

BUDGET ESTIMATES

OF

EXPENDITURE ON DEFENCE SERVICES

(ARMY, AIR FORCES AND ROYAL INDIAN NAVY)

FOR THE YEAR

1940-41

AND OF

CONNECTED RECEIPTS

SUMMARY OF ESTIMATES BY MAJOR HEADS.

	Accounts, 1938-39.			Budget Estimate, 1939-40.			Revised Estimate, 1939-40.			Budget Estimate, 1940-41.		
	Gross expendi- ture.	Receipts.	Net expendi- ture.	Gross expendi- ture.	Receipts.	Net expendi- ture.	Gross expendi- ture.	Receipts.	Net expendi- ture.	Gross expendi- ture.	Receipts.	Net expendi- ture.
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
⁵⁸ XLVII DEFENCE SERVICES— EFFECTIVE.	43,74,44,602	5,43,16,294	38,31,28,308	46,22,85,000	8,29,89,000	37,92,96,000	40,87,54,000	...	40,87,54,000	45,35,81,000	...	45,35,81,000
⁵⁹ XLVIII DEFENCE SERVICES— NON-EFFECTIVE.	8,56,88,194	45,73,861	8,11,14,333	8,62,88,000	45,37,000	8,17,51,000	9,04,78,000	63,41,000	8,41,37,000	8,61,14,000	44,77,000	8,16,37,000
60. TRANSFERS TO FROM DEFENCE RESERVE FUND.	-24,42,641	...	-24,42,641	-92,47,000	...	-92,47,000	...	...	...	...	...	...
TOTAL	52,06,90,155	5,88,90,155	46,18,00,000	53,93,26,000	8,75,26,000	45,18,00,000	49,92,32,000	63,41,000	49,28,91,000	53,96,95,000	44,77,000	53,52,18,000

SUMMARY OF ESTIMATES UNDER MAJOR HEAD 58/XLVII—DEFENCE SERVICES—EFFECTIVE.

	Accounts, 1938-39.			Budget Estimate, 1939-40.			Revised Estimate, 1939-40.			Budget Estimate, 1940-41.				
	Gross expenditure.	Receipts.	Net expenditure.	Gross expenditure.	Receipts.	Net expenditure.	Gross expenditure.	Receipts.	Net expenditure.	Gross expenditure.	Receipts.	Net expenditure.		
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.		
MAIN HEAD 1.— NORMAL COST OF DEFENCE SERVICES—EF- FECTIVE	43,74,44,602	5,43,16,294	38,31,28,308	46,22,85,000	8,29,89,000	37,92,96,000	36,76,63,000	...	(a)	36,76,63,000	...	(a)	36,76,63,000	
MAIN HEAD 2.— LUMP PROVI- SION FOR IN- CREASE IN PRICES.	25,00,000	...	(a)	25,00,000	2,00,00,000	...	(a)	2,00,00,000
MAIN HEAD 3.— WAR MEA- SURES CHARGE- ABLE TO INDIAN REVE- NUES.	3,85,91,000	3,85,91,000	6,59,18,000	6,59,18,000
TOTAL	43,74,44,602	5,43,16,294	38,31,28,308	46,22,85,000	8,29,89,000	37,92,96,000	40,87,54,000	...	40,87,54,000	45,35,81,000	45,35,81,000	

(a) Lump sum provision of which no details are given.

	Accounts, 1938-39.	Budget Estimate, 1939-40.	Revised Estimate, 1939-40.	Budget Estimate, 1940-41.
	Rs.	Rs.	Rs.	Rs.
MAIN HEAD 3.—WAR MEASURES CHARGEABLE TO INDIAN REVENUES.				
SUB-HEAD A.—CERTAIN MEA- SURES OF MILITARY DE- FENCE.				
MINOR HEADS—				
(a) Indian Territorial Force	21,00,000	53,64,000
(b) Indian States Forces	1,00,000	2,00,000
(c) Auxiliary Force	10,26,000	12,26,000
(d) Miscellaneous additional units and formations	6,73,000	17,41,000
(e) Nepalese Contingent	58,000	7,57,000
(f) Training Schools	3,03,000	6,39,000
(g) Port Defence	6,76,000	11,72,000
(h) Aliens Camp	1,85,000	4,47,000
(i) Censorship expenses	6,99,000	13,61,000
TOTAL SUBHEAD A.	58,20,000	1,29,07,000
SUB-HEAD B.—CERTAIN MEA- SURES CONNECTED WITH AIR DEFENCE	3,51,000	11,31,000
SUB-HEAD C.—CERTAIN MEA- SURES CONNECTED WITH LOCAL NAVAL DEFENCE	33,91,000	59,70,000
SUB-HEAD D.—STORES	75,14,000	1,67,80,000
SUB-HEAD E.—WORKS	17,79,000	73,49,000
SUB-HEAD F.—MISCELLANEOUS	62,36,000	1,97,81,000
SUB-HEAD G.—WAZIRISTAN	35,00,000	20,00,000
SUB-HEAD H.—PAYMENT TO HIS MAJESTY'S GOVERN- MENT ON ACCOUNT OF EXTRA COST OF EX- TERNAL DEFENCE TROOPS	1,00,00,000	..
TOTAL MAIN HEAD 3.	3,85,91,000	6,59,18,000

	Accounts, 1938-39.	Budget Estimate, 1939-40.	Revised Estimate, 1939-40.	Budget Estimate, 1940-41.
	Rs.	Rs.	Rs.	Rs.
MAJOR HEAD 59.—DEFENCE SERVICES—NON-EFFECTIVE EXPENDITURE.				
MAIN HEAD 1.—ARMY.				
MINOR HEAD (a) REWARDS FOR MILITARY SERVICES.				
Detailed heads.				
(1) Payments in connection with Victoria Cross, Military Cross, Order of British India, Indian Order of Merit, etc.		5,63,000		5,62,000
(2) Annuities and gratuities		30,000		32,000
(3) Jangi-Inams		9,55,000		9,52,000
(4) Decorations and Medals		2,31,400		23,000
TOTAL MINOR HEAD (a)	16,18,316	17,79,400	18,37,000	15,69,000
MINOR HEAD (b) PENSIONS.				
Detailed heads.				
(1) Pensions and Gratuities to Europeans and their families		22,58,000		22,78,000
(2) Pensions and Gratuities to Indians and their families		3,09,95,000		3,07,73,000
(3) Miscellaneous		4,04,600		4,80,000
(4) Equated payments of Committed or Capitalised value of pensions under Civil Service Regulations		12,31,000		13,11,000
(5) Equated payments of Committed or Capitalised value of pensions under Military Regulations		9,55,000		10,59,000
(6) Allowances to officers on Special Unemployed list		..		30,000
TOTAL MINOR HEAD (b)	3,57,81,788	3,58,43,600	3,92,88,000	3,59,31,000
MINOR HEAD (c)—ENGLAND.				
Detailed heads.				
(1) Payments to War Office for retired pay, etc., of British Forces for service in India.		1,67,34,000		1,66,72,000
(2) Pensions and gratuities to Europeans and their families		3,36,00,000		3,33,84,000
<i>Deduct</i> —Chargeable against Civil Departments		—34,00,000		—33,60,000
(3) Pensions and gratuities to Indians and their families		23,000		22,000
(4) Indian Military Service Family Pensions		..		..
(5) Miscellaneous Military decorations and medals, medical treatment of retired Officers, etc.		88,000		91,000
(6) Allowances to Officers on Special Unemployed List		..		4,72,000
TOTAL MINOR HEAD (c) England	4,64,39,090	4,70,45,000	4,82,79,000	4,72,81,000
MINOR HEAD (d) EXCHANGE	3,07,143	..	..	..
TOTAL EXPENDITURE, MAIN HEAD 1.	8,41,46,337	8,46,68,000	8,94,04,000	8,47,81,000

	Accounts, 1938-39.	Budget Estimate, 1939-40.	Revised Estimate, 1939-40.	Budget Estimate, 1940-41.
	Rs.	Rs.	Rs.	Rs.
MAIN HEAD 2.—AIR FORCES.				
MINOR HEADS—				
(a) REWARDS FOR MILITARY SERVICES	605	4,000	7,000	1,000
(b) PENSIONS	13,255	62,000	11,000	15,000
(c) ENGLAND—				
Detailed heads.				
(1) Payment to Air Ministry for retired pay of R. A. F. British personnel for service in India		5,10,000		2,94,000
(2) Pensions		9,000		9,000
TOTAL MINOR HEAD (c)	5,15,973	5,19,000	61,000	3,03,000
MINOR HEAD (d) EXCHANGE	3,665	..	..	..
TOTAL EXPENDITURE MAIN HEAD 2	5,33,498	5,85,000	79,000	3,19,000
MAIN HEAD 3.—ROYAL INDIAN NAVY.				
MINOR HEAD (a)—INDIA.				
Detailed Heads :—				
(1) Pensions		1,20,460		1,17,050
(2) Pensions paid under Admiralty scheme		3,000		3,000
(3) Awards from civil compassionate fund to civilians paid from Defence Estimates		1,540		1,540
(4) Equated payments of Computed or Capitalised value of pensions under Civil rules		27,000		27,150
(5) Equated payments of Computed or Capitalised value of pensions under Military rules		17,000		26,260
(6) Fractional differences		..		..
TOTAL MINOR HEAD (a)	1,69,628	1,69,000	1,69,000	1,75,000
MINOR HEAD (b)—ENGLAND.				
Detailed heads :—				
(1) R. I. N. retired pay and miscellaneous pensions		9,70,000		9,39,000
.. Deduct—Chargeable against Civil Departments		—1,04,000		—1,00,000
TOTAL MINOR HEAD (b)	8,33,692	8,66,000	8,26,000	8,39,000
MINOR HEAD (c) EXCHANGE	5,039	..	..	..
TOTAL EXPENDITURE MAIN HEAD 3	10,08,359	10,35,000	9,95,000	10,14,000
TOTAL EXPENDITURE MAJOR HEAD 59.	8,56,88,194	8,62,88,000	9,04,78,000	8,61,14,000

	Accounts, 1938-39.	Budget Estimate, 1939-40.	Revised Estimate, 1939-40.	Budget Estimate, 1940-41.
	Rs.	Rs.	Rs.	Rs.
MAJOR HEAD XLVIII.—DEFENCE SERVICES, NON-EFFECTIVE.				
RECEIPTS.				
MAIN HEAD I.—ARMY.				
MINOR HEADS—				
(a) Rewards for Military Services		8,000	8,000	3,000
(b) Pensions		8,92,000	8,92,000	8,72,000
(c) England—				
Detailed heads :—				
(1) Recoveries from Imperial Government in respect of overseas service, Indian troops :—				
War Office for retired pay, etc.		34,58,000		34,14,000
Other Pensionary contributions		60,000		72,000
(2) Recoveries from Civil Revenues, etc. in respect of pensions charged to "Army" in previous years		80,000		80,000
(3) Refund of short service gratuities		1,000		1,000
(4) Hospital stoppages of retired officers and miscellaneous receipts		32,000		32,000
TOTAL MINOR HEAD (c)		36,31,000	37,35,000	35,99,000
TOTAL MAIN HEAD I	45,63,209	45,31,000	46,35,000	44,74,000
MAIN HEAD II.—AIR FORCES.				
MINOR HEAD (a)—INDIA.				
Detailed heads :—				
(1) Fractional differences				
(2) Decorations and medals				
TOTAL MINOR HEAD (a)				
MINOR HEAD (b)—ENGLAND.				
Miscellaneous Receipts			17,03,000	
TOTAL MAIN HEAD II			17,03,000	
MAIN HEAD III.—ROYAL INDIAN NAVY.				
MINOR HEAD (a)—INDIA.				
Recoveries on account of pensions		3,000		
MINOR HEAD (b)—ENGLAND.				
Miscellaneous		3,000	3,000	3,000
TOTAL MAIN HEAD III	10,852	6,000	3,000	3,000
TOTAL RECEIPTS—MAJOR HEAD XLVIII	45,73,861	45,37,000	63,41,000	44,77,000

Budget, 1941-42

Finance Member's Speech

The task which falls to me of placing before this House an account of the main developments since the last annual budget was discussed, has on the present occasion been somewhat lightened by the fact that I made a financial statement during the last session in November 1940, in the course of which I drew the picture of our finances as it then presented itself. As the facts then brought out will be relatively fresh in the minds of Hon'ble Members, I shall today devote myself largely to bringing that account up to date, and in particular to a description of the progress of India's war effort in the field of the defence services and of supply. This course, in addition to meeting what I am sure is the desire of this House, will also furnish the most suitable basis for an understanding of our financial position. I shall also take this opportunity of furnishing a fuller explanation of the operations recently announced in connection with the repatriation of a large part of our sterling debt.

2. When speaking of the Indian economic situation in my first Budget Speech, I qualified my reference to the favourable features which were then manifest by emphasising the extent to which the continuance of prosperity was dependent on our ability to export freely overseas. The events of last spring and summer deprived us of our markets on the European Continent and caused a serious deterioration in the volume and facility of the shipping services available for our use. These factors, together with a temporary decline in confidence, which reduced the willingness to hold stocks, resulted in a marked fall of prices in the summer of 1940. This recession has, however, been magnified in some quarters to undue proportions, and it is well to view the facts in proper perspective. In the first nine months of the fiscal year 1938-39, our exports to all destinations amounted to 122 crores; in the first nine months of the present fiscal year they amounted to 144 crores. Thus the development of new export markets very largely compensated for the loss of old ones. In the second place, prices as a whole are still some fifteen per cent higher than they were at the beginning of September 1939 and those of certain commodities, e.g., raw materials, are considerably higher. Thirdly such indices as are available of general economic conditions in India, such as railway traffic and postal receipts, continue to reflect an improvement over pre-war conditions.

3. To this improvement the steadily growing war effort most powerfully contributes. Last year that effort, on the side of the production of stores and of commodities required in connection with the war had barely begun; the tide of production is now rising rapidly and may be expected to exercise a generally beneficial effect upon the volume of employment and therefore upon the size of the national income. The holding of the Eastern Group Conference in this country and the establishment, consequent upon the deliberations of that Conference, of an inter-Imperial Supply Council at Delhi, illustrate in striking manner the position of India in the present war. No one would wish to see repeated the period of hectically inflated prices which ruled towards the end of the last war, but we can rely upon steadily increasing industrial effort during the present one, with consequences which seem likely permanently to affect India's position among the industrial nations of the world. The expansion in the demand for the products of Indian industry and the organized efforts which Government are making to increase the supply of trained workers must create an enhanced productive power which will be available in

the period after the war, to improve the standard of life in India and to help to lessen the dependence of its growing population upon agriculture and secondary employment.

FINANCIAL YEAR, 1939-40

4. I will now recapitulate briefly the results of the financial year 1939-40. As I explained in the course of my statement last November, the surplus of that year which in our revised estimates we had taken at Rs. 91 lakhs, actually increased to Rs. 7,77 lakhs and the amount transferred to the Revenue Reserve Fund was thus augmented by as much as Rs. 6,86 lakhs. This was the result of an improvement of Rs. 6,81 lakhs in revenue and a reduction of Rs. 5 lakhs in expenditure.

On the revenue side Customs receipts, after the sharp drop that had occurred at the outbreak of war, not only recovered to their previous level but during the closing months of the last financial year, were abnormally high. This was in large part due to the laying in of stocks, the effect of which is seen in corresponding decreases in the receipts of the following year, so that for a fair comparison the estimates and returns of both years should be considered together. In the same way the very large receipts from the abnormal Salt clearances of last winter were off-set by a corresponding reduction in receipts in the current year; the actual receipts last year exceeded our revised estimate by Rs. 1,86 lakhs while those for the current year are likely to be half a crore below the budget estimate based on the normal annual consumption.

The profits from small coin increased by a further Rs. 37 lakhs. Railway earnings also recorded a further improvement so that the surplus payable to general revenues, though still short of the full contribution, increased by Rs. 72 lakhs.

In addition there were increases of Rs. 21 lakhs under Corporation Tax and Rs. 1,07 lakhs under Income-Tax over our revised estimates, which themselves allowed for an appreciable rise over the new high level established by the actuals for the previous years. To some extent this increase may be taken to reflect the additional revenue due to the provisions of the Income-Tax Amendment Act, the yield from which was bound to be a matter of conjecture.

This increase in Income-Tax raised the divisible pool of the total taxes on income other than Corporation Tax from Rs. 13,76 lakhs to Rs. 14,66 lakhs. While we had expected that Rs. 2,38 lakhs would be payable to the Provinces from 1939-40, the amount turned out to be Rs. 2,83 lakhs. In addition to this the arrears due on account of 1938-39 were finally certified as Rs. 39 lakhs instead of Rs. 41 lakhs as provisionally reported. As the sum distributed to the Provinces in March 1940 was Rs. 2,79 lakhs, there is a balance of Rs. 43 lakhs to be paid to them along with their share for the current year.

FINANCIAL YEAR, 1940-41

5. I come now to the current year 1940-41. Our revised estimates for revenue, excluding the additional Rs. 6,86 lakhs available in the Revenue Reserve Fund show a net improvement of Rs. 4,21 lakhs compared with the budget estimates. Against this, however, our revised estimates for expenditure show a net increase of no less than Rs. 19,54 lakhs, of which Rs. 18½ crores are on account of the Defence Services and Rs. 1,04 lakhs are for expenditure borne by the Civil Estimates, mainly on account of schemes connected with the war. Thus while the budget estimates provided for a nominal surplus of Rs. 5 lakhs and last November I put the estimated deficit, before taking into account the revenue from the fresh taxation then imposed, at about Rs. 13 crores, we now estimate that the deficit on the current year will be Rs. 8,42 lakhs. The improvement is due to the additional revenue that has since accrued, including the further payment of Rs. 2,81 lakhs from the Railways as a refund of arrears of contribution, which has already been explained to the House in the speech of the Railway Member.

Revenue

6. War time conditions are naturally reflected in our reduced receipts from Customs. Against actuals of Rs. 45,88 lakhs for 1939-40, we had estimated for 1940-41 a total of Rs. 39,16 lakhs, while we now estimate this year's receipts at only Rs. 37,75 lakhs. Our receipts under this head are of course affected not only by the cessation of trade with enemy countries but also by the interruption and deflection of shipping. In addition we have had to conserve our resources by restricting imports of many commodities in order that the foreign exchange so saved may be available for the more urgent requirements of the war. Under Excise there is a drop of Rs. 2,10 lakhs from Sugar. As the House is aware, the sugar industry in the main producing areas of the United Provinces and Bihar has during the present year been beset with difficulties. The maintenance in the previous season of artificially high prices for cane together with over-production led during the summer months to a situation in which large stocks were held up in the factories. The industry accordingly found itself in difficulties in the matter of finance and revenue was slow to come in. As a remedy for this it was urged upon us that there should be either a reduction in the duty or that collection of a portion of it should be postponed. After negotiations with the two Provincial Governments a scheme was finally adopted under which the Government of India undertook to lend to the Provincial Governments funds sufficient to enable them to advance to the industry a sum equal to Re. 1 per maund on existing stocks, to be used in part payment of duty. This, combined with some lowering of prices, helped to alleviate the position, though the industry in those two provinces continues, for reasons unconnected with the Central Excise, to be faced with problems of great difficulty. In consequence we do not now expect that the collections of sugar excise duty in the current year will exceed Rs. 3,15 lakhs as compared with our budget estimate of Rs. 5,25 lakhs.

7. I have already mentioned that our revenue from Salt in the current year is expected to be Rs. 50 lakhs less than the budget estimate. Railway earnings have, however, come to our assistance and the sum they are now expected to pay to Central Revenues under the Railway convention is Rs. 7,15 lakhs, which with the additional refund of Rs. 2,81 lakhs is Rs. 4,65 lakhs more than was provided in the budget estimates. The sum of Rs. 7,15 lakhs is made up of the full contribution of Rs. 4,63 lakhs, which is 1 per cent of the capital at charge less the loss on strategic railways, Rs. 30 lakhs as arrears of contribution from the previous year, and a further Rs. 2,22 lakhs as one-third of the excess over the first Rs. 3 crores of the remainder which would normally be transferred to the Railway Reserve Fund. Other increases are Rs. 92 lakhs under Currency and Mint mainly from the larger circulation of small coin and Rs. 65 lakhs in the surplus of the Posts and Telegraphs Department; while Taxes on Income other than Corporation Tax, including Excess Profits Tax and the Central surcharge imposed during the year show a rise of Rs. 3,30 lakhs, a part of which goes to increase the share of the Provinces from the budgetted sum of Rs. 3,00 lakhs to Rs. 3,73 lakhs.

As regards Excess Profits Tax the extent of the preliminary work proved even greater than had been expected with the result that returns were not due from assesses before the end of November. The subsequent stages of the assessment proceedings bristle with practical difficulties owing to the complexity of the computations. And to the difficulties ordinarily associated with E.P.T. there is the added difficulty of a separate depreciation computation owing to the change over in the Income-tax law to the written down value basis for depreciation. For these reasons the progress of E.P.T. assessment work has been, and is, very slow and therefore the actual receipts in the current financial year are not expected to exceed Rs. 2 crores. A substantial portion of the original estimated receipts for 1940-41 will accordingly go to swell the collections of 1941-42. This sum may be taken as of the order of Rs. 1 crore.

Expenditure

8. *Defence Services.*—Turning to the expenditure side of the current year, I will now deal with the aspect which overshadows all others, namely, the Defence Services. In my speech introducing the Supplementary Finance Bill last November I gave the House an indication of the extent to which our budget estimate of defence expenditure for 1940-41 was likely to be upset as a result of the momentous developments in the war situation during the early months of that year. I described in some detail the various activities in which India was engaging to meet the direct and indirect threats to her security arising out of the changed conditions. At that time it was estimated that India's share of the financial commitments involved in those activities would amount eventually to roughly Rs. 33 crores on account of initial outlay and Rs. 16 crores per annum on account of recurring charges, while the budget estimate of Rs. 53½ crores for defence expenditure during 1940-41 would be exceeded by at least Rs. 14½ crores. The three months that have passed since then have been a period of steady and rapid progress in the development of India's war effort and I propose at this stage to give the House some particulars of this progress and the achievements already secured or in prospect.

In the interests of security it is not possible for me to bring the figures in every case up to date but what I am going to say will, I hope, show clearly enough that the immensely complicated business of producing efficient modern forces is going forward with speed and energy. In some directions we are, it is true, still held back by the difficulty in obtaining materials which we cannot as yet produce in India and also by the shortage of skilled personnel of various categories. Subject, however, to these limitations, the resources of India are being intensively utilised and developed.

9. The total strength of our armed forces is now well over half a million men of all arms and further expansion is proceeding. Provision has been made for the raising of new armoured and mechanised cavalry regiments; new Indian field artillery regiments, regular infantry battalions, engineer units, more M. T. Sections and all the highly trained and specialised ancillary troops required for modern warfare. The Fighting Vehicles School has continued to expand; a new Cadet Wing has been opened at the Artillery School and an anti-aircraft training centre has been established which is designed to train several hundred students a month. The R. I. A. S. C. Officers' Technical School has been further expanded and its output is now 7 times what it was at the outbreak of war. Mechanical transport training establishments have still further increased and apart from mechanised cavalry, artillery and infantry, who train their own men, the output of trained drivers has grown to 40 times what it was in August 1939. Two new Signal Training Centres have been opened and the training establishments of Sapper and Miner Units have more than doubled since November last.

10. It is impossible to exaggerate the importance of adequate training establishments in an expansion of the scale of that which we are now carrying out. Troops may be gallant and well equipped but they are not likely to succeed in modern war unless their standard of training is very high indeed. The training of the Indian Army has, it is admitted on all sides, been shown to be excellent. This has been proved beyond question by the part which they have played in the recent great victories, where they overcame a well armed and numerically far stronger enemy at surprisingly small cost to themselves. I have dwelt at some length upon this aspect of our war efforts as it is upon this that the pace of our expansion depends. We have no intention of sacrificing efficiency for mere numbers but are determined to follow as closely as possible the high standards which have been set and which have so dramatically and decisively proved their value in the past few weeks.

11. Many of the new units we have raised are now completing their training and a number have already taken up active rôles. When the expansion of the army in India began, owing to difficulties in obtaining equipment, the number of armoured units and artillery regiments included was less than we would have desired. Improvements in the supply situation, however, both in India and the United Kingdom, have now made it possible to remedy this deficiency and our plans include the transformation into armoured and light-armoured regiments of the whole of the existing cavalry and the raising of additional regiments of this kind. With regard to artillery, increasing assistance from His Majesty's Government, both in personnel and equipment, has made it possible to ensure that we do not fall short in this component.

12. With regard to equipment generally His Majesty's Government have recently agreed to a standing arrangement under which India will receive a substantial fixed proportion of the output of the United Kingdom. As a result of this arrangement, steady supplies of all kinds of equipment unobtainable in India, such as guns, machine tools, optical instruments, wireless and other signalling equipment and anti-gas equipment are now forthcoming and will enable us to push forward with the modernisation of our normal defence garrison, and with the equipment of the forces now being raised on a scale adapted to the requirements of modern war.

13. The growth of the Royal Indian Navy which I summarised last November, has continued unchecked; the programme of ship-building in India has been further expanded and the recruiting and training of officers and men to man the new construction is proceeding apace. All instructional establishments have been greatly increased in capacity; a new Signal School is being built and a start has been made with a large new Gunnery School. Other new Naval establishments are in process of development. Some idea of the increase in work being carried out in the Government Dockyard may be gathered from the figures of workmen of all classes and trades employed there. Before the war, the figure was 1,168; it has now risen to nearly 5,000. In addition to meeting our own requirements, a great deal of work has been carried out on behalf of His Majesty's Government in connection with the arming and protection of both British and Indian merchant shipping, and also in the provision of repair facilities to ships of the Royal Navy.

14. As regards the Air Force the difficulties arising from deficiencies of equipment and experienced technical personnel which I mentioned on the last occasion as holding up the expansion of this Arm have recently been considerably lessened. A number of modern aircraft and connected equipment are in sight from American sources and further supplies are expected which will go a considerable way towards completing and modernising the equipment of the squadrons now in India, as well as setting free machines for the training of new squadrons. The arrangements for training personnel have also been considerably improved. Close liaison between the civil and air force training schemes has been established and a proposed amalgamation and re-organization of all available facilities will provide Air Force elementary flying training schools formed around existing flying clubs and an expanded service flying training school. All these institutions will be operating to full capacity in the near future. A start has been made with the formation of the reserve to which I alluded and the training both of officers and airmen is being pushed forward as rapidly as the capacity of the schools permit and as fast as instructional and maintenance personnel and equipment become available. The scheme for establishing aeroplane manufacture in India has reached a new stage and there is now little doubt that the year 1941 will witness the appearance of the first aeroplanes to be produced in India. This achievement, memorable in itself, should prove of great value in speeding up the expansion of India's air force—a development to which we attach supreme importance.

15. The position in regard to the vital matter of supplies has, I am glad to say, substantially improved since I last addressed the House. The Government Ordnance and Clothing factories have been working at the highest pressure for some time past and an indication of what this means can be gathered from the fact that whereas before the war the average number of workmen employed in those factories was under 17,000, the number has now risen to over 45,000 and the curve of production is still rising. Steps have recently been taken to supplement the output of these factories by taking over railway and private workshops and utilising their resources for the production of munitions of war. The Roger Mission, which has been investigating the possibilities of expanding India's output of war supplies has now submitted its reports to His Majesty's Government who are giving them their urgent consideration. We hope that the result will be that India will before long be able substantially to increase her output of munitions.

With a view to stimulating private enterprise and co-ordinating the resources of the country to the fullest extent possible a thorough reorganisation of the Supply Department has been carried out during the last few months and this is already resulting in an increasingly close liaison and co-operation between that Department, other Departments of Government and Indian industry.

16. Mention may also be made here of another important development which is likely to lead to a great improvement in the supply field. Until recently the work of the Supply Department, in so far as it related to compliance with overseas demands was seriously hampered by the fact that the placing of orders in this country to meet such demands was dependent on the receipt of firm indents. Owing to the enormous fluctuations in the demands so placed on the Supply Department and the immediate urgency attaching to most of them it was found impossible to ensure prompt compliance or to make forward arrangements in such a manner as to prevent dislocation of the productive activities of the country and ensure that supplies were obtained at reasonable prices. These difficulties were presented to His Majesty's Government who have now agreed to a forward programme of supply covering the estimated requirements over a period of about two years ahead. The Department of Supply is thus able to enter into forward commitments within the limits of this programme and so maintain an even flow of production.

17. A further improvement in the supply position has been rendered possible by the receipt of authority from His Majesty's Government to purchase vehicles, machine tools and other essential war requirements in the United States and Canada, to the extent necessary to meet our needs for a considerable period ahead. The restrictions previously placed on such purchases owing to the difficulties regarding dollar exchange had been seriously hampering the process of modernising our Army in India and equipping the newly raised units. An officer has been placed on special duty in America with the object of discovering and effecting purchases of such supplies as are available to India from this source.

Last, but certainly not least in this tale of progress, the deliberations of the Eastern Group Conference will shortly bear fruit in the shape of the institution of an Eastern Group Supply Council to be located in India which will in due course co-ordinate the requirements of various Empire countries and forces operating east of Suez and will ensure that the resources of the participating countries are utilised to the fullest advantage for the successful prosecution of the war.

18. These tremendous developments in the supply field must necessarily give a great stimulus to Indian industries. One of the most important results has been the investigation of the possibilities of establishing new industries

in India for the production of stores that have hitherto been imported. The list of stores required both in India and to meet overseas demands is constantly under review and items formerly placed in the category of imported stores are continually being transferred to the indigenous category, a result of the discovery either of methods of producing them in India or of suitable domestic substitutes. As typical examples of this I may mention web equipment, and lubricating oil, bichromates, and acetic acid, which formerly imported, are now being produced in India, while the substitution of cotton canvas for flax canvas, fish oil for codliver oil, and various Indian varieties of drugs for those previously imported has enabled us to transfer their source of supply from abroad to India. This process has been particularly marked in the case of medical stores and whereas prior to September 1939, 77 per cent of the items included in the priced vocabulary of medical stores were imported the corresponding percentage after 18 months of war is only 46.

From this brief review it will, I think, be realised that India has in addition to providing for her own local defence been able to make a noteworthy contribution to the success of the common cause in the provision both of highly trained troops and high grade material. That contribution is increasing rapidly in quantity and is not diminishing in quality.

19. I must now revert to the purely financial aspect of this remarkable picture of India's war activities. As a result of the further measures which I have just described coupled with the general improvement in the supply position, the estimates of extra cost that were given to the House last November are out of date. Our latest assessment of the cost of all measures to which we are now committed and which were not envisaged at the time of preparing the defence budget for 1940-41, indicates that they will ultimately involve initial outlay of approximately Rs. 52 crores and Rs. 19 crores additional recurring expenditure per annum. The initial outlay and full recurring cost will not of course all come forward in the first year but it is estimated that during 1940-41 the increase in India's defence expenditure on account of these measures will amount to roughly Rs. 17½ crores.

20. I may perhaps remind the House here that the allocation of war expenditure between India and His Majesty's Government is still governed by the settlement arrived at between the two Governments which was fully explained in my budget speech of a year ago. In accordance with the principles underlying this settlement any forces now being raised that India may agree to send for service overseas cease to be an Indian liability on leaving India and the whole initial cost of raising, training, and equipping such forces as well as the subsequent recurring charges are borne by His Majesty's Government. The details of the revised estimate of defence expenditure for 1940-41 amounting to Rs. 72,02 lakhs are as follows:—

	(Rs. in lakhs)
(1) Basic normal budget	36,77
(2) Effect of rise in prices on (1)	2,53
(3) India's war measures	24,31
(4) Non-effective charges	8,41
	72,02

The increase of Rs. 53 lakhs in item (2) over the corresponding budget figure is mainly due to the increases of emoluments granted during 1940-41 to British and Indian troops as a war concession. In so far as these increases would have raised the cost of India's normal garrison the extra cost is included under this head. The increase of Rs. 17½ crores in item (3) has already been explained.

Out of the total provision of Rs. 24·34 crores for India's war measures approximately Rs. 15 crores represents the initial cost of such measures; the balance consists of recurring expenditure. The revised estimate for non-effective charges—item (4)—has for the present been fixed at the normal budget level of 1939-40 but discussions are in progress with His Majesty's Government with a view to reaching a settlement that will regulate the allocation of these charges as has already been done for effective charges. The effect of the war on these charges obviously cannot be foreseen though happily there has so far been no appreciable increase owing to the absence of heavy casualties. I should here point out that the increase of Rs. 24·31 crores shown against item (3) over our normal defence expenditure by no means reflects the full magnitude of India's war effort since it excludes the cost of supplies and services rendered by India to His Majesty's Government, which is substantially greater than this amount.

I should also mention here that His Majesty's Government besides paying in full for all such supplies and services are providing free of charge much of the equipment needed for the modernisation of the Army in India and for the initial equipment of units now being raised in pursuance of our expansion scheme.

Civil Estimates

21. The principal items mainly responsible for the increase in Civil expenditure, such as the schemes for the training of the Air Force Reserve and that for war technicians, were explained in some detail in my Statement last November and I will not repeat the account which I then gave to the House. Though the additional civil expenditure then accounted for was approximately Rs. 2,30 lakhs, the actual net increase in civil expenditure works out at only Rs. 1,04 lakhs. In the first place there is a reduction of Rs. 71 lakhs in Interest charges. This is mainly due to smaller payments on account of Post Office Cash Certificates and Savings Bank Deposits and to lower interest rates on our short-term debt, the volume of which has also been reduced in recent months by the success of the Indian Defence Loans. Again, on account of a change of accounting procedure, which also brings about a corresponding reduction on the revenue side, the amount of Rs. 67 lakhs received from Burma as her share of pensionary charges is now to be taken in reduction of expenditure instead of as a revenue receipt under Payments by Burma.

22. Thus our Revised Civil Estimates for the current year are expected to amount to Rs. 40,11 lakhs as compared with the Budget Estimate of Rs. 39,07 lakhs. With the net Defence Expenditure placed at Rs. 72,02 lakhs our total expenditure is estimated at Rs. 112,13 lakhs as against our total revenue of Rs. 103,71 lakhs. We are therefore left with a deficit of Rs. 8,42 lakhs in the current year. As, however, the amount provided for the reduction or avoidance of debt was Rs. 3 crores, the net addition to our indebtedness is only of the order of 5½ crores.

FINANCIAL YEAR, 1941-42

23. I now come to the financial year, 1941-42. Our total revenue estimates amount to Rs. 106,39 lakhs as compared to Rs. 103,71 lakhs in the revised estimates of this year. Though there is no further balance available in the Revenue Reserve Fund, which provided Rs. 7,77 lakhs in the current year, this is more than made up by the first full year's receipts from the Excess Profits Tax and the Central Surcharge imposed last November. We have to allow for a further drop of 3 crores under Customs, but larger receipts are anticipated from Central Excise Duties and Salt. Also the contributions to be paid to General Revenues by the Posts and Telegraphs Department and Railways are estimated at Rs. 38 lakhs and Rs. 22 lakhs respectively higher than their increased contributions in the current year.

Revenue

24. Against our current year's estimate of the yield from Customs duties of Rs. 37,75 lakhs, we have taken for 1941-42 the still lower figure of Rs. 34,75 lakhs. War time factors already described in connection with the current year's receipts must be expected to continue to affect our revenue from Customs adversely, and under present conditions no one can foresee when the process will end, or the extent to which these factors may operate in the coming year. I can only say that our estimates are based on the assumption that present tendencies will continue and that there will be no violent change.

25. Our total estimates for Central Excise Duties show an increase of Rs. 1,75 lakhs almost entirely on account of sugar. We have raised our next year's estimate of the total yield from ordinary Corporation Tax and Income-Tax by approximately half a crore to Rs. 21½ crores taking account of the fact that the assessments will be based on incomes derived from a full year of war profits. At the same time the surcharge imposed for Central purposes is expected to produce Rs. 5,68 lakhs. In the light of general trading conditions during the current year the yield from Excess Profits Tax for the year 1941-42 is estimated at Rs. 7½ crores, which with the carry-over of Rs. 1 crore from the current year gives a total estimate of Rs. 8½ crores. Though Excess Profits Tax receipts are included in the total Taxes on Income, the share payable by Companies, which is roughly estimated at five-sixths, falls under Corporation Tax and thus goes in full to Central Revenues. The Excess Profits Tax on incomes other than those of Companies is expected to yield Rs. 1,42 lakhs and the divisible pool of Income-Tax to increase on account of this from Rs. 16,47 lakhs to Rs. 17,93 lakhs. The share of the Provinces is thus expected to reach the figure of Rs. 4,46 lakhs as compared with Rs. 3,73 lakhs this year.

26. There is also an increase of Rs. 60 lakhs under Salt as compared with the Revised. With the utilisation of the large stocks carried over from last year, we count on the usual demand for fresh supplies next year and in consequence take our estimate of Salt revenue at the average figure of Rs. 8,30 lakhs. We are allowing for a decrease of Rs. 1,21 lakhs in Mint receipts as compared with our revised estimates for 1940-41. We have now decided that from next year an average figure of Rs. 45 lakhs from the profits from the circulation of small coin is to be taken to Revenue and any balance over this figure credited to a Suspense Account which will be available to even out the receipts over a series of years. For in years when there is a large demand for small coin the profits are abnormally high, while in others when there is a net return from circulation there is a loss to Government. The new procedure will tend to keep the revenue receipts from this source stable from year to year and will mitigate instead of aggravating the difficulties experienced in years of depression on this account. Under Currency however there is an increase of Rs. 1,25 lakhs. We are taking the Government's share of the Reserve Bank's profits, Rs. 1,17 lakhs higher on account of the higher interest which will be earned on the rupee securities held by the Bank in place of their sterling balances, and the receipts from the Currency Note Press are expected to improve by Rs. 8 lakhs. Included under Other Sources of Revenue are Rs. 63 lakhs on account of War Risk Insurance premia, the payment of which into the Fund created for this purpose is provided under expenditure.

27. *Posts and Telegraphs*.—For next year the revenue of the Posts and Telegraphs Department is expected to be Rs. 13,49 lakhs and expenditure Rs. 12,09 lakhs. The larger revenue is almost wholly due to the effect of the increases in rates. The expenditure reflects the normal growth of pay and pensionary charges in an expanding service, with some additions to maintenance charges and to the contribution to the Renewals Reserve Fund due to the rise in the prices of stores and in the value of the assets.

In my last Budget Speech I reminded Hon'ble Members that under the system of commercialisation of accounts of the Posts and Telegraphs Department the surplus of the Department forms a reserve for it on which interest has to be paid by General Revenues. I also indicated that the procedure by which the general tax-payer obtains immediate relief by incurring a future liability could not be extended indefinitely. The recent increase in rates being a measure of taxation the Posts and Telegraphs Department cannot claim the extra revenue on this account as part of its ordinary surplus. The estimated extra revenue due to this factor, namely, Rs. 33 lakhs in 1940-41 and Rs. 1,00 lakhs in 1941-42, will therefore be transferred outright to general revenues. Further the recent surpluses of the Department are due largely to war conditions, and Government traffic has contributed substantially to them. It has been decided that on the accumulated surplus beyond Rs. 1,00 lakhs the Department will not be credited with any interest. For the present this change in the former procedure is considered a sufficient adjustment to war circumstances.

The licences of the Bengal, Bombay and Madras Telephone Companies expire in 1943. It has been decided not to renew the licences and negotiations are in progress to acquire by purchase the shares of the companies in order that the change-over may be effected smoothly. A "Government Telephone Board" has been formed to run the business in the interim period. The new arrangement is expected to start functioning about the beginning of the next financial year. An addition of Rs. 4,75 lakhs to the Telephone Development Fund will be necessary to finance the "Government Telephone Board". A proposal for a supplementary grant for this purpose will be brought forward later in this session.

Expenditure

28. *Defence Services*.—The Defence Budget for 1941-42 amounts to Rs. 84,13 lakhs made up as follows :—

	(Rs. in lakhs)
(1) Basic normal budget	36,77
(2) Effect of rise in prices on (1)	3,55
(3) India's war measures	35,40
(4) Non-effective charges	8,41
	84,13

The increase over the revised indicated at item (2) is due to the fact that the increases in emoluments granted as a war concession to British and Indian troops took effect from various dates in 1940-41 whereas they will be in force throughout 1941-42.

The growth of expenditure on India's war measures has already been explained at length. The effect of this growth on the defence budget for 1941-42 is shown at item (3) the increase over the revised being Rs. 11,09 lakhs. Approximately half the total amount of Rs. 35,40 lakhs provided for India's war measures represents the initial cost of these measures, the balance consisting of recurring charges. I should like here to impress upon the House the fact that in these estimates of Defence Expenditure only such specific schemes and measures as are definitely under way or in sight have been provided for.

Our Defence plans have to be adapted from time to time to meet the ever changing war situation, which means that additional projects are constantly being undertaken, and it is clearly impossible to make any forecast of the cost of such unforeseeable items. The provision for non-effective charges has been retained at the normal figure for 1939-40 for the reasons already given. Here too as I have remarked in connexion with the revised estimates the figures exclude the value of supplies and services rendered by India to H. M.'s Government. The charges borne by that Government on this account during 1941-42 are expected to be more than double the amount of India's war expenditure.

Civil Estimates

29. Our Civil expenditure estimates show increases amounting to Rs. 2,61 lakhs in all as compared with the current year's revised estimates. There are first the additional sums on account of the full year's working of the various schemes arising out of the war which were started in the course of the current year. Thus next year the training of the Air Force Reserve is expected to cost Rs. 33 lakhs and the Scheme of Technical Training to provide the needs of skilled labour of the technical branches of the Defence Services and Ordnance and munitions factories a further Rs. 93 lakhs. Under this scheme, which provides for the training of 15,000 men by the end of March 1942, nearly 2,000 men are already being trained at different training centres and their number is increasing every day. Of the total cost of Rs. 1 crore, over 85 per cent of which is for stipends to trainees and their training fees, it is now estimated that Rs. 7 lakhs will be spent in the current year and the remainder next year. Then there are a number of new items of essential expenditure which the Standing Finance Committee have approved for inclusion in the budget. These include the share of the subsidy to this year's Haj pilgrimage to be paid by the Government of India to meet the extra cost attributable to war conditions, the establishment of a new Broadcasting station at Karachi, and a further programme of Civil Aviation Works. Rs. 5 lakhs are to be spent in the course of next year on the new Broadcasting House to be built at Delhi. Rs. 9 lakhs are being provided for a new high power transmitter for broadcasts to countries outside India, intended for the benefit of Indian nationals abroad and to enable India to present her point of view, as well as to counteract enemy broadcasts in those countries. A third Mint is to be constructed to cope with the present large coinage demand, which has increased so enormously as the result of the war. As soon however as the situation returns to normal, it is proposed to close down the existing Calcutta Mint and to transfer all serviceable plant to the new Mint so that the present valuable but congested site can be sold to defray a large part of the cost of the scheme. A substantial share of the new expenditure included in the Budget is on account of the Department of Supply which has continued to expand throughout the year to meet the ever growing demands. The great developments in the production of war material, as well as the re-organisation of the Department carried out last December have already been described in connection with Defence. As regards the effect on industry of the orders placed on behalf of overseas Governments it may be mentioned that these have included 2½ million yards of jute canvas, 3½ million yards of a new jute and cotton fabric, 12 million yards of khaki materials, as well as 14 million yards of canvas valued at over Rs. 1,40 lakhs. At the same time the woollen industry's whole production has been absorbed to meet war demands. The production of army boots, harness, saddlery, and leather equipment which is now 30 times the pre-war average, has resulted in large orders for the tanning industry and increased demands for hides. New manufacturing plant to meet the requirements of chemicals formerly drawn from Europe are under construction. 400,000 tons of timber and over a million railway sleepers have been purchased for military requirements while wooden articles like tent poles, camp furniture and packing

cases to the value of Rs. 60 lakhs have been made by Indian workmen from timber grown in the country. The total value of all these orders placed on behalf of His Majesty's Government and other allied Governments up to the middle of January exceeded Rs. 82 crores. This gives some indication of the necessity for the expansion of the Department's purchasing organisations. The expenditure on this account has increased from the figure of Rs. 23 lakhs originally provided in the budget for the current year to Rs. 58 lakhs as now estimated for next year.

SUMMARY

30. I can now summarise the figures for 1941-42. The expenditure detailed in the civil estimates comes to Rs. 42,72 lakhs as compared with Rs. 40,11 lakhs for the current year, and with the provision for the Defence Services placed at Rs. 84,13 lakhs, our total expenditure estimates amount to Rs. 126,85 lakhs. The figures are therefore—

	(Lakhs)
Revenue	106,39
Expenditure	126,85
	<hr/>
Prospective Deficit	20,46
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WAYS AND MEANS

At this stage I propose to deal with the Ways and Means position as it has developed in the course of the last twelve months, when despite the grave repercussions of the war the credit of the country has been fully maintained at its previous high level.

31. *Defence Loans.*—Our loan programme for the year was merged in the Indian Defence Savings Movement which was launched early in June with the issue of Six Year Defence Bonds, Ten Year Defence Savings Certificates and Interest-free Bonds. From the 1st August we made these Six Year Defence Bonds the mainstay of our loan programme and removed the previous maximum on individual holdings. These Defence Bonds met with a ready and increasingly popular reception, and when we closed them on the 25th January, subscriptions totalled nearly 45 crores, 31½ crores having been tendered in cash and the balance by conversion of the 5 per cent Loan, 1940-43. As from 1st February we issued on terms slightly more favourable to the tax-payer a second 3 per cent Defence Loan with a longer currency and repayable at par. The results of these Defence Loans, the total receipts from which in a period of eight months have amounted to over Rs. 50 crores, testify to the strength of India's financial credit and are a good augury for the future. But I must take this opportunity of emphasizing the desirability of an even more intensive mobilisation of the country's savings if India's war effort is to continue to be financed in the most satisfactory way. However generous the donations for war purposes may be—and no one can fail to be impressed with the response so far made—it is obvious that the total of the sums received as donations can only form a very modest fraction of the amount required to finance the war effort. The fulfilment of that requirement calls for the efforts of every individual to save to the best of his capacity and to invest his savings in one or other of the different types of Defence Loan, which we have instituted to serve different needs. In addition to the Loans already described, we have started a Defence Savings Provident Fund for all Government servants which makes it easy for these classes to make regular investments. Subscriptions to this are already approaching the scale of half a

crore a year. We shall shortly have in operation a simple system of facilitating popular saving by means of a new scheme of Post Office Savings Bank Accounts, the amounts in which will be repayable not on demand but a year after the end of the war. This will afford further facilities to those of limited means who desire to invest their savings so as to assist the war effort. In order to encourage deposits of this kind, the rate of interest has been fixed at 1 per cent higher than the existing rate on ordinary Postal Savings Banks Accounts.

During the current year Government exercised their option of repaying the 5 per cent Loan, 1940-43 and thereby effected an appreciable saving in our interest charges. Next year we are making provision for the repayment of the 3 per cent Bonds, 1941, the outstanding balance of which, about Rs. 10½ crores, falls due for payment on the 15th September next.

32. *Sterling Position.*—Owing to the continued improvement in the country's balance of trade, the Reserve Bank have been able to purchase large amounts of sterling which in the first ten months of the current year aggregated approximately £47 millions. At the same time with large payments being received in the United Kingdom on account of recoverable war expenditure and the cost of supplies made to His Majesty's Government the amount of remittance required by Government has diminished to vanishing point. For our ordinary sterling requirements, excluding the amount that will be required to finance the debt redemption operation now pending, are now expected to amount to no more than £1 million in the current year, while next year instead of having to remit funds to the Secretary of State we actually expect a refund of £26 million.

33. *Repatriation of Sterling Debt.*—As I explained in my Budget Speech last year, these acquisitions of sterling continued to enable the Reserve Bank to put large amounts at our disposal for the repatriation of our sterling debt. Considerable open market purchases were made in London, particularly in the early months of the year and the total acquired in this way now stands at approximately £28½ million. As the securities market improved, however, and as the floating stock was removed, it became increasingly obvious that purchases on this scale would no longer be possible except at a cost of pushing prices up beyond a reasonable level. In these circumstances, the British Government came to our help by issuing orders under their special war powers compelling holders resident in the United Kingdom to sell their stocks to them for delivery to us at the market prices prevailing at the time of the order. The Reserve Bank agreed to provide the sterling and to guarantee the immediate financing of a scheme framed on these lines to cover all our terminable obligations, that is to say, all our sterling debt which has to be repaid on fixed dates, amounting to a total which at the prices of acquisition may be taken as approximately £90 million or Rs. 120 crores. The whole of this will, of course, not have to be paid in sterling because a certain amount, though how much we do not know yet, is held by persons who are not legally considered as resident within the United Kingdom and to whom, therefore, the order does not apply. These may be residents either in India or elsewhere. As regards the latter, the Reserve Bank has made arrangements with the Bank of England that, subject to the English regulations regarding export of capital abroad they will make an offer to non-resident holders to sell their securities on the basis of the prices fixed for their compulsory acquisition. I anticipate that many of the holders will avail themselves of this offer because once the bulk of the debt has been paid off the remaining stocks will not be easily marketable in London and it would therefore be to the advantage of the holders to dispose of them and choose some other investment. We had also to decide what terms should be given to these stocks when held by residents in this country and we decided that we would

pass a corresponding compulsory order of acquisition at the same price as those fixed in London. To avoid disturbing the portfolios of insurance companies and other investors, however, we decided that we would elaborate the scheme which I mentioned to you last year of creating rupee counterparts so as to give Indian holders the option of taking over such counterparts to the extent of the nominal value of their holdings worked out at the rate of 1s. 6d. to the rupee. I hope that this offer will be largely accepted as it will be both to the holders' advantage and ours: it will be to our advantage as it naturally lessens the immediate payments which we have to make and it will be to theirs, because the sterling prices of these loans were slightly lower than those of corresponding rupee securities, so that they should gain to a slight extent on the change.

34. This brings me to the machinery for financing the operation. There are clearly two stages: first, we buy the sterling from the Reserve Bank and secondly, we have to obtain rupees to pay for that sterling. It would be obviously quite impossible to attempt to borrow this immediately from the market even apart from our Defence borrowing requirements, and it would be inconsistent with the policy which we are following with the co-operation of the Reserve Bank of maintaining money at as cheap a level as is possible without inflation so as to minimise the burden of the war. We have found it impossible, within the limited time at our disposal, and in the absence of more definite information than is available at present of the amounts held by investors in the United Kingdom, in India and elsewhere to decide on the permanent arrangements for this purpose, but for budgetary purposes and as an interim measure pending more detailed consideration, we are adopting the procedure of maintaining the *status quo*, and of issuing in lieu of these sterling loans rupee counterparts which will bear the same rate of interest and be payable on the same dates, the only difference being that, in future, they will be payable in rupees and not in sterling. Later we shall have to determine, in consultation with the Reserve Bank, a procedure which will be simple and fair both to the general tax-payer and to the Bank, which has co-operated so readily and promptly with the Government in financing this important transaction, and which will at the same time avoid any necessity for an automatic increase in our short-term debt which might entail dangerous inflationary consequences later.

35. The proportion in which the Reserve Bank will distribute the securities taken up by it between its Issue and Banking Departments as a longer range holding is for that bank to determine in the light of circumstances as they develop and in co-operation with Government. It is obvious, however, that the cancellation of this large block of sterling liabilities with its reduction in our overseas obligations to the extent of well over £3 million a year does permanently strengthen our external position and consequently makes it reasonable for the Reserve Bank to hold a somewhat lower proportion of external assets than previously. There is, of course, no necessity or intention of reducing the minimum percentage of the external assets which they must hold under the Act, that is to say, 40 per cent of their note liabilities, nor is there any necessity, as has been suggested in some quarters, to effect a statutory revision of the prices at which they hold their gold. All that was necessary was to remove the restriction on the maximum amount of Government securities which the Reserve Bank can hold in their Issue Department and that has been effected by the abolition of the proviso to Section 33 (3) of their Act. This does not in any way affect their statutory responsibilities under the Act. It merely gives them a freedom of choice which they did not have in the past, as to the proportions in which they should hold Government securities or internal trade bills. It is also unnecessary, and we do not propose, to alter the limits on the Government securities which they can hold in the Banking Department.

I am afraid that it will not be possible to give precise figures until the 10th March when the returns asked for by the Bank of England and ourselves will have been received, but we are confident that the Indian securities market is so healthy that the finance of this large operation can be effected without detriment to Indian security prices and that, on the contrary, the effect on them is more likely to be stimulating.

36. The House will no doubt appreciate fully to what extent this single operation, which is the largest of its kind ever carried out in this country, will improve the financial position of India. When it is complete, we shall not only have reduced the Government of India's external debt by about Rs. 120 crores, by replacing the sterling liabilities thus cancelled with corresponding rupee liabilities, but shall also have reduced such of our interest charges as are payable in sterling by as much as 50 per cent over the last six years. Taking the whole period since 1935, and including the amounts of sterling Railway annuities and debentures discharged each year and the transfer of our liabilities in respect of sterling family pensions, we shall have reduced our sterling obligations by over Rs. 220 crores, of which about Rs. 145 crores will have been repatriated since the beginning of the war.

37. In the past, Indian opinion has been much pre-occupied, perhaps unduly so, by the so-called "drain", that is, the sum-total of the external obligations, on capital and interest account, which had of course to be met by providing sterling in London—the counterpart of the physical exports out of the sale proceeds of which these amounts were raised. It will be obvious to the House that the conversion of external into internal debt will diminish the strain upon the ultimate cash-reserves of the country—our holdings of gold and other external assets—which tends to manifest itself when, in consequence of world-events over which we have no control, the value of our overseas trade declines. There has been in certain quarters a disposition to doubt the value of these conversion operations, since they have involved a reduction for the time being, at least, in the size of the sterling holdings of the Reserve Bank. These holdings have risen greatly since the outbreak of the war, an increase which has given rise to much criticism. Even after the reduction involved in the present operations, our sterling reserves will still be in the neighbourhood of Rs. 80 crores, a figure almost exactly the same as the average sterling holdings during the last full pre-war year. But, in fact, it is not the absolute size of the reserve which matters, but the size of the reserve in relation to the magnitude of the most pressing liabilities against which it is held. Our cash reserves are held in the first instance as a protection against external liabilities, failure to meet which would instantly react upon India's financial credit. By these operations we reduce the size of our external obligations and therefore permanently strengthen our position. I may emphasize again that these operations do not affect the size of our gold reserves in the least and do not involve any change either in monetary policy or in the day-to-day operations of the currency system.

38. The immediate object of the transactions was the replacement of sterling by rupee obligations and the real gain to the country lies in the liquidation of external obligations which might prove an embarrassment in future. Even otherwise Government are likely to be immediate gainers though at present it is not possible to estimate with any approach to accuracy the immediate effect on our revenue position. The profit due to the difference between the rate of interest earned by the Reserve Bank on its sterling investments and the redemption yield of the securities acquired at the prices paid must ultimately accrue, practically entirely, to Government either through the increase in the profits of the Reserve Bank, to the extent to which these securities are held by it, or directly to the extent to which Government

hold these in their own portfolio, or cancel them from the funds which they borrow from the market. Later as the market gradually absorbs these liabilities in whatever form they will ultimately take, whether as rupee counterparts of the sterling loans they replace, or in the form of a simpler scheme of converted loans of suitable maturity, the gain may be reduced but against such reduction will, of course, be set off the increased receipts from income-tax.

39. In my judgment these operations cannot fail greatly to strengthen India's credit. There can be few countries in the world to-day fortunate enough to possess sufficient liquid resources to repatriate a large portion of their external debt, whilst leaving their Central Bank in a position of unchallengable strength. In relation to the growing resources of India our external debt will now be of remarkably modest proportions. Should a situation ever arise in which India were required to raise capital abroad—a contingency which I for one do not foresee—the fact that our existing external liabilities are so small would obviously be of the greatest importance in determining the rate of interest which we would be required to pay.

40. There is of course another aspect of our repatriation operations at the present time and that is the manner in which they assist His Majesty's Government to finance the prosecution of the war. It is obvious that if India repays her creditors in London, then particularly at the present time and in the present conditions of the London money market the greater part of the sums so disbursed will be re-lent to His Majesty's Government probably in the form of investment in the Defence loans and will thus become available for Britain's use in a more permanent form than when they formed part of the balances of the Reserve Bank and were invested in sterling Treasury Bills. To this extent we may well feel gratified that India in improving her own position has also contributed to facilitating the war-time problems of Britain.

41. *Treasury Bills.*—Apart from financing these repatriation operations, we would have reduced the value of treasury bills outstanding by about eight crores in the current year, despite the large expansion in Defence expenditure and the heavy outgo from Postal Savings Banks and Cash Certificates which would ordinarily have necessitated a large increase in our floating debt. For these factors have been largely offset by the favourable response given to our Defence Loans, the capital receipt of Rs. 12 crores from the Reserve Bank on account of the Re. 1 notes and silver rupees issued to them and the fact that the payment of five crores to the Reserve Bank provided for against a return of surplus rupee coin was not required. For the moment we are reckoning on a decrease in Treasury Bills of Rs. 3½ crores during the two years taken together.

42. *Post Office Cash Certificates and Savings Banks.*—It will be observed from the Ways and Means statement, which is printed with the Explanatory Memorandum on the Budget, that the figure for net repayments of Post Office Cash Certificates has been increased in the revised estimate for the current year from Rs. 1½ crores to Rs. 10 crores, while for Postal Savings Banks deposits we are providing for a net outgo of Rs. 19 crores against the receipt of Rs. 2 crores taken in the budget. For during the period of uncertainty following the fall of France last summer there were large withdrawals from Postal Savings Banks and heavy discharges of Cash Certificates, coupled with a tendency to hoard savings in the unproductive form of silver rupees. Since then however there has been a marked and progressive improvement and for next year we are assuming a net deposit of Rs. 2 crores in Postal Savings Banks and a net repayment of Rs. 6 crores of Cash Certificates, the popularity of which has naturally been affected by the issue of Defence Savings Certificates, which provide a very similar and in some ways more attractive form of investment.