

# **The Quest for Equity in Development**

MANMOHAN SINGH

GOKHALE MEMORIAL LECTURE, 1986

GOKHALE INSTITUTE OF POLITICS AND ECONOMICS,  
Pune 411 004

The R.B.R.R. Kale Memorial Lecture, 1986 was given by Dr. Manmohan Singh, Deputy Chairman, Planning Commission, Government of India, on 2nd June, 1986 at the Institute. The subject of his lecture was "The Quest for Equitable Development."

Born in September 1932, Dr. Manmohan Singh obtained his D.Phil. at Oxford University and he was awarded Adams Prize, University of Cambridge in 1956. He taught at Punjab University and Delhi School of Economics till 1971. Between 1971 and 1976 he worked as Economic Adviser to the Ministry of Foreign Trade and Chief Economic Adviser to the Ministry of Finance, Government of India. From 1976 to 1980 he was Secretary to Government of India, Ministry of Finance and worked as Member Secretary, Planning Commission between 1980-82. In 1982, he was appointed Governor of Reserve Bank of India until he assumed the present position of Deputy Chairman, Planning Commission in 1985.

Dr. Manmohan Singh has attended various International conferences, worked as consultant to UNCTAD, ESCAP and elected Honorary Fellow of St. John's College, Cambridge in 1982 and Hon. Professor, Jawaharlal Nehru University.

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**ORIENT LONGMAN LIMITED**

*Regd. Office :*

5-9-41/1 Bashir Bagh, Hyderabad 500 029

*Other Offices :*

Kamani Marg, Ballard Estate, Bombay 400 038

17 Chittaranjan Avenue, Calcutta 700 072

160 Anna Salai, Madras 600 002

1/24 Asaf Ali Road, New Delhi 110 002

80/1 Mahatma Gandhi Road, Bangalore 560 001

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## The Quest for Equity in Development

Manmohan Singh\*

I am very grateful to Prof. V.M. Dandekar and Prof. Nilkanth Rath for inviting me to deliver this year's Rao Bahadur R.R. Kale Memorial Lecture.

2. Shri Kale was a highly enlightened and generous individual. He had the courage of his convictions and was therefore never afraid to swim against the tide of popular opinion. His donation of Rs. 1,25,000 for founding the Gokhale Institute of Politics and Economics proved to be the crowning act of his distinguished career. I join you all in paying homage to the memory of this great man.

3. The Gokhale Institute is to-day a premier national institution of higher learning and research. Its scholars have made an outstanding contribution to enhance our understanding of the dynamics of poverty, underdevelopment and social change. The powerful impact of the research work of the late Prof. D.R. Gadgil and more recently of that of Prof. V.M. Dandekar and Prof. Nilakantha Rath on some important aspects of economic policy planning in India is well known to economists in this country. The whole nation is indebted to them for their truly massive contribution to the development of the Gokhale Institute as a great centre of learning.

4. Scholars at the Gokhale Institute have taken a deep interest in issues relating to social justice and eradication of poverty. As a humble tribute to their outstanding contributions, I have therefore chosen "The Quest for Equity in Development" as the main theme of my lecture. I propose to discuss the extent to which we have succeeded in our quest for a just society, the factors which are responsible for the shortfall in progress and the lessons we can draw from past experience for purposes of future planning. The issues are undoubtedly exceedingly complex and I am acutely aware of my own limitations for dealing with such complex issues. Nevertheless, I do hope that what I have to say on this subject will help to promote a more informed debate on the strategies, programmes and policies for achieving greater equity in the process of development.

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\* Text of Rao Bahadur R.R. Kale Memorial Lecture delivered at Gokhale Institute of Politics and Economics in Pune on 2nd June, 1986. The opinions expressed in this lecture are the personal views of the author and should not be attributed to the Planning Commission.

## EQUITY : OBJECTIVES AND ACHIEVEMENTS

5. An abiding concern for equity and social justice was a distinctive feature of the national movement for India's freedom struggle. In particular, both Gandhiji and Jawaharlal Nehru-always emphasised that political freedom would acquire its true significance only if it helped to remove the chronic poverty which afflicted a majority of the Indian people under the colonial rule.

6. The promotion of social justice figures prominently in the Directive Principles of State Policy as enshrined in our Constitution. Thus in Article 38 as originally approved by the Constituent Assembly, it was laid down that "The State shall strive to promote the welfare of the people by securing and protecting as effectively as it may a social order in which justice, social, economic and political, shall inform all the institutions of the national life." The concern with social justice was further elaborated in Article 39 which states that "The State shall, in particular direct its policy towards securing -

- a) that the citizens, men and women equally have the right to an adequate means of livelihood;
- b) that the ownership and control of the material resources of the community are so distributed as best to subserve the common good;
- c) that the operation of the economic system does not result in the concentration of wealth and means of production to the common detriment;
- d) that there is equal pay for equal work for both men and women;
- e) that the health and strength of workers, men and women, and the tender age of children are not abused and that citizens are not forced by economic necessity to enter a vocation unsuited to their age or strength."

7. The importance attached to social justice was further emphasised when Parliament adopted in December 1954 "the socialist pattern of society" as the objective of social and economic policy. Subsequently, in the 1970s the Constitution itself was amended and it proclaimed India as "a sovereign socialist secular democratic republic." In addition, another clause was added to Article 38 to the effect that "The State shall, in particular, strive to minimise the inequalities in income, and endeavour to eliminate inequalities in status, facilities and opportunities not only amongst individuals but also amongst groups of people residing in different areas or engaged in different vocations."

8. In pursuance of the Directive Principles of State Policy enshrined in the Constitution, all the Five Year Plans have laid considerable emphasis on the establishment of a social order based on justice and offering equal opportunity to every citizen. Although plan objectives for social justice have not been stated in precise quantitative terms, it has been fairly obvious that promotion of social justice involves:

- a) Removal of poverty and provision of a minimum level of income which will ensure tolerable living standards for all the citizens;
- b) Progressive reduction of inequalities of income and wealth.

9. While our country has made significant all round social and economic progress since Independence, our achievements in terms of the various indicators of social justice have been less striking. For example, until the late 'seventies, there was no firm indication of a downward trend in the proportion of people living below the poverty line. The Planning Commission's estimates based on the latest National Sample Survey (NSS) data for 1983-84 show a sharp reduction in the proportion of people living below the poverty line from 48.3 per cent in 1977-78 to 37.4 per cent in 1983-84. Nevertheless, the fact that even after 35 years of planning, 37.4 per cent of our population should be living below a most austere defined poverty line is a cause for serious concern.

10. While reliable data on the distribution of income and wealth are not readily available, the available NSS data on consumer spending indicate only a very small increase in the share of bottom 30 per cent in total consumer spending between 1958-59 and 1983-84. Of course, since data on private consumption do not take into account the substantial expansion that has taken place in social services like education and health, it is possible that the NSS data may understate the improvement in the standard of living of the bottom 30 per cent of population. Even then, when one takes into account the fact that currently only 36.23 per cent of the population is literate (the proportion of literacy among women being 24.82 per cent) and that infant mortality in our country is still as high as 105 per 1000 live births, one cannot be very certain that expansion of social services has changed very substantially the position relating to inequalities as revealed by the NSS data.

11. Why is it that only limited progress has been made in the realisation of the goal of social justice? For an objective analysis of this issue, we need to examine the impact of various policy instruments relied upon in our development plans for achieving social justice. An examination of successive plan documents brings out the critical role assigned to the following elements as part of the over-all strategy to achieve greater social justice:

- a) a high rate of economic growth;
- b) progressive expansion of the public sector;
- c) effective regulation of the private sector;
- d) reorientation of fiscal and monetary policies;
- e) institutional reforms involving in particular land reforms and increasing cooperativisation of the rural economy; and
- f) launching of special programmes for disadvantaged groups/areas.

12. In what follows, I shall discuss the role that each of these elements was expected to play in promoting social justice, the contribution it actually made, the reasons for the contribution having fallen short of the original expectations and the lessons we can draw from past experience for purposes of future planning.

#### GROWTH, POVERTY AND INCOME DISTRIBUTION

13. The contribution that an acceleration of the rate of growth makes to the improvement of living standards has been a recurrent theme of mainstream economics. Long ago, Adam Smith himself had emphasised the role of sustained growth in reducing the incidence of poverty. In this context, he stated:

"It deserves to be remarked, perhaps, that it is in the progressive state which the society is advancing to the further acquisition, rather than when it has acquired its full complement of riches, that the conditions of the labouring poor, of the great body of the poor, seems to be the happiest and the most profitable. It is hard in the stationary, and miserable in the declining state. The progressive state is in reality the cheerful and the hearty state to all the different orders of the society. The stationary is dull, the declining melancholy."<sup>1</sup>

14. Development defined as a sustained increase in per capita national income no doubt creates a potential for a rise in the standard of living of the poorest sections of the community. The increased demand for unskilled labour in the process of development helps to raise the level of employment or the real wage rate depending on the conditions of labour supply. Similarly, in so far as development is associated with increased productivity of agriculture, it may lead to higher incomes for small and marginal farmers. Besides, technical progress leading to increased productivity of the wage goods sectors can have a favourable effect on the real wage rate. However, the actual impact of development on absolute poverty depends on the



institutional arrangements for the ownership and use of means of production, the intensity of the growth process itself, the conditions of supply in the labour market and the extent of State intervention in economic processes.

15. As regards inequality in the size distribution of income, there is the famous Kuznets' inverse - U hypothesis in terms of which the overall inequality first increases and then decreases but may still be higher at the end of the process than at the beginning.<sup>2</sup> Thus, at least in the initial stages, the free play of market forces cannot be relied upon to bring about a reduction in the inequality of income and wealth. It is necessary to evolve a deliberate policy of State intervention to achieve this objective. In devising policy instruments, an important consideration must be to ensure that redistributive policies do not hurt the basic process of growth and capital accumulation. In an open society, redistributive policies often meet stiff resistance from the entrenched privileged groups. However, the political difficulties and the social tensions associated with redistributive policies are likely to be more manageable in a fast expanding economy as compared to a static economy. This is due to the fact that in an expanding economy with rising per capita income, it is possible to redistribute incomes at the margin in favour of the poor without an absolute reduction in top level incomes.

16. For all these reasons, our Five Year Plans have explicitly recognised that a high rate of economic growth sustained over a long period is an essential condition for achieving a rising level of living for all citizens, and especially for those in low income groups or lacking the opportunity to work. The First Five Year Plan had a modest growth target of 2.1 per cent. However, the growth target in the succeeding plans was 4.5 per cent or more.

17. Between 1950-51 and 1978-79, the underlying trend rate of growth of national income was 3.5 per cent per annum, with that of agricultural production and industrial production being 2.7 per cent and 6.1 per cent respectively. In per capita terms, income grew at an average annual rate of 1.3 per cent, which, after allowing for the rising share of investment in national income, meant a modest 1.1 per cent per annum rise in per capita consumption. This sort of growth performance obviously could not make a significant impact on poverty.

18. Available studies indicate a significant relationship between the trend of agricultural production and incidence of rural poverty.<sup>3</sup> However, since agricultural production until the mid-seventies grew at a rate not much higher than the rate of population growth and also because the realised agricultural growth was highly unevenly distributed regionally, it is not surprising that studies of rural poverty do not reveal a strong downward trend in the incidence of rural poverty until the mid-70s.

19. Calculations of growth rates are sensitive to the choice of base and terminal years. However, by now, there is evidence to the effect that the overall rate of growth of the economy as well as the agricultural growth rate have shown an improvement since the mid-seventies. The overall growth rate since then has averaged 4.3 to 4.5 per cent while agricultural production has increased at an average annual rate exceeding 3 per cent. The significant reduction in the incidence of poverty between 1977-78 and 1983-84 seems to have been facilitated by this favourable turn in the growth performance of the economy.

20. Growth does trickle down. However, for the trickle down effect to operate forcefully, growth must be fairly high in relation to the rate of population growth and it must be sustained for a fairly long period of time. In particular, the contribution of sustained agricultural growth is crucial for the removal of poverty. Thus, the realisation of the aggregate growth target and the agricultural production targets of the Seventh Plan will have a major impact on the realisation of the plan target of a further reduction of 10 per cent in the proportion of people living below the poverty line.

#### THE ROLE OF AN EXPANDING PUBLIC SECTOR

21. Right from the very beginning, our Five Year Plans have laid emphasis on the strategic role of the public sector both for accelerating growth and for promoting a more equitable distribution of income and wealth. Thus it was stated in the document of the First Five Year Plan:

"It is clear that in the transformation of the economy that is called for, the State will have to play the crucial role. Whether one thinks of the problems of capital accumulation or of the introduction of new techniques or of the extension of social services or of the overall alignment of the productive forces and class relationships within society, one comes inevitably to the conclusion that a rapid expansion of the social and economic responsibilities of the State will alone be capable of satisfying the legitimate expectations of the people. This need not involve complete nationalisation of the means of production or elimination of private agencies in agriculture or business and industry. It does mean, however, a progressive widening of the public sector and reorientation of the private sector to the needs of a planned economy."<sup>4</sup>

22. Coming as it did soon after the adoption of the Industrial Policy Resolution of 1956, the Second Five Year Plan spelled out in greater detail the role of the public sector in the industrialisation of India. To quote the Second Five Year Plan:

"The use of modern technology requires large scale production and a unified control and allocation of resources in certain major lines of activity. These include exploita-

tion of minerals and basic and capital goods industries which are major determinants of the rate of growth of the economy. The responsibility for new developments in these fields must be undertaken in the main by the State, and the existing units have also to fall in line with the emerging pattern."<sup>5</sup>

"Public ownership, partial or complete, and public control or participation in management are specially required in those fields in which technological considerations tend towards a concentration of economic power and wealth."<sup>6</sup>

"In a growing economy which gets increasingly diversified there is scope for both the public and the private sectors to expand simultaneously but it is inevitable, if development is to proceed at the pace envisaged and to contribute effectively to the attainment of the larger social ends in view that the public sector must grow not only absolutely but also relatively to the private sector."<sup>7</sup>

23. In pursuit of these objectives, the period of the Second Plan and the Third Plan saw a rapid expansion in the role of the public sector in the basic and capital goods industries such as steel, machine building, chemicals, fuel and power. The nationalisation of 14 major commercial banks in 1969 and of the general insurance soon thereafter completed the process of socialisation of the financial sector which began in the 1950s with the nationalisation of the erstwhile Imperial Bank of India and of the life insurance business. The 1970s also saw nationalisation of the coal industry and of oil refineries in the private sector, thereby making the public sector almost wholly responsible for supply of commercial energy in the country.

24. Outside the areas where the public sector was to play a dominant role, the Industrial Policy Resolution stated that preference would be given to the cooperative mode of organisation over the joint stock companies in the private sector. As a result, the role of cooperatives in sectors such as cotton spinning and production of sugar has expanded very considerably.

25. The basic philosophy of industrialisation as embodied in the Second and the Third Plans was based on the following assumptions:

- a) Modern industry characterised by economies of large scale and agglomeration inevitably leads to concentration of sizeable economic power in the hands of a few individuals if it is allowed to operate in the private sector.
- b) Historically, profits of capitalist enterprises have been the most important source of capital accumulation and also inequalities of income and wealth. Socialisation of these profits would accelerate the pace of accumulation as non-essential consumption of private

capitalists would be eliminated. In addition, socialisation of profits would prevent growth of concentration of economic power and lead to a reduction of inequalities of income and wealth associated with private ownership of property.

26. In the initial stages, the public sector expansion was financed by taxation, domestic borrowing at low and very often negative real rates of interest and through external assistance secured on concessional terms. Given the very favourable terms for financing investment in the public sector, a profit making public sector could have a major impact both on the process of accumulation and distribution of income and wealth. However, these expectations have not been fulfilled because of the persistent inability of the public sector to generate reasonable profits in its operations. Significant profits have been generated only by the oil sector, some financial and trading enterprises and a few enterprises in the manufacturing sector. Indeed if depreciation is valued at replacement rather than historical cost, contribution to public savings of public enterprises in such important sectors as coal, steel, fertilizer, power and transport would turn out to be negative.

27. Both continued operational inefficiency and persistent reluctance of political authorities to adjust prices in face of cost increases beyond control are responsible for this outcome. So long as the present trends persist, the potential contribution that the public sector can make to the acceleration of the growth process and the reduction of disparities in income and wealth will not be fully realised. With the disappearance of revenue surpluses of general Government to finance public sector investments and low internal resource generation in the public sector, the further expansion of the public sector can be sustained only by increased borrowing at home and abroad. With a steady rise in the domestic interest rates in the last seven or eight years and the declining trend in concessional aid from abroad, the redistributive impact of an expanding public sector, financed increasingly by borrowing on commercial terms could diminish very fast.

28. Issues relating to the efficient operation of public sector enterprises, particularly those concerning autonomy and accountability and the relationship between the Government and public enterprises, have been endlessly debated for nearly three decades. Yet the process of reform has still to gather necessary momentum. Considering that in our country demands such as privatisation have no widespread support, we have to rely on the public sector to carry forward the process of accumulation and modernisation. This is possible only if the public sector can generate much larger internal resources for its expansion than it has done in the past. A failure to generate adequate internal resources will not only affect the pace of public sector investment but will also limit the country's ability to devote larger resources for expansion of social services and

the anti-poverty programmes. In the process, the cause of both growth and equity is bound to further suffer. Thus a reform of the public sector designed to enhance its resource generating capacity emerges as a key issue of development policy.

#### REGULATION OF THE PRIVATE SECTOR

29. A major assumption of planning in India has been that reliance on physical controls is inevitable in an under-developed economy characterised by structural rigidities. To quote the document of the First Five Year Plan:

"For one to ask for fuller employment and more rapid development and at the same time to object to controls is obviously to support two contradictory objectives."<sup>8</sup>

30. The plan documents recognise that physical controls are administratively cumbersome and may act as disincentives but it has also been felt that "lack of them may create inequalities and hardships to the prejudice especially of classes that need protection most."<sup>9</sup>

31. Broadly speaking, physical controls have taken the following forms:

- a) Price and distribution controls,
- b) Import controls,
- c) Regulation of industrial capacities through a system of industrial licensing.

32. As regards the price and distribution controls, the underlying assumption has been that they are needed to protect the vulnerable sections of the community against inflationary pressures which are inherent in the development process. To quote again from the Second Five Year Plan:

"In a developing country, the basic trend of Government operations in the fiscal and monetary fields is inevitably expansionist. It follows that a curtailment of public expenditure and other curbing devices to control inflation ought to be used in the last resort.

There is always a certain lag between the creation of new incomes and the increase in available supplies on which they can be spent. Agricultural production may fall short of the mark for reasons beyond human control. Other bottlenecks may emerge. Yet a development programme cannot be abandoned or scaled down at the first appearance of difficulties or bottlenecks. A measure of risk has to be taken. This means that there must be correspondingly preparedness to adopt physical controls and allocations as necessary, and these controls and allocations, as experience has shown, cannot work unless they form a fairly integrated system."<sup>10</sup>

33. The plan documents do emphasise that controls on prices and distribution of essential commodities should not be regarded as sufficient by themselves; and that their imposition should be accompanied by measures simultaneously to increase supplies. Yet until recently there was inadequate recognition of the need to fix administered prices at levels which would give producers an adequate incentive to expand production. As a result, shortages tended to persist giving rise to black markets. Moreover, price controls on essential commodities often provided encouragement to diversion of scarce investible resources for the production of uncontrolled less essential commodities. Besides, as the network of price and distribution controls expanded, their administration became all the more cumbersome giving rise to further distortions. As a result, the price and distribution controls did not yield the expected favourable results in terms of improved distribution of income.

34. Fortunately, since the early 1970, there has been a growing awareness that the effectiveness of price and distribution controls is greatly reduced if their number is allowed to proliferate, unmindful of the obvious administrative constraints. Moreover, in fixing prices of controlled commodities, Government have shown increasing awareness of the need to encourage expansion of production. As a result, shortages of essential commodities seem to have declined very substantially in recent years.

35. As regards import controls, their use is inevitable in a situation in which available supplies of foreign exchange are much lower than the sum total of demands for foreign exchange. However, if exports do not increase, the administration of import controls becomes more and more cumbersome, particularly when the economic structure becomes more diversified. Intensification of import controls has often given rise to a pattern of effective protection which encourages production of less essential commodities and also distorts the pattern of income distribution. Yet the reform of the import regime cannot make much headway if export earnings do not go up substantially. The persistence of import restrictions throughout the planning period of 36 years is a manifestation of the continued weakness of India's export effort. The improvement in the foreign exchange situation during the second half of 1970s provided a stimulus to a reform of the rigid import control regime. As a result, shortages of imported raw materials and components have now ceased to be a major cause of under-utilisation of industrial capacities. However, the structure of effective protection implicit in the present system is still far from rational in terms of its allocative impact. Consideration is now being given to replace import controls by tariffs on a gradual basis. However, progress in this direction will greatly depend on the emerging balance of payments situation.

36. The Second Plan period witnessed a considerable expansion of physical controls in the form of industrial licensing restrictions, designed to control the growth of the private sector in accordance with plan priorities and with a view to curbing concentration of economic power in the hands of a few. The dominant philosophy was that "the public sector has to grow and grow rapidly" and the private sector has to play its part within the framework of the comprehensive plan accepted by the community.<sup>11</sup> The extensive powers available to the Government under the Industries (Development and Regulation) Act were sought to be used to control the growth of large existing businesses, and to encourage growth of new entrepreneurs, small scale and medium enterprises and cooperative organisations.

37. When the Third Plan came to be drafted, it was known that "dealing with the problems of concentration of economic power, there is already general agreement on the broad objectives, and the necessary legislative and other sanctions needed are in fact available for the greater part."<sup>12</sup> However, subsequently it was considered necessary to strengthen the provisions of industries (Development & Regulation) Act by the enactment of the Monopolies and Restrictive Trade Practices Act so as to control more effectively the concentration of economic power in private hands.

38. Industrial licensing is rather easy to administer when the industrial structure is relatively simple. However, as the economic structure becomes diversified, it becomes more and more difficult to predict the likely medium term demand for a large number of inter-related products. Thus, industrial licensing cannot prevent emergence of imbalances between demand and supply. At the same time, restrictions on the growth of firms often stand in the way of full utilisation of economies of scale and progressive upgradation of technology. Besides, controls on expansion cause considerable delay and thereby prevent businessmen in responding speedily to the emerging challenges. It is now generally agreed that the continuation of an extensive system of import controls. Industrial licensing and other restrictions on the growth of efficient firms have led to the perpetuation of a highly protected inefficient industrial structure, with little competitive pressure and incentive for cost reduction and quality improvement.

39. The preceding argument does not imply that the concern about the conservation of scarce domestic savings and foreign exchange resources for essential priority sectors or about the need to encourage the growth of new, small scale and medium enterprises or about the concentration of economic power is unjustified. What is being suggested is that the control system we have devised has significant social and economic costs and it has also not been able to prevent diversion of scarce resources to low priority uses. Nor has it been sufficiently effective in preventing concentration of economic power or in bringing about a significant

redistribution of income and wealth. Thus in the interest of both growth and equity, it is necessary to streamline and simplify the control mechanism. Careful planning of large capital intensive and import intensive projects is no doubt unavoidable. However, in several cases the objectives sought to be achieved by industrial licensing and involving detailed case by case examination of each proposal, could be realised through simpler administrative devices. For example, the diversion of scarce resources to low priority industries could be stemmed by specifying a negative list of industries whose growth is to be discouraged in a plan period. In the same manner, the desire to promote greater regional balance could be satisfied by having a negative list of locations where expansion of industry was to be discouraged. The small scale and new entrepreneurs could be better helped through positive promotional measures designed to overcome their handicaps, such as in their access to the capital markets, rather than by curbing the growth of large efficient firms. The attempt to control monopoly by restricting the expansion of more efficient firms imposes significant social costs on the economy and this approach could be replaced by more effective policing of restrictive trade practices and other devices which can lead to the use of market power in a manner detrimental to the public interest. Similarly, while import controls and the protection they and the tariff afford to the domestic industry cannot be dismantled particularly in a situation of acute shortage of foreign exchange, we must begin to take greater notice of the social costs of excessive protection. Economists in our country have shown inadequate recognition of the fact that protection of one industry implies taxation of another. The discrimination implicit against exports in the present structure of protection has hurt our country's ability to promote exports and have a more viable balance of payments. Thus, as a beginning, the level of protection granted to an industry whose output enters as an input into a large number of other industries should be kept under systematic review. In particular, no industry should be granted protection for more than ten years at a time and the grant of protection should be accompanied by a concrete programme of cost reduction and quality improvement. At the end of ten years, there should be a thorough review of the industry's performance before conceding its claim for further protection. In this way, we may be able to introduce in our industrial structure some pressure for reduction of costs and quality improvement. Physical controls at strategic points may be unavoidable in a planned economy. However, an over extended system of physical controls which cannot be effectively administered may be counter productive. In the absence of reform, a low level equilibrium may well persist involving significant costs in terms of lost opportunities of both growth and greater social justice. Fortunately, the need for reform is now widely recognised and Government has taken several measures to streamline and simplify the control system.



## THE ROLE OF FISCAL AND MONETARY POLICIES

40. Our plan documents have been conscious of the positive role of fiscal measures in reducing inequalities of income and wealth. However, they have also shown awareness of the limitations of fiscal policy as a device for redistribution of incomes. As early as the Second Plan, it was recognised that "the Indian income tax is highly progressive and apparently the scope for enlarging public revenue or reducing inequalities through a stepping up of these rates is not large."<sup>13</sup> There was also the realisation that "some of the measures which might reduce inequalities are apt to react adversely on incentives."<sup>14</sup> The Second Plan referred to the favourable impact of an expenditure tax on incentives to save and work but it also recognised the various administrative difficulties in instituting an expenditure tax as a substitute for income tax. The Plan also referred to the redistributive potential of Estate Duty but it also noted ruefully that this duty which had been imposed in the First Plan period had not yielded any significant revenue.

41. Overall, our plan documents have stressed the need for measures to check tax evasion and a widening of tax base by bringing in wealth and property as a possible means of reducing inequalities. The successive plans have also noted the heavy reliance on indirect taxation in our tax system. While recognising that the indirect taxes tend to be regressive in terms of their redistributive impact as compared to direct taxes, the plan documents have taken the pragmatic view that for obvious administrative reasons the heavy reliance on indirect taxation could not be avoided in the present stage of our development.

42. Altogether, our plan documents have shown a realistic appreciation of the potential of fiscal policy in curbing inequalities of income and wealth. Yet there is ample evidence that even the available potential has not been realised. This is because until the mid-seventies, populist pressures often stood in the way of a genuine tax reform. In the mid-fifties, despite Lord Kaldor's plea for moderation and a maximum marginal income-tax rate of 45 per cent, his proposals for expenditure tax, wealth tax, gift tax and capital gains tax were superimposed on an already steeply progressive income-tax. Tax compliance suffered not only because of a highly unrealistic tax rate structure but also because of a visible deterioration in the quality of tax administration. In this manner, the growing tax evasion became a principal source of generation of black incomes. Fortunately, in recent years there has been a growing realisation that confiscatory rates of direct taxes do not serve the cause of equity in a mixed economy and that moderation in taxation coupled with a firm resolve to enforce tax compliance can be productive of better results. If this approach leads to faster growth in direct tax revenues and a rise in the share of direct taxes in total tax collections, it will help to promote the cause of equity.

However, in a mixed economy the redistributive impact of taxation should not be overestimated.

43. As regards credit policy, successive Five Year Plans have emphasised the need to reorient the deployment of bank credit to finance the credit needs of hitherto neglected sectors. In particular, since 1954 there have been significant developments in the expansion and institutionalisation of rural credit. In 1984-85, the cooperative credit institutions disbursed Rs. 3250 crores as compared with Rs. 214 crores in 1960-61. There are today 97000 primary agricultural credit societies with a membership of 650 lakhs. The number of rural branches of commercial banks (including regional rural banks) has gone up from 1505 in June 1969 to 29821 in June 1985. Special emphasis is being laid on meeting the credit needs of small and marginal farmers, landless labourers and rural artisans.

44. The country today has an impressive credit structure which can greatly help to accelerate the tempo of rural development by providing the requisite credit support at reasonable rates of interest. Unfortunately, the vast latent potentialities of this structure for promoting growth with social justice have not been fully realised because of inadequate emphasis on local level planning, the continuing weakness of development administration at the grassroot level, the increasing politicisation of institutions such as cooperatives and the growing incidence of wilful default on the part of more powerful and influential borrowers. This happens to be another area which ought to figure prominently on the agenda for reform.

45. Our development plans have recognised the role of overall fiscal and monetary discipline in regulating the ebb and flow of economic activity. However, adequate effort has not been devoted to reconciling the requirements of short term management of aggregate demand and the imperatives of medium term development. At times, the underlying expansionary bias of fiscal and monetary policies has led to severe inflationary pressures particularly when overall excess demand in the system happened to coincide with poor harvests. The resulting inflationary pressures have not only distorted resource allocations but have also led to a rise in the prices of essential commodities with inevitable adverse effects on income distribution. Increased reliance on deficit financing and indirect taxes has at times weakened the income redistribution impact of other policies favouring the poorer sections.

46. Since the mid-70s, the improvement in the balance of payments by permitting increased imports of essential commodities in periods of shortages, has helped to neutralise to some extent the adverse price effects of domestic supply-demand imbalances. Besides, the more favourable outturn on the food front and accumulation of large food stocks with the public sector have helped to keep food

prices as well as inflationary expectations in check. Higher agricultural production and stable food prices are known to have had a favourable impact on rural poverty as well. The food buffer stock and a viable system of public distribution provide valuable protection to more vulnerable sections in the event of an inflationary price rise.

47. The balance of payments position is now by no means very comfortable and, judging by past trends, food stocks can also be depleted if we run into an adverse weather cycle lasting more than one year. Thus, continued vigilance on the inflation front is absolutely necessary. Deficit financing beyond limits of prudence can be a very regressive method of resource mobilisation. It can affect adversely pursuit of both growth and equity.

#### INSTITUTIONAL REFORMS

48. Land being the primary resource in an agrarian society, successive Five Year Plans have laid considerable emphasis on a just and rational pattern of land ownership and land tenure. The main elements of the land reforms policy have been five-fold viz.:

- i) abolition of intermediary tenures;
- ii) tenancy reforms comprising regulation of rent, security of tenure and conferment of ownership rights on tenants;
- iii) ceilings on land holdings and distribution of surplus land;
- iv) consolidation of holdings; and
- v) compilation and updating of land records.

49. The abolition in the 1950s of intermediary tenures like zamindaris, jagirs, inams etc. which prevailed in nearly 40 per cent of the area of the country was a major achievement. As a result, more than 20 million tenants have been brought in direct contact with the State. Besides, an estimated 6 million hectares of waste, fallow and other classes of land have been vested in the State, a large proportion of which has been distributed to the landless and marginal landholders.

50. Subsequent developments have, however, not been very encouraging. The Sixth Plan summed up the position in the following words:

"The land reforms policy, outlined above, which has been under implementation, is a comprehensive one and has been nationally accepted. If the progress of land reforms has been less than satisfactory it has not been due to flaws in policy but to indifferent implementation. Often, the necessary determination has been

lacking to effectively undertake action, particularly in a matter of implementation of ceiling laws, consolidation of holdings and in not vigorously pursuing concealed tenancies and having them vested with tenancy, occupancy rights as enjoined under the Law."<sup>15</sup>

51. Since the inception of land ceilings programme, a total of 29.40 lakh hectares have been declared surplus. Of this, 23.19 lakh hectares have been taken possession of and 17.52 lakh hectares have been distributed to 33.76 lakh persons. The area declared surplus till now is less than 2 per cent of the cultivated area. Even so, a large extent of land out of the declared surplus is held up due to litigation and is not available for distribution. Clearly, there has been a lack of political will to implement faithfully the legislation on land ceilings.

52. In the First and the Second Five Year Plans, it was felt that schemes of land redistribution, essential though they were, might not confer significant benefit on the landless. Therefore, planners took the view that we must think in terms of more basic institutional changes which would create conditions of equality for all sections of the rural population. Small and uneconomic holdings were seen to be at the root of many of the difficulties in the way of agricultural development and cooperative farming, though on a voluntary basis, was seen to be the way out. However, the planners looked beyond cooperative farming and towards the cooperative management of the entire village economy for the basic reconstruction of the village economy to create conditions of equality of opportunity for the landless agricultural workers. The village panchayat was to become the agency for land management and land reform in the village. To quote the First Five Year Plan:

"The possibility of achieving greater social justice through regulation of contractual terms between different constituent elements in the village is soon exhausted. Apart from sharpening the conflict of interest within the rural community, proposals for further regulation became in effect proposals for sharing poverty. While the objective of family holdings with increasing emphasis on cooperative methods of organisation may represent the most practical action to principle of "land for the tiller", the objective fulfilment of this very principle requires that there should be a more comprehensive goal towards which the rural economy should be developed."<sup>16</sup>

53. The process of democratic decentralisation implicit in the establishment of the Panchayati Raj institutions in the mid-50s created expectations of a revolutionary change in the structure of administration at the grassroot level. These institutions were visualised as the path finders of a new non-violent transformation of our rural society. However, these expectations have not materialised. As pointed

out in the document of the Seventh Five Year Plan, "in terms of instruments of planning community development, the Panchayati Raj institutions have been reduced to an extremely peripheral status" and "they have for a variety of reasons not been actively and effectively involved in the implementation of rural development programmes except in a few States."<sup>17</sup> The plan document also notes, "On the other hand it has been seen that wherever this has happened the quality of programme implementation has been decidedly better."<sup>18</sup>

54. Proposals for cooperative farming and cooperative village management met with strong resistance from the entrenched privileged groups in the rural areas. As a result, no worthwhile progress was made for the implementation of these proposals. Thus, with the arrival of the new agricultural technology, it was found expedient to shift the emphasis from cooperativisation of the rural economy to promotion of input oriented agricultural development in areas of assured rainfall or irrigation. The focus of attention thus shifted to taking advantage of the development potential offered by progressive farmers. By the time the Fourth Plan was launched, it was realised that this strategy could accentuate disparities in income not only between small and large farmers but also between different regions. This recognition led to the adoption of special programmes designed to increase the productivity and earning capacity. However, the emphasis was on provision of inputs and adoption of new technologies. No attempt was made to revive the earlier interest in cooperative farming and cooperative village management.

#### SPECIAL PROGRAMMES FOR UNDER-PRIVILEGED GROUPS

55. In the Sixties, the realisation that the normal processes of development could not take care of the interests of small and marginal farmers and agricultural workers and the lack of progress in the direction of cooperative farming and cooperative village management led to search for some special programmes for the uplift of these groups. Thus, the Third Plan laid emphasis on a large scale programme of rural works especially in densely populated regions and seeking to provide supplementary employment during periods of under-employment in the slack agricultural season. In the Fourth Plan, the recognition that the rural works programme could not yield results commensurate with the expenditure because it was not integrated into local level planning, led to the merger of this programme into an area development oriented Drought Prone Areas Programme. Problems of poverty are most acute in those 130 districts which receive low to medium rainfall under 1125 mm and also have limited irrigation facilities. Therefore, the Fourth Plan envisaged a substantial expansion of dry farming projects seeking to develop an integrated package of technology suited to these areas.

56. Since the new agricultural technology tended to add a further dimension of disparity between those who have the resources to make use of it and those who have not, the Fourth Plan suggested the establishment of Small Farmers Development Agencies charged with the responsibility of helping small but potentially viable farmers by ensuring availability of inputs, services and credit through the existing institutions. To focus more sharply on problems faced by the Scheduled Tribes and the Scheduled Castes, the Tribal Sub-Plan approach was adopted in the Fifth Plan, and in the Sixth Plan, Special Component Plans were formulated for the Scheduled Castes. These resulted in earmarked allocations for the Tribal Sub-Plan and the Scheduled Caste Programmes, in addition to the general programmes of economic development undertaken by the Central and State Governments.

57. In the initial stages, the special programmes were in the nature of experimental programmes. As such, their impact was rather small. It was only in the Sixth Plan that the coverage of various special programmes expanded significantly so that one could begin to feel their impact. Thus, the Sixth Plan launched a nation-wide National Rural Employment Programme designed to provide gainful employment in rural areas to the extent of 300-400 million mandays per annum and create durable community assets. In addition, on 15th August, 1983, a new employment promotion programme called Rural Landless Employment Guarantee Programme was launched with a view to providing guarantee of employment to at least one member of every landless household upto 100 days in a year and by creating durable assets for strengthening the infrastructure of the rural economy. Similarly, the Sixth Plan witnessed the launching of a large scale programme of asset endowment under the IRDP designed to develop self-employment ventures in a variety of activities in rural areas. The target was to cover 15 million beneficiaries at the rate of 600 per block per year. With a view to diversifying the occupational structure, it was stipulated that 33 per cent of the beneficiary coverage should be in the secondary and tertiary sectors. The assets provided to the selected households were financed through a mix of Government subsidies and institutional credit on an average subsidy credit ratio of 1:2. The capital cost of the assets was subsidized to the extent of 25 per cent for small farmers, 33.3 per cent for marginal farmers, agricultural labourers and rural artisans and 50 per cent for the Scheduled Tribes. A family could receive upto Rs. 3000 by way of subsidy. In drought prone areas, the limit of subsidy ceiling was Rs. 4000 while for the tribal beneficiaries it was Rs. 5000.

58. The various anti-poverty programmes are sought to be further expanded in the Seventh Plan. As to their impact, the picture is a mixed one. This is not surprising since they were expanded very substantially in the Sixth Plan, often without prior preparations for the build up of supporting infrastructure. There are inherent difficulties

in asking the poorest of the poor to assume the entrepreneurial functions, including risk and uncertainty, that inevitably go with any self-employment venture. For the very poor, as Prof. Rath has argued so cogently, it may often be more productive to lay emphasis on provision of wage employment. With regard to the IRDP, there have also been complaints about the wrong identification of beneficiaries (benefits being cornered by really not so poor persons), leakages (subsidy being misappropriated by bank officials and block development officials and other local functionaries), and poor income generation (due to faulty project preparation, lack of effective supervision of credit and failure to provide timely technical assistance to deal with unexpected problems that may arise in project implementation). Similarly, in employment promotion programmes, there have been complaints that for want of adequate emphasis on comprehensive area development and effective project preparation, there is often a dearth of viable project proposals. Thus, a disproportionate amount of expenditure seems to have been spent on the building of roads. There are also persistent complaints that the implementing structures continue to be a weak element and that grassroot level official functionaries often lack both the motivation and technical skills to discharge their onerous responsibilities.

59. Given the magnitude of rural poverty, there is now general agreement in the country that large scale employment schemes and self-employment promotion programmes have to be accepted as an integral part of our long term development strategy. There is also agreement that the mix of the two sets of programme could be varied depending on specific circumstances of each region or block. It further appears that the current situation in which a large number of beneficiary oriented and area development programmes seem to be operated in isolation is not conducive to optimal use of available scarce resources. It is also becoming apparent that the various anti-poverty programmes can make a lasting impact on employment only if there is an increase in agricultural productivity and incomes which can generate higher demand for the output and services provided by workers in the secondary and tertiary sectors.

60. For all these reasons, the time has come to integrate these programmes, including programmes for social services, into the framework of comprehensive local level planning. Unfortunately, local level planning has yet to take firm roots. As part of strengthening the local level planning capabilities, the technical expertise of the rural development administration at all levels will need to be substantially upgraded. Too often, there has been a tendency in our country to believe that rural development can be brought about rather cheaply. This is a mistaken belief. In addition, if various leakages are to be avoided, it is necessary to revive and revitalise the Panchayati Raj institutions as a means of enlisting requisite public cooperation

and support for programmes of grassroots development. Furthermore, it must also be appreciated that the pace at which these programmes can be expanded in the future is a function of both financial resources and build-up of administrative capabilities at the grassroots level. It is only on the basis of a sound and elastic public financial system that we can devote increasing volumes of resources simultaneously for productive investments, social services and anti-poverty programmes.

#### CONCLUDING REMARKS

61. In the preceding analysis, I have tried to highlight the reasons for our limited gains in terms of social justice under planning. This analysis brings out that progress towards poverty eradication can be accelerated by:

- a) a fairly high rate of economic growth maintained over a long period;
- b) a sustained increase in agricultural production;
- c) an expanding public sector with a growing capacity for generation of internal resources; and
- d) a combination of efficiently administered programmes designed specifically to increase incomes and productivity of the poorer sections and to improve their access to basic social services particularly education and health.

62. Physical controls at strategic points and sound fiscal and monetary policies are no doubt also essential for an orderly management of the economy. However, in view of the inherent administrative constraints, one must not overestimate the redistributive potential of either physical controls or fiscal policies. Indeed past experience shows that an over-extended system of physical controls and a seemingly progressive tax system which cannot be made effective are often counter-productive in terms of their impact on both growth and equity.

63. As to the future, I remain convinced that even within the overall framework of the existing development strategy for which there is today a broad national consensus, it is possible to make much faster progress towards the removal of poverty in years to come. However, the underlying potential can be realised only if policies and programmes are so oriented as to fulfil the following conditions:

- a) We are successful in stabilising the aggregate growth rate of economy at a minimum level of 5 per cent per annum.
- b) Agricultural growth rate is stabilised at close to 3.5 to 4.0 per cent per annum, there is greater regional



balance in agricultural development and particular attention is paid to increasing the productivity of small and marginal farmers.

- c) The satisfaction of basic human needs is given on overriding priority in resource allocation and there is a clearer indication of national priorities so that scarce resources are not diverted to less essential uses.
- d) There is a major reform of the public sector so as to enhance its internal resources generating capacity to finance its future expansion.
- e) The elasticity of the tax system is improved through a rate structure which is realistic and through administrative reforms which induce stricter enforcement and compliance.
- f) Inflationary pressures are kept strictly under control and in particular, through arrangements such as adequate buffer stocks, prices of foodgrains are prevented from rising unduly in years of drought.
- g) The industrial sector is freed of such controls which serve no useful social purpose so that it can grow at an average annual rate of 8 per cent leading to faster growth of public revenues and employment outside agriculture.
- h) The requisite political will is generated to implement sincerely the nationally accepted policies regarding ceilings on land holdings, protection of share croppers and consolidation of holdings.
- i) The various area development and beneficiary oriented programmes are integrated into a consistent package based on detailed analysis of local needs, resource potential and capabilities. There should be a revamping of the administration of agricultural and rural development programmes, with much greater emphasis being placed on upgradation of technical and managerial skills and improvement of motivation of functionaries at the grassroot level.
- j) The Panchayati Raj institutions and the cooperative movement are revitalised so as to provide effective public support and assistance which are vital for the success of programmes of rural development.
- k) Social services particularly Education and Health are expanded fast enough to universalise elementary education and to reduce infant mortality rate to no more than 60 per 1000 live birth. Greater equity in the access to basic social services is essential for progress towards greater equity in development. Apart

from improving the capabilities of the poor to participate in economic processes more effectively, emphasis on education, particularly of girls and on reduction of infant mortality rate, will help to generate a climate conducive to the acceptance of the small family norm, without which a substantial improvement in living standards of the poor may not be possible.

64. The country has now the necessary administrative, managerial, technical and financial capabilities to soften very considerably the harsh edges of extreme poverty. It has of course to be emphasised that the progress towards a just society is not merely one of providing more income and job opportunities or more equal access to the basic social services. Determined action will be necessary to reform and refashion our social and economic institutions so that barriers to social mobility and progress rooted in the rigidities of our social structure are removed. We have a long journey ahead of us in our quest for a more equitable society. What is required is that the collective will of the nation is brought to bear on this problem so that we can mobilise all our latent resources for a successful social and economic transformation of Indian society.

#### Foot-notes

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## R.B.R.R. KALE MEMORIAL LECTURES

<u>Lecture</u>	<u>Subject</u>	<u>Year</u>
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3. B.R. AMBEDKAR	Federation versus Freedom	1939
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7. S.G. VAZE	The Formation of Federations	1943
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