

**INDIA'S FIRST BUDGET SPEECH**  
**SPEECH OF SHRI R.K. SHANMUKHAM CHETTY, MINISTER OF FINANCE**  
**INTRODUCING THE BUDGET FOR THE YEAR 1947-1948**

I rise to present the first Budget of a free and independent India. This occasion may well be considered an historic one and I count it a rare privilege that it has fallen to me to be the Finance Minister to present this Budget. While I am conscious of the honour that is implied in this position, I am even more conscious of the responsibilities that face the custodian of the finances of India at this critical juncture. I have no doubt that in the discharge of my responsibilities I may count on the sympathetic and wholehearted co-operation of every Hon'ble Member in this House.

2. It is not necessary to dwell at any length on the political developments which have led to the momentous changes that have taken place since the Budget for the current year was presented to the Legislative Assembly last February. The partition of the country has cut across its economic and cultural unity and the growth of centuries of common life to which all the communities have contributed. The long-term effects of the division of the country still remain to be assessed and we are too near the events to take a dispassionate view. When the ashes of controversy have died down, it will be for the future historian to judge the wisdom of the step and its consequences on the destiny of one fifth of the human race. Whatever might be the immediate political justification of partition, its economic consequences must be fully appreciated if the two Dominions are to safeguard the interests of the ordinary man in both the new States. Regions which have functioned for centuries on a complementary basis have been suddenly cut asunder. To have had as a single economic unit a subcontinent peopled by a fifth of the human race meant by itself a great advantage for the teeming millions of its population an advantage not fully realised, and perhaps not properly utilized while the unity was a fact. While it may be a comparatively easy matter to make the necessary political adjustments resulting from partition, it would require time, patience, goodwill and mutual understanding to effect the adjustments necessitated by the economic consequences of partition. Economically India and Pakistan have each points of advantages and disadvantages. In general, it may be said that, while India is much the stronger at present in industrial production and mineral resources, Pakistan has some advantage in agricultural resources, especially foodstuffs. But the complementary character of their economies is even deeper than is indicated by this generalisation. The compelling forces of economic necessity must create a friendly and cooperative spirit between the two Dominions and I trust that, when the present passions subside and normal conditions of life return, our people will work together to secure that, notwithstanding the political division, the economic life of the common man is not injured. So far as we are concerned, the Indian Union with its population of nearly 300 millions will be the second largest country in the world next to China. Our economy is more balanced than that of most countries and, in spite of the setbacks resulting from partition, our large natural resources and sound financial position will enable us to launch a vigorous economic plan for substantially raising the living standard of our people.

3. The Budget Statement that I am presenting today will cover a period of 7½ months from the 15<sup>th</sup> August, 1947 to the 31<sup>st</sup> March, 1948. I may briefly explain the circumstances in which it has been necessary to present a fresh Budget for this period. With the division of the country and the emergence of two independent Governments in place of the old Central Government, the Budget for the current year 1947-48 passed by the Legislature last March ceased to be operative. Although under the transitional provisions of the constitution, Government could authorize the expenditure necessary for the rest of the financial year, it was felt that it will be in accordance with the public wish that a Budget should be placed before the representatives of the people at the earliest possible moment. There is nothing spectacular about my statement and there will be no surprises associated with a Budget. I shall place before the House our estimate of revenue and expenditure for this period and I shall try to indicate in broad outlines the pattern of the economic life of the country and the problems that we will have to face in the immediate future.

## PARTITION ARRANGEMENTS

4. Before I proceed to deal with the estimates for the year, the House would doubtless wish to have a brief account of the broad details of the partition and its immediate financial and economic results. As soon as the decision to divide the country was taken, a Partition Council, consisting of the representatives of both the future Governments, was set up to implement the decision. A number of Expert Committees, on which both the future Governments were equally represented, were appointed under the aegis of the Partition Council to work out the administrative and other consequences of the partition. These Committees, some of which are assisted by a number of departmental subcommittees, dealt with all aspects of the problems arising out of the partition such as the transfer of staff and organisations, the division of assets and liabilities, the arrangements for the coinage and currency. In the two Dominions, the trade and economic relations between them, the continuance of economic controls and so on. These Committees had to complete their work in a matter of four to six weeks and the House will appreciate that in the short time available to deal with these issues, some of which were of the utmost complexity and importance, it was not possible to reach an agreement on all matters before the 15<sup>th</sup> August 1947 when the two Dominions came into existence and took over the Government of their respective territories. A number of important points were accordingly left over for further consideration by the two Dominions and, in the absence of an agreement between them, for reference to an Arbitral Tribunal which has been set up. Among the important issues on which it has not been possible to reach an agreement, I may mention the allocation of debt between the two Dominions, the method of discharging the pensionary liability, the valuation of the Railways, the division of the assets of the Reserve Bank and the division of the movable stores held by the Army. Some of these issues are likely to go before the Arbitral Tribunal and the House will not expect me to say anything further about them at this stage. It was also found impossible to reconstitute the Armed Forces between the two Dominions and allocate the military stores, equipment and installations between them before the 15<sup>th</sup> August 1947. For the completion of this work, and for clothing, feeding and paying the Armed Forces till their reconstitution had been completed, a Joint Defence Council representing the two Dominions with an independent Chairman and with a Supreme Commander responsible to the Council, has been set up. This Council was originally expected to complete its work by the 1<sup>st</sup> of April 1948 but it is now hoped that this may be mostly achieved by the end of this month.

5. The long range fiscal, financial and economic relations between the two Dominions still remain to be considered, but for the rest of the current year the intention is to maintain, within the framework of the agreements arrived at, the status quo before the partition. For the present both the Dominions will continue the existing taxes and duties, there will be a free movement of trade between them without any internal barriers and the import and exchange controls of the two Dominions will be co-ordinated. It has also been agreed that till the end of September 1948 the two Dominions will remain under a common currency system managed by the Reserve Bank, although from the 1<sup>st</sup> April next Pakistan will have its own overprinted notes and coin. So far as revenue is concerned, each Dominion will ordinarily retain what it collects but in respect of income tax on assessments for 1946-47 and earlier years and uncollected demands on the date of the partition an arrangement for sharing the receipts arising in both the Dominions has been arrived at. In the matter of the division of assets and liabilities, it has not been possible, as I have explained earlier, to reach an agreement on a number of important points including the allocation of debt and the discharge of the liability for pensions. But the responsibility for the outstanding liabilities of the old Government could not, obvious reasons, be left vague and undetermined and the only practicable course was for one of the Dominions to accept the initial liability to the creditors and settle with the other the contribution to be made by it. The initial liability for the outstanding loans, guarantees and financial obligations of the late Central Government at the time of the partition and for the pensions chargeable to it has been placed by law on the Indian Dominion subject to an equitable contribution from Pakistan. I am sure the House will welcome this decision because in the interests of the credit of both the

successor Governments it is obviously undesirable to leave those who had lent money to the previous Government or had earned pensions under it in any doubt as to the Government they should approach for their dues.

## **REVIEW OF ECONOMIC CONDITIONS**

6. There has been a marked deterioration in the economic situation in the country since March last. The situation has been aggravated by the large scale disturbances which burst out suddenly, more especially in the Punjab and the North- West Frontier Province. Apart from the serious economic consequences arising out of these disturbances, the human misery that it has caused cannot be measured in terms of money. Thousands of innocent lives have been lost in the two Dominions and migration on a scale unprecedented in history has taken place. The total number of people involved in this mass migration of population has reached colossal figures on either side giving rise to problems of great magnitude affecting the economy of the country. The Immediate effect of these tragic developments has been to divert the attention of the Government almost completely from normal activities. There has been an almost total breakdown of the economy of the East and West Punjabs. While Government have done and are doing everything possible to relieve the immediate distress and suffering of the refugees, the formulation of long-range plans for their rehabilitation raises formidable issues both in the financial and administrative fields. These problems have imposed a heavy burden on the Central exchequer, the magnitude of which it is not possible to assess at present. The budget of the Central Government for the next few years will be materially affected by this unexpected development in the country, Our whole programme of post-war development will have to be reviewed in the light of this context.

7. The food position has continued to cause grave anxiety both to the Provincial Governments and the Central Government. The country has just weathered a serious threat of a breakdown of its rationing system. The results of the "Grow More Food Campaign" have been on the whole disappointing. During the three years 1944- 45, 1945-46 and 1946-47 we had to import from abroad 43.80 lakhs of tons of foodgrains at a cost of over 127 crores of rupees. During the current year from April to September we have already imported 10.62 lakhs of tons of foodgrains at a cost of over 42 crores of rupees. Apart from its being a constant source of anxiety, the reliance on the import of foodgrains from abroad of such magnitude imposes a heavy strain on the finances of the Government. In recent years our exchange difficulty is almost entirely due to the import of foodgrains on such a large scale. The meagre exchange resources available to us are consumed by the purchase of foodstuffs abroad with the result that we have to impose the most stringent restrictions on the import of many other essential articles. The various steps necessary for making the country selfsufficient in foodgrains must now claim the highest priority. The implementation of this policy must largely depend on the Provincial Governments though the Government of India has been and will always be prepared to afford all possible help In this direction. We have sent a mission to Australia for the purchase of the surplus wheat of that country and we are hoping that we might be in a position to get from Australia a substantial quantity of wheat during the next year. An expert committee under the Chairmanship of Sir Purushottamdas Thakurdas has been examining the food position in the country and the Committee has submitted an interim report which is receiving the attention of the Government.

8. The deterioration in the economic situation has been particularly noticed in respect of prices which have shown an unchecked upward tendency. Between the 5<sup>th</sup> April and the 9<sup>th</sup> August this year the Economic Adviser's index number of wholesale prices rose by 7 points while the Bombay cost of living index advanced by 14 points. Taking the Bombay cost of living index number, while it was 243 in August 1945 it rose to 267 in August 1946 and reached 284 in August 1947. The chief factor which has contributed to this development is the general decline in agricultural and industrial production In the country due partly to the wide prevalence of communal disorders and generally to the increasing Industrial unrest. While the supply position has been deteriorating, increases in wages and salaries given by private employers and the Government had the effect of augmenting the purchasing power of the

people and widening the gap between current money income and production of goods. The situation would not have been so bad if the unbalance between money and goods was confined to these factors only. The most disturbing factor which affects the situation today is the unspent balances of individuals and institutions accumulated during the peak years of Inflation which are being spent on the deferred wants of individuals, repairs to industry and on the building of trade inventory. In other words, the money demand for goods is colossal compared to their local production. While the inflation in war time was due to the large increases in currency circulation (which rose from Rs. 172 crores in 1939 to over Rs. 1200 crores at the end of 1945) without any tangible increase in the supply of goods the present Inflation is not due to further increase of currency but to a steady fall in the supply of goods. Although the total available money, whether currency or bank deposits, has slightly fallen it has spread out more among a wider circle of people in the form of wages and salaries and thus the actual purchasing power in the hands of those who spend it on ordinary goods has greatly increased. But the supply of goods has meanwhile fallen and has resulted in an upward trend of prices. To take only a few examples of the marked fall in internal production, it may be mentioned that as against a production of 4,600 million yards of mill made cloth and 1,500 million yards of handloom cloth in 1945 the production this year is estimated at 3,900 million yards and 1,200 million yards respectively. The production of steel in the current year is also expected to show a drop of nearly 400,000 tons compared with the peak production of 1,200,000 tons during the war. The production of cement has also grown steadily worse, the estimated production this year showing a drop of 700,000 tons over the capacity of over 2½ million tons. In recent months the production of coal has shown some improvement, but so far as the consuming public is concerned, this has been more than neutralised by difficulties in transport resulting in large accumulation of coal at the pit heads. Transport and other difficulties explain the drop in production to some extent, but this is also partly due to labour unrest and strikes.

9. If the economy of this country is to be placed on a sound footing and maintained in a healthy condition, it is of the utmost importance to increase internal production. The chances of increasing the supplies of commodities by imports are not very bright. Until recently we had a fair chance of sizable imports of consumer goods from the British Commonwealth countries from accumulated balances, but with the blocking of the major part of these and the growing adverse balance resulting from the large scale importation of foodgrains, the hope of procuring supplies from abroad is growing weak. We have therefore to fall back on our own resources. Government have recently announced their scheme for increasing the production of cotton textiles which, if worked in a spirit of co-operation between industry and labour, will result in the production of an additional 1,000 million yards over the estimated production of the current year. It is intended to explore the possibilities of restoring the level of production in other fields in a similar manner. I am fully conscious of the fact that any policy of stabilisation must aim not merely at the increase of production of both consumer and producer goods but also at the pegging of money incomes at an agreed and accepted level so that the increased volume of trading resulting from the increase of production may neutralise the inflationary effects of the large volume of uncovered money income. If this policy is to be carried out successfully, it would require an appreciation of the situation by labour and its wholehearted co-operation.

## **REVENUE**

10. I shall now proceed to a brief review of the financial position for the rest of the current year. But I must warn the House that the estimates now presented must be treated as very tentative as it has not been possible to assess with any measure of accuracy the effects of the partition on our revenue and expenditure. I hope it will be possible to present a more accurate picture when the revised estimates are placed before the House along with the budget for the next year.

11. I have budgeted for a revenue of Rs. 171.15 crores and a revenue expenditure of Rs. 197.39 crores. The net deficit on revenue account in the period covered by these estimates will be Rs. 26.24 crores. But the final figure may be higher because the actual amount likely to be required for meeting the expenditure

in connection with the relief and rehabilitation of refugees is still very uncertain and some help may also have to be given to the new Provinces of West Bengal and East Punjab for which, in the absence of any reliable data, no provision has been included.

12. The revenue receipts, as I have said, are estimated at Rs. 171.15 crores. Customs receipts have been placed at Rs. 50.5 crores and take into account the effect of the recent restrictions on imports for conserving our foreign exchange resources. Income tax is expected to yield Rs. 29.5 crores on account of E.P.T. and Rs. 88.5 crores on account of ordinary collections. Although the Niemeyer Award has now ceased to have effect it is proposed to maintain the share of the Provinces in the income tax revenue at approximately the same level as now after making an adjustment in respect of the Provinces and parts of Provinces now included in Pakistan. The Centre will retain Rs. 3 crores out of the Provincial moiety as provided in the original budget. On this basis, the divisible pool of income tax is estimated at Rs. 66 crores and the Provincial share at Rs. 30 crores.

13. Revenue from the Posts and Telegraphs Department is expected to amount to Rs. 15.9 crores and the working expenses and interest to 13.9 crores leaving a net surplus of Rs. 2 crores. The outright contribution of the department to general revenues will be three-fourths of the realised surplus, the department retaining the balance. The department will get a rebate of interest on its share of the accumulated profits in the past which, after allowing for the portion of the department transferred to Pakistan, is expected to amount to Rs. 71 crores. As regards the contribution from Railways we do not expect anything in the current year. The House is already aware of the reasons for this from the Railway Budget.

## **EXPENDITURE**

14. The total expenditure for the year is estimated at Rs. 197.39 crores, of which Rs. 92.74 crores is on account of the Defence Services, the balance representing Civil expenditure. Following the customary procedure, I shall first deal with the Defence Estimates which remain, as in the past, the largest single item of expenditure.

## **DEFENCE SERVICES**

15. The reconstitution of the Armed Forces in India into two Dominion forces was an inevitable consequence of the partition of the country. This decision came at a time when the Armed Forces were in the process of rapid demobilisation. While a substantial measure of demobilisation had already been achieved, the process was arrested as a consequence of the decision to divide the remaining forces between the two Dominions on a communal cum optional basis. The strength of the Army at the time stood roughly at 410,000 troops. After the completion of the reconstitution of the Army, India will have roughly 260,000 troops. An organisation under a Supreme Commander, acting under the direction of the Joint Defence Council, was set up and made responsible for carrying out the reconstitution, and for general administrative control of the entire Armed Forces until the completion of reconstitution. From the 15<sup>th</sup> August 1947, however, the operational control of the troops in each Dominion was transferred to the Dominion Government. It was originally expected that the reconstitution would be completed by the 31<sup>st</sup> March 1948. But the Armed Forces Headquarters of each of the Dominion have been able to take over administrative responsibilities in a greater measure and earlier than was originally anticipated and the reconstitution of the Forces has in consequence been accelerated. It is now expected that this will be completed in the more important fields by the end of this month when the Supreme Commander's organisation will be disbanded.

16. The future size and composition of the Armed Forces have been engaging the attention of Government, as it is obvious that they must be related to the altered strategic needs of the country as well

as to its reduced financial resources. Under the pre-partition demobilisation plan the Army was to be reduced to about 230,000 men for undivided India by the 1<sup>st</sup> April, 1949 against which we shall have about 260,000 men for our share alone after the reconstitution of the Armed Forces. Due to the widespread communal disturbances in the Punjab and the sporadic outbursts of disorder in other parts of the country, there has been an unprecedented call on the Armed Forces in aid of the civil power. Government have accordingly come to the conclusion that the existing Forces should be retained until the 31<sup>st</sup> March 1948 but the position will be reviewed next month. The financial effect of this is that in spite of a reduction of revenue resources the expenditure on Defence Services will be running higher than it normally should during this year. In the present fluid conditions it is impossible to forecast the position in 1948-49.

17. India had never an adequate Navy or Air Force and the effect of the partition has been to reduce them still further, so far as the Dominion of India is concerned. It is obvious that even without the disturbances there could be no question of an overall demobilisation in these services. The future development plans of these services are under consideration.

18. The complete nationalisation of India's Armed Forces in the shortest time possible is the accepted policy of Government. Due, however, to various reasons which are now a matter of history, we have had a shortage of Indian officers for filling some of the posts in the technical services and the senior appointments, This holds good to a varying degree for all the three services. It was therefore decided to employ a number of British officers who volunteered to stay, for one year in the first instance, from the 15<sup>th</sup> August 1947. As these officers hold the King's Commission they were transferred to a special list of the British Army and the Supreme Commander assumed control over them. When subsequent developments indicated that the Supreme Commander's office may not continue beyond the 31<sup>st</sup> December 1947 it was decided to terminate the services of these British officers by the same date, leaving it to the two Dominions to offer fresh terms to any British officers they may wish to employ. The British officers have, therefore, been served with three months' notice, as laid down in their present terms of service, with effect from the 1<sup>st</sup> October 1947. The number of British officers whom it is essential for India to retain and the terms of service to be offered are now under the active consideration of Government. It may, however, be stated that the number of British officers to be retained will be relatively small and it is hoped that all operational Commands, at least in the Army and the Air Force, will be filled by Indian officers.

19. As has already been announced, an agreement was reached with the United Kingdom Government that the withdrawal of the British Forces from India should commence immediately after the transfer of power and completed as early as possible. The first detachment of British troops actually left India on the 17<sup>th</sup> August 1947. It was hoped at one time that the withdrawals would be completed before the end of 1947 but due to shipping difficulties it now appears that this may take up to April 1948. The British troops remaining in the country have, however, no operational functions. Except two R.A.F. Transport Squadrons the rest are merely awaiting repatriation.

20. The rapidly changing conditions this year have made it difficult to frame a close estimate of Defence expenditure and the position is further complicated by the fact that the proportion in which the joint expenditure incurred by the Supreme Commander's organisation should be allocated between the two Dominions is yet to be decided. On the best estimate that can be made at this stage, the net expenditure on Defence Services during the period 15<sup>th</sup> August 1947 to 31<sup>st</sup> March 1948 is estimated at Rs. 92.74 crores. The following main factors have contributed to an increase in the expenditure;

- (1) The decision to suspend demobilisation and to withdraw troops from overseas.
- (2) The implementation of the Post-war Pay Committee's recommendations in respect of Defence Services personnel. No provision for this was included in the original estimates.
- (3) The movement of troops and stores in connection with the reconstitution of the Armed Forces.

(4) The calling out of troops in aid of the civil power during the disturbances in the Punjab and elsewhere. The withdrawal of British troops from India earlier than was anticipated originally has resulted in a saving but this has been to some extent counterbalanced by expenditure in moving them to the United Kingdom and other destinations.

### **CIVIL ESTIMATES**

21. Details of the estimates under individual heads are given in the Explanatory Memorandum circulated with the Budget papers and I propose to draw the attention of Hon'ble Members to only the more important items included in them. As I have explained elsewhere, the initial liability in respect of the outstanding debt of the late Central Government and the pensions chargeable to it has been placed on the Indian Dominion subject to the levy of an equitable contribution from Pakistan. The contribution still remains to be settled and, for the present, no credit has been taken in these estimates for any recovery from Pakistan. The estimates also include Rs. 2221 crores on account of subsidies on imported foodgrains and a lump sum provision of Rs. 22 crores for expenditure on the evacuation, relief and rehabilitation of refugees from Western Pakistan. I have briefly referred elsewhere to the problems raised by the widespread communal disturbances in the Punjab and the North West Frontier Province and the mass migration of refugees between the two Dominions. There are two aspects to this problem viz., the short term one of giving immediate relief to the refugees pouring into this country from Pakistan, practically destitute, and the long term one of resettling them in India. All the resources at the disposal of the Government of India have been mobilised in arranging the evacuation and relief of these refugees and the railways and the Armed Forces have been utilised to the maximum extent possible on this work. It is not possible to estimate the expenditure likely to fall on Central revenues on account of these developments and I have provisionally included a sum of Rs. 22 crores on this account in the Revenue Budget. In addition, a sum of Rs. 5 crores is being included in the ways and means budget for advances to the East Punjab Government. But I must mention that this does not give any idea of the magnitude of the burden that may be placed on Central revenues by these developments. Indeed, the basis on which the expenditure on relief and rehabilitation should be shared between the Centre and the East Punjab, the province most vitally affected, still remains to be decided and may take some time to decide. Whatever the final arrangement in this behalf may be, I have no doubt that it is the desire of all sections of the House that financial considerations should not stand in the way of affording relief to these

Unfortunate people and in alleviating their sufferings in one of the most poignant human tragedies that could take place outside a war. 22. Before I leave this subject I should like to give a brief analysis of the total provision included for civil expenditure, so that a balanced view of the position may be obtained. Of the total provision of Rs. 104½ crores, Rs. 44½ crores are accounted for by the expenditure on refugees and the subsidising of imported foodgrains, leaving Rs. 60 crores for normal expenditure. This includes Rs. 5 crores for tax collection, obligatory expenditure of Rs. 221 crores on payment of interest and pensions and provision for debt redemption, Rs. 2 crores on planning and resettlement and Rs. 12 crores for expenditure on nation building activities such as education, medical, public health, the running of scientific institutions and scientific surveys, aviation, broadcasting etc. in which the Centre largely supplements the work of the Provincial Governments by providing valuable assistance by way of specialised services and research, leaving a balance of Rs. 18½ crores for the ordinary expenditure on administration, civil works etc. This expenditure only constitutes 18 per cent of the total civil expenditure included in the budget. In addition to the expenditure of Rs. 12 crores on nation building activities mentioned above, provision has been made in the Capital Budget for a grant of Rs. 20.39 crores to Provincial Governments for development and Rs. 15 crores for loans.

### **WAYS AND MEANS**

23. I shall now turn to give a brief account of the ways and means position. The budget for the current year provided for a borrowing of Rs. 150 crores but this target will not be reached. Owing to the communal disturbances in the country and the uncertainties of the political situation, the securities market

was very unsettled in the opening months of the year and no loan was actually floated before the 15<sup>th</sup> August 1947. After the doubts about the political future had been cleared by the decision to partition the country, there was some improvement in the position and although the market has been fairly steady in recent weeks, there is not as yet any large sustained demand for investment. Government issued early this month a fifteen year loan for Rs. 40 crores carrying interest at two and three quarter per cent with facilities for holders of the 31 per cent. Loan 1947-50, falling due for discharge on the 15<sup>th</sup> of that month to convert their holdings. The loan was issued at the beginning of the busy season and was not expected to be oversubscribed. But the public still seem to be hesitant in taking up Government loans and if their holding off is due to any lingering doubts about the responsibility for the repayment of the outstanding debt, I hope they will be reassured by what I have stated elsewhere that the Indian Dominion remains responsible to the bondholder. The need for money is now as urgent as ever if Government are to finance their own development plans and assist the Provincial Governments to implement their plans for development. There is also the short-term aspect to this problem, viz. the urgent necessity to counter the inflationary forces which are still present by withdrawing from the public as much surplus purchasing power as possible through Government loans.

24. Hon'ble Members must have noticed that in recent months there has been some criticism in certain quarters of the cheap money policy of the Government. At the last Annual General Meeting of the shareholders of the Reserve Bank the Governor of the Bank made some observations on this question. Under the influence of that eminent economist the late Lord Keynes, cheap money has been the cardinal feature of the monetary policy in many countries. It is no wonder that the Government of India fell in line with this trend in monetary policy. The House will realise that there is no absolute criterion by which to judge the propriety of rates at which Government borrow in the market. In the long run it is mainly a question of keeping a balance between the demands of Government on the market and the demands of Industry so that the available funds in the country are used to the best advantage. In the United Kingdom where the pursuit of this policy culminated in the issue of a 21 per cent irredeemable loan last year, attempts are being made to consolidate the progress made so far and not to proceed further in the same direction. I realise that if there is the need for such a cautious policy in a country where the economy is mature and the money and capital markets are highly developed, it is all the more necessary in the case of an economically backward country like India. Our efforts will now be directed towards consolidating and stabilising the position so far gained. There is no intention on the part of the Government to reverse the policy and thereby jeopardize the interests of those who have trusted the Government with their money. Our borrowing programme will be such as will enable us to obtain the funds required by Government as cheaply as possible without in any way affecting the flow of investment into industry. It is also my intention to reorganise the small savings movement which was considerably expanded during the war years, so that it might be retained as a peacetime organisation with the primary purpose of encouraging savings among the middle classes. In cooperation with the Provincial Governments, steps will be taken to place the movement on a permanent footing. I take this opportunity of appealing to the chosen representatives of the people in this House to co-operate with Government fully in their borrowing programme. If the standard of living of our people is to be substantially raised by undertaking large schemes of development, both the rich and the middle classes should come forward to place their savings at the disposal of the Government.

### **STERLING BALANCES**

25. The House will, I am sure, be interested to get some information on the subject of the sterling balances, the recent agreement regarding which between ourselves and His Majesty's Government in the United Kingdom I placed on the table of the House a few days ago. The peak figure which the sterling balances reached was Rs. 1,733 crores on the 5<sup>th</sup> April 1946. Thereafter, they have declined very rapidly. At the end of March 1947 they stood at Rs. 1,612 crores showing a reduction of Rs. 121 crores in twelve months. In the middle of July 1947, from when our new agreement became effective, they stood at about Rs. 1,547 crores. We had thus drawn as much as Rs. 65 crores in a little over six months. These large



decreases were due largely to heavy imports mainly of food grains and of consumer goods, of which the country had been starved during the period of the war. They also reflected some movement of capital from India, largely British.

26. This rapid depletion of the sterling balances caused some anxiety to the Government of India. These balances represent the entire foreign exchange reserves of this country and it is of the utmost importance that they should not be lightly frittered away on the import of unessential and luxury articles or on luxury living in foreign countries for they thereby reduce pro tanto the capacity of this country to finance capital and developmental expenditure abroad. The view of the Government of India is that these reserves should not be used to finance deficits in the balances of payments on what may be called normal current account. Our aim should be to meet our normal day-to-day requirements from abroad through the earnings of our current exports and we should draw upon these accumulated reserves, broadly speaking, only for the purpose of purchasing capital goods, the import of which is necessary for developing the agricultural and industrial productivity of the country.

27. With this aim in view, the Government of India decided to follow a more restrictive import policy from the second half of the calendar year 1947. Broadly speaking, that policy consists of dividing imports into three categories: free, restricted and prohibited. Imports of food, capital goods, the raw materials of industry and certain essential consumer goods are free and no exchange restrictions are placed upon their import. Consumer goods which are not absolutely essential are licensed on a quota basis, while others which in the context of the economy of this country must be regarded as totally unessential and luxury imports have been altogether prohibited. Together with the restrictions on imports were introduced certain restrictions on remittances abroad, in particular on the transference of Indian capital. These new policies are now showing the effects which they were calculated to have and the reduction in the sterling balances between the middle of July and the beginning of November 1947 has only been Rs. 21 crores. I should like to point out, however, that in one substantial respect the import policy now in force differs from that in force previously, in that in the licences issued for the licensing period June to December 1947 no discrimination has been made between currencies and imports from the dollar area have been allowed on the same basis as imports from the sterling area. This position, which the House will no doubt welcome, has been brought about by the terms obtained by us in our interim negotiations on the sterling balances. The main features of this agreement, which holds good to the 31<sup>st</sup> December 1947, are that the Indian sterling balances have been divided into two accounts which may well be likened to a deposit account and a current account. The current account has been opened with a credit of £65 millions. All fresh earnings of foreign exchange are credited to the current account and all balances in the current account are available for expenditure in any part of the world including the United States of America. The deposit account is not available for ordinary current transactions but can be drawn upon only for certain limited purposes such as the repatriation of British capital from India, the payments of pensions, provident funds and gratuities outside India and certain other defined categories of payments.

28. Shortly after this agreement had been signed there arose the dollar crisis. The strain on the dollar reserves of the United Kingdom Government was felt by them to be so great that they were compelled to break their agreement with various countries regarding the free convertibility of sterling into dollars. I am glad to be able to report to the House that our agreement stands unaltered and intact and that as long as we have any balance to our credit in the current account we shall be able to spend it without question in any currency area. The United Kingdom Government have, however, appealed to us for our co-operation in the matter of saving dollars and we have promised them this co-operation. We are now engaged on a review of our import policy and are investigating other means to save dollar expenditure and we may have, I fear, to reintroduce in the next licensing period the discrimination in favour of imports from the sterling area which we removed only so short a time ago. We trust, however, that it will be possible so to arrange this discrimination as not to injure the vital needs of the country's economy.

## **EMPIRE DOLLAR POOL**

29. The country has always displayed an interest in the arrangement commonly known as the Empire Dollar Pool. As has been explained before, the arrangement is that the countries of the sterling area hold all their foreign exchange reserve in sterling, selling currencies which they do not need to the Bank of England and buying from the Bank of England currencies of which they are in short supply. As a consequence, there is always in the custody of the Bank of England a pool of foreign exchange from which members of the sterling area can buy for sterling the currencies which they need. A more correct name for this arrangement would be "the Sterling Area Pool of Foreign Exchange". It has come to be known as the Empire Dollar Pool only because the most important of the foreign exchanges in the pool is the United States dollar.

30. Figures have been published by Government from time to time of India's earnings of dollars and other hard currencies and of her expenditure of these currencies and I shall now bring these figures up to date. From September 1939 up to the 31<sup>st</sup> March 1946 we earned Rs. 405 crores worth of United States dollars and spent Rs. 240 crores worth of United States dollars, leaving a surplus of Rs. 165 crores. On the other hand, in the same period we spent net Rs. 51 crores worth of other hard currencies, namely those of Canada, Switzerland, Sweden and Portugal so that our net surplus on hard currency account was Rs. 114 crores. During the year 1946-47 we had a deficit in the balance of payments with the United States of Rs. 15 crores, having earned Rs. 83 crores and spent Rs. 98 crores, and a deficit in the balance of payments with other hard currency countries of Rs. 7 crores. It may therefore be assumed that we contributed net to the pool between September 1939 and March 1947 Rs. 92 crores worth of hard currencies, which is the equivalent of 275 million dollars. During the quarter April to

June 1947 we have had a net deficit on hard currency account of Rs. 15 crores. It will be observed, therefore, that since the financial year 1946-47 we have been consistently drawing on the pool for our dollar requirements and that we are at the moment also in heavy deficit with the United States and other hard currency countries. Generally speaking, however, I would say that, thanks to our policy of foreign exchange restriction, we hope to end the year in a fairly comfortable financial position externally. What definite policy we will follow from the next year I am not now in a position to say because our agreement terminates at the end of this year and we do not yet know what kind of agreement will replace it. I fear, however, that in view of the dollar crisis which has threatened not only the United Kingdom but the entire world, we may be in somewhat greater difficulty in the matter of dollar exchange than we are now. We hope to enter shortly into further discussions with the United Kingdom Government on the subject of the sterling balances.

## **POSTWAR PLANNING AND DEVELOPMENT**

31. The House will remember that in the budget for the current year provision of Rs. 100 crores was made for development expenditure, including a provision of Rs. 45 crores for grants to Provinces. The partition of the country has naturally affected the scale of this expenditure as the Government of India are no longer concerned with the expenditure on development in the Provinces and areas now included in Pakistan. When the partition of the country was decided upon, Provincial Governments were informed last July that so far as the period up to the 15<sup>th</sup> August 1947 was concerned, the Government of India would make advance payments to cover expenditure on approved schemes up to the maximum of the proportion of the budget grant for this period. The Provinces were also advised not to enter into any major commitments that were likely to embarrass either of the successor Governments. It has since been decided that for the remainder of the year grants will be available to the Provinces now remaining in the Indian Dominion on the same scale as was originally planned subject to a proportionate adjustment on account of the division of the Punjab and Bengal and the transfer of most of the Sylhet district to East Bengal. In the estimates now placed before the House a provision of Rs. 20.39 crores has been included for grants to Provinces and a sum of Rs. 15 crores for loans to them.

32. In the last budget speech my predecessor drew attention to the fact that the resources available to the then Central Government for planning and development were likely to be less than was originally estimated. What he said then for the then Central Government is equally applicable to the present Government and in the light of the reduced resources likely to be available it may be necessary to redraw the development plans and rearrange their priorities. This does not however mean that there has been any change in the Government's policy of giving all the assistance in their power to the Provincial Governments for implementing their development schemes. It merely emphasises the need for the Provinces mobilising all the resources for this purpose and I have no doubt that this is recognised by the Provinces themselves. The House will appreciate that there is a large measure of uncertainty about the future allocation of resources between the Centre and the Provinces and till this is decided it will be difficult to make any forecast of Central resources or determine the extent to which they will be available for development and I hope to take this question of reexamining the development schemes with the Provincial Governments shortly. Meanwhile, all the approved schemes of development will be continued and the necessary funds will be made available for them. Having given this assurance on behalf of the Central Government, I would earnestly urge on the Provinces the need for conserving all their resources and securing the most rigid economy in expenditure. As I have stated, the whole basis on which post-war development plans were conceived has now been upset. The substantial revenue surpluses which were anticipated in the Central budget will now be turned into substantial deficits. In the context of this new development, the need for utilizing all the available funds in the most effective manner possible should be appreciated by the Provincial Governments.

33. In the Central field the progress on development schemes is being maintained and we are going forward with all the sanctioned schemes particularly those schemes of development with long range benefits to the country. In this connection, the House will be interested to know that an agreement has been reached between the Central Government and the Provincial Governments concerned regarding the setting up of the Damodar Valley Authority. Another scheme which is likely to be taken up very shortly is the construction of the Hirakud Dam in Orissa at an estimated cost of Rs. 48 crores, the benefits from which will include irrigation for over a million acres, 350, 000 kilowatts of power and a considerable degree of protection from floods to the coastal districts of Orissa. It is hoped shortly to reach an agreement on this project with the Orissa Government and the Orissa States after which the actual work of construction would begin early in 1948. It is also proposed to concentrate on the construction of the Bhakra Dam in the East Punjab.

## **THE DEFICIT**

34. I have carefully considered if any part of the deficit for this year should be covered by additional taxation and I have come to the conclusion that it should be left largely uncovered. If, for any reason, our ordinary expenditure threatens to outrun our revenue there will be a clear case for either reducing the expenditure to within the available revenue or raising additional revenue to meet the expenditure. But the circumstances during the period under review have been abnormal and the deficit is entirely due to these abnormal factors. The expenditure estimates include Rs. 22 crores for the evacuation and relief of refugees while subsidies for imported food grains are expected to cost Rs. 22½ crores. Defence expenditure is also considerably inflated due to the slowing down of demobilisation following the partition of the country and the necessity to maintain larger forces than would normally be necessary. It must also be remembered that no credit has been taken in the estimates for Pakistan's share of the expenditure on pensions and interest. If these factors are allowed for the budgeted deficit of Rs. 26.24 crores will be converted into a surplus. Notwithstanding this I feel justified in tapping any available source of income if it could be done without adding to the burden of the ordinary man. After a careful consideration of all the available sources I have decided to replace the existing export duty of three per cent on cotton cloth and yarn by a duty of four annas per square yard on cotton cloth and six annas a pound on cotton yarn. In a full year this will yield Rs. 8 crores but in the current year the net additional

revenue will amount to only Rs. 165 lakhs leaving a final deficit of Rs. 24.59 crores. A bill to give effect to this proposal will be introduced at the end of my speech.

## **GENERAL FINANCIAL POSITION**

35. This is the eighth consecutive deficit budget and the House may well ask itself if our revenue position is sound. I have myself no hesitation in answering that question with an emphatic 'yes'. The years covered by these budgets have been overshadowed by the greatest war in history and no country, whether neutral or belligerent, has been able to escape its economic effects or its aftermath. The deficits in the war years were wholly due to the high level of Defence expenditure and were met as far as possible by raising additional taxation. The return to peace time conditions has been slower than we anticipated and even this tardy progress has been retarded by the recent partition of the country and the unhappy developments in the Punjab. I have just mentioned the large burden thrown on this year's budget by the unavoidable expenditure on refugees and the payment of subsidies for foodgrains. In addition, the expenditure on Defence is much higher than it would be in a normal year. If these special factors are taken into account it will be seen that we have not been living beyond our means or heading towards bankruptcy. I do not wish in any way to minimize our present difficulties or to underrate the effort required to surmount them but I have no doubt that once we reach fairly normal conditions and are able to reduce our Defence expenditure to peacetime proportions and curtail our reliance upon import of foodgrains we should be able to balance the budget. It will be too optimistic to expect normal conditions for the next year but I feel that with a determined all round effort we should be able to achieve this result in 1949-50.

36. And what about the general financial position of the country? Here again while there is no room for complacency there is equally no reason to take a pessimistic view. There is no doubt that economically and strategically the partition of the country has weakened both the Dominions created by it and it to a truism that an undivided India would have been in every way a stronger State than either. But the Indian Dominion with its acceding States would still cover the larger part of the country, with immense resources in men, material and industrial potential. Our debt position is also intrinsically sound and for a country of its size, India carries only a relatively small burden of unproductive debt. Our external debt is negligible and we have considerable external resources in the accumulated sterling balances. At the beginning of this year the total public debt and interest bearing obligations of undivided India stood at roughly Rs. 2,531 crores of which only Rs. 864 crores represented unproductive debt and Rs. 36 crores. external debt, while her external reserves amounted to over Rs. 1,600 crores. The share of Pakistan in these has not yet been determined but it is unlikely to affect the broad proportions of this picture.

37. The only disturbing features in the position are the persistence of inflationary trends and the unsatisfactory food position to both of which I have drawn attention elsewhere. The only real answer to inflation is to increase our internal production and thereby close the gap between the available supplies and the purchasing power in the hands of the community which in present circumstances imports cannot bridge. Till this position is reached the community must conserve its purchasing power by lending it to Government. As regards food, I am sure the House will agree that the country cannot depend indefinitely on imports. For one thing this places us at the mercy of foreign countries for our vital necessities and for another large scale Imports of foodgrains seriously affect our foreign exchange position and threaten to consume the bulk of the available resources which are badly required for the industrialization and development of the country. We must concentrate our energies on producing as much food as possible within the country. I suggest that this is not an impossible task, for after all the total Imports from abroad, which have never touched more than 21 million tons in any year so far, represent only a fraction of the total foodgrains amounting to 45 million tons we produce, although they make a large hole in our available foreign exchange.

38. I should like to make a few observations on the criticism made in certain quarters that the level of taxation introduced in the last Budget has seriously affected the incentive for Investment. In their last Annual Report the Central Board of Directors of the Reserve Bank of India have observed "There seems little doubt now that the severity of the last Budget is defeating its own purpose and is hindering the formation of capital for productive purposes. Unless correctives are applied without delay, there is a danger of the very foundations of society and economic life of the country being undermined by deepening penury and despair". A pronouncement of this kind coming from such an authoritative source must receive serious notice. I have no doubt in my mind that it was not the intention of the Government to so arrange its taxation policy as to stifle the growth of Industry in the country. On the contrary, it is of the utmost importance that the country should be industrialised rapidly so as to secure increased production and a widening range of employment for the people. There is no need for any serious difference of opinion based on more ideological differences. Whatever might be the ultimate pattern of our economic structure, I hold the belief that for many years to come there is need and scope for private enterprise in industry. We cannot afford to lose the benefit of the long years of experience which private enterprise has gained in the building up of our industrial economy. I believe that the general pattern of our economy must be a mixed economy in which there is scope both for private enterprise and for State enterprise. Before I present the annual Budget to this House next February, I shall make a careful examination of the consequences of our taxation policy and endeavour to make any adjustments that may be necessary to instill confidence in private enterprise. In the meantime, I may assure the House that it is not the policy of the Government to hamper in any way the expansion of business enterprise or the accumulation of savings likely to flow into investment.

#### **CONCLUSION**

39. I would conclude the Speech with an appeal to this House and through the House to the country at large. For the first time in two centuries we have a Government of our own answerable to the people for its actions. A to the duty and the privilege of such a Government to render an account of its stewardship to the representatives of the people, but it has also the right to ask for the co-operation of the entire community in the carrying out of the accepted policies. Events of the last few weeks have unmistakably shown that the political problems arising out of our status have not yet been fully solved. While we have secured freedom from foreign yoke, mainly through the operation of world vents and partly through a unique act of enlightened self abnegation on behalf of the erstwhile rulers of the country, we have yet to consolidate into one unified whole the many discordant elements in our national life. This can be achieved only by the rigorous establishment of the rule of law which is the only durable foundation on which the fabric of any democratic State can be raised. Respect for law is essentially a matter of political training and tradition and transition from a dependent to an independent status always makes it difficult. In the initial stages to secure that unflinching obedience to the rule of law which always acquires a new meaning in a new political context. If the fabric of the State is not built on durable foundations, it will be futile to try and fill it with the material and moral contents of a good life. If India, just risen from bondage, is to realise her destiny as the leader of Asia and take her place in the front rank of free nations, she would require all the disciplined effort her sons can put forth in the years immediately ahead. The willing help and co-operation of all sections of the community is required in maintaining peace and order, in increasing production and in avoiding internecine quarrels whether between communities or between capital and labour. I am sure my appeal for this help and co-operation will not go in vain.

**(November 26, 1947)**