CHAPTER III

INCOME DISTRIBUTION AND SAVINGS MOBILIZATION

The divergence between the potential and actual surplus available for development constitutes the central problem in the study of savings. It is necessary to diagnose this malaise so that with increasing incomes the divergence, instead of being allowed to increase may be narrowed down. In this chapter the strategy for generating and mobilizing savings will be considered in relation to the problem of the distribution of income. An attempt will be made to study two problems emanating from this: (i) Why is the rate of saving in an underdeveloped economy like India low despite a fairly unequal distribution of income? (ii) How far can an underdeveloped economy reduce the prevailing inequalities of incomes without adversely effecting its prospects of savings and economic development? Before analysing these problems in detail it may be worthwhile to indicate briefly the salient features of these problems in their historical perspective.

I

Adam Smith discussed the problem of the distribution of income as it affects capital accumulation. He held that accumulation and economic progress requires a shift of income from those who utilize the resources less productively to those who utilize them more productively. Among the classical writers

it was, however, Ricardo who attached crucial importance to the problem of income distribution during the process of growth. He considered the determination of the laws which govern this distribution as "the principal problem in political economy". An attempt was made by him to demonstrate how inequality, when in favour of the profit sector, plays a functional role in the process of economic growth. To him the rate of capital formation falls and stagnation ensues only when the income distribution is no longer in favour of the profit sector.

It is true that Ricardo was primarily interested in the determination of the laws which govern distribution rather than the range and magnitude of production. This does not, however, mean that he did not touch the problem of development. Though his analysis is somewhat ambiguous, his essential contribution was in showing the manner in which distribution is affected during the process of change.


4 Regarding his analysis of distribution Dalton writes, "It is seldom clear whether he is dealing with rent per acre, profits per cent, wages per head, or with aggregate rent, profits and wages or with the proportions which these three aggregates bear to the total produce". See his "Some Aspects of the Inequality of Incomes in Modern Communities", London, Routledge & Kegan Paul, 1949, p.52-53.

The classical case for income inequality - both sectoral and personal - was based upon two assumptions, viz. (i) saving and capital accumulation solely rest with the private enterprise; (ii) capital accumulation depends mainly upon profit earners; wage earners spend their almost entire income upon consumption. The justification of income distribution in favour of the richer sections was based upon the belief that capital accumulation mainly depends upon the abstinence of the rich.6

The available historical evidence corroborates the classical thesis that the existence of inequality is an important factor in the determination of the magnitude of saving and the rate of growth. The experience of Japan during the period of its industrial revolution indicates that unequal distribution of income was a major factor in supplying the necessary funds for development.

The resources necessary for capital formation were secured in Japan directly from heavy land taxes thereby shifting the benefits of increasing agricultural productivity to the industrial sector.7 Inspite of considerable increase in agricultural

6 It should be noted, that even when they emphasise the importance of the "abstinence of the rich", they knew the advantages of "the economy of high wages". Several passages in the writings of Adam Smith, Ricardo and Malthus, Maculloch and Senior, J.S. Mill and Bentham reveal their concern for the human factor.


productivity (it nearly doubled during the period 1885-1915) the standard of living of the people in the rural areas did not improve as a result of such a policy. The land tax revised in 1873 was so high (it amounted to nearly 13 per cent of the value of a normal crop) that many farmers were forced to sell their land in order to pay the tax revenue. The concentration of income in rural areas was utilized for accumulation when landlords were paid government bonds in return for the confiscation of land. The same was the case in urban areas where wages lagged behind profits. Taxation was lenient on large incomes and property. Lockwood cites the figures of the distribution of household income in Japan by income classes. It shows that even in 1930 nearly 7 per cent of the households received nearly 40 per cent of the income, while lower 57 per cent of the households secured only 23 per cent of the income. He is, however, sceptical about the reliability of the income figures of upper income groups which are likely to be underestimates. Thus during the initial period of industrialization Japan followed a policy which - both directly and indirectly - encouraged savings and capital formation and checked consumption. Moreover, state expenditure for social security, consumer services etc. was non-existent so that emerging inequalities

8 Between 1883-1890 over 3,50,000 producers suffered forced sales for arrears in payment. See Norman, E.H., "The Emergence of Japan as a Modern State", New York, 1940, p.144.

and insecurities were allowed to grow without any political counteraction. In the initial stages of industrialization the distribution of income was fairly even in England also. In England significant increases in agricultural productivity took place only after the middle of the nineteenth century. The flourishing trade and industry helped the process of accumulation. Landlords, merchants and industrialists were able to amass enough resources which can be utilized for industrial development. We do not have reliable statistics regarding the distribution of income in England in the eighteenth century. The estimates of income distribution given by Gregory King for the year 1688 suggests the prevalence of wide disparity in the distribution of income. A high degree of inequality is suggested by Ashton for this period. He writes, "what is certain is that the differences of income remained great; eighteenth century society was emphatically not egalitarian."¹⁹ No attempt was made by the State to change the existing pattern of the distribution of income.¹¹ England introduced income tax only in 1799 to be subsequently abolished in 1816 with the end of Napoleonic Wars. Similarly, the principle of progression in the system of taxation was accepted as late as 1909-10.


The unequal distribution of income played its part in the advanced countries of today during the initial phase of their industrialization. Kuznets has made a historical study of the correlation between the distribution of income and economic growth. On the basis of the available data regarding countries like U.S.A., U.K., and Germany, he puts forward some tentative conclusions. According to his thesis there is a long swing of inequality in the secular income distribution, widening in the early phases of economic growth when the transition from pre-industrial to the industrial civilization was most rapid, becoming stabilized for a while, and then narrowing in the latter phases. The phases of increasing inequality, according to Kuznets, for U.K., U.S.A. and Germany were during 1780-1850, 1840-1890 and 1840-1890's respectively. The above data suggests that during the industrial revolution increasing inequality played its part in financing the process of development.

Thus the historical evidence supports the classical tenet that one of the pre-requisites of development is the prevalence of the unequal distribution of income. However, the classical dictum has not remained unchallenged. Malthus, one of the classical writers himself, indicated the possibility of under-consumption as a result of inequality. Marx also exposed the conflict of interests that the process of development involves.

Marx, however, instead of advocating a policy of a more equitable distribution of income, predicted, on the basis of his dialectic materialism, the possibility of a proletariat revolution. The economic dislocations resulting from the great depression focussed attention upon the relationship between inequality of income and wealth, saving and economic development. One of the most important lessons of the Keynesian analysis has been that, beyond a point, unequal distribution of income may, instead of accelerating, retard economic growth. A more equitable distribution of income, by maintaining the effective demand, is likely to sustain and increase employment and output in the economy. In his *General Theory*, Keynes unequivocally pronounces that the existence of the inequality of income and wealth is one of the outstanding failures of our society.* Welfare considerations apart, even economic considerations led him to think that equality is necessary if the economy is to maintain the level of employment and output. It is usually argued that inequality is necessary since growth of capital depends upon individual savings. However, Keynes points out that up to full employment growth of capital does not depend upon the low propensity to consume, but is held back by it.13 The Keynesian analysis had a relevance to the advanced countries of

* See Ch. 24

his time. However, it also led underdeveloped countries to think of equality in relation to development, though the reasons behind its justification and the purpose for which it was advocated were slightly different.

It is interesting to consider here the arguments that are usually advanced in favour of equality even while recognising the need for rapid development. It is argued that a high degree of income inequality is no longer necessary under the present day circumstances. A highly skewed distribution of income helped the advanced countries of today to initiate the process of industrialisation because of several reasons; (a) Inequality at that time increased saving and investment because the opportunities and inducements for conspicuous consumption were not as great as they are today; (b) The concentration of income and wealth took place in favour of individuals and classes known for their frugality and productive investment; (c) Absence of any organised trade union movement and the egalitarian legislation made the way clear for the operation of the economy on such lines.

There is yet another reason for the justification of such inequality. Inequality was justified because only individual savings were important for capital formation. Excessive personal inequalities may no longer be tolerated under the modern social framework. Moreover such an inequality may not be necessary with the emergence of both the government and corporate sectors for financing development.
The problem of the distribution of income may now be considered in relation to the strategy for realising a high rate of saving in an underdeveloped economy like India. It is tempting to suggest in this context that the distribution of income should be in favour of sectors and classes having higher saving propensities. The distribution of income - both sectoral and personal - will have to be skewed if the higher rate of saving is to be realised for rapid economic development. A favourable treatment of the corporate sector having a high saving propensity may be recommended. The expansion of the corporate sector will have the added advantage of providing the necessary industrial base for self-sustained growth. The saving rate can as well be raised if the distribution of income is favourable to the unincorporated business enterprises. Along with its high saving propensity, the high employment potential of this sector strengthens its claim for favourable treatment. The diversion of income towards the state may also be justified if, with its high saving rate, it leads to a better utilization of the available scarce resources. With the same logic the distribution of income in favour of the agricultural sector is viewed with concern since its saving propensity is usually lower.

Two important points emerging from the above analysis may be noted: (1) if the distribution of income is in favour of sectors having higher saving propensities, the saving rate may
increase. A simultaneous expansion of Government, corporate and non-corporate sectors may prove advantageous to each other. In a different sense these sectors are also competitive to each other since all of them have to draw their resources from the same savings pool. (ii) Lower saving rate in the agricultural sector may not justify an unfavourable distribution of income for that sector. The distribution of income may be rendered unfavourable through heavy taxation or the creation of adverse terms of trade. Such a policy may have adverse effects upon the incentives for production in this sector. Besides this, its political feasibility also remains doubtful within a democratic framework. Again, the resources available in the agricultural sector may be, by nature, non-transferable, (i.e. human labour). Finally, in India agricultural sector, which provides on an average nearly 50 per cent of the national income, cannot be neglected in any attempt to boost up the rate of saving. Therefore, positive measures will have to be taken to raise the rate of saving in this sector itself.

In formulating the policy regarding the distribution of income in India, three important points will have to be borne in mind. (i) Measures will have to be taken to reduce the excessive inequalities in the distribution of income. (ii) A large amount of resources will have to be diverted towards the Government for investment purposes. (iii) The reduction of inequalities or the diversion of resources towards the state
should be consistent with the maintenance of adequate incentives for productive savings and investment in the private sector.

With this background we take up first the problem of the sectoral distribution of income in order to pinpoint the factors responsible for the low rate of savings in India. The sectors that we have in mind are three, namely, the government sector, the corporate sector and the household sector. Our study of the distribution of income and the generation of savings in various sectors is guided by three main considerations: (i) If a particular sector has or is likely to have a relatively higher saving propensity with which it can play a decisive role in increasing the savings pool, that sector should be expanded rapidly. (ii) If the saving propensity is lower in a particular sector efforts should be made to increase the saving rate in that sector through deliberate measures. (iii) In so far as the individual income inequalities are concerned, what is more relevant is a study of income utilization rather than income distribution. If the saving rate is to be raised, a country will have to control its expenditure flow and pattern in such a way that it restricts, to the extent necessary, unnecessary expenditure (either on conspicuous consumption or unproductive investment or both) and encourages productive outlay (either on essential consumption or productive investment or both). We take up this problem of income inequality in our discussion of savings of the household sector. Let us now consider the problem of savings in relation to the various sectors of the economy.
III

(1) THE GOVERNMENT SECTOR: A CASE OF LOW RATE AND MAGNITUDE OF SAVING;

Low rate of Government saving is one of the factors responsible for the low level of savings in the Indian economy. One of the peculiar features of the Indian economy is that while the share of the State in total planned investment outlay is increasing, its share in the generation of total savings has remained considerably lower. We have given below the figures of the relative shares of public and private investment during the three plans.

PERCENTAGE SHARE IN TOTAL INVESTMENT OF PUBLIC AND PRIVATE SECTORS:

<table>
<thead>
<tr>
<th></th>
<th>Public Sector</th>
<th>Private Sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>First Plan</td>
<td>46.4</td>
<td>53.6</td>
</tr>
<tr>
<td>Second Plan</td>
<td>54.1</td>
<td>45.9</td>
</tr>
<tr>
<td>Third Plan</td>
<td>60.6</td>
<td>39.4</td>
</tr>
</tbody>
</table>

NOTE: The figures exclude transfer of funds from public sector.

The above figures indicate that the share of the public sector in total investment is increasing. In the Third Plan out of the savings of every ten rupees earmarked for investment, nearly six will be invested by the public sector.

As contrasted to this the position regarding savings in the Government Sector is not very encouraging. The estimates of government savings as given by the Reserve Bank do not show any
clear trend regarding savings. It shows fluctuations throughout the period 1950-51 to 1958-59. During this nine year period Government savings as a proportion of total savings fluctuated between 11 per cent to 15 per cent barring two exceptional years 1951-52 and 1955-56 when the proportions were 38.2 per cent and 7.6 per cent respectively. For the entire nine year period the Government Sector provided nearly 14 per cent of the total savings. This formed only 1 per cent of the national income during the period 1950-51 to 1958-59. Apart from its contribution to the total savings pool, we can also judge the performance of the Government Sector on the basis of the saving-income ratio. This, in fact, provides the most crucial test regarding the capacity of the Government Sector to generate savings. It is from this point of view that the Government Sector's performance may not be found to be very encouraging. The average saving-income ratio for the Government Sector which was at 10.3 per cent during the First Plan, came down to 9.2 per cent during the first three years of the Second Plan. The average saving-income ratio for the entire period of 1950-51 to 1958-59 amounted to only 9.7 per cent.

A word of caution is in order. These figures are likely to underestimate the importance of Government in the process of development. The above saving estimate does not take into account the current expenditure of the Government which is of a developmental nature. If the role of the state is to be viewed in its proper perspective a study of the developmental and non-developmental expenditure of the state (apart from current and capital
expenditure) should prove useful. The Reserve Bank's budget studies give figures of developmental and non-developmental expenditures incurred by the Government. Viewed in this context, the Government's performance on revenue account may be considered satisfactory. What we would like to stress is that there is both a necessity as well as a scope for increasing saving in the Government sector.

If the State wants to play a decisive role in raising the savings rate in the economy, it will have to generate more savings than what has been the case at present. An increase in Government saving is both necessary and possible. If the total savings pool is to be raised the State's share in total savings should increase. There are two important reasons for the expansion of Government saving. (i) With the expansion of the public sector, the State will be responsible for generating a larger share of the national income. In the context of the scarcity of resources, the public sector should be called upon to yield increasing surpluses. (ii) In order to fulfil its investment targets the State will also raise additional resources through taxation. The extent to which the level of Government saving will be raised will depend upon the size of the gap between Government receipts and its expenditure. The gap can be widened either by increasing the receipts or by reducing the expenditure.

It seems that there is scope for both in the Indian economy. We take up in chapter five, the problem of raising additional resources.
IV

THE CORPORATE SECTOR: A CASE OF HIGH RATE AND LOW MAGNITUDE OF SAVINGS

What has been the position regarding the corporate saving in the Indian economy? Corporate Sector contributes only a small fraction of the total savings in the Indian economy. For the period of nine years from 1950-51 to 1958-59 its contribution to the total saving pool amounted to 5 per cent. The Corporate Sector's savings show considerable year to year fluctuations. They were at an abnormally low level of Rs.4 crores in 1952-53, while they exceeded Rs.50 crores in the years 1951-52, 1955-56 and 1956-57. If the saving performance of the Corporate Sector is considered with three yearly averages, its share in total savings seems to have declined in recent years. If the nine years for which the estimates are available are divided into three sub-periods of three years each it shows that in the last period (1956-57 to 1958-59) the share of the Corporate Sector in total saving has declined to 3.7 per cent as compared to 5.2 per cent in period I (1950-51 to 1952-53) and 5.3 per cent in period II (1953-54 to 1955-56).

The corporate sector in some of the advanced countries like U.S.A., U.K., Japan and Australia provides between 25 to 50 per cent of the total savings. The share of the corporate sector in

14 The Reserve Bank estimate of the corporate sector includes savings of non-financial Indian Joint Stock Companies, Banks, Industrial Credit and Investment Corporation, Non-life Indian Insurance Companies and Cooperative Institutions.
total private saving was considerably high in Ceylon (70 per cent) and Japan (53 per cent) during the period 1950-59. The main reason behind this was the large share of the corporate income in total national income.\* 

The contribution of the corporate sector to the total savings pool will depend upon its size and its propensity to save. It is true that the size of the Corporate Sector in India is very small. The share of the Corporate Sector (joint stock companies) in the domestic net product at factor cost was only 12 per cent in 1957-58.\(^\text{15}\)

The saving propensity of the Corporate Sector will be considered now. Its saving rate is higher as compared to other sectors in India. According to the Reserve Bank estimate Corporate Saving rate for the period 1950-51 to 1958-59 was at 35.8 per cent. This may be considered as a fairly high rate when compared to the saving rates of other domestic sectors. However, two important points deserve to be mentioned here. (1) Corporate saving rate has not always remained high when it is compared with the saving rates of corporate sectors in advanced countries like U.K. and U.S.A. (2) Inspite of year to year fluctuations the saving rate on the whole seems to have gone down. While internal financing, 

mainly through depreciation and free reserves, provided nearly 60 per cent of the resources in the First Plan, the corresponding figure for the Second Plan comes to only 45 per cent. Among the external sources the companies have raised the needed resources mainly from borrowings from banks. Banks which provided nearly 6 per cent of the funds in the First Plan provided nearly 16 per cent of the funds in the Second Plan. Saving/income ratio for the corporate sector (non-government financial as well as non-financial companies) during the recent years also indicate the same trend. The corporate sector's saving rate which was at 37 per cent in the First Plan declined to 32.4 per cent during the first three years of the Second Plan.

The expansion of this sector can play a strategic role in boosting up the rate of saving in the economy. The total saving which may be generated from this sector will depend upon the total income that it generates, the dividend policy that it follows and the type of taxation policy that the government adopts. Expansion of this sector not merely increases the total pool of savings in the private sector, it also supplies a large amount of resources to the government sector. The government

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16 See "Finances of Indian Joint Stock Companies", in R.B.I. Bulletin Vol. XVI, No. 6, June 1962, p. 859. The percentages for the First and Second Plans are based upon the surveys of 750 and 1000 comprise respectively. The study included non-government sector and excluded banking, insurance and investment companies, companies and associations functioning not for profit and companies limited by guarantee.
should, therefore, devise its policy in such a way that it encourages corporate savings on the one hand, and brings additional revenue to the state on the other. The problem of corporate taxation is taken up in chapter five.

It may be argued that the retention of profits and their reinvestment will lead to the concentration of economic power in the hands of a few. Excessive concentration of economic power may not be compatible with the goal of an egalitarian society. Several important points should be noted in this connection. Firstly, the problems of ploughing back of profits and the resulting excessive concentration of economic power has a relevance more in an advanced economy than in an underdeveloped developing economy. Retention and reinvestment of profits may not always be dangerous in the initial stages of development. Secondly, in an expanding economy the processes of both concentration and dispersion might be operating simultaneously. Reinvestment of profits may lead to a process of the concentration of economic power. On the other hand, the expanding investment opportunities in a developing economy may lead to the emergence of new enterprises leading to a dispersion of economic power. The ultimate impact upon the economy will depend upon the relative importance of both these tendencies. Finally, a modern Government is empowered to control and regulate such concentration of economic power. With these powers the state can avoid excessive concentration of power or the inappropriate utilization of resources.
We may add a few words about cooperatives forming a part of the corporate sector. This sector has succeeded only partially in generating or mobilizing savings. Table No. 3.1 gives some statistics regarding the cooperative sector.

The figures suggest that the savings of the cooperatives are at a low level. It has not succeeded in generating adequate savings. It is true that the cooperative sector is gradually expanding. The statistics regarding the number of societies, paid up capital etc. indicate that the movement is gradually progressing. Again such an institutional setup should have enabled the economy to mobilize more savings from the rural areas. However, the figures of individual savings in cooperative deposits and securities suggest that the success achieved in this sphere is limited. It is true that mobilization of savings from the rural areas with low levels of incomes is difficult. With increasing productivity and improved marketing within the agricultural sector it should be possible to strengthen the resource position of the cooperatives.

V

THE HOUSEHOLD SECTOR: THE DILEMMA OF A DEVELOPING ECONOMY.

In this section the problem of the personal distribution of income will be considered. The object of this chapter is, it may be recalled, to find out the causes for the low rate of

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17 See issues of "Review of the Cooperative Movement in India" published biennially by the Reserve Bank of India.
18 All-India Rural Credit Survey Committee has analysed in detail the causes of failure of Cooperative Movement. See "All-India Rural Credit Survey", Bombay 1954, Vol. II, Ch. 21, 22.
### TABLE NO. 3.1

**GENERATION AND MOBILIZATION OF SAVINGS BY COOPERATIVES IN INDIA AT CURRENT PRICES (IN CRORES OF RUPEES AT CURRENT PRICES)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Savings of Cooperatives</th>
<th>Individual savings through Deposits</th>
<th>Securities</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950-51</td>
<td>7.0</td>
<td>5.2</td>
<td>2.7</td>
</tr>
<tr>
<td>1951-52</td>
<td>5.3</td>
<td>6.5</td>
<td>3.8</td>
</tr>
<tr>
<td>1952-53</td>
<td>2.2</td>
<td>5.6</td>
<td>1.4</td>
</tr>
<tr>
<td>1953-54</td>
<td>1.7</td>
<td>5.1</td>
<td>6.2</td>
</tr>
<tr>
<td>1954-55</td>
<td>2.7</td>
<td>11.3</td>
<td>4.9</td>
</tr>
<tr>
<td>1955-56</td>
<td>6.3</td>
<td>17.6</td>
<td>7.0</td>
</tr>
<tr>
<td>1956-57</td>
<td>8.6</td>
<td>19.5</td>
<td>10.1</td>
</tr>
<tr>
<td>1957-58</td>
<td>8.4</td>
<td>4.3</td>
<td>16.4</td>
</tr>
</tbody>
</table>

1. Relate to Agricultural year ending 30th June

Source: M.C.A.E.R., "Savings in India", See table 3.4 and 4.3.1.
saving despite the existence of inequality of income and wealth. It is also proposed to consider the extent to which the twin objectives of greater equality and higher savings can be reconciled. In this context, we may, in the beginning, consider some of the important issues having a bearing on our problem.

Modern democratic welfare states have accepted as one of their goals the reduction of inequalities of income and wealth. The realization of this goal will have to be considered in relation to the optimal utilization of resources in the economy. The type of problem that India is facing is of special significance in view of the fact that it tries to achieve both rapid development and a reduction in the inequalities of income. The Planning Commission realises that development along these lines has not so far been attempted on any significant scale under democratic conditions. "There are no historical parallels or plans of action which could be regarded as providing an answer to this special problem facing underdeveloped countries." In the First Five Year Plan the conflict between the goals of development and equality - at least in the short run - has been justified to a certain extent. The document of the First Five Year Plan states, "While it would be wrong in this sphere to think in static terms and to condone the existence or accentuation of sectional privileges, it is no less important to

19 Govt. of India, "Second Five Year Plan", Delhi, 1956, p.33.
ensure a continuity of development without which, in fact, whatever measures, fiscal or other, might be adopted for promoting economic equality, might only end up in dislocating production and even jeopardizing the prospects of ordered growth.°

However, with the passage of time the thinking on these lines has evolved a definite policy. In the Third Five Year Plan, for example, it is very clearly stated that although excessive inequality may promote savings and capital formation it is not compatible with democratic socialism. The Planning Commission has also accepted as reasonable the recommendation of the Taxation Enquiry Commission for a ceiling on income at 30 times the average family income after tax. It hopes to achieve this gradually over a period of two or three plans.°

It should be obvious that unequal distribution of income

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20 Govt. of India "The First Five Year Plan", Delhi, 1952
See p. 51, 40.

21 Government of India, "Third Five Year Plan", Delhi, 1961, p. 16, 17.
by itself cannot guarantee higher saving and investment. Capital accumulation takes place only when the distribution of income is in favour of sectors and individuals having higher propensities to save and invest. Therefore the problem of the type of inequality is as important as the problem of the degree of inequality.

22 U.N., World Economic Survey 1960 seems to have failed to emphasize this aspect when it says that "since higher income groups tend to save a larger proportion of income, it would be expected that the level of household saving would tend to be greater in countries where the share of the higher income groups in total income is greater" (p.72). Since data are not available by the size distribution it tries to relate the degree of inequality to the share of income from property and entrepreneurship in total income. On the basis of the figures given in Tables 2.10 and 2.11 (which we have given in the table 3.2.) it tries to establish possible relationships.

It writes, "In Venezuela and Panama, for example, in contrast to the Congo and Honduras, the smaller share of income from property and entrepreneurship may have to some extent accounted for the lower level of household saving", though the data do not allow any "firm conclusions". The reason for this is that mere inequality cannot explain the level of savings. As will be seen from the table, Columbia, Brazil and Spain have same rates of saving with widely different shares of income from property and entrepreneurship; or share of income from property and entrepreneurship is the same in Venezuela and Panama (the countries quoted by U.N. Report.) and yet their saving rates vary considerably. The same thing is observed if we compare, say, Costa Rica and Jamaica or Honduras and Philippines. Thus the figures given by the report hardly support their hypothesis. The main reason behind this seems to be the failure of the report to stress the relationship between the type of inequality and saving.
### TABLE NO. 3.2

RELATIONSHIP BETWEEN INEQUALITY AND THE SAVING AS A PERCENTAGE OF HOUSEHOLD DISPOSABLE INCOME

<table>
<thead>
<tr>
<th>Country</th>
<th>Income from property and entrepreneurship (Percentage)</th>
<th>Saving as % of households disposable income 1950-59</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trinidad and Tobago</td>
<td>41</td>
<td>7</td>
</tr>
<tr>
<td>Congo</td>
<td>42</td>
<td>7</td>
</tr>
<tr>
<td>Honduras</td>
<td>52</td>
<td>7</td>
</tr>
<tr>
<td>Rhodesia &amp; Nyasaland</td>
<td>41</td>
<td>6</td>
</tr>
<tr>
<td>Venezuela</td>
<td>26</td>
<td>5</td>
</tr>
<tr>
<td>Costa Rica</td>
<td>37</td>
<td>5</td>
</tr>
<tr>
<td>Columbia</td>
<td>61</td>
<td>4</td>
</tr>
<tr>
<td>Brazil</td>
<td>48</td>
<td>4</td>
</tr>
<tr>
<td>Spain</td>
<td>32</td>
<td>4</td>
</tr>
<tr>
<td>Ecuador</td>
<td>45</td>
<td>4</td>
</tr>
<tr>
<td>Ceylon</td>
<td>46</td>
<td>3</td>
</tr>
<tr>
<td>Jamaica</td>
<td>38</td>
<td>1</td>
</tr>
<tr>
<td>Philippines</td>
<td>56</td>
<td>-2</td>
</tr>
<tr>
<td>Panama</td>
<td>29</td>
<td>-4</td>
</tr>
</tbody>
</table>

Sources: U.N. World Economic Survey 1960, compiled from tables 2.10 and 2.11.
The problem of the reduction of inequalities and the achievement of rapid growth has a bearing upon the levels of consumption also.

It is sometimes argued that only equal distribution of income can sustain mass producing consumer's goods industries in advanced economies. Unequal consumption levels associated with inequality may adversely affect the economic progress of a country. When Nurkse talked of balanced growth he implied the existence of "inverse correlation between economic growth and income inequality". Though Strassman has argued for the validity of this thesis for advanced countries only it has some relevance even in underdeveloped economies. His thesis propounds two things for advanced countries: (i) increasing consumption (ii) equality in consumption levels. He doubts the validity of the policy of redistribution of income in an underdeveloped economy. It is true that what is required in an underdeveloped economy is special efforts for increasing investment rather than consumption. However, it is not difficult to justify a policy of increasing essential consumption up to a certain minimum level even in an underdeveloped economy. The current literature on development rightly emphasises the importance of human factor in economic development. The second point regarding equality in consumption levels is also relevant. In view of the interdependence of consumer preferences, a wide disparity in con-

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sumption levels is not likely to promote savings necessary for development. If certain sections of the society are allowed to enjoy a high standard of living, it may have adverse effect upon the masses of the people.

Finally, apart from the problems of welfare of the people or their consumption levels which are by themselves very important a certain minimum investment in human capital is also necessary if the economy is to grow spontaneously and rapidly. The goals of reduction in inequalities and higher rates of growth are not as inconsistent as is sometimes made out to be. It is true that if the resources are concentrated in the hands of rich people, they may invest them productively. However, the growth rate may at times be higher if these resources are taken over by the State and wisely invested in building up human capital. In other words, investment in human capital rather than physical capital may be more conducive to a higher rate of growth. Such a transfer of resources becomes all the more necessary and justifiable, when the concentration of income with the upper income groups is wasted for conspicuous consumption or unproductive investment. Such a redistribution and reallocation of resources in the economy strengthens the case for state initiative in the process of development. So long as the economy largely depends upon private sector for generation of savings, however, the fiscal policy of the state will have to be such that it does not curb the incentive to save and invest productively.
The distribution of income will have to be such that it appropriately reconciles, to the extent necessary, the claims of welfare and incentive and initiates a process of development, which brings both "greater production" and "better distribution." Every country will have to find out, albeit approximately, what can be called the optimum level of inequality.

With these preliminary remarks, we now consider the problem of the distribution of income in both the urban and rural areas and their rates of savings. The available empirical evidence, suggests that the inequality of income and wealth is as great, if not more, in an underdeveloped economy as in an advanced economy. Low rate of saving in a country may be partly explained by the low level of incomes. However, savings usually flow from upper-income groups and the unequal distribution of income should increase their saving capacity. We may consider now the saving performance of both the urban and rural sectors.

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We may briefly consider the saving performance of the urban sector in relation to the distribution of income. Saving estimates for the urban sector are given in table No.3.3.

The above figures suggest that savings in the urban sector have increased considerably during the last few years. Savings in absolute terms increased from Rs.216 crores in period I to Rs.449 crores in period II and to Rs.530 crores in period III. The share of the urban household sector in the total household savings which was at nearly 55 per cent in period I went up to nearly 70 per cent in the subsequent periods. Its contribution to the total savings also increased from 40 per cent in period I to nearly 60 per cent for subsequent periods. Urban sector's saving as a percentage of national income has doubled when savings of period I and III are compared. The urban saving income ratio shot up from 9.5 per cent in period I to nearly 16 per cent in period II. In period III it increased up to nearly 17 per cent though the rate of increase has fallen as compared to the previous period. An idea of the urban household sector's high saving propensity can be had from the fact that its saving/income ratio for the entire period 1950-51 to 1958-59 was almost double (14.5) as compared to the national s/y ratio.

We may consider the behaviour of savings of this sector in some detail. It has been found that the lower-income group (upto Rs.3,000) do not save anything on an average.25 Such a low income

<table>
<thead>
<tr>
<th></th>
<th>Period I</th>
<th>Period II</th>
<th>Period III</th>
<th>1st Plan</th>
<th>First 5 years</th>
<th>1950-51 to 1958-59</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Urban households saving (at 1948-49 prices)</td>
<td>216</td>
<td>449</td>
<td>530</td>
<td>339</td>
<td>530</td>
<td></td>
</tr>
<tr>
<td>2. Average s/y ratio</td>
<td>9.5</td>
<td>16.0</td>
<td>16.9</td>
<td>12.6</td>
<td>16.9</td>
<td>14.1</td>
</tr>
<tr>
<td>3. As % of total saving</td>
<td>40.1</td>
<td>59.6</td>
<td>60.0</td>
<td>51.6</td>
<td>60.0</td>
<td></td>
</tr>
<tr>
<td>4. As % of National Income</td>
<td>2.4</td>
<td>444</td>
<td>4.7</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. As % of total household saving</td>
<td>54.8</td>
<td>70.5</td>
<td>71.6</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The disposable income of the group was nearly 63 per cent of the total urban income. The high-income group (with income above Rs.3000) consisted of nearly 11 per cent of the urban households and it secured 37 per cent of the total urban income. The saving rate for the upper-income group can be found out with the available data. It is assumed that net saving of the lower-income group in urban sector is zero. The total average disposable income (1953-54 to 1956-57) for the upper-income group was about Rs.1056 crores. The average saving for the urban sector for the same period amounted Rs.494.4 crores. Thus the average saving income ratio for the upper-income group comes to about 47 per cent. This may be considered as a fairly high rate of saving.

However, two points may be mentioned here. Firstly, the achievement of such a high rate of saving through inequality has also led to large variations in consumption standards. The N.S.S. surveys of consumer expenditure bring out this fact very clearly. Secondly, all those savings are not available for productive investment. It has been found that nearly 1/3rd of the savings are not invested productively in the urban sector. The efforts for reducing inequality and increasing savings will have to check both excessive consumption inequality and unproductive investment.

26 See the paper given by Ojha, P.D., and Bhatt, V.V., on "The Distribution of Income in India", in R.B.I.Bulletin Vol.XVI No.9, Sept., 1962, p.1357. All the figures referred to here are averages for the period 1953-54 to 1956-57.

Before discussing the policy implications of such a programme, we may review the performance of the rural sector. Since the persistence of a lower rate of saving in the agricultural sector has been viewed with concern, it is proposed to analyse the performance and prospects of this sector in greater detail.

**RURAL HOUSEHOLD SECTOR: A CASE OF LOW RATE AND MAGNITUDE OF SAVING**

The increasing flow of income towards rural sectors has been viewed at times with scepticism in so far as the problems of raising the saving rate is concerned. It is argued that since the rate of saving in the rural sector is relatively lower as compared to the urban sector, a higher rate of saving requires a distribution of income in favour of urban sector. We have indicated earlier certain practical difficulties involved in such a policy. It may be too broad a generalization to say that a certain class or sector has a higher or lower rate of saving as compared to other classes or sectors. It may be that usually higher income groups save a larger fraction of their income as compared to lower income groups. However, it may be equally true that certain sections in higher income groups may have lower saving rate as compared to their counterpart in lower income groups. The same argument holds good for rural-urban sector comparison. It is because of this reason that perhaps it is not advisable to suggest a pattern of the distribution of income favouring certain sectors or classes. The variations in the rates of saving as between different classes and sectors.

*We have used data available either for rural or agricultural sector, though we are mainly interested in the agricultural sector which forms a bulk of the rural sector.*
lead us to believe that no single criteria or policy measure can be fixed up regarding income distribution. Probably, several measures combined together may give us an effective policy for mobilizing savings.

We may first consider the saving effort made by the rural sector. Table No.3.4 gives figures regarding the rural savings. Savings in the rural sector increased from Rs.178 crores in period I to Rs.188 crores and Rs.210 crores in periods II and III respectively. The rural household saving as a percentage of total household saving which was at 45 per cent in period I remained at nearly 30 per cent during the subsequent periods. The rural household saving as a percentage of total saving declined from 33 per cent in period I to nearly 24 per cent in period III.

The saving estimate as given by the Reserve Bank is an underestimate as it excludes non-monetary direct investment and inventory accumulations. No reliable estimate of inventory accumulation is available. The amount of direct investment has been roughly estimated. Direct savings will constitute nearly 40 per cent of the total gross savings in rural sector. This estimate is supported by the fact that the ratio of cash expenditure to the total outlay on consumption and production is nearly 0.6.

TABLE NO. 3.4

SAVING OF THE RURAL HOUSEHOLD SECTOR
(₹. crores at current prices.)

<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td>1. Rural household saving</td>
<td>178</td>
<td>188</td>
<td>210</td>
</tr>
<tr>
<td>2. Average a/y ratio</td>
<td>2.6</td>
<td>2.6</td>
<td>2.7</td>
</tr>
<tr>
<td>3. As % of total saving</td>
<td>33.1</td>
<td>25.0</td>
<td>25.8</td>
</tr>
<tr>
<td>4. As % of National Income</td>
<td>1.9</td>
<td>1.8</td>
<td>1.9</td>
</tr>
<tr>
<td>5. As % of household saving</td>
<td>45.2</td>
<td>29.5</td>
<td>20.4</td>
</tr>
</tbody>
</table>

Source: R.S.I. Bulletin, August 1961
If the direct saving is taken into account, the net saving rate for the rural sector will be slightly higher.

The saving performance of the rural sector does not seem to be very encouraging. It is true that in the rural sector nearly 97 per cent of the households are in the low-income group (i.e. below Rs.3,000). We may assume that this group does not have any net saving. However, the upper-income group does not seem to have saved a high proportion of their income. The average yearly savings of the rural sector during the period 1953-54 to 1956-57 amounted to Rs.191 crores. The total average disposable income of the upper-income group in the rural sector amounted to nearly Rs.852 crores. If the entire saving of the rural sector is contributed by the upper-income group, their s/y ratio will be about 21 per cent. This ratio is quite low when it is compared with the s/y ratio of the upper-income group of the urban sector (46.9%). The above figures for the rural sector suggest that a large part of the income of upper-income group is spent for consumption purposes. Though we do not have any reliable data, it is certain that a part of this small magnitude of saving must be going towards unproductive investment.

Within the rural sector the saving rates are different for agricultural and non-agricultural sectors. The Reserve Bank has given separate estimates for the agricultural sector. The

* This and the subsequent figures used are taken from R.B.I. estimates.
estimates exclude saving through direct investment and inventory accumulation. Table No. 3.5 gives the relevant data for the years 1951-52 and 1956-57.

The savings of the agricultural sector were negative to the tune of Rs. 67 crores in the year 1951-52. However, in the subsequent years the agricultural sector might have saved positively. This is indicated by the estimate for the year 1956-57. In 1956-57 the savings of the agricultural sector amounted to Rs. 131 crores in the total rural savings of Rs. 238 crores. Though the agricultural sector generates more than 90 per cent of the rural sector income, it contributed only 57.5 per cent of the rural savings. The available data for estimating the savings in the agricultural sector are weak; however, the above figures broadly suggest that the voluntary saving rate in the agricultural sector is quite low.

It may be noted that the level of forced savings through taxation is also quite low for the rural (agricultural) sector. The forced saving imposed upon this sector is comparatively lower and the burden is not increasing proportionately with increasing incomes. Direct taxes (like land revenue, agricultural income tax, betterment levy etc.) contributed much less in relation to the increase in agricultural income and formed only a small percentage of the total agricultural income. As we shall see in chapter 5, the burden of direct taxes upon the agricultural sector is not only low absolutely but has increased only slightly during the last decade.
<table>
<thead>
<tr>
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</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>126</td>
<td>126</td>
<td>206</td>
<td>206</td>
</tr>
<tr>
<td>Housing</td>
<td>76</td>
<td>65</td>
<td>64</td>
<td>76</td>
</tr>
<tr>
<td>Non-farm business investment</td>
<td>11</td>
<td>17</td>
<td>12</td>
<td>33</td>
</tr>
<tr>
<td>Net purchase of bullion and ornaments</td>
<td>12</td>
<td>29</td>
<td>13</td>
<td>23</td>
</tr>
<tr>
<td>Net financial investment</td>
<td>15</td>
<td>17</td>
<td>17</td>
<td>17</td>
</tr>
<tr>
<td>Repayment of debt</td>
<td>136</td>
<td>51</td>
<td>329</td>
<td>198</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>378</strong></td>
<td><strong>325</strong></td>
<td><strong>553</strong></td>
<td><strong>555</strong></td>
</tr>
<tr>
<td>Deduct borrowing</td>
<td><strong>445</strong></td>
<td><strong>130</strong></td>
<td><strong>422</strong></td>
<td><strong>327</strong></td>
</tr>
<tr>
<td><strong>Net Saving</strong></td>
<td><strong>-67</strong></td>
<td><strong>195</strong></td>
<td><strong>131</strong></td>
<td><strong>238</strong></td>
</tr>
</tbody>
</table>

The burden of indirect taxation is relatively higher upon the urban sector. In 1953-54, the incidence of indirect taxes per capita in rural area amounted to Rs.0.69 as against Rs.1.62 in urban areas. In the year 1958-59 the burden increased up to Rs.0.93 per capita in rural areas against Rs.2.70 in urban areas. The burden of indirect taxes per capita in urban area is almost three times that in rural areas. If we consider the burden in terms of its proportion to consumer expenditure the burden on urban area is almost double as compared to rural areas. While recognizing the limitations of such estimates of incidence, a study of the incidence on parallel income groups broadly suggests that the burden on middle and upper income groups in the rural sector is relatively lower.

It will be quite appropriate to stress here the strategic role that the agricultural sector has to play during the process of growth. It is recognised that the two important indicators of economic growth in an underdeveloped economy are the increasing agricultural productivity and secular decline in the relative importance of agriculture in the generation of national income. The experience of the last decade of planning in India suggests that any programme of rapid industrialization can not succeed without developing agriculture. During the process of growth agriculture has to generate the surplus in one form or the other.

29 The 1953-54 estimate is of the Taxation Enquiry Commission and 1957-58 estimate is based upon the results of a survey conducted by the Ministry of Finance, Dept. of Economic Affairs.
It is only through the development of agriculture that we can have the food surplus for expanding population, raw materials for expanding industries, growing markets for industrial products and loanable funds for further development. It is thus the multiple, distinctive, but converging consequences of the revolution in agriculture which give it peculiar importance in the period of pre-conditions.  

The above analysis provides sufficient justification for a rapid development of the agricultural sector. However, a large amount of resources are necessary for this development. What should be the contribution of the agricultural sector for this development? Should it be a surplus, self-sufficient or a deficit sector? It is sometimes argued that agricultural sector should provide the surplus resources for industrialization. Agricultural sector can provide the surplus loanable funds for industrial sector only when it is fairly advanced. The Indian agriculture will achieve the final phase of development after a pretty long period when capital-intensive labour-saving techniques can be employed. In the present context it will be too much to expect the Indian agriculture to provide savings for industrial sector.


Can the agricultural sector remain a deficit sector, as it is in India at present? If the agricultural sector is a deficit sector, the necessary funds for its development will have to come from the non-agricultural sector. We will have to consider here a number of questions. Can the non-agricultural sector raise adequate resources for this purpose? If these resources are not diverted to the agricultural sector, can it utilize these resources more fruitfully? What is the scope of raising additional resources from the agricultural sector? It seems that any diversion of savings towards agricultural sector will deprive the non-agricultural sector of the necessary funds for the development of the industrial sector. The value of such a transfer also seems to be limited in view of the considerable requirements of the agricultural sector in India. In this context the agricultural sector should be made to contribute the resources required for its own development. In other words, it should be transformed from a deficit dependent sector into a self-sufficient sector. With the passage of time agricultural sector may be expected to provide a surplus for other sectors.

The data provided by N.S.S. and R.C.S. and its follow-up surveys suggest that there are large inequalities of consumption, income and wealth in the agricultural sector. It seems that unless some deliberate efforts are made this inequality is likely to increase. There are two reasons for this. (1) It has been found that normally the benefits of various developmental programmes go to the higher income classes, (2) If, due to inflation, the
the terms of trade are favourable to the agricultural sector, the benefits usually go to higher income classes having marketable surplus.

If the existing and increasing inequality is to be reduced and the resources going to the top classes are not to be wasted in conspicuous consumption and unproductive investment, the government will have to reduce the non-functional inequality existing in the rural area. However, the surplus resources mobilized from the upper income groups may not be sufficient to meet the requirements of rapid development. Therefore, appropriate devices may have to be found out to mobilize adequate resources from the middle and lower income groups. With the given distribution of income and the subsistence standard of living of the majority of farmers, it will be too much to expect them to save out of their subsistence incomes. Forced savings out of the present subsistence levels of incomes may not be feasible politically. However, if the productivity in agriculture is increasing, a part of the incremental income can safely and legitimately be tapped up by the state.

Thus the problem of increasing savings - both voluntary and forced - is vitally linked up with increasing productivity and incomes in the agricultural sector in India. However, in spite of the efforts made in this direction, the results achieved so far are not very encouraging. The agricultural productivity in India is estimated to have increased at the annual average rate of
1.6 per cent during the last decade.\textsuperscript{32}

There is a way out to increase savings and investment in the initial stages when the levels of productivity and incomes are low. At this stage savings in kind can play a relatively more useful role. The scope for such an effort has been realised; however, the success achieved in this sphere is limited. Direct investment can be increased by evolving an appropriate action-oriented programme. The success of such a programme will depend upon the type of leadership available at the village level.

The amount of savings that can be forced upon the people will depend upon its linkage with several factors. (1) Such efforts are likely to succeed if linked with increasing incomes, tapping up a part of the incremental income, (2) They are likely to succeed if they are linked with the expenditure pattern of the people in such a way that they tax inessential consumption and unproductive investment, (3) The chances of success will also be brighter if such efforts are linked up with local projects.

VI

In the context of the above considerations what should be the policy of the Government regarding the distribution of income? How will it reconcile the claims of the reduction of inequalities with that of raising adequate funds for rapid economic development? It may be pointed out at the outset that the reduction of existing

\textsuperscript{32} See Rao, V.K.R.V., Presidential Address at the 21st Conference of Agricultural Economics.
inequalities by itself will not solve the problem of raising the standard of living of the people. At the same time, in the present context, it is difficult to justify the inequality which is devoid of social purpose. Political democracy, to be meaningful, requires the reduction of gross economic inequality. Apart from justice, there is another and more cogent argument for such a policy. Development requires at least in the short period sacrifices on the part of the masses. The demand for sacrifice is made precisely when they are least capable of making such sacrifices. Under the circumstances, they can hardly be expected to make the necessary sacrifices without a guarantee for a reasonable share in the fruits of progress.

As the economy develops the state should see to it that no one remains below a minimum level of income. In the initial stages of development such a national minima may not include all the necessities of life.

In the light of the above analysis we may suggest the criteria regarding the policy of the distribution of income.

1. Distribution of income should be such that it encourages savings as against conspicuous consumption

2. Distribution of income should be such that it encourages productive as distinguished from unproductive savings.

3. The distribution of income should be such that it leads to a progressive reduction in private income inequalities consistent with rapid development of the economy.

The acceptance of the above criteria suggests the following policy measures.
1. REDUCTION OF CONSUMPTION INEQUALITY:

It is, perhaps, not possible to completely eradicate the existing inequalities of income and wealth within a very short period. What is probably objectionable in the short run is not so much the inequality of income as of consumption. A wide disparity in the consumption standards is neither justifiable nor desirable in the context of the need for more resources. It will, therefore, be necessary for the government to check and reduce the expenditure on conspicuous consumption. The Indian experience so far does not suggest that adequate measures have been taken to curb such expenditure to the extent desired. The conspicuous consumption can be reduced directly by heavily taxing the luxury articles and indirectly by changing the attitudes and habits of the people in favour of productive saving.

(2) PROMOTION OF FUNCTIONAL INEQUALITY:

Two types of inequalities may be justified or accepted in this context. (i) inequality arising out of work, (ii) inequality which promotes saving and productive investment in socially desirable channels.

(1) INEQUALITY DUE TO WORK: A certain amount of inequality is bound to persist in the economy, and is also necessary as an incentive to work. The degree of such an inequality will depend upon the differences in the efficiency of various individuals and classes. As the "Stakhonovite Movement" of Russia indicated, this is necessary for increasing the efficiency in the economy.
Such a system pays those who are more efficient and diligent and penalises those who are inefficient and indifferent. The degree of inequality that may be permitted will depend upon various factors, like, the overall state of the economy, the level of per capita income, consumption habits and saving preferences of the people, the need for additional resources, and the social values and attitudes prevailing in the society. It will, of course, be necessary to put a ceiling beyond which such inequality may not be allowed to exceed. The Planning Commission has already accepted the ceiling for this purpose. It may be necessary to keep in view the important issues emerging from this analysis. Fixation of upper ceiling is important, however, if this is to be meaningful, it should be accompanied by a fixation of minimum income below which no one will be allowed to go. From the viewpoint of social justice, this is more important and probably more difficult than the attainment of upper ceiling.

(ii) INEQUALITY PROMOTING SAVING AND PRODUCTIVE INVESTMENT:

The problem before a country like India is, how to remove the existing inequality which is not the result of genuine work differentials. This naturally involves drastic changes in the existing pattern of distribution. However, it may not be feasible to do so in the short run without adversely affecting the supply of total savings. At the same time the existence of such inequality cannot be justified unless it serves some social purpose. Efforts should, therefore, be made by the state
to induce the higher income classes to save more and invest the resources productively according to planned priorities. Various fiscal incentives and concessions may be necessary to divert these incomes into socially desirable channels.

It should be the endeavour of the state to see that in the long run (in the sense of specific phased long-term programmes) there is a gradual reduction of inequality. The funds may be taken over by the State for the expansion of the public sector. It can be argued that such a transfer of resources from individuals to the state is not meaningful so long as the total pool of savings remains the same. Such an effort is considered superfluous in so far as the problem of mobilizing additional resources is concerned. Such a transfer may be justified if the state utilizes the funds in a better way as compared to the private sector. It is true that inequality of whatever type and magnitude is not necessary when the state itself is a major force in initiating the development process. This argument implicitly assumes that the state will utilize the resources more productively.

However, when the resources are transferred to the State, the problem is not merely one of the efficiency with which the state utilizes the funds. The argument underlying the expansion of the public sector is more basic. When the resources are transferred from the private individuals to the state it does not remain a mere transfer of resources. Such a transfer also helps eventually in reducing the private inequalities. It should be clear from the above analysis that the necessity of excessive
private inequalities has been reduced to a large extent with the emergence of the state as a major partner in the development process. It may be argued that if the public sector expands considerably in order to mobilize more funds, the concentration of power will shift from private individuals to the public officials and politicians. This is a real danger against which any developing economy will have to guard itself. Whether and to what extent such a power will be abused will ultimately depend upon the vigilance of the people and the democratic traditions that they might have imbibed. Can an underdeveloped economy avoid such an eventuality and at the same time achieve the goals of greater equality and larger savings? The expansion of the decentralised sector is, perhaps, essential and inevitable if both these objectives are to be attained simultaneously.

For this purpose the decentralised sector will have to be technologically viable and economically efficient. It is in this context that the growth of medium and small-scale industries and cooperative sector assumes strategic importance in Indian planning.

In the meantime, if more resources are to be generated and mobilized while reducing the private inequalities of income and wealth the state will have to play a decisive role at three levels.

(i) The state will have to bear gradually a greater responsibility of generating income than what has been the case at present.

(ii) The state will have to mobilize more funds - both through forced saving (by heavily taxing non-functional inequality)
and borrowing (by promoting functional inequality) - in order to increase productive investment.

(iii) The state will have to control the flow of income and expenditure as between different sectors and classes in such a way that it promotes capital formation.