The Appeal of Confiscation

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A RATHER special programmatic point in the economics of underdevelopment (see author's article on the subject in the Special Number 1959. pp 986-996—Ed) is discussed, probably for the first time in serious economic literature, by M Bronfenbrenner in an article provocatively entitled "The Appeal of Confiscation in Economic Development" ('Economic Development and Cultural Change', Vol III, No 3, April 1955). Working on the basis of somewhat restricted models in which development is started off solely by diverting a large part of existing 'property income' into developmental investment, Bronfenbrenner argues that the appeal of confiscation in financing economic development is not 'pure propaganda' in the sense of economic fallacy. It is a serious device for initiating rapid industrialisation. He is careful to point out that confiscation may take various forms: it may or may not involve substantial violence and destruction; it may be a capital levy at rates close to 100 per cent; it may be 'nationalisation' with compensation totally or partially wiped out by rapid inflation.

His analysis is mainly based on a comparison of three models: Model I Economic Stagnation; Model II—Confiscation, Russian Style; Model III Confiscation, Chinese Style. Model III differs from Model II only in so far as a part of the confiscated property income flow is diverted into immediate enhancement of 'service income' (higher industrial real wages and tax relief to peasants). Model II gives the highest rate of growth. Model III also breaks stagnation, though growth is slower compared to Model II, but it reaches the common people more rapidly. Care is taken not to idealise the results of confiscation. Allowances are made for inefficiencies in resource allocation, in innovations, the increased population growth rate and (in Model III) for diversion of income immediately from savers to spenders. The conclusion is that the appeal of confiscation is almost irresistible for underdeveloped countries. An incidental point cleared up is why the older industrial countries did not succumb to this appeal. There was some confiscation: the British confiscated property in India, some constituent States of the USA repudiated debts. But eighteenth and nineteenth century governments were less adequately equipped to execute development projects than modern governments of underdeveloped countries.

Democratic Alternatives

Bronfenbrenner next discusses whether underdeveloped countries can substitute confiscation by various democratic alternatives' of inducing propertied classes to save more and mobilising increased savings for development. This is dismissed as producing results which are likely to be too little and too late. Also dismissed as futile is 'imperialistic repression of confiscation' in the modern form of military assistance to 'dependable' governments in underdeveloped countries. A third alternative remains, which is discussed more fully. Can the advanced capitalist countries compete with the appeal of confiscation by making sufficiently large amounts of capital available at sufficiently attractive terms?

Bronfenbrenner argues that if such capital inflow into underdeveloped countries is to stave off confiscation, it must not only be 'large' and 'attractive,' but flow at an accelerated rate. This is because as foreign capital investment increases, it presents a greater 'temptation' to the confiscator (because its absolute volume increases), requiring greater 'ransoms' for continued protection. At any one time, confiscation can be restrained only when the difference between future expected aid and the value of capital 'confiscable' in the present, is large. The inflow of foreign capital must, therefore, not only continue but accelerate, "with no upper limit in sight until the borrowing country has achieved development at a rate satisfactory to Its leaders".

Barriers to Capital Flow

There are, however, two barriers to such a capital inflow: an external barrier in the underdeveloped country, and an internal barrier in the lending country. The externa1 barrier has not been discussed by Bronfenbrenner but by Henry J Bruton ("Growth Models and Underdeveloped Economies", 'The Journal of Political Economy', August 1955). Quoting Professor Evsey D Domar ('Essays in Economic Growth') Bruton points out that such a continued inflow of capital requires a continued export surplus (which, moreover, will have to accelerate in Bronfenbrenner's model). While not impossible conceptually, this is unrealistic (for various reasons noted in Section IX of my article "The Economics of Underdevelopment"). The ' internal' barrier to such capital outflow from the 'mature' economies of the West has been mentioned by Bronfenbrenner. Despite 'maturity', capital remains scarce for purely domestic uses (eg, to finance the modern 'technological revolution' of the postwar years, though some modern techniques may turn out to be 'capital-saving' in the long run; to say nothing of military expenditure). Domestic investment thus retains priority, leaving only a trickle for underdeveloped countries. For these reasons, Bronfenbrenner endorses current Western policy of economic neo-isolation' or withdrawal from the underdeveloped world. Such a policy, on his reasoning, invites immediate confiscation of existing Western assets or at least accelerates confiscation. But it is the 'least worst' policy from the Western point of view. Not only because there is no practical alternative, but because there are countries where this reasoning does not apply. More important of these exceptions are the thinly-populated oil rich countries, and, somewhat unexpectedly, the Soviet Union and the People's Democracies. In the case of the former, until a fuel-revolution destroys Western demand for mineral oils, the yield of capital is likely to be high enough to satisfy simultaneously foreign investors and domestic planners. In the case of the latter, the already achieved high growth rates makes confiscation irrelevant for economic reasons.

The value of this analysis cannot be doubted. Incidentally, mutatis mutandis, it can be applied to the problem of advanced socialist countries assisting underdeveloped countries. In this case, also, capital scarcity in the advanced countries will impose a still more stringent internal barrier. The external barrier, too, will probably be intractable, if only because the advanced socialist countries have learnt to manage without large scale intake of underdeveloped countries' staple exports. These barriers are likely to cramp Soviet assistance to underdeveloped countries. Of course, the directly growth-motivated Soviet public opinion is more likely than profit-motivated Western opinion to make outright gifts of capital goods. It is also likely to agree more readily to convert capital loans into gifts in the event of balance of payments difficulties (so that there is no problem created by the 'appeal of confiscation' here). Moreover, there are no barriers to the transmission of planning techniques, which can be of great value (provided there is no 'mechanical transplantation').

Proportion of Property Income

Nevertheless, Bronfenbrenner's analysis can be improved upon. A critic may point out that while his 'Stagnation Model' explicitly includes an allowance for depreciation of capital, his growth models do not. This, however, does not necessarily invalidate his growth models. A more serious objection can perhaps be advanced against his assumption that a simple diversion of existing property income in the stagnation model to developmental investment will in itself suffice to initiate development. This is based on the assumption of a high proportion of property income to national income in real terms In the stagnation model, the diversion of a part of which is sufficient to procure an assortment, of capital goods of the right composition to initiate development. The alleged high proportion of property income to national income in the stagnation model has been deduced from dubious monetary estimates which include far too many Imputed values' for many marketed and all non-marketed goods and services. And the estimation of the 'capital value' as well as the internal composition of the initial investment required is a difficult problem to which Amartya Kumar Sen has drawn attention in a recent article ("Some Notes on the Problem of Choice of Capital Intensity in Developmental Planning": 'Quarterly Journal of Economies', November 1957). It is hard to generalise about this problem, though planners do, of course, make concrete estimates in specific conditions and quite often succeed in sparking development.

That is why 'the appeal of confiscation' has in general been less strong than here visualised, at any rate as a device for initiating development. In the special context of exceptionally low production and national income caused by the dislocation of war and civil war (as in Russia and China), the quick diversion of property income via confiscation may be essential to restore production (without much new development), and so set the stage for initiating rapid development. Expropriation helped reconstruction and merely set the stage for development, which came later with the Five Year Plans.

Why Appeal Is Weak

In the underdeveloped countries of today, there is a further reason why the economic appeal of confiscation should be weak. They are much more involved than Russia or China were in the network of world trade, and their exports are much more precariously placed. After the Revolution, Russia's exports were mainly grain and timber, which were fairly stable, though the crash in values in the 1930 depression imposed special strains. After war and civil war, China was much less involved in world trade. In contrast, exports from contemporary underdeveloped countries are important but are threatened by substitutes, so that their exports cannot be easily raised. But this also means that their exports can be more easily reduced than, say. in the nineteenth century. While this imposes a barrier on further capital inflow, it also weakens the appeal of confiscation *to* initiate development. Declining exports during development complicates the problem of repayment and servicing of capital inflows, It may also precipitate the problem of transferring redundant unemployed labour in export industries to new industries (which is best handled gradually). Decline in exports may be induced by advanced capitalist countries deliberately as retaliation against confiscation. Diversion of these exports to socialist countries may help meet the situation (e g, as diversion of Egyptian cotton exports to the Soviet Union did during the recent Suez War). But their 'absorptive capacity' is not likely to be sufficiently large.

The above argument is, of course, subject to qualifications. When there is rapid industrialisation, the problem is essentially a short-term one, As development gets going, the importance of capital goods imports, and therefore of matching staple exports, will decline. The jolt given by declining exports will be less. And in the time-period which matters, the retaliatory power of the Western countries may be strictly limited. It may not be easy for Western private-enterprise economies, even if they are 'steered* for other purposes, to make the drastic adjustments required to replace their intake of underdeveloped countries' exports by substitutes. But the fact remains that it is the explicit neglect of balance of payments problems by Bronfenbrenner which has produced such a strong case for confiscation. Their incorporation makes the results less conclusive.

Appeal Grows Stranger

However, the criticism made above does not invalidate but serves to strengthen the second part of Bronfenbrenner's analysis dealing with fresh capital inflows from the West to spark development. Even though the initial appeal of confiscation is less strong than he supposes, it remains true, as he says, that the appeal grows stronger ELS the value of foreign capital invested increases. This is however not so much because the 'temptation to confiscate' grows. With development, national income will certainly grow. The growth in the absolute volume of foreign capital inflow will not necessarily increase the 'temptation to confiscate': the proportion of foreign capital to total capital and of return on foreign capital to the saving ratio' of the economy is more likely to fall (unless the rate of return on foreign capital is abnormally high and service charges accumulate at compound interest as in K A Naqvi's recent models ("Foreign Capital and the Problem of Foreign Exchange: Enquiry D, The inflow of foreign capital is likely to be checked for other reasons. Any growth in foreign capital invested means servicing and repayment requirements which dictate rising exports from underdeveloped countries. From the point of view of both creditor and debtor countries, this will increasingly involve, export of those 'material goods' which the advanced countries themselves produce. This will really involve repayment either in the form of unemployment or 'more leisure' in the advanced countries, which, as we have seen, is unreal. For other reasons, Western communities may be forced to accept large scale 'structural unemployment' or go over to a 'leisure economy'. But the need to help out the underdeveloped countries is hardly likely, on present indications, to persuade them to do so. Western refusal to accept payments can then compel the developing economies to repudiate debts: in this sense, the 'compulsion' rather than the 'appear to confiscate may grow in the developing countries,

Around Bombay Markets

Still Marking Time

Thursday, Morning

DALAL STREET'S trading pattern last week did not indicate any decisive trend. The 'general tone, however, appeared distinctly steady. Activity was predominantly professional and interest was very selective. Bulls were not aggressive but they seemed to be picking up courage. Sellers were reserved. Bears were inclined to cover their sales on setbacks. The wide swings in prices since about the middle of July have shaken both bulls and bears. Seems surprising. But that is what it is.

Automobile shares continue to he in the limelight because of the industry's growth prospects. All manufacturers seem equally optimistic about getting Government permission for producing small cars which have a vast market. Cotton Mill shares are holding remarkably firm on the belief that cloth might become scarce in the none-too-distant future. Only last year, the mill industry complained about the crisis of accumulation. What a turn! Food prices are higher than last year and so are cloth prices. Where is the consumer resistance now?

Steel and Cement shares are making a mixed showing. Tata Steel have ceased to be popular with bulls but Indian Iron are heading for a new high level. Not surprising. Tisco cut its dividend; Indian Iron maintained it. Among Cements, A C C go virtually abegging (once they occupied the pride of place among the blue chips) but Digvijay keep firm because of the rising trend in West Coast Paper. Shipping shares are without friends. Tata Chemicals are oppressed by talk of lower dividend.

According to technical analysts, the market is moving in a big trading area, the outside limits being set by the July top and the subsequent bottom. A trading area denotes a period of uncertainty. This is the time when the market makes a fresh assessment of various factors influencing the trend of equities. That the market should find it difficult to make up its mind is not ununderstandable. Declining yields and the steady growth of the investible funds are pulling the market in opposite directions.

Cash shares continue to hold firm with business limited only by the volume of offerings. Too much money seems to be chasing too few shares. Several new issues are expected in the market now that the State Loans are out of the way. Tisco issue is the biggest, Indian Dyestuff, Simp'ex Mills, Amar Dye Chem, Larsen and Toubro, Hindustan Aluminium, Baroda Rayon, Mandya National Paper, Sassoon Mills arc some of the companies which have only been awaiting the exit of the State Governments from the field. Considering the fancy premiums enjoyed by some of the new shares, the success of these issues can be taken almost for granted.

A Word about Bombay Burmah

A word about Bombay Burmahs interim dividend would seem necessary. The directors have recommended an interim dividend of Rs 7.50 on old shares and Rs 3 on new shares for the year to May 31. Is the dividend tax-free, without deduction of tax or taxable? Nobody can tell. According to informed sources the dividend is tax-free. One hopes they are right. But there is nothing in the information provided by the Company to suggest that it is really so.

The Company cannot get away with the excuse that it has made no departure in its procedure for announcing the dividend. For in the past when no mention was made about the tax along with the dividend, it was taken for granted that the dividend was tax-free. But it is very different now. With the Company's financial year ending after March, dividend becomes payable under the new system of corporate taxation where tax has to be deducted at the source. Unless otherwise mentioned, dividends are to be considered as taxable. It is unfortunate that the market should be left guessing about the dividend, particularly when Bombay Burmah are a leading speculative counter.

Equally disappointing is the Company's despatch which says nothing more than that the tea crop amounted to 69.51 lakh pounds in 1958-59 against 67.38 lakh pounds in 1957-58. For tea is not the only source of income of the Company. In the 1957-58 accounts, realisation from tea constituted only half of the total income. If the Company desires to keep its shareholders well informed it should furnish more detailed information. Giving figures only of tea crop can be very misleading. Better withhold such scanty information.

Oilseeds

Doing Well

OILSEEDS were generally firm but holiday feeling had a restraining effect on activity. The previous week's rally was continued into the week under review and the market saw its best on August 17. But heavy corrective profit-taking and some bear pressure encouraged by reports of beneficial rains in the producing areas erased nearly all the earlier gains and closing prices on August 19 did not show any noticeable variations from their previous week's levels.

Groundnut February which had risen from Rs 166.50 to Rs 169 slipped back to Rs 166.75. The maturing contract improved from Rs 189 to Rs 194 but only to react to Rs 191.50. Castor September and May contracts which had been marked up from Rs 154 and Rs 155.75 to Rs 155 and Rs 157.75 eased again to Rs 153 and Rs 155.50 respectively. Linseed September were unchanged over the week at Rs