India's population growth between 1800 and 1921 was low (0.4 to 0.5 percent) and subject to high fluctuations. But mortality rates began to fall in the early twentieth century as a result of fewer famines, better health care and possibly improvements in nutrition. However, high birth rates did not decline. As a result, between 1914 and 1946, India's rate of population growth climbed to 1.2 percent per year.

In this primarily agricultural society, cultivation patterns and livelihood risks depended on the distribution of rainfall. Mean annual rainfall in India ranges from more than 70 inches on the western coast and Bengal delta to 30 inches or below in large parts of the interior. Areas with high rainfall tended to grow rice; those with low rainfall focused on coarser grains or millets. Rice and rainfall were generally associated with high population densities and low ratios of land to labor—because the combination of rice and rainfall normally meant lighter impact of famines and greater requirement for farm labor.

The eastern coastal areas where British colonial rule first established itself had abundant water, fertile land, dense populations, well-developed foreign trade and relatively hierarchical societies. Land in these areas could sustain high rents and, thus, a prosperous rent-earning class, who were rarely peasants themselves. The interior regions conquered later were drier and more sparsely populated. Peasantry here was less hierarchical, kinship units powerful, and these units tended to control land collectively. Farming here coexisted with extensive raising of livestock. From a mix of ecological and political reasons, the government invested heavily in extending canal irrigation in the drier interior regions.

Between 1885 and 1938,

cultivable area increased by 60 million acres, of which over half was irrigated.

The latter half of the nineteenth century saw agrarian commercialization driven by translocal markets. Early in the nineteenth century, India's product markets were constrained by multiplicity of weights and measures, backward and risky transportation systems and extensive use of barter. But global technological advances and British administration weakened these constraints and enabled closer integration of markets. Agricultural prices consistently rose. Transactions costs fell.

Land sales, land prices and rents increased. Credit transactions expanded. Labor became more mobile and more market oriented, and millions went overseas. Profit 2 Coastal Madras, a rice region that saw canal construction on a large scale, was an exception.

The wage indices were estimated by Mukerji (1959, 1960, 1961). opportunities led to changes in resource use. For example, in what had been the drier millet zones, after irrigation, a basket of "cash crops" became common, like wheat, cotton, oilseeds, sugarcane and tobacco. The value of India's exports quintupled between 1870 and 1914. Agricultural goods accounted for 70 to 80 percent of the exports.

In the decades after 1900, the momentum for growth in agricultural output slowed The three conditions that had made agrarian expansion possible in the late nineteenth century all weakened in the interwar period. Cultivable "waste" lands became scarce, investment in water slowed and so did the world economy. One interpretation of this slowdown is that the resource-based, trade-driven growth had reached its limits. Some growth continued in cotton and wheat, but it was increasingly dependent on yield-per-acre rather than acreage, in other words, dependent upon seeds developed or adapted in government laboratories rather than on wider access to water. That said, the principal source of agricultural stagnation was a crop and a region that had participated in a rather limited way in the whole transition—specifically, rice in Bengal. Thus, historians have also looked for other hypotheses for the slowdown with Bengal in mind.

One theory focuses on class structure. In densely populated, rain-fed, rice-based areas like Bengal, the British had conferred property rights upon formerly rent-earning groups, perpetuating their power and

blocking the way for basic restructuring in rural society. In the drier millet-based regions where "land was plentiful and hands few" (Stokes, 1994), the state made revenue arrangements directly with the peasants, creating a positive incentive for private investment.

Another explanation, complementary rather than competing with the former, involves resource endowments. In the Bengal delta, income from rice had to be shared between too many people dependent on land. By early in the twentieth century, population growth in this region had led to the cultivation of inferior land.

The rice areas that did well commercially, such as coastal Madras, had lower population densities and received canal irrigation that made it possible to combine rice with dry season crops.

Whatever factors were behind the stagnation of agricultural output, they were long lasting. The regional patterns of agricultural growth and stagnation since independence have been similar to the regional pattern of growth and stagnation in the colonial period. Pockets of rural poverty today emerged as pockets of rural poverty in the latter half of colonial rule. Areas that experienced a "green revolution" in the 1970s and 1980s were already advancing during British rule. Land in India has been scarce in an absolute sense from about 1900. By and large, success in breaking the resource barrier after 1947 has depended on irrigation, seeds, chemical fertilizers and, to some extent, exploitation of forests and pastures.

Production And Wages

	Index of production			*Index of real of income in traditional industry*	*Index of real wages*		
	Food crops	*Non-food crops*	*Modern industry*		*Modern Industry*	*Non-agricultural, outside modern industry*	
						Skilled	*Unskilled*
1900–01 to 1904–05	100	100	100	100	100	100	100
1934–35 to 1939–40	103	146	293	127	185	160	151

How did the commercialization of agriculture under colonialism contribute to standards of living?

Between 1890 and 1950, no marked change in average real wages seems to have occurred. But real income per worker increased, which suggests that nonwage incomes must have risen. At one end, nonwage incomes represented the earnings of the "small peasant," who relied mainly on family labor, tilled land barely enough for subsistence and who usually had insecure property rights. At the other end were "rich peasants," who had secure property rights, controlled enough land to generate a surplus, employed laborers, had better access to credit or were creditors themselves. As a rule, rich peasants gained from commercialization—that is, returns to capital increased. The evidence on small peasants is mixed. In some cases, they did well; in other cases, they gained in the nineteenth century, but regressed in the twentieth. On a limited scale, the small peasant turned into a laborer. Instances of the peasant losing land have received exaggerated importance in academic debates on the impact of colonialism. In one extreme view, such instances symbolized a general rural decline and dislocation caused by colonialism (Patel, 1952). In a more sober view, stories of such reversal were neither very general nor attributable to colonialism. After all, in the long run, the Indian small peasant faced a steady fall in land-worker ratios due to population pressure.

Although there is no strong evidence to suggest the laborers became better off overall with the commercialization of agriculture, wages did rise in the major cash crop regions. Further, colonialism brought changes in the laborer's social position. In precolonial India, laborers came from castes whose primary duty was to perform labor. Many were akin to serfs, and some were actually salable. In the colonial period, this serfdom or slavery declined. The element of compulsion and force in employment weakened. Various forms of social oppression, such as enforced dress codes and codes of conduct with respect to upper castes, weakened, too. The possibility of migrating to the cities and to other British colonies made occupation.

Industry

India's workforce is not significantly more industrial today than a century ago. In 1901, 13.9 million industrial workers formed 10.5 percent of the

workforce, as shown in Table I. In 1991, 28.4 million workers made up 10.2 percent of the workforce. The share of industry in national income has grown from 11.1 percent in 1900—1910 to 16.4 percent in 1940—1946, to 27 percent in 2000. India's independence in 1947 did not represent any marked break in the pace of industrialization as measured by employment or share of national income.

In describing industrialization in colonial India, it is necessary to begin with a distinction between traditional and modern industry. Modern industry (or large-scale industry) involved use of machinery, regulation and factories subject to some form of modern managerial practices. By contrast, in "traditional" industrial firms, machinery, size, regulation and hierarchical management played no significant role. Both traditional and modern industry shared one feature: intensive use of labor and/or locally available raw materials. The main examples of large-scale industry were cotton and jute mills. Examples of traditional industry include handloom textiles, leather manufactures, metal utensils, pottery, food processing, woodwork and carpets and shawls. Large-scale industry employed 2—3 percent of India's industrial workers about 1900 and a little over 10 percent at 1947. Its share of the national income generated in manufacturing increased from less than 10 percent to 40 percent over this time.

Factory employment in the colonial period was overwhelmingly dominated by the textile industry: mills for cotton and jute spinning and weaving; cotton ginning firms and jute presses; and a few large firms in wool and silk spinning and weaving. The other mechanized industries were paper, sugar, matches, cement and steel. Technology and the capital goods were imported, but even significant Indian mills used a far higher proportion of labor to capital than the comparable factor proportions in the same industries in Britain. These modern factories were concentrated in two provinces, Bombay and Bengal. The attraction of these provinces, especially that of the cities of Bombay and Calcutta, derived from their position as major centers of transportation and large settlements of maritime traders.

Notes

Modern industry was essentially a product of India's contact with Britain. In cotton and jute mills, the idea of a mill, the technical knowledge, the equipment and capital intensity, a part of the capital and a section of the engineers at first came from Britain. The dependence on British precedence led to ways of organizing work that did not exist before. It gave rise to cities such as Calcutta or Bombay; shaped urban labor markets; encouraged the growth of railways, ports, laws, banks and technical schools; and was a force behind the modernization of services.

At the start of colonial rule in the 1850s, India's capital market institutions were inadequate to channelling household savings to industrial investment. The real cost of capital was astronomical. It is not surprising that the pioneers in modern industry came almost entirely from communities that had specialized in trading and banking activities—that is, those who could raise money more easily. By and large, fixed capital in modern industry came from its own sources of funds or from borrowings from within a small set of people known to each other.

Factory labor was a new form of work in India in the middle of the nineteenth century. Machinery, migration, urbanization and discipline were new ingredients in the workers' lives. Did these changes improve income and welfare? From the early 1900s to the late 1930s, real wages of mill workers did increase quite substantially in the cotton mills of western India and marginally in the jute mills of the . Most workers earned wages that were too little or too insecure to think of growing roots in the city and giving up connections with land and agricultural labor. However, the chances of occupational and income mobility were greater in the cities than in the villages. The city dwellers never suffered the threat of famine to the same degree as the rural population.

Historians have asked why modern industry remained limited in India. Two points of view exist on this question. Morris (1983) suggests that the scale of India's home market was small for goods that used machinery. Bagchi (1970) suggests that the home market was shared by Indian and imported manufactures and that the colonial government did not protect Indian industry sufficiently from low-cost imports. For

example, India never developed a capital goods sector and did not see the kind of boost to machinery production associated with railway construction in mid-nineteenth century United States. India's railroads, the largest railway system in Asia, imported nearly all its equipment until the interwar period. Behind this policy, there was an explicit encouragement from the government to "buy British" and possibly a disregard for experiments because the government guaranteed rates of return on private investment in the railways.

By focusing on the extent of demand for products of modern manufacturing, both arguments sidestep the issues of resource endowments and high cost of capital in India. Wider usage of machinery, whether for home or export markets, was not cost effective due to the high cost of capital and the scarcity (and cost) of skilled labor.

Machinery was used in those exceptional industries that processed raw materials abundantly available in India and for which the machines and technicians could be easily imported. If we look away from this segment, the general situation was exactly as resource endowments would imply, that is, a vast world of traditional manufacturing, consisting of tool-based industrial production performed in homes or small workshops.

Standard narratives of Indian industrialization have often neglected traditional industry from a mistaken belief that imports and modern industry killed it. Research on national income first challenged such a view, showing that income per worker increased quite significantly in this sector between 1900 and 1947, as shown in Table **Production And Wages**.

Part of India's textile industry did become obsolete, but this theme cannot be generalized. A different perspective that has taken shape more recently argues that the key dynamic in traditional industry was not that it became obsolescent, but rather that it was affected by commercialization in product and input markets (Roy, 1999).

Commercialization involved a number of shifts: increasing integration of the market for the products of traditional manufacturing; a shift away from production for own use or use as gifts and tributes to production for market; and a shift from local to longer-distance trade. As markets

Notes

integrated, competition within the crafts intensified. There was decline of older institutional forms and the rise of new ones that used labor more efficiently. In particular, there was a decline in two types of non specialized workers: women working in household industry and a group the early censuses called "general labor," which performed a variety of laboring tasks in the villages and some manufacturing on the side.

Leather manufacture gives an example of how commercialization affected traditional manufacturing. This was originally a rural craft performed mainly by rural serfs. In most places hides were bartered, but even where a market formally existed, servitude arose both from caste hierarchy and the interlocking of markets—the fact that the main customer of the leather artisan was also the peasant-employer. By the 1870s, an export market had arisen for leather, along with a need for different kinds of processing. These changes weakened the serfdom of leather makers and enabled the rise of migrations into the city, the merchant-owned urban factory and wage labor. The case of handloom weaving is more well studied.

Competition between traditional handloom manufacturing and the modern power loom manufacturing was acute, and the share of traditional manufacturing eroded steadily throughout the nineteenth century. However, hand— and power—weaving also served segmented markets, and those segments of hand-weaving that did not compete with modern textile manufacturing saw a pattern of expansion in demand, commercialization and urbanization, along with technological and organizational change. A range of traditional manufacturing industries intensive in craftsmanship—carpets, shawls, engraved metals or silks—were always urban and commercial. But the extent of urban concentration increased, and there was a qualitative change in clientele from powerful local patrons to exports. If Bombay and Calcutta with their large-scale factories represent one face of industrialization in India, numerous medium-sized towns, such as Agra, Benares, Moradabad, Sho-Iapur, Madurai or Jaipur, illustrate the strength of labor-intensive industry that arose from traditional roots.

Craftsmanship was a resource contributing to industrialization in India. In the largest industry, handlooms, wages did not rise for the ordinary weaver. But earnings of the skilled weaver probably increased, and rates of profit were high, possibly rising, in the two decades or so before the Great Depression. We again have a scenario where returns to semiskilled labor are uncertain, but returns to capital and craftsmanship increased.

This process illustrates industrialization based on utilizing labor more productively, rather than on replacing labor by machinery. In that respect, colonial India was not fundamentally dissimilar to early industrialization elsewhere in the presence of surplus labor, such as "protoindustrialization" in eighteenth-century Europe or industrialization in twentieth-century east Asia. Commercialization started the process. There was persistence, even strengthening, of traditional organization in the short run. But underneath that stability, a movement toward a labor market slowly began. In one respect, colonial India was different from these other cases. In Europe, modern industry had indirect roots in traditional industry. In India, the two developed side by side.

Global Mows of Trade and Capital

India was a more open economy in the colonial period relative both to the eighteenth century and to the first 40 years of its independence. Before the nineteenth century, foreign trade was a negligible activity for India's economy as a whole, though it was significant for certain regions. The ratio of trade to domestic product increased from I to 2 percent around 1800 to a little less than 10 percent in the 1860s to 20 percent by 1914. After 1947, the trade-GDP ratio in India steadily fell. It was 8 percent in 1970, but has more recently risen to 13 percent in 1985, 16 percent in 1990 and 20 percent by the mid-1990s.

International flows of income and capital were also relatively larger in the colonial period than before or after. Net income from abroad formed 1—2 percent of national income in India before World War I. Net income from abroad was well below I percent of national income between 1950 and the mid-1980s. Until the Great Depression, India typically ran merchandise trade surpluses. In addition, India received

financial investment from abroad in industry, commerce and infrastructure.

In the international accounts, these two net receipts were balanced by three items of net payment: purchase of gold and silver, remittances made by the private sector and remittances made by the government. Government transactions were closely connected with the balance of payments. India's government during the colonial period borrowed heavily abroad to finance its investment and other commitments. Repayment of these loans, along with regular remittance on account of charges made by Britain for costs of the administration of India, was a large net payment item in India's foreign transactions.

The money supply in colonial India was mainly influenced by the balance of payments. The primary objective of monetary policy was to stabilize the exchange rate. Stabilization of prices and outputs was meant to happen automatically. However, when Indian interests and Britain's interests came in conflict, stabilization in Britain's external account was usually in the minds of those who decided Indian affairs.

One of the most striking features of colonial India, and an enduring puzzle, is the extremely low rates of investment. Net investment was 2—4 percent of national income. Investment in machinery accounted for about half a percent of national income. The low rate of investment has been attributed to colonialism. In an accounting sense, the relatively large remittance abroad on the government account implied a lower capacity to import—and the period was one when a great deal of the machinery and raw materials needed by industry was imported.

Critiques of colonialism emphasized payments on government account, infamous as "drain." These remittances held an element of transfer, in that some of the services for which payments were due were overpriced. The British administrative elite, for example, was paid as grandly as its counterpart in pre-colonial Mughal India. However, a great deal of government expenditure was made for services that India needed but could not supply on its own, such as pensions to teachers and engineers or payment of debts raised to finance railways and irrigation. After all, Britain and India were worlds apart in their technical, scientific and

managerial capabilities. "Drain," therefore, is extremely difficult to separate out from legitimate factor payments. Even before separation, the scale of government remittances, typically 0.5—1 percent of national income may not appear large enough to bear the "drain theory."

Explanation of low rates of investment has tended to focus on these colonial features. But it is hard to explain the low level of private investment as a result of remittances abroad from India's government. A climate of high uncertainty took a toll on the desire to invest. The hunger of Indians for gold and silver took a toll on productive investment. The slow pace of institutional development on the financial side was also a negative factor. The traditional system normally did not deal in deposits and was thus inadequate in channeling household savings into productive uses. Such a development had to await joint stock banks, which expanded only late in the interwar period, that too in a highly unsteady fashion.

India's Growth During the Colonial Period

The early colonial period between 1858 and 1914 saw positive economic growth for India. The rate of growth was small by modern standards, but not trivial by contemporary standards. India's real national income grew at over I percent between 1868 and 1914, per capita income at a little less than 1 percent. These growth rates appeared to be rising late in the nineteenth and early in the twentieth century. One estimate shows that real national income grew at 1.8 percent and per capita income at 1.2 percent between 1865 and 1885, close to what Britain experienced in the last quarter of the century (Mukherjee, 1935, p. 65).

By contrast, the interwar period of the 1920s and 1930s was a difficult time, for the world economy, for India, for Britain and for India-Britain relations. On the positive side, India's market for modern and traditional industry grew, in the case of the former owing to limited tariff protection. There was growth too in non-food crop production. On the negative side, there was acute stagnation in food production.

Check your progress

1. Discuss about the cotton industry in pre 1914 era.

2. Discuss about mineral industries in pre 1914 era

10.3 LETS SUM UP

Industrial development was to a great extent a by-product of certain interrelated developments like improved transport and communications, growth of foreign trade and consequent accumulation of commercial fortunes.

Railway building and maintenance had effects more far reaching than the open-ing up of the interior and exposing agriculture to the market economy. It released some of the latent potentialities for industrial development.

The major features of industrial development in India during this period were as follows:

The decline traditional handicrafts paved the way for the transformation of the Indian economy. Despite many difficulties, a better state of affairs was discernible so far as industrial activities were concerned. Educated Indian was becoming more and more eager to take to technical education. Capital was overcoming its proverbial shyness. Steam was fast replacing manual power and serious attempts were made to start new industries.

10.4 KEYWORDS

Cotton, jute, mineral, World War 1, pre war industry

10.5 QUESTION FOR REVIEW

1. Discuss the Indian economy in pre WW1 era.

2. Write about modern industries from 1850 to 1914.

10.6 SUGGESTED READINGS

The Cambridge Economic History of India, Vol 2by Meghnad Desai

Economic History of India by Tathagata Roy

10.7 ANSWERS TO CHECK YOUR PROGRESS

1. Hint – 10.2
2. Hint – 10.2

UNIT 11 – INDUSTRIAL GROWTH AND INDUSTRIAL LABOR DURING BRITISH RAJ

STRUCTURE

11.0 Objective

11.1 Introduction

11.2 Industrial Growth And Labor

11.3 Lets Sum Up

11.4 Keywords

11.5 Questions For Review

11.6 Suggested Readings

11.7 Answer to check your progress

11.0 OBJECTIVE

Focuses on Colonial state and industrial growth,

Focus on Rise of industrial labour, labour force in large scale industry, type of labour movements, changing social composition of industrial labour.

11.1 INTRODUCTION

In this unit an overview of the way the British restructured the indigenous economic system of India to suit their objective of maximum exploitation is attempted. It could be seen that it was a mindless wreckage of a sound and flourishing system that ensured the prosperity of all the people particularly the large masses of the population living in the rural areas- villages-of India. This overview is given based on the researches that had already been carried out in this area by various

scholars, particularly such veterans as Dadabhai Navaroji, Romesh Chandra Dutt et al. The views of more recent researchers are also incorporated. A closer examination of the strategies used by the British colonialists in the 18" and 19" centuries would enable one to discern the: striking parallels between those strategies and the ones employed by the present transnational and multinational corporations operating in India under the aegis of globalization.

11.2 INDUSTRIAL GROWTH AND LABOR

Britain (and all the rest of Europe) had reached the limits to growth imposed by the resources of its own territory before the colonial era. The only way it could expand and grow economically was, as Adam Smith said, by altering 'its situation with respect to other countries'. Adam Smith, while referring to China, Egypt and India acknowledged that they were "the wealthiest in the world, chiefly renowned for their superiority in agriculture and manufactures".' He also mentioned that they were much richer than Europe. The process by which these great civilisations were reduced to penury, and then, to dependency upon Western wealth, is known in commercial circles today as "asset stripping": the extraction of all valuable assets after the take-over of the victims. 'Like the parasitic wasps' victims, India's people and resources were to be processed and digested-but kept barely alive- for the benefit of England alone. Another analogy was used by John Stuart Mill: India was England's "cattle farm". 117e East India Company (EIC) was the pioneering transitional company par excellence. In 1727. the EIC Governor declared that every "Company servant" was permitted to improve his fortune in any way that he chose. The British monopoly in rice trade gave them a clear 900 per cent profit. Robert Clive, a subaltern in the Madras Infantry Regiment, began his distinguished career with the forcible extraction of a mere £ 15,000 from the ruler of a minor state just south of Bombay. Cilve's defeat of the Nawab of Bengal in 1757 was the result of a conspiracy with a Persian traitor, Mir Jafar. With the Nawab killed in a battle, Clive installed Mir Jafar in his place and, fixes this favour, claimed from his £30,000 a year. Although he did not collect the

first amount in full, the Encyclopaedia Britannica states: "In the context of contemporary values these grants (!) equalled.. ..about one-seventeenth of the then annual revenue of Great Britain". However. it was not so much the proportion of input capital to the revenue that was important to Britain, as was its proportion to capital available for investment. The devastation and improvement which the British accomplished in Bengal, legalised by the British Parliament's licence to loot, was rapidly expanded to the rest of India, and continued till 1947. Within the next half century after Clive, it was estimated that between £500 and 1,000 million was transferred Britain by thousands of men who came out as paupers and turned into multimillionaire within a few years.

Numerous Indian rulers were deposed and puppets installed in their place. with each of the latter paying "compensation" to the British. The British demanded such wealth which they claimed they would have otherwise had from the plunder of each particular territory. Many of India's rulers preserved their people and territories fro in British rule by agreeing to pay this tribute. Others, yet to be disposed, were made to pay for the British armed forces used to keep them in bondage. When they had impoverished themselves due to these extractions, the rulers were loaned money by British officers and others, with interest of around 50% per annum. Such payments forced the rulers to raise tax rates or to surrender portions of their land to the lenders.* A whole series of measures were employed to legalise trickery. The British set up a mint in Calcutta and, as Adam Smith revealed, the gold coins it produced were "rated too high for the value which it bears in the market of Bengal. In 1.835, the EIC introduced its silver rupees as the standard coin in British-occupied India, there in by demonetizing all Indian currencies. 'The constant manipulations of the currency of India in the interests of Britain, once more foreshadows the machinations of the WB and IMF today. when they insist upon the devaluation of our currencies. 'Tribute is transference of a portion of the annual revenue of a subject country to the ruling country, without any material equivalent being given in exchange. Britain claimed that it did not extract any tribute from India.

The word "tribute", too harsh for sensitive British ears, was replaced by the less aurally offensive but equally pauperizing "Home Charges" in

either case. It was India's payment of the privilege of being ruled and exploited by Britain. Further capital was siphoned off by manipulating the Indian trading deficit with Britain and by the increasingly large interest payments on the Indi art Public Debt. In reporting a meeting of the Anti-Opium Society in 1888, a London paper stated: So far are we frown taxing ourselves for India's benefit that we are regularly taxing India, for our own benefit.

The proceeds of the opium monopoly and of the salt tax together only amount to ten millions, while the home charges of the Indian Government are Fourteen millions sterling's. But while we as a nation are thus pocketing one-fourth of the Indian revenue, we still have the effrontery to talk of the sin of the opium trade and the barbarity of' the salt tax. Before the 1914-18 War, India financed more than two-fifths of Britain's total deficits, in ensuring Britain's balance of payments surplus. By the end of the 1939-45 War. Malaysia's rubber and tin, African's gold and other minerals, and particularly the Middle East's oil, became added means by which Britain maintained her balance of payments. No doubt, as Clive himself said, India was "a country of inexhaustible riches and one which cannot fail to make its masters the richest corporation in the world". But the continuous transfer of so much wealth involved a constant drain of huge quantities of gold, silver, precious stones and other goods. The consequent shortage of capital, particularly silver currency contributed enormously to the destruction of internal trade and industry.

Taxation

In 1758, a tax of 10% on the produce of the landed estates in Bombay was imposed by the EIC to meet its extravagant expenses, to build fortifications and other works for maintaining its war with the French in India, and for extending its occupation here. In 1765, the EIC forcibly obtained the "right" tax collect land revenue in Bengal. The profits from this enabled them to further increase their armed strength and to monopolize the production and marketing of commodities. The EIC levied a tax on all salt produced in India, obtaining revenue of more than f I. million per year, during the last years of its rule. This excessive tax

compelled impoverished trillions to reduce the quantity of salt consumed to less than one-half the amount declared by the medical authorities to be absolutely necessary for health, if not for life itself. The British imposed or enhanced taxes on land, trades, occupations and commodities. In South India, the taxes were raised from 12 to 16% of the gross agricultural produce to 50%. The tax was calculated on what the farmer obtained in a good agricultural year. If, for any reason, he had a bad crop he would almost surely make a loss because the amount of tax remained fixed. Such oppressive taxes led to the decay of the excellent traditional agricultural, industrial and trading systems. The taxation policies of the British served to enrich the rich and impoverish the poor-as most such policies still do today. In 1929, the people of India were taxed more than twice as heavily as the people of England The percentage of the taxes in India, as related to the gross product, was more than doubled that of any other country.' While most of the taxes extracted by the British went out of the country, much of the revenues extracted by Indian rulers went back to the people, with on14 about 5% being retained by the ruler in 1750. The actual producers got 70% hack. 10% went to religious, cultural and educational projects, 7.50% to economic services and the police, another 7.5% to the army and the political aristocrat.

Other Exchanges There were several other processes by which Britain enriched itself and impoverished India: the destruction of artisans industries so that Britain could sell her industrial products, purchases made in Britain that could have been made in India, making India bear the burden of supporting a huge army to keep itself under subjugation, employing its own countrymen in all the well-paid jobs. When the EIC was "nationalized" by the British Parliament in 1858, plunder by the hundreds of EIC servants was replaced by the burden of high salaried and pensioned bureaucrats, probably making it the most expensive administration in the world. Nearly all high officials were British living in palatial buildings; surrounded by dozens of servants to do everything from keeping them cool with pankhas (hand operated ceiling fans) to looking after their children while they attended innumerable parties. The 13rilish in India imported their clothes and their horses, and even the

houses they liked in were constructed with wood and iron brought from Europe.

Indians paid for the maintenance of the army that oppressed them. In 1918, an Excess Profits Tax was imposed to pay in part only in part-for the "defence of India. This army was much larger than anything required for the defence of the country, the only possibility of attack coming from other European armies. Total Cash Transfers Charles Forbes, who stayed 22 years in India and returned to England to become a member of Parliament, spoke in the House of Commons in 1836, of '"plundering the people of India day after day and year after year to an extent horrible to be contemplated. He stated that could "total annual drain from India could be little short of five million sterling". This included & 630,000 paid in dividends to the proprietors of the EIC added that "In fifty years they had extracted from India more than would be sufficient to pay off the national debt". And this was after the Napoleonic Wars, when England's national debt shot up astronomically. As a member of the Court of Directors of the EIC, Forbes was unlikely to be significantly biased against England. In the last decade of the 19th century, the average annual remittance to England was 20 million. The military and civil charges and pensions alone rose from £7 trillion per annum in the 1870's, to over £20 million per year in the 1890s and much more afire that The British in effect, created an elaborate apparatus whereby they compelled India to pay for the privilege of being oppressed and exploited. Similar machinery for the extraction of wealth now exists in the instruments of the WB and the IMF. From 1895 to 1898 the total amount transferred is estimated to be more than £1,000 million. From 1898 to 1939, the transfers more than doubled. Further wealth was extracted in the form of priceless manuscripts, antiques, jewellery, and so on. The British Museum is probably the largest depository of' stolen goods in the world today, with the Louvre and similar museums not far behind Most of the items in them were supposed to be gifts, though they would be called bribes now. If an Indian took a present he was said to be corrupt but if a Company's servant took a "gift", he was collecting a legitimate perquisite. This gives just a brief glimpse of some of the processes of continues impoverishment, which transformed India from

one of the richest regions in the world to a state of utter destitution by the time the British departed. Economic Consequences of the British Conquest India had been conquered by other foreign powers before the British, but the invaders settled in India. The difference of the British conquest lies in the fact that it led to the emergence of a new political and economic system whose interest were rooted in a foreign soil and whose policies were guided solely by those interests. Whereas the early invaders Indianized themselves, the British tried to keep a distance between them and the Indian people and thus created the distinction erstwhile unknown to Indian history-the concept of foreign rulers and the Indian subjects.

The British rule has been generally divided into two epochs, first the rule of the East India Company ranging from 1757 to 1858, and second, the rule of the British Government in India from 1858 to 1947. The establishment of the British rule itself was a slow and lengthy process, extending over more than a hundred years. The British conquest which started in 1757 with the Battle of Plassey was completed only by 1858. During this period England was passing through the period of changes in the techniques of production which revolutionized manufacturing. The coming of the Industrial Revolution which synchronised with period of British conquest helped by the British to sell machine-made goods in India in competition with Indian handicrafts. The British conquest led to the disintegration of the village community partly by the introduction of the new land revenue system and partly by the process of commercialisation of agriculture. The new land system and the commercial agriculture meant untold exploitation of the Indian peasantry and the country was consequently plagued by frequent famines. The British were not interested in developing India a such the growth of railways or the spread of irrigation or the expansion of education or the creation of revenue settlements were all initiated with one supreme goal, i.e. to accelerate the process of economic drain from India. To understand the economic consequences of the British conquest, it would be convenient to study them under the following heads:

(1) Decline of Indian Handicrafts and progressive ruralisation or the Indian economy;

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(2) Growth of the new land system and the commercialisation of Indian agriculture. Decline of Indian Handicrafts and Progressive Ruralisation of the Indian Economy Before the beginning of Industrial Revolution in England, the East India Company concentrated on export of Indian manufactured goods, textiles, spices etc. to Europe where these articles were in great demand. The Industrial revolution reversed the character of India's foreign trade. Tremendous expansion (of productive capacity of manufacturers resulted in increased demand of raw materials for British industry and the need to capture foreign markets for finished products. As a first step, attempts were made to restrict and crush Indian manufacturers. On the other hand, efforts were made to commercialise agriculture so as to step up the export of those raw materials required by British industry. The Indian textile handicrafts were the first to be hit. The decline of this industry started a chain reaction leading to the speedy decline of other handicrafts.

The process of decline of handicrafts \+as accelerated by the development of the means of transport. The principal causes that led to the decay of handicrafts were as follows: - (a) Disappearance of Princely Courts. The growth of quite a number of industries and towns was possible owing to the patronage of Nawabs, Princes, Rajas and Emperors who ruled in India. The British rule meant the disappearance of this patronage enjoyed by the handicrafts. Cotton and silk manufacturers suffered especially besides, the artisans who manufactured specially designed articles for display and decoration of courts also suffered because of a decline in the demand for works of art. Hostile Policy of the East India Company and the British Parliament The British were always guided by their own interests, and never bother effects of their policies on the people of India in terms of unemployment, human suffering, famines, etc. They formulated certain policies, and propagated them but when conditions changed in England they were quick to reverse them. The British used tariff with the object of protecting their woollen and silk manufactures on the one hand and of raising additional revenues to finance continental wars, on the other. The period 1882 to 1894 was one of complete free trade. By the time, England had developed industrially to such an extent that unrestricted competition of British manufactures

with Indian handicrafts led to their decline. It was only when England rose to the position of industrial supremacy that free trade was advocated by the British economists and administrators thus, the British manufacturers employed the arm of political injustice in order to exploit the Indian market. The selfish policy of the British imperialists crippled Indian industries and helped the process of industrialisation in Britain. Competition of Machine-Made Goods The large-scale production that grew as a result of Industrial Revolution meant a heavy reduction in costs. It also created a gigantic industrial organisation and, consequently, the machine - made goods began to compete with the products of Indian industries and handicrafts. This led to the decline of textile handicrafts -the largest industry of India. Whereas the British emphasized the free import of machine-made manufactured goods, they did not allow the import of machinery as such. The decline of Indian handicrafts created a vacuum which could be filled by the import of British manufactures only. Thus. India became a classic example of a colonial country supplying her imperialist rules raw materials and foodstuffs and providing, markets for the manufactures. The opening of the Suez Canal in 1869 reduced transport costs and thus made the exploitation of the Indian market easier:

The Development of New Forms and Patterns of Demand With the spread of education a new class grew in India which was keen to imitate Western in dress manners, fashions and customs so as to identify itself with the British officials. This led to a change in the pattern of demand. Indigenous goods went out of fashion and the demand for European commodities, got a fillip. Besides, there was a loss of denied resulting from the disappearance of princely courts and nobility. Thus, the British rule silently but surely, alienated the Indians not only from Indian culture but also diverted in its favour their form and pattern of denied for goods. The destruction of Indian handicrafts had far-reaching economic consequences. It led to un-employment on a vast scale. Since textile industry was the worst sufferer in this process, the weavers were hit the most Lord William Bentinck reported in 1834: “the misery hardly finds a parallel in the history of commerce. The bones of cotton weavers are bleaching the plains of lndia.7 Another consequence of the decline of

handicrafts was the compulsory back to the land movement. The British destroyed the institution of Indian handicrafts but did not care to provide an alternative source of' employment The unemployed craftsmen and artisans shifted to agriculture and increased the proportion of population dependent on land. This trend of the growing proportion of the working force on agriculture is described as 'progressive Ruralisation' or 'deindustrialization of India'. In the middle of the nineteenth century, about 55 per cent of the population was dependent on agriculture, in 1901 it was about 68 per cent, the proportion went up to about 72 per cent in 1931. Thus, the increased pressure of population on land was responsible for progressive sub-division and fragmentation of holdings. It led to an increase in land-rents charged from tenants. It mean: an increase in the number of landless labourers. Thus the crisis in handicrafts and industries seriously crippled Indian agriculture. Commercialisation of Indian Agriculture Another noteworthy change in Indian agriculture was its commercialisation that spread between 1850 - 1947. Commercialisation of agriculture implies production of crops for sale rather than for family consumption. At every stage of the economic history of the nation, a part of the agricultural output has been is produced for the market. Then, what distinguished commercial agriculture from nominal sales of marketable surplus? It was as deliberate policy worked up under pressure from British manufacturer-industrialist and merchant to acquire more and more of raw materials for the British Industries.

By offering a higher bait of market price, the peasants were induced to substitute commercial crops for food crops as the former were more paying than the latter. Consequently, the peasants shifted to industrial crops and in some districts, the movement for commercial agriculture became so strong that the peasants started buying foodstuffs from the mandis for their domestic needs. This led to fall in the production of food and consequently this period is marked by the occurrence of most terrible famines and this happened for the first time in the economic history of India commercial agriculture was also, to some extent, the result of the mounting demands of land revenue by the state and excessive rent by the landlords from the peasantry. The process of commercial agriculture

necessitated by the Industrial Revolution was intensified by the development of an elaborate network of railways in India, after 1850. Railways linked the interior of the country with ports and harbours. Urban marketing centres and thus Indian agriculture began to produce for world markets. Large quantities of wheat from Punjab, jute from Bengal and cotton from Bombay poured in for export to England. The same railways which carried commercial crops from the various parts of the country brought back the foreign machine made manufactures to India. Thus, railways, and link-roads connecting the hinterland of the country with commercial and trading centres were instrumental in intensifying commercial agriculture on the one hand and sharpening competition of machine-made goods with Indian handicrafts, on the other. These factors led to the ruin of Indian industries.'

The Nature of Famines in India

Before the advent of modem means of transport, especially railways, the famines in India were localised scarcities of food in those regions where the crops tiad shrunk on account of bad rains etc. Both the construction of railways and the growth of trade after 1860 brought about a radical change in the nature of famines. Previously, a famine meant extreme hunger and the population had to undergo suffering on account of lack of food because there were no means of transporting the surplus food grain even it' it was available in other parts of the country. The position after 1860 was that the rapid means of transport made it possible to carry food from one region 1.0 the other without much loss of time. But periods of famine were invariably periods of high food prices and extensive agricultural unemployment. Therefore. the mass of the poor people found it impossible to purchase food. Consequently, the earlier famines were described as food shortages hut later once are more appropriately described as purchasing power famines. The Famine Commission (1889) made it abundantly clear when it emphasized that food was "always purchasable in the market though at high prices and in some remote places at excessively high prices". Two factors were responsible for pushing up food prices, despite the favourable effect of railways in moving food grains rapidly. First, an impending storage of food meant hoard and speculation which helped to push up the price

level very fast. Secondly, government did not allow any decrease in the export of food grains even in the lean years.

Consequently, speculator and the Government both accentuated the gravity of the problem Causes of Famines there is no doubt that the immediate cause of famines was the failure or the unreasonableness of rains. It is common knowledge that the means of irrigation were undeveloped and rainfall played a crucial role in agricultural production. Famines were a common occurrence in the dry regions and areas with a rainfall varying between 15 and 60 inches. The areas affected most by famines were Bihar, West Bengal, Orissa, Rajasthan. Tamil Nadu, Maharashtra, Andhra Pradesh and Karnataka. Failure of rains caused an absolute deficiency which resulted in great famines but unreasonableness of rainfall also proved destructive to crops and, there he. created food scarcity. India a country wholly or mainly depending on rainfall, rain can be considered as the most dominant factor determining agricultural production to understand the real factors which led to the occurrence of famine again and again in India-while they were banished after 1850 from Europe-it is quite desirable to understand the economic and sociological transformation that took place during the British rule.

The New Land System the British created a class of landlords so as to affix responsibility for land revenue, but the British left the process of rent fixation to the free market mechanism. The increasing demand for land for a growing agricultural population led to an exorbitant increase in rents, land was transformed in this process to an attractive capital asset. Thus there was a great desire among that: money lending classes to acquire land. The rise in prices of land enhanced the value of the security in the form of land against which peasants could borrow. This led to increase in agricultural debt of the Indian peasantry, repeatedly exposed to uncertainties. The high rates of interest charged by the moneyed classes made it impossible for the peasants to repay their debts. Gradually lands passed on to the money lending classes. The dispossession of the peasantry by the moneylenders added to the process of pauperisation of the cultivating classes. Thus. the new land relations which embodied the creation of a class of landowners and a class of cultivators (whether on a tenancy basis or a daily wage) separated

ownership from cultivation. The landlords were interested in extracting high rents, leaving a pittance with the cultivators. The investment on land fell sharply because the cultivators had to part off with a major portion of the produce in the form of rent of land to the landlords and interest to the moneylenders. This created in Indian agriculture a built-in depressor.

Thus, the new agrarian relations were disincentive-ridden and helped only to effect agricultural production adversely and retarded the process of agricultural development. The Impact of Colonial Rule Colonisation also had a deep impact on the repeated occurrence of famines in India. The destruction of the Indian handicrafts increased unemployment in the rural areas. Whereas in England, surplus labour from rural areas was quickly absorbed in new industries created in the process of industrialisation, nothing of this kind happened in India. The industrialisation of the Indian economy would have deprived England of a ready market for its goods and so the colonial interests were opposed to the development of industries in India. Thus labour thrown out of employment in traditional industries could only burden subsistence agriculture. Let us again put. into the witness-box, a few European observers. We can well begin with no less a person than the Premier of England, Mr J. Ramsay MacDonald, who says, "For days one goes through the land, and sees nothing but thin bodies toiling, toiling, trudging, trudging, trudging. India is the home of the poverty-stricken, and this was borne in upon mc all the more that its poverty was embodied in forms of the most perfect human grace." And later he declares: "The poverty of India is not an opinion, it is a fact Poverty of the Masses and the Economic Exploitation Dadabhai Navoroji a distinguished Indian economist, in his classic paper on the ‘Poverty of India' (1876), emphasized that the drain of wealth and capital from the country which started after I757 was responsible for absence of development. of India. According to Dadabhai Navoroji The drain consists of two elements - first, that arising from the remittances by European officials of their savings, and for their expenditure in England for their various wants both there and in India: from pensions and salaries paid in England: and second that arising from remittances by non-official Europeans.

This implies that India had to export much Indore than she imported in order to meet the requirements of the economic drain. During the period of the East India Company, an outright plunder in the form of gift exactions and tributes was carried out. Dadabhai Navoroji, Y.S. Pandit and S.B. Saul have estimated the annual drain for various periods. Taking the estimates based on the balance of payments alone, Saul's figure for 1880 amounts to 4.14.0 of the Indian national income. Irfan Habib, therefore, writes: "The fact that India had to have a rate of savings of 4% of its national income just to pay the Tribute must be borne in mind when economists speak of the lack of internal capacities for development, or the low per capital income base, from which the British could not lift the Indian's however, much they tried".' The economic drain of wealth prevented the process of capital creation in India but the British brought back the drained out capital and set up industrial concerns in India owned by British nationals. The government protected their interests and thus the British could secure almost a monopoly of all trade and principal industries.

The British component of industries established in India further drained off Indian wealth in the form of remittances of profits and interests. Moreover, the British finn dominated the Indian industrial scene and stifled the growth of Indian enterprise in industry. Thus, the economic drain which commenced right from the inception of the British rule acted as a drag on economic development till 1947. Leaving the bird’s-eye-view of affairs obtained from these snapshots, let us examine the situation at closer range. We find the old-time skilled handicraftsman and artisans have lost their trade, and no industry has replaced them, but these men have been driven back to the land to eke out a precarious living with a slightly increased population. Part of the year they work, but when the dry season sets in, they are left idle. The relative increase in population during the last century is very much lower in India than it has been in Europe. According to the Statesman's Year We observe the foreign trade of the country has changed from an export of manufactures articles to an import of such merchandise, and an export of raw materials. The cotton textiles as a cottage industry have disappeared leaving rioting to take their place. There has been a large number of famines, and these

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is more devastating ones in the last half a century than throughout the past of India's long history Everywhere the administration appears to be practically in the hands of European officers who naturally work with their return passage in their pockets. Their interests are not identified with the interests of those who in they govern, nor are they responsible to them. Their feet indeed rest on Indian soil, but their laces are turned homeward. The sons of the soil who were once the administrators have been reduced to an ill-paid community clerks.

When the nation gets no return to its effort, will this not be sufficient in itself to reduce a country to poverty in the course of years'? The unproductive expenditures. When the nation gets no return for its effort, will this not be sufficient in itself to reduce a country to poverty in the course of years? The unproductive debts were mainly incurred by the British in conquering India itself, and in financing wars of imperial interests in Asia, and Africa, leaving India to pay the bill. In addition, India's 'trustees' made a 'gift' to themselves of one hundred million pounds during the World War, while at that time India suffered losses, computed by Prof. Shah to be 180 crores. As these enormous debts were incurred in quarrels not her own, and in pursuit of interests not identical with hers, it is hardly fair to saddle India with these charges.

Check your progress –

1. Discuss about the steady industrial progress in India.

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2. How industrial labour came into being?

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11.3 LETS SUM UP

The British economists have always held the view that the backwardness of the Indian economy and its failure to modernize itself was largely due to the value: system, i.e., spiritualism, asceticism, the caste system, joint family, etc.: Similarly, the British economists have always argued that Indian capital was proverbially shy, it always sought safe avenues of investment and thus lacked the basic quality of adventure, which is an essential condition for dynamic entrepreneurship. Dr.Bipin Chandra who has examined the impact of colonial rule in modernizing India rejected both these arguments for absence of modernization as mere shibboleths. He wrote "It is a historical fallacy to assume that India these under British ride did not undergo a fundamental transformation, or that it remained basically traditional". But the modernization of India was brought within the political parameters of a colonial economy. Thus, the colonial links between India and Britain resulted in the progress of the Industrial Revolution in Britain while it meant the modernization of those sectors of the Indian economy which strengthened the process of integration of the Indian economy with British capitalism.

11.4 KEYWORDS

Industrial revolution, Industrial labour force, labour unions, trade unions

11.5 QUESTIONS FOR REVIEW

1. What were trade unions?

2. Discuss about the industrial labour union concept.

11.6 SUGGESTED READINGS

Romesh Chandra Dutt .The Economic History of India. Vol. l

Dadabhai Navaroji. Poverty and British Rule in India

11.7 ANSWERSTO CHECK YOUR PROGRESS

1. Hint – 11.3

2. Hint – 11.3

UNIT 12 - SHIFT FROM DIRECT TO INDIRECT TAXES

STRUCTURE

12.0 Objective

12.1 Introduction

12.2 Direct To Indirect Taxes

12.3 Lets Sum Up

12.4 Keywords

12.5 Questions For Review

12.6 Suggested Readings

12.7 Answer to check your Progress

12.0 OBJECTIVE

To learn about the direct tax system in British era

To know about the shift to indirect taxes

12.1 INTRODUCTION

In the recent years, India has been viewed as an attractive and dynamic investment destination, and has witnessed an increased presence of multinational enterprises (MNEs) and a consequential increase in cross-border trade. This has created an opportunity to the Government for improving tax system of the country to treat the globalization benefits effectively. In India, since the inception of globalization and liberalization policies, a host of significant developments have taken place in the tax system. On the other hand, the present status of tax reforms have their roots in the past developments and history of taxes in ancient, medial and modern

India. The understanding of this sequential development gives us an idea about where we stand and what should be our next course.

12.2 DIRECT TO INDIRECT TAXES

TAX – THE CONCEPT Taxes are as old as civilizations. Taxes are imposed so that a government may perform its traditional functions (i.e. defence and maintenance of law and order), undertaking welfare and developmental activities and to make provision for public goods and services to satisfy.

Collective needs of public "It has also to pay its own administration"1. The government needs financial resources for these purposes and taxation is a tool or method of transferring money from private to public hands. "Taxation is necessary because what the government gives it must first take away". TAXES IN ANCIENT INDIA References to taxes in ancient India are found in Arthashastra the famous work of Kautilya (also known as Chanakya and Vishnugupta). Arthashasrta embodies values, norms, and beliefs pertaining to public administration, economics, ethics and diplomacy. Taxes in ancient India were levied both in cash and in kind and were collected by local officers. Major sources of revenue for the king included land tax, octroi, taxes on liquor shops, gambling houses and on professionals like dancing girls. In his work Raghuvansa, Kalidasa, the greatest Sanskrit scholar of ancient India, observed, "Just as the sun extracts water from the reservoirs and gives it back in the form of showers, so does the ruler extract tax from his subjects and give it back to them in the form of prosperity". Kautilya's reference to commodity tax in the book Arthashastra is of significance and can be quoted as follows4: Taxes in cash and kind included are: 1.Customs duty (Sulka) which consists of import duty (Pravesya), Export duty (Nishramya) and Octroi and other gate tolls (Dwarabahiri Kadeya).

2. Transaction tax (Vyaji) including manavyaji (transaction tax for crown goods).

3. Share of production (Bhaga) including 1/6th share (Shadbhaga).

4. Tax (Kara) in cash.

5. Taxes in Kind (Pratikara) including labour (Vishti) supply of soldiers (Ayudhiya).

6. Countervailing duties or taxes (Vaidharana).

7. Road cess (Vartani).

8. Monopoly tax (Parigha).

9. Royalty (Prakriya).

10. Taxes paid in kind by villages (Pindakara).

11. Army maintenance tax (Senabhaktham).

12. Surcharges (Parsvam).

TAXES DURING BRITISH RULE

Prior to 1947, India was a dependency of the United Kingdom and encompassed the entire area which now forms the three countries of India, Pakistan and Bangladesh. It consisted of the British Indian Provinces, and the Indian Princely States. The political and economic scene changed greatly after 1947 when India emerged as an independent country merging with itself the former Princely States (called Part B States), but excluding areas of the other two countries mentioned above. Although it is desirable to trace historical developments of a subject to understand its present features and trends, the changed circumstances noted above fail to provide comparable data for the purpose. Therefore, only a brief account of the tax system prevailing prior to Independence is presented here.5The tax system of British India reflected characteristics of a traditional agricultural economy. Revenues of the Central Government were dominated by customs duties as domestic requirement for manufactured goods were met mostly by imports, chiefly from Britain and other Commonwealth countries. Import duties were levied on almost all items of imports whereas major items subject to export duties were jute and tea in which India enjoyed near-monopoly in the world market. Various customs and tariff enactments were passed from time to time but the following two were the main; (i) The Sea Customs Act, 1878, and (ii)

The Tariff Act, 1934. After Independence, the Sea Customs Act and other allied enactments were repealed by a consolidating and amending legislation entitled the Customs Act, 1962. Similarly, the Tariff Act of 1934 was repealed by the Customs Tariff Act, 1975. Another important source of tax revenue for the Central Government was excise duty levied on a few commodities. Excise taxation in its modern form dates back to 1894 when for the first time a duty at the rate of 5 per cent ad valorem was imposed on cotton yarn of more than twenty counts. Excise at the rate of 6 annas6 per Imperial Gallon was imposed on motor spirit in 1917 and on kerosene at the rate of one anna per Imperial Gallon in 1922. Another landmark in the history of excise taxation was the year 1934 when excise duties were imposed on sugar, matches, and steel ingots. Duties were imposed on tyres in 1941 and on vegetable products, and tobacco in 1943, mainly to meet the exigencies of war finances. The year 1944 saw excise duties being imposed on coffee, tea and betel nut. Cigarettes came within the excise net in 1948 and mill-made cotton cloth in 1949. Before 1944, excise duties were levied under separate enactment for different goods, e.g. tobacco levies were imposed under the Tobacco (Excise Duty) Act, 1943. About 16 such separate laws were consolidated into the Central Excises and Salt Act and the Central Excise Rules, 1944. Among the direct taxes, the only important source of revenue was the income tax introduced in India by the British in 1860 to overcome the financial difficulties created by the events of 1857. Out of a Central tax revenue of Rs.73.90 crore in 1938-39, customs accounted for Rs.40.51 crore, Central excises Rs.8.66 crore, and income tax Rs. 13.74 crore.

As for the British Indian Provinces, the chief source of income was land revenue followed by Provincial excises, mainly on liquor. Although under the Government of India Act, 1935, Provincial Governments had been authorized to levy sales tax, it formed a very low component of their revenue till Independence. The Province of Bombay levied a tax on the sale of tobacco in 1938. A retail sales tax on motor spirit and lubricants was imposed by Central Provinces (now Madhya Pradesh) in

the same year. A multi-point general sales tax was levied in Madras Province at the rate of half per cent in 1939 under the Madras General Sales Tax Act. The Princely States did not form part of the structure of public finance of British India. They had separate budgets and separate source of revenue. The maritime states imposed their own customs duties. Taxes In Independent India "It was only for the good of his subjects that he collected taxes from them, just as the Sun draws moisture from the Earth to give it back a thousand fold" -Kalidas in Raghuvansh Constitutional Provisions Pertaining to Taxation in India The constitution of India makes elaborate arrangements relating to the distribution, between the Centre and the States, of taxes, the power of borrowing, and provision for grant-in-aid by the Centre to the States. The fundamental philosophy of these arrangements is to place at the disposal of the two tiers of Government adequate financial resources to enable them to discharge their respective responsibilities under the constitution.

Distribution of Taxation Powers: Article 265 of the Constitution makes clear that no tax shall be operated without the authority of law. Entries 82 to 92B of List I in the Seventh Schedule to the Constitution refer to the taxation powers of the Union Government (Table 4.2). Entries 45 to 63 of List II in the same Schedule mention the fiscal powers of the State Governments (Table 4.3). List III does not deal with taxation. So the Center and the States have no concurrent powers of taxation. The residual powers of taxation, belong to the Center vide entry 97 of List I in the Seventh Schedule. For instance, gift tax (abolished in 1998) was imposed by the Union Government under these residual powers. Similarly, prior to the Constitution (Eighty-eighth Amendment) Act, 2003, service tax was imposed under these residual powers. The Constitution does not provide for any taxation powers to local governments. However, the implication of Article 276 is that the taxes on professions, trades, callings or employment are for the benefit of a State or of a municipality, district board, local board or any other local authority. The States on their own may assign any of the taxes in the State list to the local bodies. The taxes generally

assigned to local governments are property taxes, octroi, and taxes on vehicles.

Income and Wealth Taxes Among the direct taxes levied by the Center taxes on income and wealth are very significant from not only economic but also from social-economic point of view. Many a state government exercise their right and levy tax on agricultural income, but due to very less taxable income being available with agriculturists from revenue point of view this tax is unimportant. Owing to the significance attached to the personal income tax and corporate income tax they are briefly discussed below.

Personal Income Tax Personal income tax is levied on the incomes of individuals, Hindu undivided families, unregistered firms and other associations of persons. For taxation purpose income from all sources is aggregated. However, apart from the deduction of necessary qualified expenditures, rebate on account of life insurance premium, provident fund, etc., was earlier allowed. This rebate was, however, abolished in the Budget 2005-06. Now, out of gross total income of an individual a host of deductions are allowed prominent among them are deductions for savings and pensions, medical insurance premium and interest on educational loans. Like other countries India has a progressive income tax. Before 1974-75, the marginal rate for income tax in India was 97.75 per cent which was the highest in the world. One negative ramification of such a high marginal tax rate was that income tax became replete with exemptions, allowances, deductions and incentives.10On the recommendation of the Direct Taxes Enquiry Committee (1970), in 1974-75 the marginal rate for income tax was brought down to 77 per cent, including 10 per cent surcharge. In 1976-77, the marginal tax rate was further reduced to 66 per cent and again the same was subsequently reduced to 50 per cent, in 1985-86 as part of long-term fiscal strategy. The marginal rate for income tax was brought down to 40 per cent in the Budget 1992-93. The tax rates have been reduced at other levels also. Thus the degree of the progressivity of the schedule has been considerably reduced. Reduction in tax rates at all levels has been by and large commended in the country and proved right by way

of increased tax collection. In the Budget for 2003-04, the marginal rate of 30 per cent was retained. However, a surcharge of 10 per cent was levied on income tax if 78 total incomes exceeded Rs.8.5 lakh. "Extraordinarily high tax rates in the past were highly unrealistic. They failed to reduce economic disparities. On the contrary, they put a high premium on tax evasion and, in practice, became a major factor in the growth of black money". Raja Chelliah Committee (1991) had also favoured significant reductions in tax rates at all levels. This approach seems to be influenced by the Laffer Effect which implies that a reduction in the rate of taxation leads to more than proportionate increase in tax yield. Following the thrust of the Kelkar Task Force recommendations for the simplification of direct and indirect taxes, the income tax structure in the Budget for 2005-06 was overhauled. The Finance Minister proposed new rates for different slabs. The marginal rate of 30 per cent was made applicable to taxable income beyond Rs. 2.5 lakh. Surcharge of 10 per cent was levied on taxable income level of Rs. 10 lakh or more. Moreover, the various kinds of exemptions for savings were replaced by a single consolidated exemption of Rs. 1 lakh. Important changes were introduced in income tax structure in Union Budget 2010-11. The budget retained the basic exemption limit for individuals at Rs. 1.60 lakh as in the year 2009-10 (the basic exemption limit for women was kept at Rs. 1.90 lakh and for senior citizens Rs. 2.40 lakh). However, the 10 per cent rate was made applicable for Rs. 1.6 lakh – Rs. 5 lakh bracket, whereas earlier this was applicable for income of Rs. 1.6 lakh – Rs. 3 lakh. The 20 per cent tax rate was made applicable for incomes of Rs. 5 lakh – Rs. 8 lakh instead of the earlier bracket of Rs. 3 lakh – Rs. 5 lakh. The highest rate of 30 per cent was introduced on incomes of over Rs. 8 lakh (earlier it was Rs. 5 lakh). The limit on investments under section 80C was raised from Rs. 1 lakh to Rs. 1.2 lakh (by Rs. 20,000).

History of Taxation Pre – 1922

"It was only for the good of his subjects that he collected taxes from them, just as the Sun draws moisture from the Earth to give it back a thousand fold" – --Kalidas in Raghuvansh eulogizing KING DALIP.

It is a matter of general belief that taxes on income and wealth are of recent origin but there is enough evidence to show that taxes on income in some form or the other were levied even in primitive and ancient communities. The origin of the word "Tax" is from "Taxation" which means an estimate. These were levied either on the sale and purchase of merchandise or livestock and were collected in a haphazard manner from time to time. Nearly 2000 years ago, there went out a decree from Ceaser Augustus that all the world should be taxed. In Greece, Germany and Roman Empires, taxes were also levied sometime on the basis of turnover and sometimes on occupations. For many centuries, revenue from taxes went to the Monarch. In Northern England, taxes were levied on land and on moveable property such as the Saladin title in 1188. Later on, these were supplemented by introduction of poll taxes, and indirect taxes known as "Ancient Customs" which were duties on wool, leather and hides. These levies and taxes in various forms and on various commodities and professions were imposed to meet the needs of the Governments to meet their military and civil expenditure and not only to ensure safety to the subjects but also to meet the common needs of the citizens like maintenance of roads, administration of justice and such other functions of the State.

In India, the system of direct taxation as it is known today, has been in force in one form or another even from ancient times. There are references both in Manu Smriti and Arthasastra to a variety of tax measures. Manu, the ancient sage and law-giver stated that the king could levy taxes, according to Sastras. The wise sage advised that taxes should be related to the income and expenditure of the subject. He, however, cautioned the king against excessive taxation and stated that both extremes should be avoided namely either complete absence of taxes or exorbitant taxation. According to him, the king should arrange the collection of taxes in such a manner that the subjects did not feel the pinch of paying taxes. He laid down that traders and artisans should pay 1/5th of their profits in silver and gold, while the agriculturists were to pay 1/6th, 1/8th and 1/10th of their produce depending upon their circumstances. The detailed analysis given by Manu on the subject clearly shows the existence of a well-planned taxation system, even in

ancient times. Not only this, taxes were also levied on various classes of people like actors, dancers, singers and even dancing girls. Taxes were paid in the shape of gold-coins, cattle, grains, raw-materials and also by rendering personal service.

The learned author K.B. Sarkar commends the system of taxation in ancient India in his book "Public Finance in Ancient India", (1978 Edition) as follows:-

"Most of the taxes of Ancient India were highly productive. The admixture of direct taxes with indirect Taxes secured elasticity in the tax system, although more emphasis was laid on direct tax. The tax-structure was a broad based one and covered most people within its fold. The taxes were varied and the large variety of taxes reflected the life of a large and composit population".

However, it is Kautilya's Arthasastra, which deals with the system of taxation in a real elaborate and planned manner. This well-known treatise on state crafts written sometime in 300 B.C., when the Mauryan Empire was as its glorious upwards move, is truly amazing, for its deep study of the civilisation of that time and the suggestions given which should guide a king in running the State in a most efficient and fruitful manner. A major portion of Arthasastra is devoted by Kautilya to financial matters including financial administration. According to famous statesman, the Mauryan system, so far as it applied to agriculture, was a sort of state landlordism and the collection of land revenue formed an important source of revenue to the State. The State not only collected a part of the agricultural produce which was normally one sixth but also levied water rates, octroi duties, tolls and customs duties. Taxes were also collected on forest produce as well as from mining of metals etc. Salt tax was an important source of revenue and it was collected at the place of its extraction.

Kautilya described in detail, the trade and commerce carried on with foreign countries and the active interest of the Mauryan Empire to promote such trade. Goods were imported from China, Ceylon and other countries and levy known as a vartanam was collected on all foreign commodities imported in the country. There was another levy called

Dvarodaya which was paid by the concerned businessman for the import of foreign goods. In addition, ferry fees of all kinds were levied to augment the tax collection.

Collection of Income-tax was well organised and it constituted a major part of the revenue of the State. A big portion was collected in the form of income-tax from dancers, musicians, actors and dancing girls, etc. This taxation was not progressive but proportional to the fluctuating income. An excess Profits Tax was also collected. General Sales-tax was also levied on sales and the sale and the purchase of buildings was also subject to tax. Even gambling operations were centralised and tax was collected on these operations. A tax called yatravetana was levied on pilgrims. Though revenues were collected from all possible sources, the underlying philosophy was not to exploit or over-tax people but to provide them as well as to the State and the King, immunity from external and internal danger. The revenues collected in this manner were spent on social services such as laying of roads, setting up of educational institutions, setting up of new villages and such other activities beneficial to the community.

The reason why Kautilya gave so much importance to public finance and the taxation system in the Arthasastra is not far to seek. According to him, the power of the government depended upon the strength of its treasury. He states – "From the treasury, comes the power of the government, and the Earth whose ornament is the treasury, is acquired by means of the Treasury and Army". However, he regarded revenue and taxes as the earning of the sovereign for the services which were to be rendered by him to the people and to afford them protection and to maintain law and order. Kautilya emphasised that the King was only a trustee of the land and his duty was to protect it and to make it more and more productive so that land revenue could be collected as a principal source of income for the State. According to him, tax was not a compulsory contribution to be made by the subject to the State but the relationship was based on Dharma and it was the King's sacred duty to protect its citizens in view of the tax collected and if the King failed in his duty, the subject had a right to stop paying taxes, and even to demand refund of the taxes paid.

Kautilya has also described in great detail the system of tax administration in the Mauryan Empire. It is remarkable that the present day tax system is in many ways similar to the system of taxation in vogue about 2300 years ago. According to the Arthasastra, each tax was specific and there was no scope for arbitratiness. Precision determined the schedule of each payment, and its time, manner and quantity being all pre-determined. The land revenue was fixed at 1/6 share of the produce and import and export duties were determined on advalorem basis. The import duties on foreign goods were roughly 20 per cent of their value. Similarly, tolls, road cess, ferry charges and other levies were all fixed. Kautilya's concept of taxation is more or less akin to the modern system of taxation. His overall emphasis was on equity and justice in taxation. The affluent had to pay higher taxes as compared to the not so fortunate. People who were suffering from diseases or were minor and students were exempted from tax or given suitable remissions. The revenue collectors maintained up-to-date records of collection and exemptions. The total revenue of the State was collected from a large number of sources as enumerated above. There were also other sources like profits from Stand land (Sita) religious taxes (Bali) and taxes paid in cash (Kara). Vanikpath was the income from roads and traffic paid as tolls.

He placed land revenues and taxes on commerce under the head of tax revenues. These were fixed taxes and included half yearly taxes like Bhadra, Padika, and Vasantika. Custom duties and duties on sales, taxes on trade and professions and direct taxes comprised the taxes on commerce. The non-tax revenues consisted of produce of sown lands, profits accuring from the manufacture of oil, sugarcane and beverage by the State, and other transactions carried on by the State. Commodities utilised on marriage occasions, the articles needed for sacrificial ceremonies and special kinds of gifts were exempted from taxation. All kinds of liquor were subject to a toll of 5 precent. Tax evaders and other offenders were fined to the tune of 600 panas.

Kautilya also laid down that during war or emergencies like famine or floods, etc. the taxation system should be made more stringent and the king could also raise war loans. The land revenue could be raised from

1/6th to 1/4th during the emergencies. The people engaged in commerce were to pay big donations to war efforts.

Taking an overall view, it can be said without fear of contradiction that Kautilya's Arthasastra was the first authoritative text on public finance, administration and the fiscal laws in this country. His concept of tax revenue and the on-tax revenue was a unique contribution in the field of tax administration. It was he, who gave the tax revenues its due importance in the running of the State and its far-reaching contribution to the prosperity and stability of the Empire. It is truly a unique treatise. It lays down in precise terms the art of state craft including economic and financial administration.

History of Taxation Post 1922

1. Preliminary:

The rapid changes in administration of direct taxes, during the last decades, reflect the history of socio-economic thinking in India. From 1922 to the present day changes in direct tax laws have been so rapid that except in the bare outlines, the traces of the I.T. Act, 1922 can hardly be seen in the 1961 Act as it stands amended to date. It was but natural, in these circumstances, that the setup of the department should not only expand but undergo structural changes as well.

2. Changes in administrative set up since the inception of the department:

The organisational history of the Income-tax Department starts in the year 1922. The Income-tax Act, 1922, gave, for the first time, a specific nomenclature to various Income-tax authorities. The foundation of a proper system of administration was thus laid. In 1924, Central Board of Revenue Act constituted the Board as a statutory body with functional responsibilities for the administration of the Income-tax Act. Commissioners of Income- tax were appointed separately for each province and Assistant Commissioners and Income-tax Officers were provided under their control. The amendments to the Income tax Act, in 1939, made two vital structural changes: (i) appellate functions were separated from administrative functions; a class of officers, known as

Appellate Assistant Commissioners, thus came into existence, and (ii) a central charge was created in Bombay. In 1940, with a view to exercising effective control over the progress and inspection of the work of Income-tax Department throughout India, the very first attached office of the Board, called Directorate of Inspection (Income Tax) - was created. As a result of separation of executive and judicial functions, in 1941, the Appellate Tribunal came into existence. In the same year, a central charge was created in Calcutta also.

2.1 World War II brought unusual profits to businessmen. During 1940 to 1947, Excess Profits Tax and Business Profits Tax were introduced and their administration handed over to the Department (These were later repealed in 1946 and 1949 respectively). In 1951, the 1st Voluntary Disclosure Scheme was brought in. It was during this period, in 1946, that a few Group 'A' officers were directly recruited. Later on in 1953, the Group 'A' Service was formally constituted as the 'Indian Revenue Service'.

2.2 This era was characterised by considerable emphasis on development of investigation techniques. In 1947, Taxation on Income (Investigation) Commission was set up which was declared ultra vires by the Supreme Court in 1956 but the necessity of deep investigation had by then been realised. In 1952, the Directorate of Inspection (Investigation) was set up. It was in this year that a new cadre known as Inspectors of Income Tax was created. The increase in 'large income' cases necessitated checking of the work done by departmental officers. Thus in 1954, the Internal Audit Scheme was introduced in the Income-tax Department.

2.3 As indicated earlier, in 1946, for the first time a few Group A officers were recruited in the department. Training them was important. The new recruits were sent to Bombay and Calcutta where they were trained, though not in an organised manner. In 1957, I.R.S. (Direct Taxes) Staff College started functioning in Nagpur. Today this attached office of the Board functions under a Director-General. It is called the National Academy of Direct Taxes. By 1963, the I.T. department, burdened with the administration of several other Acts like W.T., G.T., E.D., etc., had expanded to such an extent that it was considered necessary to put it

under a separate Board. Consequently, the Central Board of Revenue Act, 1963 was passed. The Central Board of Direct Taxes was constituted, under this Act.

2.4 The developing nature of the economy of the country brought with it both steep rates of taxes and black incomes. In 1965, the Voluntary Disclosure Scheme was brought in followed by the 1975 Disclosure Scheme. Finally, the need for a permanent settlement mechanism resulted in the creation of the Settlement Commission.

2.5 A very important administrative change occurred during this period. The recovery of arrears of tax which till 1970 was the function of State authorities was passed on to the departmental officers. A whole new wing of Officers - Tax Recovery Officers was created and a new cadre of post of Tax Recovery Commissioners was introduced w.e.f. 1-1-1972.

2.6 In order to improve the quality of work, in 1977, a new cadre known as IAC (Assessment) and in 1978 another cadre known as CIT (Appeals) were created. The Commissioners' cadre was further reorganised and five posts of Chief Commissioners (Administration) were created in 1981.

2.7 Tax Reforms: Certain important policy and administrative reforms carried out over the past few years are as follows:-

(a). The policy reforms include :-

- Lowering of rates;
- Withdrawls/reduction of major incentives;
- introduction of measures for presumptive taxation;
- simplification of tax laws, particularly relating to capital gains; and
- widening the tax base.

(b). The administrative reforms include:--

- Computerisation involving allotment of a unique identification number to tax payers which is emerging as a unique business identification number; and

• realignment of the available human resources with the changed business needs of the organisation.

2.8 Computerisation: Computerisation in the Income-tax Department started with the setting up of the Directorate of Income tax (Systems) in 1981. Initially computerisation of processing of challans was taken up. For this 3 computer centres were first set up in 1984-85 in metropolitan cities using SN-73 systems. This was later extended to 33 major cities by 1989. The computerized activities were subsequently extended to allotment of PAN under the old series, allotment of TAN, and pay roll accounting. These computer centres used batch process with dumb terminals for data entry.

In 1993 a Working Group was set up by the Government to recommend computerisation of the department. Based on the report of the Working Group a comprehensive computerisation plan was approved by the Government in October, 1993. In pursuance of this, Regional Computer Centres were set up in Delhi, Mumbai, and Chennai in 1994-95 with RS6000/59H Servers. PCs were first provided to officers in these cities in phases. The Plan involved networking of all users on LAN/WAN. Network with leased data circuits were accordingly set up in Delhi, Mumbai and Chennai in Phase-I during 1995-96. A National Computer Centre was set up at Delhi in 1996-97. Integrated application software were developed and deployed during 1997-99. Thereafter, RS6000 type mid-range servers were provided in the other 33 Computer Centres in various major cities in 1996-97. These were connected to the National Computer Centre through leased lines. PCs were provided to officers of different level upto ITOs in stages between 1997 and 1999. In phase II offices in 57 cities were brought on the network and linked to RCCs and NCC.

2.9 Restructuring of the Income-tax department: The restructuring of the Income-tax Department was approved by the Cabinet in its meeting held on 31-8-2000 to achieve the following objectives:-

• Increase in effectiveness and productivityy;

• Increase in revenue collection;

- Improvement in services to tax payers;
- Reduction in expenditure by downsizing the workforce;
- Improved career prospects at all levels;
- Induction of information technology; and
- Standardization of work norms

The aforementioned objectives have been sought to be achieved by the department through a multi-pronged strategy of :

a. redesigning business processes through functionalisation;

b. increasing the number of officers to rationalise the span of control for better supervision, control and management of workload and to improve tax-payer services and

c. re-orient, retrain and redeploy the workforce with appropriate incentives in the form of career advancement.

3. Important events affecting the administrative set up in the Income-tax department:

1939

Appellate functions separated from inspecting functions.

A class of officers known as AACs came into existence. Jurisdiction of Commissioners of Income tax extended to certain classes of cases and a central charge was created at Bombay.

1940

Directorate of Inspection (Income-tax) came into being.

Excess Profits Tax introduced w.e.f. 1-9-1939.

1941

Income-tax Appellate Tribunal came into existence.

central charge created at Calcutta.

1943

Special Investigation Branches set up.

1946

A few officers of Class-I directly recruited.

Demonetisation of high denomination notes made.

Excess Profits Tax Act repealed.

1947

Business Profits Tax enacted (for the period 1-4-1946 to 31-3-1949).

Indirect Tax: An indirect tax is a tax collected by an intermediary (such as a retail store) from the person who bears the ultimate economic burden of the tax (such as the customer). An indirect tax is one that can be shifted by the taxpayer to someone else. An indirect tax may increase the price of a good so that consumers are actually paying the tax by paying more for the products. The some important indirect taxes imposed in India are as under: Customs Duty: The Customs Act was formulated in 1962 to prevent illegal imports and exports of goods. Besides, all imports are sought to be subject to a duty with a view to affording protection to indigenous industries as well as to keep the imports to the minimum in the interests of securing the exchange rate of Indian currency. Duties of customs are levied on goods imported or exported from India at the rate specified under the customs Tariff Act, 1975 as amended from time to time or any other law for the time being in force. Under the custom laws, the various types of duties are leviable. (1) Basic Duty: This duty is levied on imported goods under the Customs Act, 1962. (2) Additional Duty (Countervailing Duty) (CVD): This is levied under section 3 (1) of the Custom Tariff Act and is equal to excise duty levied on a like product manufactured or produced in India. If a like product is not manufactured or produced in India, the excise duty that would be leviable on that product had it been manufactured or produced in India is the duty payable. If the product is leviable at different rates, the highest rate among those rates is the rate applicable. Such duty is leviable on the value of goods plus basic custom duty payable. (3) Additional Duty to compensate duty on inputs used by Indian manufacturers: This is

levied under section 3(3) of the Customs Act. (4) Anti-dumping Duty: Sometimes, foreign sellers abroad may export into India goods at prices below the amounts charged by them in their domestic markets in order to capture Indian markets to the detriment of Indian industry. This is known as dumping. In order to prevent dumping, the Central Government may levy additional duty equal to the margin of dumping on such articles. There are however certain restrictions on imposing dumping duties in case of countries which are signatories to the GATT or on countries given "Most Favoured Nation Status" under agreement. (5) Protective Duty: If the Tariff Commission set up by law recommends that in order to protect the interests of Indian industry, the Central Government may levy protective anti-dumping duties at the rate recommended on specified goods. (6) Duty on 73

Bounty Fed Articles: In case a foreign country subsidises its exporters for exporting goods to India, the Central Government may impose additional import duty equal to the amount of such subsidy or bounty. If the amount of subsidy or bounty cannot be clearly determined immediately, additional duty may be collected on a provisional basis and after final determination, difference may be collected or refunded, as the case may be. (7) Export Duty: Such duty is levied on export of goods. At present very few articles such as skins and leather are subject to export duty. The main purpose of this duty is to restrict exports of certain goods. (8) Cess on Export: Under sub-section (1) of section 3 of the Agricultural & Processed Food Products Export Cess Act, 1985 (3 of 1986), 0.5% ad valorem as the rate of duty of customs be levied and collected as cess on export of all scheduled products. (9) National Calamity Contingent Duty: This duty was imposed under Section 134 of the Finance Act, 2003 on imported petroleum crude oil. This tax was also leviable on motor cars, imported multi-utility vehicles, two wheelers and mobile phones. (10) Education Cess: Education Cess is leviable @ 2% on the aggregate of duties of Customs (except safeguard duty under Section 8B and 8C, CVD under Section 9 and anti-dumping duty under Section 9A of the Customs Tariff Act, 1985). Items attracting Customs Duty at bound rates under international commitments are exempted from this Cess. (11)

Secondary and Higher Education Cess: Leviable @1% on the aggregate of duties of Customs. (12) Road Cess: Additional Duty of Customs on Motor Spirit is leviable and Additional Duty of Customs on High Speed Diesel Oil is leviable by the Finance Act (No.2), 1998. and the Finance Act, 1999 respectively. (13) Surcharge on Motor Spirit: Special Additional Duty of Customs (Surcharge) on Motor Spirit is leviable by the Finance Act, 2002. Central Excise Duty: The Central Government levies excise duty under the Central Excise Act, 1944 and the Central Excise Tariff Act, 1985. Central excise duty is tax which is charged on such excisable goods that are manufactured in India and are meant for domestic consumption. The term "excisable goods" means the goods which are specified in the First Schedule and the Second Schedule to the Central Excise Tariff Act 1985. It is mandatory to pay Central Excise duty payable on the goods manufactured, unless exempted eg; duty is not payable on the goods exported out of India. Further various other exemptions are also notified by the Government from the payment of duty by the manufacturers. Various Central Excise are: (1) Basis Excise Duty: Excise Duty, imposed under section 3 of the 'Central Excises and Salt Act' of 1944 on all excisable goods other than salt produced or manufactured in India, at the rates set forth in the schedule to the Central Excise tariff Act, 1985, falls under the category of Basic Excise Duty In India. (2) Special Excise Duty: According to Section 37 of the Finance Act, 1978, Special Excise Duty is levied on all excisable goods that come under taxation, in line with the Basic Excise Duty under the Central Excises and Salt Act of 1944. Therefore, each year the Finance Act spells out that whether the Special Excise Duty shall or shall not be charged, and eventually collected during the relevant financial year. (2) Additional Duty of Excise: Section 3 of the 'Additional Duties of Excise Act' of 1957 permits the charge and collection of excise duty in respect of the goods as listed in the Schedule of this Act. (4) Road Cess: (a) Additional Duty of Excise on Motor Spirit: This is leviable by the Finance Act (No.2), 1998. (b) Additional Duty of Excise on High Speed Diesel Oil: This is leviable by the Finance Act, 1999. (5) Surcharge: (a) Special Additional

Duty of Excise on Motor Spirit: This is leviable by the Finance Act, 2002. (b) Surcharge on Pan Masala and Tobacco Products: This Additional Duty of Excise has been imposed on cigarettes, pan masala and certain specified tobacco products, at specified rates in the Budget 2005-06. Biris are not subjected to this levy. (6) National Calamity Contingent Duty (NCCD): NCCD was levied on pan masala and certain specified tobacco products vide the Finance Act, 2001. The Finance Act, 2003 extended this levy to polyester filament yarn, motor car, two wheeler and multi-utility vehicle and crude petroleum oil. (7) Education Cess: Education Cess is leviable @2% on the aggregate of duties of Excise and Secondary and Higher Education Cess is Leviable @1% on the aggregate of duties of Excise. (8) Cess - A cess has been imposed on certain products. Service Tax: The service providers in India except those in the state of Jammu and Kashmir are required to pay a Service Tax under the provisions of the Finance Act of 1994. The provisions related to Service Tax came into effect on 1st July, 1994. Under Section 67 of this Act, the Service Tax is levied on the gross or aggregate amount charged by the service provider on the receiver. However, in terms of Rule 6 of Service Tax Rules, 1994, the tax is permitted to be paid on the value received. The interesting thing about Service Tax in India is that the Government depends heavily on the voluntary compliance of the service providers for collecting Service Tax in India. Sales Tax: Sales Tax in India is a form of tax that is imposed by the Government on the sale or purchase of a particular commodity within the country. Sales Tax is imposed under both, Central Government (Central Sales Tax) and State Government (Sales Tax) Legislation. Generally, each State follows its own Sales Tax Act and levies tax at various rates. Apart from sales tax, certain States also imposes additional charges like works contracts tax, turnover tax and purchaser tax. Thus, Sales Tax Acts as a major revenue-generator for the various State Governments. From 10th April, 2005, most of the States in India have supplemented sales tax with a new Value Added Tax (VAT).

Value Added Tax (VAT): The practice of VAT executed by State Governments is applied on each stage of sale, with a particular

apparatus of credit for the input VAT paid. VAT in India classified under the tax slabs are 0% for essential commodities, 1% on gold ingots and expensive stones, 4% on industrial inputs, capital merchandise and commodities of mass consumption, and 12.5% on other items. Variable rates (State-dependent) are applicable for petroleum products, tobacco, liquor, etc. VAT levy will be administered by the Value Added Tax Act and the rules made there-under and similar to a sales tax. It is a tax on the estimated market value added to a product or material at each stage of its manufacture or distribution, ultimately passed on to the consumer. Under the current single-point system of tax levy, the manufacturer or importer of goods into a State is liable to sales tax. There is no sales tax on the further distribution channel. VAT, in simple terms, is a multi-point levy on each of the entities in the supply chain. The value addition in the hands of each of the entities is subject to tax. VAT can be computed by using any of the three methods: (a) Subtraction method: The tax rate is applied to the difference between the value of output and the cost of input. (b) The Addition method: The value added is computed by adding all the payments that is payable to the factors of production (viz., wages, salaries, interest payments etc). (c) Tax credit method: This entails set-off of the tax paid on inputs from tax collected on sales. Securities Transaction Tax (STT): STT is a tax being levied on all transactions done on the stock exchanges. STT is applicable on purchase or sale of equity shares, derivatives, equity oriented funds and equity oriented Mutual Funds. Current STT on purchase or sell of an equity share is 0.075%. A person becomes investor after payment of STT at the time of selling securities (shares). Selling the shares after 12 months comes under long term capital gains and one need not have to pay any tax on that gain. In the case of selling the shares before 12 months, one has to pay short term capital gains @10% flat on the gain. However, for a trader, all his gains will be treated as trading (Business) and he has to pay tax as per tax sables. In this case the transaction tax paid by him can be claimed back/adjusted in tax to be paid. The overall control for administration of Direct Taxes lies with the Union Finance Ministry which functions through Income Tax Department with the Central Board of Direct Taxes (CBDT) at

its apex. The CBDT is a statutory authority functioning under the Central Board of Revenue Act, 1963. It also functions as a division of the Ministry dealing with matters relating to levy and collection of Direct Taxes. The Central Excise Department spread over the entire country administers and collects the central excise duty. The apex body that is responsible for the policy and formulation of rules is the Central Board of Excise and Customs which functions under the control of the Union Finance Ministry. The Central Excise officers are also entrusted with the administration and collection of Service tax and the Customs duty. The information contained in this UNIT is related to direct and indirect taxes imposed and collected by the Union Government. The tables giving data from 2000-01 onwards in respect direct taxes (corporation tax, income tax and other direct taxes) collected by Central Board of Direct Tax (CBDT) and indirect taxes (customs duties, union excise duties and service tax) collected by Central Board of Excise and Customs. Customs Collection Rate used in this chapter is defined as the ratio of revenue collection (basic customs duty + countervailing duty) to value of imports (in per cent) unadjusted for exemptions, expressed in percentage.

Highlights of the Direct and Indirect Taxes:

- The total revenue realization from Direct and Indirect Taxes increased from ` 1881.19 billion in 2000-01 to ` 6076.45 billion in 2008-09. The percentage share of revenue realization from direct taxes to the total revenue realization increased from 36.3% in 2000-01to 55.7% in 2008-09, whereas, the percentage share of revenue realization from indirect taxes declined from 63.7% in 2000-01 to 44.3% in 2008-09.
- Revenue collection from direct taxes increased from ` 683.05 billion in 2000-01 to ` 3382.12 billion in 2008-09. The percentage share of revenue realization from corporation tax to the total revenue realization from direct taxes increased from 52.3% in 2000-01to 63.2% in 2008-09, whereas, the percentage share of revenue

realization from income tax decreased from 46.5% in 2000-01 to 36.7% in 2008-09.

- Revenue collection from indirect taxes increased from ` 1198.14 billion in 2000-01 to ` 2446.67 billion in 2009-10. The percentage share of revenue realization from customs duties to the total revenue realization from indirect taxes decreased from 39.7% in 2000-01 to 34.5% in 2009-10, whereas, the percentage share of revenue realization from excise duties declined from 57.2% in 2000-01 to 42.1% in 2009-10. , However, the percentage share of revenue realization from service tax to the total revenue realization from indirect taxes increased substantially from 2.2% in 2000-01 to 23.5% in 2009-10.
- The total number of effective assesses of income tax and corporation tax increased from 23.00 million in 2000-01 to 32.65 million in 2008-09. The companies' assesses declined from 334261 in 2000-01 to 327674 in 2008-09, whereas, the number of individual assesses and assesses of Hindu un-divided Families of income tax increased 20.66 million and 0.55 million respectively in 2000-01 to 30.10 million and 0.77 million in 2008-09. The assesses of firms declined from 1.34 million to 1.31 million during same period, whereas, trusts' assesses increased from 0.064 million in 2000-01 to 0.071 million in 2008-09. However, the other assesses increased from 0.051 million to 0.071 million during same period.
- The customs collection rate gradually decreased from 20.2% in 2000-01 to 6.9% in 2008-09. Customs collection rate of petroleum products decreased from 10% in 2004-05 to 3% in 2008-09, whereas, customs collection rate of non-petroleum products decreased from 12% in 2004-05 to 9% in 2008-09.
- About 34% of total import duties were realized from machineries, whereas, 10.8%, 9.0%, 8.5% and 7.7% of the total import duties were realized from Gold & articles other than Gold, petroleum products, chemicals and iron & steel respectively during 2009-10.

Notes

- About 62.2% of total excise duties was realized from petroleum crude and petroleum products, whereas, 13.5% and 9.4% of the total excise duties were realized from tobacco products and Iron & steel and articles thereof respectively during 2009-10.
- 7% of total service tax was realized from telephone billing, whereas, 6.9%, 6.3% and 5.4% of the total service tax were realized from banking and other financial service, business auxiliary service and general insurance premium respectively during 2009-10.

Check your progress –

1. What is a direct tax?

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2. What is indirect tax?

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12.3 LETS SUM UP

Income Tax Act, 1860 Consequent upon the financial difficulties created by the events of 1857. Income Tax was introduced in India for the first time by the British In the year 1860. The Act of 1860 was passed only for five years and therefore it lapsed 1865. It was replaced 1867 by a licence 15 tax on professions and trades and the latter was converted into a certificate tax in the following year. It was latter abolished in 1873. Licence tax traders remained in operation till 1886 when it was merged in the income tax Act of that year. 1.4.2Income Tax Act, 1886 The Act of 1886 levied a tax on the income of residents as well as non residents in India. The Act defined agricultural income and exempted it from tax liability in view of the already existing land revenue a kind of direct taxes. The Act of 1886 exempted life insurance premiums paid by an assessed on policies

on his own life. Another important provision of this Act Hindu undivided family was treated as a distinct taxable entity. 1.4.3Income Tax Act, 1918 The Act of 1918 brought under change also receipts of casual or non-recurring nature pertaining to business or professions. Although income tax in India has been a charge on net income since inception, it was in the Act of 1918 that specific provisions were inserted for the first time pertaining to business deductions for the purpose of computing net income. The Act of 1918 remained in force for a short period and was replaced by new Act (Act XI of 1922) in view of the reforms introduced by the Govt. of India Act, 1919 (Sury, 2008). 1.4.4Income Tax Act, 1922 The organizational history of the income tax department dates back to the year 1922. " one of the important aspects of the 1922 Act 16 was that, it laid down the basis, the mechanism of administering the tax and the rates at which the tax was to be levied would be laid down in annual finance acts. This is procedure brought in the much needed flexibility in adjusting the tax rates in accordance with the annual budgetary requirements and in securing a degree of elasticity for the tax system (Tyagi, 2008). Before 1922 the tax rate were determined by the Income tax act itself and to revise the rates the act itself had to be amended. The Income tax Act,1922 gave for first time a specific nomenclature to various income tax authorities and laid the foundation of a proper system of administration as per provisions of income tax act 1922 thus, it is the income tax act 1961, which is currently operative in India

12.4 KEYWORDS

Direct taxes, indirect taxes, property taxes, wealth taxes

12.5 QUESTIONS FOR REVIEW

1. Write about the direct tax system in pre 1947 era.

2. Discuss about the indirect taxes in pre 1947 era.

12.6 SUGGESTED READINGS

The Cambridge Economic History of India Vol 2 by Neghbad Desai,

Economic History of India by Tathagata Roy

12.7 ANSWERS TO CHECK YOUR PROGRESS

1. Hint 12.2
2. Hint 12.2

UNIT 13 – TARIFF AND EXCISE

STRUCTURE

13.0 Objective

13.1 Introduction

13.2 Tariff And Excise

13.3 Lets Sum Up

13.4 Keywords

13.5 Questions for Review

13.6 Suggested Readings

13.7 Answer to Check your Progress

13.0 OBJECTIVE

To learn about the Tariff of the British Era.

To learn about the excise duty of British era

13.1 INTRODUCTION

The history of the Indian tariff has been a history of the clash of commercial interests. In the early days, the East India Company was interested in developing Indian cottage industries from which its export trade was largely drawn. It, for example, helped to organise and finance cotton and silk piece-goods and silk yarn which had a ready sale in the European markets

13.2TARIFF AND EXCISE

There soon arose a clash of interests between the East India Company and the industrial houses of England "which were sufficiently powerful to insist that it should be suspended and that the company should instead

concentrate on the export from India of the raw-material necessary for manufactures in England."

In course of time, the company became a mere tool in the hands of these vested interests who used tariff as a weapon to injure the Indian cottage industries.

By the time the crown rule was established in India, England had become the foremost industrial and commercial nation of the world. She needed not only unhindered supplies of raw-material but also unrestricted markets for her expanding industries. Meanwhile, the era of free trade had set in England.

The very country, which had imposed high import duties on articles like silk and cotton goods from India, now began to preach the gospel of free trade to her colonies. What was good for England was supposed to be good for her colonies also.

Thus a rose another clash between the interests of Indian industry which needed encouragement and protection for her survival and the English trade and manufacturing which required free trade for its expansion. The clash was once again resolved in the total sacrifice of Indian interests for the prosperity of British trade and Industry.

The financial difficulties resulting from the Rebellion of 1857 had forced the government to raise, in 1859, the import duty on cotton twist and yarn to 5% and on other articles to 10%. Next year, the duty on cotton twist and yarn was also raised to 10%. However, soon under pressure from British traders and cotton manufacturers, a process of tariff reform and reduction was set in motion.

The duty on cotton yarn was reduced to 5% in 1861 and to 3½ in 1862; the duty on cotton manufactures was brought down to 5% in 1862; and the general import duties were reduced from 10% to 7±% in 1864 and to 5% in 1875. This was the beginning of the movement by which, under cover of Free Trade Principles, the interests of Manchester were advanced at the expense of Indian industry.

Even these reduced duties, especially on cotton manufactures, came under heavy attack from the Lancashire cotton manufacturers. In 1874,

the Manchester Chamber of Commerce complained about a growing protected trade in cotton manufactures in India and prayed for the abolition of import duties levied on them.

It is well to remember in this connection that by 1870's, many western countries like Germany and U.S.A., under the stimulus of protection, had begun to emerge as industrial rivals of England. Germany raised a tariff wall in 1879; France followed in 1881, Russia in 1881-82; America raised her tariff in 1890 and 1897.

Even British Colonies were not far behind; Canada raised tariff in 1897 and Australia in 1900. As tariffs rose in Europe and America, the market for British cotton textiles was considerably narrowed and England was left with only India and China to fall back upon.

The English cause found its most ardent advocate in Lord Salisbury who repeatedly emphasised the necessity of removing the import duties on cotton goods with a view to placing the industry on a solid foundation, and of removing the growing cause of "conflict between the manufacturing interests of England and India which may before long become a political difference."

The government refused to oblige on the ground that the duties were not protective. However, with a view to softening criticism, a duty of 5% was imposed on the import of long staple cotton. The pressure, however, continued undiminished.

In 1877, the House of commons passed a Resolution that the cotton duties were protective in their nature and "being contrary to sound commercial policy" should be repealed without delay.

It had its effect when, despite financial difficulties created by the Afghan War, recurring famines, and depreciation of Silver, the duties on certain coarser varieties of cotton goods were remitted in 1878 and on all other cotton goods in 1879.

Further opportunity came in 1882 when cotton duties along with duties on most other commodities except Salt and Liquor were abolished in toto.

Meanwhile, steps had already been taken to as well abolish export duties which had been levied at a rate of 3% advalorem on practically all except certain specified articles. Beginning in 1859, these duties were gradually abolished so that by 1880, all articles except rice were exempted from the payment of these duties.

The success of free trade principles was complete. The Indian interests had been fully subordinated to the overriding requirements of English industry. The ports of agricultural India now became more open to the industries of the world than the free ports of England herself.

The few industries, which had just begun their precarious life, were now 'free' to compete with the advanced industries of England or the protected industries of the rest of the world.

For a period of 12 years between 1882-1894, the Indian custom tariff was modelled on the Free Trade Principles. It was, however, not destined to last longer. The construction of railways at fast pace, the rising military expenditure, and the falling exchange rate imposed fresh burdens on the Indian finances. Such measures as the imposition of import duty on Petroleum and increase in salt duty did not bring much relief.

Matters came to a head in 1894 when the government, faced with a deficit of Rs. 3.5 crores, desperately looked around for new sources. And finding none, it re-imposed a 5% duty on all imports. In deference to the Lancashire interests, a countervailing excise duty of 5% was imposed on Indian Yarn as well.

This excise duty, which had previously been rejected as 'costly, vexatious and inconvenient' was re-imposed not for the sake of revenue but in order to remove any element of protection which the Indian textile industry might have enjoyed.

And yet, the British manufacturer's appetite was not fully satisfied and they continued their agitation for the removal of the remotest sign of protection to their helpless dependency. Again the government obliged; the import duty on cotton manufactures was reduced from 5% to 3.5% in

1896 but simultaneously, an excise duty of 3.5% was imposed on cotton cloth produced in Indian mills.

The measure resulted in a remission of taxation amounting to Rs. 51.5 lakhs or 37% on imported goods and an increase of Rs. 11 lakhs or 300% in taxation on Indian goods. The loss was accepted despite the fact that there was a deficit, that the Afghan war was going on, that the exchange was falling and that the protective measures against famines had to be suspended.

Thus ended the controversy “When Manchester saw to her gratification that she had left no possibility of even a nominal competition on the part of her Indian rival.”

The tariff system, as established in 1894, remained un-altered in its main essentials till the First World War. In general, it consisted of a low uniform rate of duty imposed on nearly all imports except railway materials, machinery and iron and steel which were admitted duty free.

The financial burden imposed by the world war- I necessitated an enhancement of the tariff rate. In 1916, the general rate was raised from 5% to 7.5%. Exemptions were reduced; machinery other than that for cotton mills, railway materials, iron and steel were now taxed at 2.5%; duties on liquors and tobacco were considerably raised and sugar was subjected to a 10% duly.

In 1917, it was decided to make a special war contribution of £ 100 million to England and this made it necessary to impose further taxes. Cotton duty was raised to a general level of 7.5% while export duties were levied on tea and jute. In 1921, when the government was faced with an unprecedented deficit, tariff was further raised to 11%. This rate covered cotton textiles also.

The government’s dif-ficulties, however, remained unsolved and, therefore, in 1922, the general rate of duty was further raised from 11% to 15% the duty on matches was doubled and that on sugar raised from 15% to 25%.

To sum up. The fiscal policy of the Government of India, up to 1923, remained largely free trade in its working, and revenue of the

government rather than the wellbeing of the country were the dominating consideration in deciding upon the tariff rates. On top of this, came the direct and indirect influence of the British Big Business who glorified free trade to suit its purpose.

2. Changes in the Indian Fiscal Policy after World War- I:

The end of the world war- I saw certain significant developments. In the first place, foreign competition had begun to break down the British monopoly in the Indian market where her rivals, quickly seizing the opportunity, had penetrated in several directions. The danger was, as Hardinge explained, that India would become "the dumping ground for the manufactures of foreign nations."

In the second place, the end of the war witnessed a tremendous upsurge of the Indian freedom movement. In order to maintain control of India in that dis-turbed period, it was essential to secure the cooperation of the Indian 'bourgeoisie' by offering certain economic and political concessions.

In the third place, the war had proved that if the British wanted to retain India as a colony and safeguard their position elsewhere in Asia, they had to create an adequately developed industrial base in the country. One concrete result of these developments was the introduction of a system of protection in India.

In August 1917, a resolution was passed in the British Parliament which envisaged "Progressive realisation of responsible government in India as an integral part of the British Empire."

The joint select committee, which examined the Government of India Bill 1919, recog-nised that fiscal freedom should not lag behind political freedom. It, therefore, recommended the establishment of a convention that "the Secretary of State should, as far as possible avoid interference on this subject (of fiscal policy) when the Government of India and its legislature are in agreement …."

The Fiscal Autonomy convention, accepted by the Secretary of State for India in 1921, was a landmark in the history of fiscal policy in India. It paved the way for the appointment, in 1921, of the Fiscal Commission

"to examine with reference to all interests concerned, the Tariff policy of the Government of India, including the desirability of adopting the principle of Imperial Preference."

3. The Policy of Discriminating Protection:

The Commission, after a careful investigation of existing conditions, came to the conclusion that the Industrial development of India had not been 'commensurate with the size of the country, its population, and its natural resources.'

In order to secure steady industrial progress, the commission advocated the policy of protec-tion for India, but in order "to make the burden as light as is consistent with the due development of industries and avoid abrupt disturbances of industrial and commercial condition" the commission recommended discrimination in the in-dustries selected and in the degree of protection afforded.

In other words, all industries were not to be protected, but a careful selection was to be made, and only those industries were to be given protection which fulfilled certain conditions. This inaugurated the policy of Discriminating protection in India.

The Commission laid down the following three conditions for the grant of protection to an industry:

(a) "The industry must be one possessing natural advantages, such as an abundant supply of raw-materials, cheap power, a sufficient supply of labour or a large home market."

(b) "The industry must be one which, without the help of protection, either is not likely to develop at all or is not likely to develop so rapidly as is desirable in the interest of the country."

(c) "The industry must be one which will eventually be able to face world competition without protection … ."

In addition to these three main conditions, known as the Triple Formula, the commission laid down certain subsidiary conditions which, though not essential, were to be regarded as factors favourable to the grant of protection.

These were:

(1) “An industry in which the advantages of large scale production can be achieved … is a particularly favourable subject for protection.”

(2) “Another industry which should be regarded with a favourable eye is that in which there is a probability that in course of time the whole needs of the country could be supplied by the home production.”

(3) “any industry which is essential for purposes of national defence, and for which the conditions in India are not un-favourable should be adequately protected irrespective of the general conditions … laid down for the protection of industries.”

For the successful working of the Scheme, the Commission recommended the appointment of a “thoroughly competent, impartial and permanent. Tariff Board” charged with the duty of making detailed enquiries into the claims of protection and to express its conclusions in the form of detailed and definite recommendations.

The Commission felt convinced that the mere imposition of protective tariff would not, by itself, produce full industrial development and, therefore, recom-mended several supplementary measures such as changes in railway rates, greater emphasis on technical education and replacement of imported skills for promoting the growth of industries.

The above recommendations were not endorsed by five out of the eleven members of the commission. The minority objected to the policy of Discriminating Protection on the ground that it mixed up policy with procedure and laid down such rigid conditions as to impart the industrial progress of the country.

In their opinion, the fiscal policy best suited for India was protection “to be regulated by the government and Indian legislature from time to time by such discrimination as might be considered necessary in the best interests of India.” The Minority was also against Imperial Preference and wanted certain conditions to be imposed on foreign capital in India.

The Policy of Discriminating Protection, as recommended by the majority of the commission, was accepted by the government in 1923 but

with some limitations. The Resolution accepted by the Assembly did not refer to the non-fiscal recom-mendations which were considered equally important by the commission.

Further, the government appointed only Adhoc Boards in place of a permanent one recom-mended by the commission.

4. Working of the Indian Fiscal Policy:

The policy of Discriminating protection came in for severe criticism which mainly centered around the conditions laid down for the selection of industries for protection. The First condition regarding natural advantages was one which ultimately boiled down to cost of production.

Therefore, an examination of the cost of production in each industry would have been a more scientific approach to the problem than a mere description of natural advantages.

In fact, on the basis of this interpretation, the tariff board recommended protection to Glass industry although Soda Ash was not available in India, stating that dependence on imported materials was not a bar to protection provided the final costs justified it.

Similarly, in the case of the Heavy Chemicals industry, the Board observed that the absence of Sulphur in India was not an inseparable objection. And yet the government, attaching undue importance to the raw material part of the condition, disregarded the recommendation of the Board and refused protection to glass, chemicals and the worsted section of the Woolen industry.

Another serious flaw was that it laid unnecessary emphasis on the existence of an internal market as a condition for the grant of protection. As Professor Vakil points out, "if Britain keeps industries fed by foreign raw materials and is dependent upon foreign consumers there is no reason why India should not encourage industries which can be fed by her own materials irrespective of the market."

But the government thought otherwise and denied protection to the locomotive industry on the ground that the home market was not large enough.

Apart from this, the Triple Formula was mutually 'incompatible and incon-sistent.' If the first condition was satisfied, it was impossible to fulfill the second for there is no industry which possesses all the natural advantages and yet is not able to develop without protection. The Formula thus set a mutually contradictory task to the Industry applying for or enjoying protection.

The cement industry, for instance, fulfilled the first condition extremely well owing to the plenitude of natural advantages but it could not satisfy the Second and was refused protection. The case of the Tata steel was more ridiculous when it blew hot and cold by explaining its improved financial condition and, at the same time, describing its troubles least protection might be withdrawn.

While the first two conditions were mutually contradictory, the third was 'illogical and superfluous'. In fact, 'the first condition itself was explanatory of the Third', or any estimate of whether an industry would be able to eventually stand on its own feet or not had to be based on the First condition, viz, availability of raw material, market, etc. The Triple Formula, therefore, was a misleading one.

The Commission had recommended the constitution of a permanent Tariff Board. The govt. instead appointed Adhoc Boards for a duration not exceeding one year in the first instance. This practice of appointing different boards at different times "prevented the taking of long term views, the accumulation of experience and the building of an efficient body of technique and procedure."

Besides, these Boards had to function under certain limitations. They had neither any power to initiate enquiry nor to summon witnesses. Absence of such power was particularly left in the case of foreign enterprises which often did not cooperate. For instance, the Swedish Match company refused to disclose, even in confidence, the cost figures of their factories in Sweden.

Worse still was the case of the non-worsted section of the woolen industry where the govt. refused to accept the recommendation of the Board for the grant of protection on the ground that the British controlled

section of the industry had not tendered evidence and that the Board's findings did not apply to the industry as a whole.

The very composition of the various tariff boards would suggest that the Boards were appointed largely with a view to securing easy acceptance of the govt's views. In fact, as Adarkar points out, any expression of nationalist or protectionist sentiment was a sure disqualification.

This is evident from the fact that of the total number of 113 positions on the various enquiries, 71 were held by the govt. officials themselves and only 42 by non-officials.

The restrictive nature of Discriminating protection was made doubly so by the dilatory and difficult procedure laid down. The govt. was not bound to refer every application to a Tariff Board; the Tariff Board was not bound to submit its report within a specified period of time; and finally, the govt. was not bound either to accept the recommendations of the Board or the resolution of the Legislative Assembly if it ran counter to govt. proposals.

The authorities at all levels had their own notion about the time factor in the urgency of protection which was often granted when the industry was on its last legs. In the case of Match and Sugar industries, two years elapsed before protection was announced; in that of textiles, the Board and the govt. together took 2½ years before protection was granted.

At the other end, woolen industry waited for 2½ years and glass for three years only to be told that protection could not be given.

Delay by itself would not have been so objectionable were it not for the fact that the Commerce Department, in every case, sat in judgement upon the reports which were submitted by the tariff board after "laborious, searching and meticulous enquiries."

The Triple Formula did not recognise the importance of developing 'embryo' or 'potential' industries. The Board's view was that "there was no need for protec-tion unless there was something to protect." The system of Imperial Preference, under which British goods were given preferential treatment by way of lower import duties, further reduced the utility of Discriminating Protection.

According to R.P. Rutt, the Policy of Discriminat-ing protection was introduced in-order "to prepare the way for Imperial Preference" so that England could win back the Indian market from her rivals.

Accordingly, protection was given only to such industries as did not clash with British interests. For example, in Steel, India competed with Belgium and other continental countries; in textiles, with Japan and China in inferior varieties; in gold thread, with France; in Sugar, with Java; in Plywood and tea chest industry, with Finland.

In all these Industries, there was no clash between Indian and British interests and they were, therefore, favoured with the grant of protection. In the case of cement, however, the British and Indian interests were in direct conflict and that is why it was left to work out its own salvation.

In the case of Heavy chemicals, protection was directly opposed to British interests. That explains why, after a great delay, the industry was given temporary fiscal aid to be left high and dry within 18 months. The case of Magnesium Chloride was different for here the competition was with Germany.

That is the reason why, of all chemicals, Magnesium Chloride received protection at the hands of the govt. It shows that, under the circumstances, there was hardly anything like Fiscal Autonomy. Had India been free, the Policy of protection would have been directed as much against England as against the rest of the world.

Furthermore, the period for which tariff protection was given was often far too short. Except in two or three cases, the maximum period of protection was limited to seven years. In not a few cases, especially in the early days of the experiment, the period was limited to three years.

It is also noteworthy that, in some cases, protection was withdrawn temporarily or finally, or reduced substan-tially, e.g., protection was withdrawn temporarily or finally, or reduced substantially, e.g., protection was temporarily withdrawn from Steel Wire and Wire nails in 1927-32; it was finally withdrawn from various chemicals except Magnesium chloride in 1933; and it was substantially reduced in the case of a large variety of steel products under the Act of 1934.

In view of this, new entrants in the industry did not feel sure of govt. help against foreign competition. The most fundamental defect was that protection was not visualised as an instrument of general economic development but was viewed as a means of enabling particular industries to withstand foreign competition.

In others words; it was of a 'safe-guarding variety.' As Professor Bal Krishna points out, there was neither a comprehensive scheme of development nor a bold approach to implement it. The result was a lop-sided development of Indian industries.

5. Achievements of the Indian Fiscal Policy of Discriminating Protection:

In-spite of these limitations, discriminating protection was not without some tangible results. Between 1923-39, the tariff boards conducted in all 51 enquiries. These included fresh applications for protection, cases for renewal or revision of the quantum of protection and a few technical matters.

The government accepted the Board's recommendations without any change in 34 cases, in ten of which the Board had rejected the claim for protection. In all cases, government modified the recommendations before accepting them. The Board's recommendations for protection were rejected in six cases. The number of industries which actually received protection was thirteen.

They were Iron and steel including subsidiary steel industries, cotton textiles, Paper and Paper Pulp, Matches salt, Heavy Chemi-cals, Sericulture, Magnesium Chloride, Plywood and Tea chests, Gold thread, wheat and rice, the last two having been protected on government's initiative without reference to the Tariff Board. Among the industries denied protection were cement, glass, coal, Petroleum and Woolen.

The main advantage of the policy was to enable the protected industries to remain comparatively unaffected during the world trade depression when all other industries suffered considerably. Jute goods and Pig Iron were the only large scale Industries which were adversely affected.

Other protected industries not only maintained but, in several cases, recorded substantial gains so that the total output, after an initial set back in 1930, was continuously rising between 1930-38.

The Policy brought about a tremendous expansion of protected industries. During the 17 years, 1923-39, the production of steel Ingots expanded 8 fold; of cotton piece goods by 2½ times; the output of matches and paper rose by 38% and 180% respectively; and cane sugar recorded the maximum advance of a little less than 39 times from 24000 tons in 1922 to 9,31,000 tons in 1938.

Another important way in which protective tariffs tended to help Indian economy indirectly was the establishment of industries dependent on Iron and steel, Paper and cotton textiles. A number of small industries developed due to the availability of steel and steel products manufactured in India and the existence of industries like paper, cotton textiles which provided a market for their products.

As a natural consequence of the establishment of new industries and expansion of the old, there was a steady increase in employment in the country. According to Dr. Bal Krishna, total employment in the group of protected industries was about 580,000 in the year 1923 but it increased to about 881,000 by 1937.

In other words, there was an increase of 46.8% in employment among the protected industries by 1937. During the same period, the increase in the unprotected group of industries was only 23.6%.

The expansion of the indigenous cotton textile industry was an advantage to cultivators of cotton as it stimulated the production of high priced medium-staple cotton. The gains of the cultivator in the case of sugar-cane were even more substantial.

From 26 lakh acres in 1930-31, the year when protection was first granted to the Sugar industry, the area under sugar cane increased to 36 lakh acres; area under improved varieties increased from 1 million to 2.6 million acres; the Yield per acre improved from 12 to 14 tons.

To sum-up the policy of Discriminating Protection "within its limited scope — achieved a fairly large measure of success and on balance the direct and indirect advantages of protection —offset the burden on the consumers."

6. Fiscal Policy during World War II:

The Second World War, once again, exposed the weaknesses of India's in-dustrial structure. It was realised that India lacked many vital industries so neces-sary for the prosecution of the war.

At the same time, the Indian industrialists wanted to take advantage of the indirect protection provided by the war (all imports were practically cut off) and set up new industries. But there was fear of foreign competition once the war ended.

It was to allay these fears that the government gave the assurance in 1940 that the case of the 'war' industries would be sympathetically considered for the grant of protection to withstand unfair com-petition. The Reconstruction Committee also made it clear that it would be in the interests of the country to continue the policy of protection by liberalizing the Principles governing the selection of industries.

The idea was further rein-forced by the industrial Policy statement (1945) which made a distinction between the formulation of the future policy of the country and an investigation of the claims of industries started during the war period.

In order to honour the com-mitment made and pending the formulation of a long-term policy, the government appointed an interim Tariff Board, as a short-term measure, to enquire into the claims of industries started during the war.

At the same time, there was a relaxation of the conditions governing the grant of protection.

The Triple Formula was discarded and in its place, the tariff Board laid down only two conditions:

(1) That the industry was "an established one and conducted on sound business lines."

(2) That "having regard to the natural or economic advantages enjoyed by the industry and its actual or probable costs, it was likely, within a reasonable period of time, to develop sufficiently to be able to carry on successfully without protection or State assistance," or that "it was an industry to which it was desirable in national interest to grant protection and that the probable cost of protection or assistance to the community was not excessive."

As can be seen, the conditions laid down in 1945 were more 'liberal' and hence an improvement on the conditions under which the pre-war Tariff Boards worked. The most important change was the decision to allow the Board to recommend protection or assistance to those industries which it considered to be of national interest.

And the term 'national interest' was not confined ex-clusively to military and defence considerations but meant the economic welfare of the country, diversification of national economy and provision of avenues of industrial development.

Another departure was the emphasis placed on the actual or probable cost of the industry based on its economic advantages. In other words, even if some of the raw materials were not available in the country, the industry was entitled to protection on the strength of its other economic advantages.

Further, the Board was specifically asked to recommend what additional or alternative measures could be adopted to assist the industries. Realising the changed circumstances, the Board gave a liberal interpretation to the term of reference.

And yet, the new conditions were not without criticism. The requirement that an industry must be established before it could qualify for protection or assistance was a handicap specially in regard to the establishment of heavy or technically complicated industries.

Likewise, the condition about an industry being conducted on "Sound business lines" was vague or uncertain in as much as no criteria of soundness could be laid down, and it was not always easy for an industry to meet this condition, particularly if the standard was to be the average

level of efficiency of the competitive industry abroad. The Fiscal Com-mission (1949) found this criticism sound.

The Tariff Board set up in 1945 was reconstituted in 1947 for a period of three years. The new Board was authorised to investigate the claims of war industries for a period of three years as an interim measure pending the formulation of a long term policy.

One feature worth noticing was the expeditious manner in which the Interim Board conducted its enquiries. During a period of 5 years, it conducted 90 enquiries as against 51 conducted by the pre-war boards between 1923-39. Of these, 5 related to the fixation of internal prices, 46 were new cases and the remaining 39 related to the continuance or modification of protection already given.

The Board recommended protection, for the first time, to 38 industries and continuance of protection to 22 industries. A few of the important industries which received protection during this period were:

Aluminium, Antimony and other non-ferrous metals, caustic soda and Bleaching Powder, Soda Ash, Textile Machinery, Bicycles, electric Motors up to 30 H.P., Sewing machines, Sheet Glass and Batteries for motor vehicles.

Some of the prewar industries to which con-tinuance of protection was not recommended were cotton textiles, Iron and steel, paper, silver thread and Wire, Magnesium Chloride and sugar. These industries, in the Commission’s view, had already stabilized or had no serious competition to face.

Thus, the tenure of the Interim Board was event-full in certain respects. It functioned under a mixture of influences such as scarcity of commodities, adverse trade balances, direct methods of control and fears of nationalisation. It acquitted itself fairly well and did what was expected of it. But a redefinition of the fundamentals of the policy of protection was long overdue.

While far-reaching changes had taken place in national and inter-national economic outlook, the old notions of tariff protection continued to

influence policy. Consequently, the government announced the appointment of a new Fiscal Commission.

The new commission was asked to examine the working of the policy of Protection since 1922 and to recommend "the future policy which the government should adopt in regard to protection to and assistance of industries, and the treatment and obligations of the industries which may be protected or assisted and also the machinery required to implement such policy."

7. The Second Fiscal Commission, 1949-50:

The Commission rejected the old concept of protection wherein it was viewed as a method of protecting individual industries; Instead, it was accepted as a means to an end —as one of the instruments of policy which the state must employ to further the economic development of the country.

In the commission's view, the protection of industries should be related to an overall plan of economic development so as to avoid unequal distribution of burdens and an uncoordinated growth of industries.

For the purpose of granting protection, the commission classified industries into three groups:

(1) Defence and other strategic industries —they were to be established and maintained whatever the cost.

(2) Basic and Key industries —in their case, the Tariff commission was to decide the form and quantum of protection.

(3) In the case of 'other industries', the commission recommended that "having regard to the economic advantages enjoyed by the industry or available to it and its actual or probable cost of production, it is likely within a reasonable time to develop sufficiently to be able to carry on successfully without protection or assistance and/or it is an industry to which it is desirable in the national interest to grant protection or assistance and having regard to the direct and indirect advantages, the probable cost of such protection or assistance to the community is not excessive."

In addition to defining the conditions governing the grant of protection, the commission gave its opinion on certain specific issues. Firstly, it held that local availability of raw materials was not to be a condition for the grant of protection if the industry possessed other economic advantages such as internal market and availability of labour etc.

Secondly, in determining the comparative advantages possessed by an industry, not only its home market but any possible export market was also to be taken into consideration.

Thirdly, the Commission recommended that ability to satisfy the entire needs of the Home market was not to be regarded as a condition for the grant of protection.

It was enough if the industry was able to "cover a sizeable portion of the internal market within a reasonable period of time."

Fourthly, in so far as an industry used the products of the protected industry as raw material, the commission recommended the grant of "compensatory protection."

Fifthly, the Commission held that industries requiring heavy capital outlay or high degree of specialisation in personnel and plant equipment and subject to severe foreign competition should be assured of protection before their actual establishment.

Finally, the commission recommended the grant of protec-tion to agricultural commodities subject to the limitation that the number of such commodities was small and that they were selected on the basis of their relative importance and the volume of employment they offered.

As regards the methods, the commission examined the suitability of import duties, subsidies, quantitative restrictions, and administrative measures. It accepted the fact that the main reliance had to be placed on the method of import duties. In its view, the method of quantitative restrictions should be used sparingly for temporary periods against abnormal imports.

It found subsidies desirable, and, for this purpose, recommended, the creation of "Development Fund" out of the revenues collected from

protective tariffs. The commission felt that the creation of this fund would enable a consistent and continuing policy to be perused from year to year.

A new feature of the recommendations of Fiscal Commission was the insistence on the fulfilment of certain obligations by the protected industries. In the commission's view, protection can't be demanded as a matter of right; it is a privilege, a concession which carries the obligation of maintaining the highest level of efficiency so that the burden on the community is reduced to the minimum.

The commission charged the protected industry with the obligations of:

(1) Main-taining a reasonable price policy;

(2) Progressively increasing its scale of produc-tion;

(3) Attaining and maintaining the quality of its products in accordance with suitable standard specifications;

(4) Employing up to date methods and practices in production and distribution;

(5) Organising research, training apprentices and providing opportunities for practical training to technical students.

The com-mission laid down that it should be the duty of the tariff commission to review the progress of the protected industries from time to time to ensure that they carried out their obligations.

As regards the machinery for the grant of protection, the commission recom-mended the appointment of a Tariff commission, a permanent statutory body, consisting of live members including the Chairman.

The commission was broadly charged with the function of:

(1) Enquiring into claims for initial protection;

(2) Examining the case for the continuation of protection,

(3) Periodically reviewing the working of protection, particularly with ref-erence to production, costs and prices of protected industries:

(4) Undertaking price fixation enquiries for commodities;

(5) And advising the govt. on matter relating to imposition of anti-dumping duties and retaliatory measures and negotiation of trade agreements and tariff concessions.

In-order to enable the commission to carry out its duties easily and efficiently, it was empowered to summon witnesses and compel them to render essential evidence.

8. Critical Appraisal of the Indian Fiscal Policy:

The Report of the Commission undoubtedly marks a landmark in the develop-ment of economic policy in India. The most outstanding feature of the work of the commission was its comprehensive outlook. Instead of concentrating attention on particular industries, the commission viewed protection in the light of the overall needs of the country as a whole.

Another merit lay in the awareness shown by the commission that tariff protection is not the only method of promoting economic development. That is why it laid stress on other supplementary measures. A more praiseworthy feature was its emphasis on the fact that the grant of protection does not absolve the state of its responsibility.

It recommended sufficient after-care of protected industries. The obligations imposed on the protected industries was another novel and welcome feature. The commission cut new ground in recommending protection to agriculture and embryonic industries. Furthermore, the conferment of statutory powers on the Tariff commission removed a serious lacuna of the old scheme.

Although the commission thus made some significant departures from old policy, yet its findings can't be regarded as free from criticism. For instance, the first of the two conditions laid down for the grant of protection to "other industries" contained the essence of the Triple Formula which, if interpreted as rigidly as the policy of Discriminating protection, would lead to almost the same results.

Another flaw was that the commission based its recommendations on the finality of the Directive Principles and the Industrial Policy statement, 1948. They were supposed to be unchangeable whereas the industrial policy was modified in 1956.

The commission's unscientific approach in making an industry auto-matically eligible for protection if included in the economic plan of the country not only affected the efficiency of the industry but also rendered the authority of the commission ineffective and superfluous.

It is also well to remember that all industries included in the plan did not need protection and that in need could be helped by means other than protection. Tariff policy was, no doubt, made more liberal but its ultimate end was not envisaged. Protection cannot and should not be allowed to continue indefinitely.

Finally, considering the obliga-tions imposed on the protected industry, the commission failed to analyse what would happen to the economic plan of the country if particular industries lost protection for non-compliance with obligations imposed.

The government accepted the recommendations of the Fiscal Commission and set up a Tariff commission in 1952. Between January 1952 and March 1966, the Tariff commission conducted 168 enquiries in all. These included 17 inquiries into industries seeking protection for the first time, 144 inquiries of industries seeking continuance of protection and 7 review inquiries relating to protected industries.

Among the industries enjoying protection were metallurgical industries like Aluminium, Engineering industries, Bicycles, Electric transformers, Automobiles, Ball-bearing, Piston-Assembly etc., Chemicals and allied industries like Caustic soda, Soda Ash, Sheet Glass, Plastic Buttons, Dyestuffs, Calcium Carbide, Calcium Lactate etc.

The only major consumer industry enjoying protec-tion till 1963 was the match industry where a foreign concern reaped the major benefit. The industries which ceased to enjoy protection included Calcium Lac-tate, Engineer's Steel Files, Bicycle, Machine Screw and Grinding Wheels, Sewing Machines, Pencils, Preserved fruits, etc.

The Tariff commission thus played a useful role in the industrial development of India. A few protected industries like Aluminium, electric motors, power and distribution transformers, ball-bearings, bicycles and Calcium Carbide exceeded the Plan targets.

However, by recommending governmental help, which also involved expenditure of public funds, to inessential industries like artificial Silk and cotton, plastic and rayon, the Tariff commission was responsible for diverting scarce resources which could have been otherwise utilised for urgent and essential requirements like food, housing and health.

9. Imperial Preference of the Indian Fiscal Policy:

Imperial Preference implied the policy of preferential trade between the U.K. and her dominations. It was advocated as a means of preserving Imperial unity and of consolidating the British Empire both politically and economically.

The aim was sought to be realised by imposing lower custom duties on goods from the Empire Countries as against the relatively higher duties on goods from the non-empire countries. Although the question of Imperial Preference in the British Empire first took practical shape in 1897, India's participation in such a scheme was rooted only in 1903.

Lord Curzon's Government turned down the proposal on the grounds:

(a) That 1/4 of India's total imports came from non-empire countries and these were of a kind which the British Empire either did not produce or was not in a favourable position to supply;

(b) That India was dependent on her trade with foreign countries for the discharge of her international obligation;

(c) That the government would loose a large portion of the revenue it received from British and colonial imports;

(d) That she might be forced to shape her policy not in accordance with her needs but according to the interests and demand of the empire.

In view of the above, Lord Curzon concluded that from the economic stand-points, India had something, but not perhaps very much, to offer to the Empire, that she had very little to gain in return, and that she had a great deal to loose or risk.

The First World War revived the idea of pooling the resources of the Empire and turning it into one well-knit economic unit. The deliberations of the Imperial WAR Conference of 1917 led to a reversal of policy in

U.K. which now granted, on a unilateral basis, substantial preference to the members of the Empire.

This led to a re-examination of this question in India where the Fiscal commission (1921-22) re-surveyed the issue.

The commission found that Indian exports were not of a kind that could materially benefit from any scheme of preferences because "the economic advantage derived from a preference tends to be more important in the case of manufactured goods than in the case of raw-materials."

In their view, the only preferences of interest to India were those on tea, coffee and tobacco. Even in their case, the advantage was not substantial.

In the case of tea India's main competitor, Ceylon, enjoyed equal preference. Indian trade in coffee was small and there was not any large scope for increased production in India. So far as tobacco was concerned, even with preference it remained at a disadvantage in the English market because duty on tobacco was levied by weight and not by value.

Even otherwise, preference to tea or coffee or jute was of little national value to India because, as Professor Vakil points out, it was "no use obtaining concessions for a foreign Industry established in India in return for concessions in our market to the goods of another country."

On the other hand, the commission admitted that India could not grant extensive preferences to the U.K. "without imposing a serious burden on herself" because the British exports were clearly competitive so far as Indian products were concerned.

In-spite of these overwhelming arguments, the commission amazingly supported Imperial Preference as a practical policy. The reason is not far to seek.

English manufacturers had beseeched the commission to recommend Imperial Preference and, Swayed by the paramount British Imperial interests, the commission advised the Indians to regard these concessions "as a voluntary gift and not as part of a bargain" so as to strengthen "the ties which bind together the scattered units of the Empire."

The minority of the Fiscal commission, on the other hand, drew attention to the fact that the principle of Imperial Preference implied uncontrolled powers of initiating, granting varying and withdrawing preference from time to time consistently with each country's interest and on lines which were not injurious to itself.

They, therefore, concluded that India must "possess the same supreme powers as were enjoyed by the Dominions before Imperial Preference could become for her a matter of practical politics."

Ignoring the Minority's view, the commission recommended the adoption of a selective and discriminatory preference provided:

(a) That no preference was granted on any articles without the approval of the Indian legislature;

(b) That preference did not, in any way, diminish the protection required by Indian industries;

(c) And that it did not involve any appreciable economic loss to India on balance.

Accordingly, a scheme of partial and limited preferences was put into operation during the period 1923-34 when two schemes of "preferences within protection", one relating to Iron and Steel and another relating to cotton textiles, were intro-duced.

The onset of the Economic Depression in 1929 brought about a sea-change in the economic situation of the world. The development of Japan, U.S.A. and Germany as well as the aggressive economic nationalism of the period, posed a great threat to the prosperity of England and she was forced to abandon Free-trade and adopt protectionism.

It was this turn in the economic condition of England which provided the chief motive force for the Government of India's subsequent change of policy, rather "than any desire to rehabilitate India's declining foreign trade."

England, India's largest single customer as well as her chief competitor, offered her a straight choice between being included in the system of

inter-imperial preferences or being left "to herself at a time of declining trade, increasing restric-tions and shrinking markets." Thus faced, it was no longer a question of what India stood to gain but of what she stood to loose by standing outside it.

The Government of India, haunted by the fear of an imminent loss of Empire markets, hastened to improvise a scheme of preferences as an insurance against any possible loss. The U.K. was an important market for Indian exports and refusal to participate in the scheme would have involved the loss of this valuable market.

Besides, currency and exchange rates in the Sterling area were expected to be more stable than in other countries where policies were changing rapidly. In addition, England had also been forced to grant reciprocal preferences.

These considerations induced the Indian Delegation to the Imperial Economic Conference at Ottawa to enter into an elaborate scheme of reciprocal preferences with the U.K. government and other Common Wealth countries.

Under the Ottawa Agreement, India granted preference on 106 items while she received preferential treatment in respect of 40 commodities of which tea, rice, tobacco and jute were the most important. The Agreement, which was to remain in force for three years, was signed on the 20th August, 1932 and was ratified by the Indian Legislative Assembly in November, 1932.

Thus were protected British exports to India against foreign competition although, in the process, the Indian industrialist was thrown at the mercy of the British manufacturer, the biggest monopolist of the Indian market. This, in effect, meant the negation of the policy of discriminating protection.

Furthermore, Imperial Preference failed to achieve even the limited objective of maintaining India's exports to the U.K. Reviewing the working of the policy during 1938-39 to 1948-49, the Indian Fiscal Commission, 1949-50, found that India's share of the export market in

preferred articles in the U.K. fell down while U.K.'s share in the Indian market is preferred articles remained stationary.

Check your progress

1. Write the Tariff of WW1 PERIOD.

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2. Write the fiscal policy of 2nd WW.

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13.3 LETS SUM UP

We may conclude with Ganguly that the policy of Imperial Preference had at least a negative value for the U.K. in so far as it prevented a decline in her exports of hardware, chemicals, nonferrous metals, appliances and apparatus, cycles and paints in which European competition was very severe.

Whether Imperial Preference had a similar negative value for India also is doubtful in view of the fact that the possibilities of a compensatory expansion of demand for Indian exports in countries other than U.K. were not so restricted as was supposed at the time.

13.4 KEYWORDS

Tariff , Excise, Fiscal policy

13.5 QUESTIONS FOR REVIEW

1. Write the imperial preference on Tariffs.

2. Write about the excise structure of WW1.

13.6 SUGGESTED READINGS

The Cambridge Economic History of India by Meghnad Desai

Economic History of India by Tathagata Roy

13.7 ANSWERS TO CHECK YOUR PROGRESS

1. Hint – 13.2
2. Hint – 13.2

UNIT 14 – MONETARY POLICY AND CREDIT SYSTEM

STRUCTURE

14.0 Objective

14.1 Introduction

14.2 Indian Monetary Policy and Credit

14.3 Lets Sum Up

14.4 Keywords

14.5 Questions for Review

14.6 Suggested Readings

14.7 Answer to Check your Progress

14.0 OBJECTIVE

To learn about the Indian monetary policy

To learn about the credit policy

14.1 INTRODUCTION

Monetary Policy is an arm of Public Policy. It is a process by which the government, central bank or monetary authority manage the supply of money or trading in foreign exchange markets. It rests on the relationship between the rates of interest in an economy that is the price at which money can be borrowed and the total supply of money. It, thus, has set objectives and priorities, which are derived from the respective mandates of central banks. It ranges from a single objective of price stability considered to be the dominant objective of monetary policy, to multiple objectives that also include growth and financial stability.

14.2 INDIAN MONETARY POLICY AND CREDIT

Monetary Policy is an important aspect of overall economic policy. An appropriate monetary policy contributes to economic growth by adjusting money supply to the needs of growth, by directing the flow of funds in the required channels and by providing institutional facilities for credit in specific fields of economic activities. In this way, monetary policy helps a healthy growth of the economy. Monetary Policy consists of the measures taken by the central banking authority to regulate the cost and availability of credit. Monetary and credit policy operate through five interrelated factors; (i) the availability of credit, (ii) the volume of money, (iii) the cost of borrowing,(iv) the prices of capital assets and (v) the general liquidity of the economy. One of the fundamental tasks of monetary authorities in the growth context remains the creation of conditions for the effective mobilisation of the supply of actual and potential savings through the promotion of financial intermediaries and the creation of a spectrum of financial assets on the one hand and on the other the effective investment of these resources through the adaptation of the credit structure to sub-serve the needs of development.

Definition

Monetary Policy has been defined differently by various economists. According to Paul Einzig, "Monetary Policy includes all monetary decisions and measures irrespective of whether their aims are monetary or non-monetary and all non-monetary decisions and measures that aim at affecting the monetary system". Harry Johnson(1963) defines monetary policy as, "policy employing central banks control of the supply of money as an instrument for achieving the objectives of general economic policy". According D. Jha, "Monetary Policy is one important segment of an overall financial policy which has to be operated in the overall milieu prevailing in the country". Reserve Bank of India considers monetary policy for the use of instruments within the control of central bank to

influence the level of aggregate demand for goods and services. Central banking instruments of control operate through varying the cost and availability of credit, those producing desired changes in the asset pattern of credit institutions primarily the commercial banks. Thus, RBI is relatively more explicit in defining the monetary policy.

The History of Monetary Policy

Monetary Policy is as old as monetary system or as money itself. It has a long and chequered history since the days of mercantilism. Evidence proves the existence of monetary management in Greece. But before 1914, the whole thinking about monetary policy was based upon the idea of automatic gold exchange system. After World War I, the gold exchange standard collapsed and it is then the modern genesis of monetary policy took place. The 1920s inflation in Germany, and the two international conferences, one in Brussels in 1920 and the other one in Geneva in 1922, compelled the thinking about a new monetary system. The depression of the 1930s provided further stimulus to the thinking of reforms in the field of monetary management. The horizon of monetary policy has greatly widened in the recent past.

The origin of monetary management in India can be traced back to time immemorial. The reference about the Panis, the moneylenders of Southern India, in Rig Veda is an evidence of the developed state of banking or credit system in the vedicage, although the date of the origin of the coins and credit instruments is lost in the midst of antiquity. In the Mauryan era, the system of currency, credit and coinage was fully developed. Kautilya devotes a chapter in his classical book the Arthashastra on rules for mining and credit. The history of monetary management and policy in terms of central banking practices in India can be traced to as far back as January 1773, when Lord Hastings, the then Governor, and later on, the first Governor General of British India, placed before the Board of Revenue his plan for General Bank in Bengal and Bihar. The Royal Commission on Indian Finance and Currency also known as the Chamberlain Commission was set up in 1913 with J M Keynes as one of the

members who prepared a blueprint for the establishment of an Imperial Bank of India. The bank came into existence on January 1921 by amalgamating the three presidency banks as a commercial bank with some of the functions of the central bank also. In August 1925, the Royal Commission on Indian Currency and Finance also referred the Hilton Young Commission was appointed. The Commission observed that India was the only big trading country in which the currency and note issues were under direct government control. It recommended several measures to reform the monetary system. With the recommendations of the Young Commission (1925) and the Central Banking Enquiry Committee (1931),the Reserve Bank of India was established through Reserve Bank of India Act, 1934.

However, with a strong background of monetary changes, the monetary policy assumed importance since the early seventies, when strong inflationary pressures began building up in the economy. In December 1982, a committee under the chairmanship of Sukhamoy Chakravarty was appointed to undertake a review of the working of the monetary system and suggest measures for improving the effectiveness of monetary policy as an instrument for promoting the basic objectives of planned economic development. The committee made a detailed study about monetary management and made path-breaking recommendations. There were further many committees and working groups constituted to study the functioning of the financial sector and to recommend changes. The prominent among them were Narasimham Committee I and II, Tarapore Committee on Capital Account Convertibility, the Verma Committee on Restructuring of Weak Banks and the Advisory Group on Transparency in Monetary and Financial Policies. The committees have changed the way monetary policy functions.

Objectives of Monetary Policy in India

The changing economic priorities and views have led to changes in monetary policy. Hence, the focus is on demarking the objectives of monetary policy, this has gained further significance in the context of the

increasing stress on autonomy of the central bank. Thus, the main objectives or goals of monetary policy are:

1. Price Stability

2. Economic Growth

3. Full Employment and

4. Maintenance of Balance of Payments Equilibrium

The relative emphasis on any one of the objectives is governed by the prevailing circumstances.

1.Price Stability

This has been a dominant objective of monetary policy. Fluctuations in the prices bring uncertainty and instability to the economy. Rising and falling prices are both not desirable because they bring unnecessary loss to some and undue advantage to others. Therefore, in this context monetary policy has assumed paramount importance. It aims at preventing maladjustments, that is, at eliminating the causes of recession. To achieve this, investment finance has to be regulated through appropriate variations in the rate of interest in the capital market. Rate of interest is a vital link that connects the volume of money and investment in a given economy.

A Policy of price stability keeps the value of money stable, eliminates cyclical fluctuations, brings economic stability, helps in reducing inequalities of income and wealth, secures social justice and promotes economic welfare. However, there are certain difficulties in pursuing a policy of stable price level.

The problem is deciding the type of price level to be stabilised. There is no specific criterion with regard to the choice of a price level. Innovations may reduce the cost of production but a policy of stable prices may bring larger profits to producers at the cost of consumers and wage earners. Again, in an open economy which imports raw materials and other intermediate products at high prices, the cost of production of domestic goods will be high. Thus, a policy of stable prices will reduce profits and retard further investment.

Under these circumstances, a policy of stable prices is not only inequitable but also conflicts with economic growth. Therefore, price stability means stability of some appropriate price index in the sense that we can detect no definite upward trend in the index after making proper allowance for the upward bias inherent in all price index. Price stability can be maintained by following a counter-cyclical monetary policy, that is easy monetary policy during a recession and a dear monetary policy during a boom. In a nutshell, both inflation and deflation need to be regulated appropriately by the central bank.

2.Economic Growth This objective of monetary policy has acquired considerable significance in recent years. Economic growth is defined as the process whereby the real per capita income of the country increases over a long period of time. Monetary policy can lead to economic growth, by having a control on the interest rate which is inversely related to investment. By following an easy credit policy and lowering interest rates, the level of investment can be raised which promotes economic growth. Monetary policy also contributes towards growth by helping in maintaining the stability of income and prices. By moderating economic fluctuations and avoiding depression, monetary policy helps in achieving the growth objective. Because fluctuations in the rates of inflation have an adverse impact on growth and monetary policy also helps in controlling hyperinflation. Moreover, tight monetary policy affects small firms more in comparison to large firms, and higher interest rates have greater impact on small investments in comparison to large industrial investment. So, monetary policy needs to be formulated in the way that it may encourage investment and simultaneously control inflation in order to enhance growth and put a control on economic fluctuations.

3.Full Employment

Full-Employment is the ultimate objective of monetary policy. According to Keynes, "full employment means the absence of involuntary unemployment". That is full employment is a situation in which everybody who is willing to work and able to work gets work and

achieves this, Keynes advocated increase in effective demand. Burner (1961) considers "full employment is a situation where all qualified persons who want jobs at current wage rate, find full time jobs"..

4. Balance of Payments Equilibrium

This objective of monetary policy has emerged since the 1950s. The emergence of this objective is due to the phenomenal growth in global trade as against the growth of international liquidity. A deficit in the balance of payments is said to retard the attainment of other objectives as it reflects excessive money supply in the economy. As a result, people exchange their excess money holdings for foreign goods and securities. Under a system of fixed exchange rates, the central bank will have to sell foreign exchange reserves and buy the domestic currency for eliminating excess supply of domestic currency. This is how equilibrium will be restored in the balance of payments.

If the money supply is below the existing demand for money at the given exchange rate, there will be a surplus in the balance of payments. Consequently, people acquire the domestic currency by selling goods and securities to foreigners.

They will also seek to acquire additional money balances by restricting their expenditure relatively to their income. The central bank, on its part, will buy excess foreign currency in exchange for domestic currency in order to eliminate the shortage of domestic currency.

The Sukhamoy Chakravarti Committee was appointed in 1982 to review the working of monetary system. The committee submitted a comprehensive report on the objectives in 1985, defining the role of monetary policy thus:

i. Mobilisation of savings of the community and enlargement of the financial savings pool.

ii. Promoting efficiency in the allocation of the savings of the community to comparatively more productive purposes in accordance with the national economic goals.

iii. Enabling the resource needs of major enterprises in the country.

iv. Promoting price stability.

v. Promoting an efficient payment system.

Targets and Indicators of Monetary Policy

The choice of targets and indicators of monetary policy are based on the objectives of monetary policy. There are three targets of monetary policy; money supply, availability of credit and interest rates. The central bank cannot directly control output prices, hence it selects the growth rate of money supply as an intermediate target. Friedman suggests that the money supply should be allowed to grow steadily at the rate of 3 to 4% per annum for a smooth growth of the economy and to avoid inflationary and recessionary tendencies. The availability of credit, and interest rates are the other two target variables of monetary policy. They are often referred to as the "money market conditions". The monetary authority can influence the short-term interest rates. It can change credit conditions and affect economic activity by rationing of credit or other means. The central bank influences economic activity by following an easy or expansionary monetary policy through reducing short-term interest rates and a tight or contractionary monetary policy through rising short-term interest rates.

Money supply and interest rate are intermediate targets of monetary policy. They are also the competing targets, as the central bank faces a trade off as it can aim either at increasing the money supply or maintaining a level of interest rate. By targeting money interest rate it would be neglecting money supply. The general consensus of economists and policy makers is towards money supply as it is measurable, while there are a variety of interest rates. The money supply linkage with nominal GNP is more direct and predictable than the interest linkage with nominal GNP of the nation.7.6: Instruments of Monetary Policy in India There are several direct and indirect instruments that are used in the implementation of monetary policy.

- Cash Reserve Ratio (CRR): The share of net demand and time liabilities deposits that banks must maintain as cash balance with the Reserve Bank of India.
- Statutory Liquidity Ratio (SLR): The share of net demand and time liabilities deposits that banks must maintain in safe and liquid assets, such as, government securities, cash and gold. Changes in SLR often influence the availability of resources in the banking system for lending to the private sector.
- Refinance Facilities: The sector-specific refinance facilities aim at achieving sector specific objectives through provision of liquidity at a cost linked to the policy repo rate. The Reserve Bank has, however, been progressively de-emphasising sector specific policies as they interfere with the transmission mechanism.
- Liquidity Adjustment Facility (LAF): This consists of overnight and term repo/reverse repo auctions. The RBI has progressively increased the proportion of liquidity injected in the LAF through term-repos.
- Term Repos: The term repos are introduced by the RBI since October 2013. They are of different tenors (such as 7/14/28 days). They are used to inject liquidity over a period that is longer than overnight. The aim of term repo is to help develop inter-bank money market, which in turn, can set market based 236benchmarks for pricing of loans and deposits, and through that improve transmission of monetary policy.
- Marginal Standing Facility (MSF): A facility under which scheduled commercial banks can borrow additional amount of overnight money from the Reserve Bank by dipping into their SLR portfolio up to a limit (currently two percent of their net demand and time liabilities deposits) at a penal rate of interest (currently 100 basis points above the repo rate). This provides a safety valve against unanticipated liquidity shocks to the banking system. MSF

rate and reverse repo rate determine the corridor for the daily movement in short-term money market interest rates.

- Open Market Operations (OMOs): These include both, outright purchase or sale of government securities (for injection /absorption of liquidity).
- Bank Rate: It is the rate at which the RBI is ready to buy or rediscount bills of exchange or other commercial papersof commercial banks. This rate has been aligned to the MSF rate and, therefore, changes automatically as and when the MSFrate changes alongside policy repo rate changes.
- Market Stabilisation Scheme (MSS): The instrument for monetary management was introduced in 2004. Surplus liquidity of a more enduring nature arising from large capital inflows is absorbed through sale of short-dated government securities and treasury bills. The mobilised cash is held in a separate government account with the RBI. The instrument thus has features of both SLR and CRR. The

Reserve Bank of India seeks to influence monetary conditions through management of Liquidity by operating in varied instruments. Since 1991, the market environment has been deregulated and liberalised where in the interest rates are largely determined by the market forces.

Process of Monetary Policy Formulation in India

The process of monetary policy formulation in India had largely been internal with only the end product of actions being made public. The process has overtime become more consultative, participative and articulate with external orientation. The process has now been re-engineered to focus on technical analysis, coordination, horizontal management and more market orientation. The process entails a wide range of inputs involving the internal staff, market participants, academics, financial market experts and Reserve Bank's Board.

Implementation of Monetary Policy in India

Greater information on the dissemination and policy communication could lead to better policy outcome. For example, the US Federal Reserve, since 1994, appears to have been providing forward guidance, while the European Central Bank appears to be in the mould of keeping the markets informed rather than guiding it. In India, a middle path is followed by sharing of both information and analysis.

The stance of monetary policy and the rationale are communicated to the public in a variety of ways, the most important being the Governor's quarterly monetary policy statements. Further, the policy measures are analysed in various statutory and non-statutory publications, speeches and press releases. Information on areas relating to the economy, banking and financial sector is released with stringent standards of quality and timelines. Dissemination of information takes place through several channels.

International gold standard will be considered. The negative consequences of the high ex-change rate for trade will then be examined followed by a discussion of how monetary policy was used to facilitate Indian debt remittances to Britain. Finally, there will be a brief comparative discussion of how the deflationary monetary policies pursued by the Indian authorities were incompatible with the great Depression. Economic performance in Imperial Indian all Ferguson (2003: p.1) has argued that "while it is convenient for contemporary rulers in countries like Zimbabwe to blame their problems on the 'legacy of British rule', the reality is that British rule was on balance conducive to economic growth." Drawing on modern-day research in the field of development economics, he illustrates that enforced openness to trade could have been a force for convergence (sachs & warner, 1995) and that capital flows could have also acted as a channel for economic development (Clemens & Williamson, 2000). he also supports the proposition by cain and Hopkins (1993) that Britain's "gentlemanly capitalism" placed a heavier emphasise on finance than British ex-ports and extrapolates from this that British imperial policy offered "at least the opportunity of economic convergence," by creating macro institutions which conformed to a "London consensus" emphasising property rights and liberal economic policies (ferguson2003, p.19).

writing on Indian finance, Sunderland (2013, p.213) argued that "the io [India office], the bank of England, the treasury and city institutions were well aware that they stood or fell together" and thus they were willing to extend "costly favours on the understanding that these would eventually be reciprocated." thus on balance financial policy was largely favourable to India's interests. yet an interesting caveat to the pro-imperialism thesis is recognised by Ferguson himself; the case of India. Ferguson asks; "why was Indian economic performance so much worse than that of the Dominions?" while the world economy generally performed worse during the interwar years than in the years before the outbreak of the first world war, India fared particularly badly. as the figures below demonstrate, growth in real g DP percapita was demonstrably lower than in most other countries. Meanwhile, India's percent-age share of the value of world trade (in gold dollars) fell from 3.75.

CREDIT POLICY

We began the previous chapter by identifying three dimensions of land rights – the type of ownership, tenants' rights, and the right to transfer – to categorise the diversity of land tenures in colonial India.2 Chapter 3 focused on the first two dimensions, the type of ownership (raiyatwari and zamindari) and the rights of tenants. This chapter introduces the third dimension, transferability. This leads us to discuss credit, for two related reasons. In a largely agricultural economy once population has grown sufficiently and land becomes the scarce factor, it is potentially the most important form of collateral. And to the extent land is actually used as collateral or seized in lieu of repayment, credit transactions can become a cause of land transfer. The discussion of credit raises the issue of contract enforcement. Credit involves two transactions, borrowing and repayment, which are separated in time, leaving room for opportunistic behaviour by both parties. The lender is, of course, worried about repayment. The borrower, especially if illiterate or financially unsophisticated, may be concerned about fraud. These issues need to be addressed if credit markets are to function smoothly. So we study the regulation of credit contracts, not only via legislation, but also in the functioning of the courts and the implementation of their decisions. Finally, putting together our discussion of land and credit markets, we

will venture some hypotheses regarding how the structure of property rights and contract enforcement might have affected the incentive to invest and the availability of funds for investment. Rural credit was not a central concern of the Company at the beginning of its rule. Its stance changed by the second half of the nineteenth century, with the growth of population, the expansion of cultivated area, and increasing cultivation of crops for sale. The demand for credit grew and, in parallel, there was an increase in the value of the most important form of collateral, land. It was inevitable that some peasants would borrow against their land and lose it after defaulting, or would sell it to pay off loans. One might have expected that the state, especially given the influence of laissez-faire views in Britain, would view this phenomenon with some equanimity as part of the normal functioning of a market economy, in which there are winners and losers. However, this was not to be. When land loss by peasants led to protests and even "riots" the Raj reacted with great anxiety, second-guessing the legal and institutional changes it had introduced, and legislating extensively (in some regions) to prevent or discourage land transfers in relation to repayment or default on debt. Why did the Raj react so strongly?

The Mutiny of 1857 was one reason. This made the Raj fearful of rapid social change, which they believed to be its cause. But there was also a prior and subsequent history of agrarian rebellion and protest. Taken together, they led the Raj to be cautious, to not introduce policies that might undermine the agrarian social structure. This required an understanding of the key elements of this structure. The notion of the "Village Community" provided an organising idea. From the early nineteenth century at least, British officials in various regions had embraced to different degrees a view of the Indian village as a largely self-contained entity. It had internal systems of governance. It was somewhat disconnected from the larger polity – regimes could come and go without affecting it significantly. The ownership of land and responsibility for paying taxes was shared within the community. The village itself contained providers of various services, from priests to carpenters. The "Village Community" formulation received particularly strong support from officials in the North-Western Provinces, with

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Charles Metcalfe's observations regarding villages near Delhi being especially influential.4 And following the final annexation of Punjab (1849), observation of social organisation in its "tribal" north western region (discussed below) provided further impetus to the notions of "jointness" of ownership of property and village political cohesion. In 1889 Henry Maine wrote: "It was not till the English conquest was extending far to the north-west, and till warlike populations were subjugated whose tastes and peculiarities it was urgently necessary to study, that the true proprietary unit of India [our italics] was discovered."5Given this understanding, the Raj concluded that political stability required the maintenance of the economic and political cohesion of the village, which would be undermined if "immigrant" and or "non-agriculturist" lenders took possession of land. Legislation was passed in several regions in the late nineteenth and early twentieth centuries to discourage such transfer, seeking to undermine the use of land as collateral in credit transactions, or disallow its seizure after default. The spirit of these laws was to protect the reckless and naïve borrower both from the lender and from himself. After late nineteenth and early twentieth century discussion and legislation pertaining to land transfer, the next (potentially) important legislation was the Usurious Loans Act of 1918. And after the Depression, legislation to protect borrowers from predatory lenders and reduce their debt burdens was driven by a new set of factors -- the growth of nationalist and peasant movements, and the participation of Indians in provincial governance. By this point, the shortcomings of the judicial system, which made it hard to enforce credit contracts, had also been exposed in some regions. Given this understanding, the Raj concluded that political stability required the maintenance of the economic and political cohesion of the village, which would be undermined if "immigrant" and or "non-agriculturist" lenders took possession of land. Legislation was passed in several regions in the late nineteenth and early twentieth centuries to discourage such transfer, seeking to undermine the use of land as collateral in credit transactions, or disallow its seizure after default. The spirit of these laws was to protect the reckless and naïve borrower both from the lender and from himself.

Ideas for growthwww.theigc.org After late nineteenth and early twentieth century discussion and legislation pertaining to land transfer, the next (potentially) important legislation was the Usurious Loans Act of 1918. And after the Depression, legislation to protect borrowers from predatory lenders and reduce their debt burdens was driven by a new set of factors -- the growth of nationalist and peasant movements, and the participation of Indians in provincial governance. By this point, the shortcomings of the judicial system, which made it hard to enforce credit contracts, had also been exposed in some regions. The remainder of this chapter describes and analyses this history, linking it to our discussion of landownership and tenant rights. We first discuss law pertaining to the transferability of land in the raiyatwari regions, where there was little or no legislation to protect tenants. We then consider zamindari regions where, as we have seen in chapter 3, tenants were protected to varying extents. Punjab, a late and major conquest, is often considered sui generis, so we devote a separate section to it. A discussion of issues of enforcement of credit contracts, especially as pertaining to land transfer following court decrees, follows. The last two sections of this chapter discuss developments in the late colonial period, when aggressive policies to reduce debt burdens and regulate lenders were introduced, and the strain on the judicial system became more visible in some regions. In the conclusion we will argue that because law and institutions were so variable across regions and time, it is difficult to generalise regarding their implications for economic growth. We can identify locations in which at specific times law likely constrained growth. But there are also instances where, if growth did not occur, the causes will have to be found elsewhere, not in property rights or contract enforcement.

Raiyatwari regions: Bombay and Madras

The region known as the Bombay Presidency was conquered piece-by-piece, but a key date was 1818, the defeat of the Maratha Peshwa based in Poona (Pune), in the Bombay Deccan. Subsequent Company rule introduced several changes that affected credit markets. The evolution of debtor-lender relations over the next several decades led to the passing of the Deccan Agriculturists' Relief Act (DARA hereafter), an important and influential legislation. There were two critical innovations

introduced by British rule. Under the raiyatwari system there were now clear titles to land which could be sold, pledged as collateral, or seized in lieu of debt repayment. 6 Second, the adjudication of disputes moved out of the village, where methods were informal, to the district courts established by the Company where procedures were more formal and documentary evidence more important. The net effect of these changes, and increases in the value of land, was to encourage inflow of lenders, including immigrants who did not have strong local connections. This had one clear potential benefit: there was more credit available. But, as official reports and some historians tell the story, it changed borrower-lender relations in ways that hurt the peasants.

It appears that, in the pre-colonial setting, a rural lender-borrower dispute was usually adjudicated by a Panchayat or village council (see also chapter 2).7 Since the Bombay Deccan was a poor and dry region, immigrant lenders were an important source of credit.8 They were at a disadvantage when disputes were adjudicated, because they were appealing to members of village councils to rule against their peers. The Panchayats also seem to have practiced what we would today call limited liability, in the sense that they would not take the shirt off the borrower's back.9 There was, furthermore, a ceiling on the amount the Panchayat would award the creditor - twice the outstanding principal, irrespective of how much interest had accumulated. This rule, known as Damdupat, has a long history. 10 There are many references to it in treatises on Hindu Law dating back almost two thousand years.11 There was also a rule favouring the creditor, called the Pious Obligation, which made the sons and even grandsons liable for their ancestor's debts, even beyond the extent of their inheritance. Like Damdupat, the Pious Obligation could be found in ancient texts, but perhaps more to the point, it was honoured in practice.12 The Panchayat did not necessarily enforce its decrees. The lender and his employees were allowed to use coercive methods up to a point. This likely limited the geographic scope of any lender's activity. Mountstuart Elphinstone, the Governor of Bombay and a "conservative" in the sense of favouring gradual institutional change, wanted the Panchayat to remain an important judicial institution. Accordingly, the Regulations of 1827, which underpinned the legal

structure that was to develop, allowed a role for it. However, the institutions of the new political order were the ones that commanded more respect. Panchayats, therefore, were hardly used.13 Dispute resolution moved to the hierarchical system of courts, modelled on the Bengal/Mughal judicial administration set up by the Company. The new judicial system differed from the Panchayat-based adjudication in several ways. The courts placed more weight on documentary evidence. Dispute resolution did not occur in the village. In fact, the district court was often several days of travel away for the borrower. The state itself would enforce contracts. And though the Regulation of 1827 placed limits on what assets could be Ideas for growthwww.theigc.orgseized in lieu of debt repayment, imposed an interest-rate ceiling (12%), and retained damdupat, imprisonment was one possible punishment, which diluted the impact of borrower protections. The impact of these changes depended on who the borrowers and lenders were. But much of the discussion and legislation in the Bombay Deccan was driven by the relationship between the professional trader-lenders, especially immigrants, and the peasants. As the nineteenth century unfolded, several British officials made a plausible case that institutional innovations had favoured the lender. The latter was more at home with new legal procedures, more adept at book-keeping, literate, and could better bear the costs and time associated with litigation. The adjudication was now not being done by a group of the borrower's peers.

There was now a judge, driven by the letter of the law, relying heavily on the written word. Finally, the lender could rely on the state to help enforce its judgment, including seizure of land. After an early period of heavy taxation, taxes were lowered significantly by 1850. Population, cultivated area, and commercial agriculture expanded. As the demand for credit increased, more immigrant lenders moved in, relying on the new British-Indian legal apparatus for loan recovery. From quite early on, British officials were concerned about two related outcomes of this process: first, they worried that unsophisticated peasants were being defrauded by lenders and second, that land was passing from the hands of traditional cultivators to the immigrants who had no connection with land.

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In parallel with the political fears there was, at the ideological level, what Thomas Metcalf has called "the creation of difference" – the notion that Indian (at least agrarian) society was not prepared for British institutions.16 In our context, Raymond West, a judge in the Bombay High Court, provided a clear statement of this perspective. West wrote a highly influential monograph in 1873 entitled The Land and the Law in India, arguing that it was a mistake to allow land to be transferable. It gave the peasant too much access to credit (the full value of land), but s/he was not capable of handling it appropriately. This sentiment was echoed by officials in other regions, and the right to borrow against land was often described as a "fatal BOON'.

The 1860's saw a boom in cotton cultivation in the Bombay Deccan, suitable due to its black soil, because the American Civil War disrupted supply of cotton. Debt expanded considerably in this period. Prices fell after the Civil War ended, and in the late 1860's and early 1870's there were other "shocks" to the system such as increases in land taxes and adverse weather conditions. Peasants defaulted on loans and lost their lands to moneylenders. As resentments grew, moneylenders were sporadically attacked, but the crisis finally came in 1875, when peasants in four districts (Poona, Ahmednagar, Sholapur, and Satara) "rioted." The riots occasionally took the form of violence against moneylenders, but more often the rioters simply wanted to destroy the "bonds" that were proof of their debts. Some historians have questioned the magnitude of the Deccan Riots, and Neil Charlesworth once provocatively described them as a "minor grain riot." But for many of the Raj's officials this was confirmation of their fear that British innovations in land rights and law were destabilising Indian society in a politically threatening way.

What was to be done? The Deccan Riots Commission was set up to address this question. After it produced a voluminous report, the Deccan Agriculturists' Relief Act (DARA) was passed in 1879, applying to the four districts where the riots had occurred. The Act did not accept Raymond West's radical suggestion – a ban on land transfer – and focused instead on the legal process. The Act had numerous provisions. Village-level "conciliators" were appointed to facilitate arbitration, and nearby courts with munsifs (judges, usually Indian, in lower courts) were

set up to adjudicate disputes involving small sums. Mortgages had to be registered, and ex-parte judgments (absent the defendant) were discouraged. The interest rate ceiling, which had been abolished in 1855 after the abolition of usury laws in Britain, was re-instated. But the most important change was that judges were empowered to "go behind the bond," that is, investigate the entire history of transactions, and use their discretion to reduce payments, or order payment in instalments. Meanwhile, what of the two measures in Hindu law, the Pious Obligation and Damdupat? The Pious Obligation had lost its bite after the passing of the Bombay Hindu Heirs' Relief Act of 1866 which declared that a son was liable for his father's debts only to the extent he inherited his property. Damdupat was part of the 1827 regulation, as mentioned above. It was included in DARA. It remains on the books in Maharashtra and a few other places in India.

The impact of the DARA, which was extended to Sindh in 1901 and the rest of the Bombay Presidency in 1905, was controversial. While the officials associated with its formulation and implementation praised it, critics also alleged that it was driving out the lenders and credit was drying up. Borrowers and lenders colluded to side-step DARA by disguising loans as sales. The borrower would "sell" the land at a certain price, and buy it back later at a higher price, with the interest embedded in the price differential. DARA had to be modified so that even land sales could be scrutinised.

Recent research shows that DARA achieved some of its procedural goals: for instance, the incidence of ex-parte decrees declined dramatically. Judges used their discretion to reduce repayments to creditors. However, while credit did contract, this does not seem to have hurt "real" outcomes such as cropped area and yield. This finding is consistent with work on present-day India which suggests that greater access to credit does not necessarily promote agricultural growth. It appears that DARA was, overall, a moderately successful intervention, giving the borrower some protection without materially undermining the supply of credit. It can be interpreted as an exercise in moderation, moving away from an extreme in which the lender had too much power

vis-à-vis the usually illiterate borrower, to one where they were more evenly matched.

Meanwhile, what of the other major raiyatwari region, Madras? The Madras administration's attitude to land transfer was in complete contrast to that of Bombay. It argued that in Madras most lenders were local "agriculturists", not immigrant trader-lenders. So, even if land did change hands, it would not cause political unrest. Moreover, the Inspector-General of Registration of Madras argued that the new owners "in addition to capital have sufficient education and intelligence to adopt improved methods of cultivation when they are found to be profitable." His understanding of the credit market was directly at odds with the spirit of DARA. DARA had worried that loan recovery was too easy for the lender. The Madras Inspector-General thought interest rates were high because loan recovery via the courts was too costly.

The Zamindari regions: Bengal and Madras presidencies

We have argued in the previous chapter that, before the Tenancy Acts, zamindars in Bengal and Madras (under the Permanent Settlement) had good incentives to invest, since they would reap the benefits, with no additional taxes to pay. And, of course, there were no restrictions on their right to transfer some or all of the zamindari, so they did not, in principle, lack access to funds. However, after tenancy legislation was passed, incentives for landlords weakened because it was more difficult to raise rents, or evict tenants. But the strengthening of tenants' rights meant that they could now have greater confidence in profiting from their investments. Where would the funds come from? The obvious option was to mortgage the occupancy right. Was this permitted? Depending on the zamindari region and the period in question, the answer was "Yes", "Maybe, or "No." We discuss these cases sequentially.

The "yes" case, in the Madras Presidency, is easy to explain. We have seen above that in the late nineteenth century the Madras Administration had rejected out-of-hand the idea of restrictions on the transfer of raiyatwari rights. When the Madras Estates Land Act was passed in 1908, the intention was to give the zamindari occupancy tenant a status

similar to that of raiyatwari owner. So there were no restrictions on transfer of the occupancy right, or on borrowing against it. In principle, the Madras zamindari occupancy tenant had both the incentive to invest (because of protection from arbitrary rent increases and eviction) and the capacity to invest, because of the ability to collateralise the occupancy right.

The "maybe" case is more complex. The framers of the Bengal Tenancy Act of 1885 had left the issue of whether the occupancy right was transferable to "custom" or "usage." In 1894 the Government of India, driven by the political concerns we have discussed, communicated with various local governments including Bengal on the subject of restrictions on land transfer. The Government of India suggested to the Bengal government that "the effect of the Bengal Tenancy Act has been in many instances to place the raiyats at the mercy of the moneylenders." The Government of Bengal responded that since the passage of the Bengal Tenancy Act there had indeed been a substantial increase in the number of transfers of occupancy right registered, though some of this may have been simply better reporting. But most of this was not to moneylenders. Moreover moneylenders in Bengal were not "the grasping and foreign moneylenders of other parts, but persons who are agriculturists themselves, and who have a little capital which they lend out at usury." Supporting this view, the Government of Bengal enclosed a long letter from M. Finucane, who was a strong supporter of tenant rights. Using data on more than 47,000 transactions, Finucane argued that land was mainly going to other peasants and only 1 in 7 transfers was to Mahajans (moneylenders). And, he argued, "of these so-called Mahajans, however, but a small portion were probably other than substantial raiyats themselves, for these are the chief money-lenders in rural Bengal." Far from being concerned about land transfer, the Government of Bengal worried that though "custom" usually allowed free land transfer by occupancy tenants, courts might not endorse this view. The 1894 letter quoted above worried that "it is possible that the technical and narrow views which the Civil Courts may take of the evidence required to prove "custom"...may cause an ever-widening breach between the law as administered by the Courts and the general practice, so that it may

eventually be necessary to interpose by legislation to set the Courts right." This concern was well-founded, as illustrated by Palakdhari Rai versus Manners and Others.

In 1895, Palakdhari Rai, a zamindar, brought fourteen suits against Manners and Others regarding their purchase of occupancy rights in his estate. The central issue was whether or not transfer without the consent of the landlord was consistent with "custom." The munsif's court had ruled for the plaintiff (the zamindar), but this decision had been reversed by the Subordinate Judge. The zamindar appealed to the High Court which, citing a prior judgment of the Privy Council, held that for the transfer to be valid "it would be necessary in these cases either to prove the existence of the usage on the landlord's estate, or that it is so prevalent in the neighbourhood that it can be reasonably presumed to exist on that estate." Criticising the Subordinate Judge the court noted that the documents he had cited showing transfers "all relate to other villages" and it was not clear what bearing this had "upon the question of the existence of usage in the two villages in which the holdings have been purchased by Manners and which are the subject matters of this suit."

The High Court required the case to be retried. This ambiguity in law was resolved only when the Bengal Tenancy Act was amended in 1928, explicitly allowing the occupancy tenant to transfer his/her right upon payment of 20% of the sale price to the zamindar. This requirement of 20% payment was removed in 1937.The transferability of the occupancy right thus remained in legal limbo for a considerable length of time, left to the best judgment of the court regarding "custom". It is likely that this undermined the tenant's ability to borrow against this right. Land law in Bengal in (say) 1900 thus seems to have undermined the zamindar's incentive to invest (because the Tenancy Act made it harder to raise rents or evict tenants), and the tenant's capacity to invest (since the occupancy right could not necessarily be used as collateral). It is likely that some investment did occur, in part because, as we have seen in the last chapter, the provisions of the Tenancy Act were evaded, with zamindars illegally raising rents. And tenants could borrow from their zamindars, with their occupancy right as de facto collateral: the surrender of occupancy right

could then be described as being due to default in rent. Still, even if the Bengal Tenancy Act was beneficial on grounds of equity, the uncertainties created by it may have undermined economic growth. Later legislation (see below) aggravated the problem.The “No” case pertains to strong “protective” legislation in colonial India, which was passed in the adivasi areas. Adivasi translates roughly as “original inhabitant.” Adivasis’ cultural and economic practices could differ significantly from those of the more numerous Hindu peasant communities. In the colonial period they were called “tribes” and in today’s official parlance “Scheduled Tribes.” We will use the term adivasi because it is more respectful. It will also help avoid confusion with a different use of the word “tribe” in the section on Punjab, below. As we noted in the last chapter, conflict between adivasis and the colonial state/zamindar/moneylender had begun as early as 1832 in the Permanently Settled portions of eastern India.

Our focus here is on the Santals, adivasis who were proficient at forest-clearing. By the mid-1850’s they had a substantial presence in an area within the present-day Indian state of Jharkhand, where, depending on location, they were raiyatwari-type owners or zamindari tenants. After protracted tensions with zamindars (over evictions and rent-increases) and moneylenders (over land transfers) the Santals rebelled in 1855. This was a large-scale insurrection which the colonial state eventually dealt with harshly, militarily, with perhaps as many as 10,000 Santals killed. After the rebellion was crushed, the administration attempted to address its causes. A new district called the Santal Parganas was created, which was designated a “Non-Regulation” area, in that the rules and laws passed for the rest of British India would not automatically apply. According to Act XXXVI of 1855, “No law which shall hereafter be passed by the Governor-General of India in Council shall be deemed to extend to any part of the said districts, unless the same shall be specially named therein.” There would be a more paternalistic form of administration, with a strong role for the executive, especially revenue officials. However, in 1863, the Advocate-General declared the formulation quoted above ultra vires, so the “non-regulation” status became invalid. Following this, under the provisions of the weak Bengal

Rent Act of 1859 (discussed in the previous chapter), zamindars increased rents. A rule imposing an interest rate ceiling of 25% was now declared void, and “the district was fast relapsing into the position from which it had been rescued by Act XXXVII of 1855.” Renewed political unrest in 1871 led to fresh legislation in 1872.

Check your progress –

1. Discuss about the monetary policy between the 2 world wars.

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2. What is credit policy.

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14.3 LETS SUM UP

MONEY AND CREDIT, 1858–1947 The singularity of India's monetary experience derives from the fact that India witnessed practically every type of monetary regime, passing successively from a silver standard to a managed inconvertible silver currency, then almost fortuitously to the gold exchange standard; subsequently to a paper standard, a gold bullion standard, and after 1931 to a sterling exchange standard. Also, India moved from a fixed fiduciary to a proportional reserve system without ever adopting the 100 percent reserve Currency Board system of the British colonies. There were no less than six high-powered official commissions of inquiry between 1893 and 1931, a number unmatched by any other country.

Monetary Standard

The major issues, which related to the exchange rate of the Indian rupee and the size and composition of India's currency cover, were hotly debated between the principal interest groups, namely, the British business community in India, the government of India, and the India

Office in London under the secretary of state for India, and Indian public opinion, which was fractured by the rivalries between the regional financial centers, Calcutta, Bombay, and Madras.

The recent history of Indian currency falls into well-defined periods from 1835, when the silver rupee of 180 troy 11/12th fine was declared the sole legal tender. India was on a monometallic silver standard from 1835 to 1893, and a paper currency reserve with a maximum of 40 million rupees (Rs.) in government securities, the rest in silver coin and bullion, with provision for the inclusion of gold coin and bullion up to 25 percent. The period from 1893 to 1898 was one of transition because of the depreciation of the silver rupee, whose gold value had remained at fell from about 2s. since 1871, fell to 1s. (shilling) 2d. (pence) in 1892, precipitating the amendment of the Indian Coinage Act of 1879 and the Indian Paper Currency Act of 1882, following the recommendations of the 1892 Herschell Committee. The subsequent improvisations, following the recommendations of the Fowler Committee (1898) and the Act of 1899, resulted in an effective gold exchange standard, which was more economical than a gold standard and ensured practically.

14.4 KEYWORDS

Money policy, credit policy, rural credit, gold standard

14.5 QUESTIONS FOR REVIEW

1. What is international gold standard?

2. Discuss about the credit policy in Bengal and Madras Presidencies

14.6 SUGGESTED READINGS

The Cambridge Economic History of India, Vol 2 by Meghnad Desai

Economic History of India by TATHAGATA Roy

14.7 ANSWERS TO CHECK YOUR PROGRESS

1. Hint – 14.2

2. Hint – 14.2