

Report of The Indian Fiscal Commission

The Indian Fiscal Commission was appointed by the Govt. of India in October 1921 in accordance with the recommendations of a Committee of the old Imperial Legislative Council on Imperial Preference out of whose deliberations the question of Fiscal Autonomy of India mainly arose. The members of the Commission were :—Sir Ibrahim Rahimtoola, President, and Mr. J. M. Keynes, C. B. of Oxford, Mr. T. V. Seshagiri Ayyar of Madras, Prof. J. C. Coyajee, Sir M. B. Dadabhoi, Sir Edgar Holberton of the Burma Chamber of Commerce, Sir Montagu Webb of Karachi, Mr. G. W. Rhodes of Messrs Hoare, Miller & Co. Mr. R. A. Mant of the Govt. of India, and Messrs Jamnadas Dwarkadas, Ghanashyamas Birla and Narottam Morarjee, as members. About this time a rapid agitation of the Sydenham gang in England was stirring up Lancashire to fight the tendency on the part of Mr. Montagu, at that time the Secretary of State for India, to allow fiscal autonomy to India, and the strong European interest represented on the Commission gave lie to the hope that the question will be properly dealt with due regard to Indian interest. Mr. Keynes however did not attend more than a very few sittings of the Commission. The Commission began work on the 10th November 1921 at Bombay and after visiting various places to collect evidence closed its public work in April 1922, and signed its report on the 6th July 1922. The report consists of two parts ; one, the unanimous report signed by all the members, and the other, the Indian minority report signed by all the Indian members including the President, except Sir M. B. Dadabhoi.

Summary of the Main Report

Principal Recommendations.

(1) (a) That the Government of India adopt a policy of Protection to be applied with discrimination along the lines indicated in this report.

(b) That discrimination be exercised in the selection of industries for protection and in the degree of protection afforded, so as to make the inevitable burden on the community as light as is consistent with the due development of industries.

(c) That the Tariff Board (see below) in dealing with claims for protection must satisfy itself—

(i) That the industry possesses natural advantages.

(ii) That without the help of protection it is not likely to develop at all, or not so rapidly as is desirable, and

(iii) That it will eventually be able to face world competition without protection.

(d) That raw materials and machinery be ordinarily admitted free of duty, and that semi-manufactured goods used in Indian Industries, be taxed as lightly as possible.

(e) That industries essential for purposes of National Defence and for the development of which conditions in India are now unfavourable, be adequately protected, if necessary.

(f) That no export duties be ordinarily imposed except for purely revenue purposes, and then only at very low rates ; but that when it is considered necessary to restrict the export of food-grains, the restriction be effected by temporary export duties and not by prohibition.

(2) That a permanent Tariff Board be created whose duties will be, *inter alia*, to investigate the claims of particular industries to protection, to watch the operation of the Tariff, and generally to advise Government and the Legislature in carrying out the policy indicated above.

(3) (a) That no general system of Imperial Preference be introduced ; but

(b) That the question of adopting a policy of preferential duties on a limited number of commodities be referred to the Indian Legislature after preliminary examination of the several cases by the Tariff Board.

(c) That if the above policy be adopted, its application be governed by the following principles :—

(I) That no preference be granted on any article without the approval of the Legislature.

(II) That no preference given in any way diminish the protection required by Indian industries.

(III) That preference do not involve on balance any appreciable economic loss to India.

(d) That any preference in which it may be found possible to give to the United Kingdom be granted as a free gift.

(e) That in the case of other parts of the Empire preference be granted only by agreements mutually advantageous.

(4) That the existing Cotton Excise Duty, in view of its past history and associations, be unreservedly condemned, and that Government and the Legislature start again with a "clean slate", regulating their excise policy solely in the interests of India.

Subsidiary Recommendations

(5) That the proviso to Section 20 of the Sea Customs Act be repealed, and that Customs Duty be ordinarily levied on goods belonging to Government.

(6) That difficulties in the shape of shipping rebates or unfair advantages like dumping, depreciated exchanges, bounty-fed imports from abroad be investigated, and where possible, removed.

(7) That industrial development be promoted by giving a more industrial basis to primary education and providing opportunities for training apprentices, and organisations for increasing the mobility of labour.

(8) That no obstacles be raised to the free inflow of foreign capital, but that Government monopolies or concessions be granted only to companies incorporated and registered in India with rupee capital, such companies to have a reasonable proportion of Indian Directors, and to afford facilities for training Indian apprentices.

(9) That the tariff be not ordinarily employed for retaliation or as a means of aggression.

(10) That the tariff be elaborated with a view to remove ambiguities, and that the system of specific duties and Tariff valuations be cautiously extended.

Details of the Report.

On the first point, *viz.*, the tariff policy of the Government of India, the conclusion of the Commission is stated in the following words :—" We recommend in the best interests of India the adoption of a policy of protection to be applied with discrimination along the lines indicated in this report." The decision in favour of a policy of protection rather than one of free trade is based on a careful analysis of the probable gain and loss in Chapters IV, V and VI. It is shown that the industrial development of India has not been commensurate with the size of the country, its population and its natural resources, and that India will derive great advantages in many directions from a considerable development of Indian industries. It is then pointed out that the conditions for a rapid industrial advance are suitable and that without the stimulus of protective duties the advance will not be sufficiently rapid. The necessity of continuing to derive a high revenue from the tariff, which is apparent from a consideration of the financial situation, is also held to lead inevitably towards protection. On the other side of the account the loss involved by the burden of increased prices and the effect of this burden on various classes of the community is examined.

It is shown that the exercise of discrimination in the selection of industries for protection and in the degree of protection afforded will ensure that the inevitable burden on the community is kept as light as is consistent with the due development of industries. The final conclusion is that, apart from the strong Indian sentiment in favour of protection, the balance of advantage on economic grounds is heavily on the side of the policy recommended.

The Policy Justified

The justification of the policy rests largely on the manner in which it is worked, as it is held that any type of indiscriminate protection would entail a sacrifice on the part of the mass of the people out of proportion to the results. This accounts for the great importance attached by the Commission to the Tariff Board which it proposes should be constituted. The Tariff Board will be the instrument by means of which the policy will be "applied with discrimination." It is proposed in Chapter XVII that the Tariff Board should be a permanent body consisting of three members of high standing and ability. The main duties of the Board will be to investigate and report on the claims of particular industries to protection, to watch the operation of the tariff, and generally to advise the Government and the Legislature in applying the policy in detail. The functions of the Board would be advisory, and not executive, but stress is laid on the necessity of making public its findings and recommendations.

Principles are laid down by the Commission in Chapter VII for the guidance of the Tariff Board. The three main conditions which should be satisfied in the case of an industry claiming protection are :—

- (a) That the industry possesses natural advantages ;
- (b) that without the help of protection it is not likely to develop at all or not so rapidly as is desirable ; and
- (c) that it will eventually be able to face world competition without protection.

As a qualification of these general conditions it is recommended that industries essential for purposes of national defence, and for the development of which conditions in India are not unfavourable should if necessary, be adequately protected. Further, the general principles are laid down that raw materials and industrial machinery should ordinarily be admitted free of duty, and that partly manufactured goods used in Indian industries should be taxed as lightly as possible. The taxation of articles to which protectionist considerations do not apply will be outside the purview of the Tariff Board and will be regulated in accordance with the financial needs of the country.

Various supplementary measures are indicated in Chapter VIII as necessary in addition to protective duties, if full industrial development is to be attained. A more industrial bias should be given to primary education, opportunities should be provided for the training of Indian apprentices, and organizations for increasing the mobility of labour should be developed. The consideration of legislation against dumping is suggested, such legislation not to take the form of a general automatic measure, but to provide for the imposition of a dumping duty only in the case of particular commodities, and only when it has been established that dumping is taking place to the detriment of an Indian industry. Precautions are also suggested against imports from a country in which the exchange is seriously depreciated and against any system of export bounties granted by foreign countries. Reference is also made to the complaints of Indian industries against the railway rates policy and coastal shipping rates, and suggestions are made for meeting those complaints. The possibility of legislation directed against shipping rebates is suggested.

The tariff policy in India cannot be confined merely to a consideration of import duties. There are two other important classes of duties which are at present levied in India in connection with the tariff excise duties and export duties, and the Commission devotes two chapters to each of these. With regard to excise duties a general examination is made in Chapter IX of their nature, justification and effect and certain principles limiting their imposition are suggested. A separate Chapter (X) is given to the Indian cotton excise the history of which is described in detail. The conclusion of the Commission is that the existing duty should, in view of its past history and associations, be unreservedly condemned, that the British Government should announce its intention of allowing the Government of India to decide, in agreement with the Indian Legislature, what action should be taken, and that the Government of India and the Legislature should then begin with a clean slate and take such measures as the interests of India require.

Export Duties

Export duties are dealt with in Chapters XI and XII. The conclusions of the Commission are that export duties tend to injure the home produce and that they should therefore not be utilised for protective purposes. They may, however, under certain circumstances be imposed for revenue purposes, but they should be imposed with great caution, they should be imposed only on articles in which India has a monopoly or semi-monopoly, or in every case the duties

should be moderate. The only exception to these principles which the Commission recognizes is when the price of foodstuffs shows a tendency to rise to dangerous heights. In such a case the Commission holds that it may be necessary to restrict the export of food grains and that as there are grave objections to direct Government prohibition or regulation of exports, the least objectionable measure would be a temporary export duty on food grains.

The Commission makes no definite recommendations regarding the treatment of particular industries, holding that it had not sufficient material for the purpose, and that the necessary enquiries must be made by the Tariff Board. When, however, any principle laid down by the Commission admits of direct application, this is indicated, and accordingly the Commission definitely recommends the abolition, as early as possible, of the import duties on machinery and coal, and the export duties on hides and tea.

The second main subject referred to the Commission was the question of Imperial Preference and this is dealt with in Chapter XIII. The conclusions of the Commission are that any general system of preference to British products would involve a serious burden which it would not be reasonable for India to shoulder, while, on the other hand, the possibilities of advantage to India from preferences granted to her exports are limited. At the same time India may be in a position in certain cases to grant preferences which would be of assistance to British industries and would not cause appreciable economic loss to India. The advantages on broad Imperial grounds of recognizing the principles of Imperial Preference are pointed out, and it is suggested that the question of granting preferences on a limited number of commodities be referred to the Indian Legislature after preliminary examination of the several cases by the Tariff Board. If this policy is adopted it is recommended that its application be governed by the following principles :—

(a) That no preference be granted on any article without the approval of the Legislature.

(b) That no preferences should in any way diminish the protection required by Indian Industries.

(c) That preference should not involve any appreciable economic loss to India after taking into account the economic gain which India derives from the preference granted her by the United Kingdom.

The above proposals relate entirely to preference to the United Kingdom, and it is recommended that any preference which it may be found possible to grant to the United Kingdom should be granted as a free gift. In the case of the other parts of the Empire a different policy is recommended. It is suggested that the principle

of reciprocity should be followed, i.e., that preference should be granted only as the result of agreements mutually advantageous.

Review of Final Chapters

In Chapter XIV the tariff is dealt with in its more technical aspect. The Commission recommends that the system of specific duties and tariff valuations should be extended cautiously and that the description of articles in the tariff should be elaborated. The system of double tariffs which prevails in most protectionist countries is condemned as unsuitable to Indian conditions, and the undesirability of employing the tariff as a means of aggression or, unless in exceptional circumstances, for purposes of retaliation is emphasized. The Commission recommends that in the interests of Indian industries customs duties should ordinarily be levied on goods belonging to the Government.

Chapter XV is devoted to a consideration of the attitude to be adopted towards foreign capital. The economic advantages of foreign capital to the country are explained, the present feelings of opposition to it are indicated, the restrictions on its employment which have been suggested are examined, and the conclusion is drawn that in the interests of the country no obstacles should be raised to the free inflow of foreign capital. It is, however, recommended that Government monopolies or concessions should be granted only to companies registered and incorporated in India with rupee capital, having a reasonable proportion of Indian Directors and affording facilities for training Indian apprentices.

The position of Indian States is considered in Chapter XVI. It is pointed out that Indian States are closely concerned both as consumers and as producers in the tariff policy adopted for British India, but that their views on that policy coincide generally with those expressed in other parts of India, and that their interest will be fully safeguarded under the scheme of protection recommended.

The report begins and ends with a reference to the relations between India and Britain. In the first chapter stress is laid on the pronouncements of the British Government regarding the principle of fiscal autonomy for India. In the last Chapter the Commission explains that its recommendations have been based solely on the interests of India, but it also gives its reasons for holding that in this matter there is no real antagonism of interests between the two countries, and that a more prosperous India will mean a more prosperous Britain. The two most important chapters in the Report are the V. (Page 861) which deals with *Protection*, and the VIII. (Page 875) which deals with *Imperial Preference*. These are quoted in full in the following pages.

The Choice between Free Trade and Protection.**The Tariff Policy Recommended.**

55. The main subject on which we have been asked to report is the tariff policy of the Government of India. This means in effect that we have to decide whether a policy of free trade should be continued or whether industrial development, the importance of which we have explained in preceding chapter, should be stimulated by a protective tariff. We think it convenient to state at once the conclusion on this point at which after the most careful consideration we have arrived. **We recommend in the best interests of India the adoption of a policy of protection to be applied with discrimination along the lines indicated in this report.** In this chapter we shall give the reasons which have led us to recommend the adoption of a policy of protection rather than one of free trade, and in the two succeeding chapters we shall explain why we hold that the policy of protection must be applied with discrimination, and will outline the principles in accordance with which discrimination should in our opinion be applied.

Strong feeling in favour of Protection.

56. We have mentioned in Chapter I the longstanding and insistent demand of the public for a revision of the tariff policy, and in the course of our tour, during which we heard evidence at all the chief centres in India, we received abundant proof of the wide extent of that demand. Not only the industrialists, who might be expected to benefit directly from a policy of protection, but traders and other classes of the community whose immediate interests might seem likely to suffer showed themselves preponderatingly in favour of protection. The evidence which was placed before us on behalf of Indian States was also to the same effect. We found a general conviction that the interests of the country required a policy of protection, and in face of that a disinclination even to consider whether the individual would or would not be injured.

Its Causes.

57. This desire for a policy of protection has in many cases been strongly reinforced by a consideration of India's past. Travelers relate that before the advent of Europeans India was a country of great wealth. The riches of the courts of the Moghals, the beauty and quality of certain of India's manufactures, in particular of her cotton goods, and the lucrative trade that attracted western adventurers to this country, are matters of common knowledge,

These writers, however, seldom glance at the economic conditions in which the great mass of the people lived. Patriotic Indians to-day looking round on the present condition of their country see that the old fame and relative importance of India's manufactures have diminished, whilst great masses of their countrymen are still poor and many are insufficiently fed and clothed. Contrasting this state of affairs with the treasures of the Moghals and the world reputation of the Dacca muslins and other Indian manufactures, and searching for the cause of this great change, many think that it is to be found in the policy of free trade, which they believe to have been imposed on India not in her own interests, but in the interests of the British manufacturers. They see that other countries such as Japan have developed their manufactures to a remarkable degree under a system of protection, and they believe that Indians are fully capable of doing the same. They think that, if India were allowed freedom to decide her policy in her own interests, she would regain her economic prosperity. The feeling that this path to riches is barred by an outside power, and the suspicion that that outside power is actuated by selfish motives tend to stimulate the belief in the great results that would accrue from the adoption of a policy of protection. All these ideas are further reinforced by the new spirit of national pride, a spirit which in all countries tends to the encouragement of protectionist feeling by demanding so far as possible that the nation should manufacture what the nation uses.

Examples of other Countries.

58. The protectionist feeling in India to which we have referred is strengthened by a consideration of the tariff systems prevailing generally throughout the world and the relatively backward condition of Indian industries under a policy of free trade. With the exception of the United Kingdom all the great industrial nations of the world shelter their industries behind a protective wall, and claim to owe their prosperity to the tariff protection which they enjoy. The general movement in Europe towards free trade, which appeared to be setting in with the conclusion of the famous commercial treaty between England and France in 1860, lasted only for a few years, and was followed by a strong reaction, never perhaps stronger than in recent years, towards protection. In 1879 Germany definitely adopted a policy of protection, from which she has never departed, and under which she had made up to the outbreak of the war astonishing industrial progress. In 1881 France turned her back on the free trade tendencies which had never really met with popular approval. In 1899 Japan, freed

from the trammels of the treaty restrictions, utilised her autonomy to establish a protective tariff, which was considerably intensified in 1911. The United States, industrially one of the foremost countries in the world, has had ever since the time of the Civil War a very high protective tariff, and at the present moment appears to contemplate raising it still higher. The British Dominions too have without exception utilised the right of framing their tariff policies in their own interests to protect their industries by high duties.

Conditions in England

59. India can thus point to numerous precedents for the adoption of a policy of protection. Even in the case of England it may be noted that her industrial foundations, like those of all other countries, were laid under a system of high protection. The Lancashire cotton industry in its infancy was protected by an import duty which, according to the evidence of Professor Hamilton, stood for a number of years at about 65 per cent. *ad valorem*. The English textile manufactures were further protected by a legal prohibition of the use of various competing foreign cloths. It is true that the great industrial development took place as the result of the mechanical inventions which revolutionised industry at the close of the 18th century, and that the part which the tariff bore at this stage was insignificant. Nevertheless the fact remains that it was not until English industries had attained a marked pre-eminence that the tariff was felt to be a hindrance to industrial development. Moreover the movement towards free trade was largely directed, in its earlier stages at any rate, by antagonism to the protection not of industrial, but of agricultural, interests.

60. The conditions in England for three quarters of a century have been unlike those in most countries, and particularly unlike those in India. England's economic life depends on the export of manufactured articles, the raw materials for which are largely imported. The maintenance of this vital export trade is obviously likely to be fostered by a policy based on free trade principles. In India on the contrary there is an abundant supply of raw materials and a very large home market supplied in great part by foreign manufactures, whilst the export of Indian manufactures, though offering possibilities of considerable development, is comparatively small. But even in the special conditions of England doubts have been frequently raised as to the wisdom of too rigid an adherence to the free trade doctrine, and since the war departures from it have actually been made, as illustrated by (a) the duty of 33 and one-third per cent. on motor cars (which has a protective effect), (b) the Safeguarding of Industries Act, and

(c) the recent removal of the excise duty on sugar to encourage the nascent sugar beet industry.

Public sentiment considered

61. We do not wish however to rest the case for protection in India on the sentiment of the Indian people or the example of other countries. We have considered most carefully the economic arguments, and we hope to show that the policy which we advocate will stand this crucial test. But at the same time we have set forth frankly what we conceive to be the main bases of Indian protectionist feeling, because, though we do not advocate the adoption of a tariff policy on other than the reasoned grounds which follow, we feel that it is important to realise that behind our reasoned advocacy is a strong public sentiment, and that while we shall treat a question of such moment to the future of India from the strictly economic point of view, it has also a political aspect which is at least worthy of notice.

The proposition of free trade

62. In considering the issue between free trade and protection it is necessary in the first place to examine the theoretical basis of the subject and to set forth what we understand to be the principles which are generally accepted by modern economic authorities on these difficult questions. The old free trade doctrine of the classical economists may be said to have rested on two propositions. It was assumed, firstly, that the capital and labour of a country, if left unfettered by any kind of Government regulation or restriction, would naturally be applied to those industries which would yield the greatest economic return. The capital and labour of a country both being limited in quantity, it is evidently of the utmost importance that they should be applied in the manner which will yield the best economic results, and it was held that the free interplay of economic forces would best determine the direction of the capital and labour of a country into those industries in which it has a comparative advantage over other countries. The second proposition was that the best economic results, both for the world as a whole and for individual countries, would be obtained by each country applying its capital and labour to those industries in which it had the greatest comparative advantage, and then exchanging the products of those industries for articles which it was not able to produce so cheaply itself. This is the principle of the international division of labour.

Their qualifications

63. Both these propositions have a *prima facie* validity which is not seriously contested. But they state only tendencies, and

tendencies may be over-ridden by special circumstances. We are thus led to an examination of the generally recognised qualifications of these propositions.

64. In the first place there may clearly be cases in which the free interplay of economic forces will not secure the best utilisation of the capital and labour resources of a country. In the competitive struggle an initial advantage may prove to be a permanent advantage. A fully developed industry in one country may be able under conditions of unfettered competition to hinder the development of the same industry in another country possessing equal or even greater natural advantages. In these circumstances the latter country may never, or only after long delay, succeed in applying its labour and capital to the best advantage of which they are capable, owing to the initial difficulties in making a start. These considerations were stated many years ago with admirable lucidity by John Stuart Mill, who wrote, "The superiority of one country over another in a branch of production often arises only from having begun it sooner. There may be no inherent advantage on one part or disadvantage on the other, but only a present superiority of acquired skill and experience. A country which has this skill and experience yet to acquire may in other respects be better adapted to the production than those which were earlier in the field."

65. The argument as stated above applies primarily to particular industries which are handicapped at the start by the competition of fully developed rivals, and could be used irrespective of the stage of industrial development attained by the country in which the new industry, finds itself. But the argument has been applied with special force to industrially new countries in competition with those in which industries have long been established. The classical expression of this argument is to be found in the works of List, whose economic theories have exercised such a profound influence on the policy of the great protectionist countries. It is summed up by a modern English economist, Professor Pigou, who, in dealing with List's arguments, writes as follows :—

"The main element of productive power, whose development involves a long process, is a population trained in the general atmosphere of industrial pursuits. If a country is entirely agricultural and has no important class of artisans or factory workers, the skill required for starting any particular kind of mill will be very difficult to get. Masters, foremen and workmen must first be either trained up at home or procured from abroad, and the profitableness of the business has not been sufficiently tested to give capitalists confidence in its success." For a long time, therefore, it is improbable that any work

* List's "National System of Political Economy."

which may be started will be able to compete on equal terms with established foreign rivals—and that in spite of the fact that the industry in question may be one for which the country has great natural advantages. On the other hand, in a country which is already largely industrial, the initial difficulty involved in starting a new industry is likely to be much slighter. For much less time is required to obtain from among a people already accustomed to many varieties of factory work, hands capable of carrying on a new variety of it. Further, in an industrial community, those other important elements of productive power, organised systems of transport and of credit, which, in an agricultural country, may need themselves to be built up before manufactures can be profitably established, are presumably already in existence."

66. The *prima facie* advantages too of the international division of labour are subject to certain qualifications. It may be that in some circumstances the greatest amount of wealth would be secured by a degree of specialisation which could not be regarded as conducing to the general interests of the country. In other words there are objects of state policy different from, and more important than, the mere acquisition of wealth. A country might produce the greatest amount of wealth by devoting itself wholly to agriculture, and yet such a one-sided development, in virtue of its effect on the national character and institutions, might not be in the wider interests of the country as a whole. Similarly, considerations of national defence may set legitimate bounds to the extension of the principle of international division of labour.

Circumstances in which protection is justifiable

67. So far we have indicated what we take to be the circumstances in which economic theory might justify departures from the principle of free exchange of commodities between nations. It is admitted that in all such cases restrictions on free exchange involve some immediate economic loss. We turn once more to the economists for their verdict as to the circumstances in which such loss may justifiably be incurred. In the passage already referred to John Stuart Mill says, "The only case in which, on mere principles of political economy, protecting duties can be defensible, is when they are imposed temporarily (especially in a young and rising nation) in hopes of naturalising a foreign industry, in itself perfectly suitable to the circumstances of the country. A protecting duty, continued for a reasonable time, will sometimes be the least inconvenient mode in which the nation can tax itself for the support of such an experiment." List expresses himself more emphatically, "The nation must sacrifice and give up a measure of material prosperity in order to gain culture, skill and powers of united production; it must sacrifice some present advantages in order to insure to itself future ones." There is one idea common to both writers—a

present loss for a future gain. The gain we have already indicated. We now turn to consider what constitutes the loss.

The Burden of protection arising from increased prices

68. The burden of protection arises from the increase in prices. It is obvious that an import duty tends to raise the price not only of the imported article, but also of the competing locally produced article. Cases are analysed by the economists in which for special reasons or for temporary periods the normal result does not follow, or follows only partially. But, broadly speaking, there is no dispute as to the tendency of import duties to raise the prices of the articles taxed. Further, when import duties are placed on a wide range of articles, there is a tendency for the general level of prices in the country to be raised; the rise is not confined to the particular articles taxed. For this phenomenon there are various causes. In the first place the import duties tend to check the volume of imports, with the result that a favourable balance of trade is created. This favourable balance is settled mainly by the import of the precious metals, and so far as these find their way into the currency, thereby increasing its amount, the general level of prices tends to rise. In India this argument must be applied with caution, for the precious metals when imported are largely used for other purposes, and comparatively small quantities are likely to go to swell the volume of the currency. A less theoretical argument is that the increased cost caused by import duties enters generally into the cost of production of all articles manufactured in the country and into the cost of transportation. Duties on cotton cloth or on sugar, for instance, may raise the expenditure of the employees of an industry; to meet such increased expenditure higher wages are required; higher wages mean higher cost of production, and this in turn means that the product requires to be sold at a higher price. Instances might easily be multiplied. It may, we think, be taken as the view accepted by economists that a general increase in import duties tends to produce a general rise in prices in a country, and not merely a rise in the price of imported articles and such locally produced articles as directly compete with them.

Gradual diminution of the burden.

69. It is not our intention to suggest that the burden on the consumer arising from protective duties is necessarily permanent. On the contrary, if the industries to be protected are selected with due discrimination, the burden should gradually diminish and eventually cease altogether. But the process of diminution is not likely to be rapid, or to commence immediately. So long as foreign imports continue to enter in appreciable quantities, the price of the

goods must in general be regulated by the price of the foreign imports; that is to say, the consumer will be paying the full foreign price *plus* the import duty. As the home industry develops in efficiency and reduces its cost of production, there will be at first no reduction in prices, but the decrease in the cost of production will merely go to swell the profits of the home industry. This will lead to the more rapid development of the home industry and will hasten the time when it is able to supply the home market almost in full. As foreign imports dwindle to small proportions, prices will become regulated more and more by internal competition, and the consumer will then begin to derive the benefit from the increased efficiency of the local industry, and may in the end obtain the goods as cheaply as if he were free to import them without a duty. If the industry is one for which the country possesses marked natural advantages, he may even obtain them more cheaply.

70. We have indicated both the present loss and the future gain which a policy of protection might in general be expected to bring. We now come to the practical problem, which is to determine whether the circumstances of India are such that a stimulation of her industrial development by means of protective duties will bring in the end a gain to the country as a whole greater than the immediate loss.

71. In Chapter IV we have stated our opinion that the industrial development of India has not been commensurate with the size of the country, its population and its natural resources. In considering how these conditions can best be remedied it is necessary to attempt to diagnose the causes from which they have arisen. The Industrial Commission mentioned various factors as having operated to retard industrial development, for instance, the natural conservatism of the people, the inefficiency of labour, the absence of industrial and technical education, the lack of business enterprise, the shyness of capital for new undertakings, and the want of proper organization for utilising such capital as is available.

Industrial aptitude in the past

72. Some of these factors might suggest the idea that Indians were lacking in certain qualities necessary for success in industrial pursuits, and that therefore one of the foundations for a profitable application of protection, namely a people fitted to make good use of it, was absent. We do not think that this idea is supported by past experience. If we take history as a guide to the future, we see that there have been times when the manufacturers of the country attained a high degree of excellence and were well-known beyond its borders. As the Industrial Commission explained, India was at one time famous "for the high artistic skill of her

craftsmen," and it was not until the industrial revolution of the 18th century that she began to fall behind in the industrial sphere and that in the words of the Industrial Commission "the erroneous idea that tropical countries, with their naturally fertile lands and trying climate, were suited to the production of raw materials rather than to manufactures" developed. The cotton manufactures of India which were exported in large quantities throughout Asia and Europe, the skill in shipbuilding which was at one time freely utilised by the East India Company, the working of iron which in the old days had been brought to a considerable pitch of excellence, the manufacture of steel sword blades commanding a great reputation in foreign countries, the exports of silk textiles and sugar, all prove that Indians exhibited a natural aptitude for industrial work, and that the present relative backwardness in this respect should not be regarded as indicating any obstacle to a wide development of industries in the future.

Differences in natural aptitude diminishing

73. Further, the unevenness of development to which the Industrial Commission drew attention appears to be due in part to a striking difference in natural aptitude for industries, which can be traced in different communities in India. For centuries the people of Western India have shown a marked instinct for commerce : and from commerce they have moved naturally to industries, so that at the present time they divide with the European community the industrial leadership of India. But the people of Bengal, Madras and Burma have in general neglected industrial pursuits, and if industries have established themselves within their borders, have left their development to others. It would take us beyond our province to attempt to trace these tendencies to their origin, whether it may be found in a fertile soil providing a livelihood in return for little labour, or in a social system which exalts the less material side of life, in economic conditions which produce a class of middlemen living parasitically on the profits of the land, or in historical traditions which attract the most enterprising classes to administration. Whatever the causes of this neglect in the past, we feel that in many parts of the country a change has come over the spirit of the people, and that what is lacking now is more often the opportunity than the will. We think, therefore, that so far as the comparatively slow development of industries in India has been due to lack of natural aptitude or interest, this factor will become progressively of less importance, and that a time has come when India is prepared to take advantage of any stimulus applied to her industries.

Industrial development requires to be stimulated by protective duties

74. The question which we have to determine is whether the industrial development at which we aim can be attained without the stimulus of protective duties, and if not, whether the advantage to the country arising from this industrial development will outweigh the burden which protective duties will impose. The Industrial Commission, which was debarred from considering questions of tariff policy, made a number of important recommendations for the development of Indian industries, involving the abandonment of a *laissez faire* policy. But we hold that these measures by themselves will not produce that marked impetus for which the time and conditions are now ripe. Education can be improved, banking facilities can be extended, technical assistance can be offered to industries, but what is mainly wanted is a policy that will inspire confidence and encourage enterprise, and we do not think that the recommendations of the Industrial Commission provide this. Professor Pigou at the close of the passage which we have already quoted draws the following weighty conclusion: "From these considerations it follows that the case for Protection with a view to building up productive power is strong in any agricultural country which seems to possess natural advantages for manufacturing. In such a country the immediate loss arising from the check to the exchange of native produce for foreign manufactures may well be outweighed by the gain from the greater rapidity with which the home manufacturing power is developed. The 'crutches to teach the new manufactures to walk' as Colbert called protective duties, may teach them this so much earlier than they would have learnt it, if left to themselves, that the cost of the crutches is more than repaid." The words might almost have been written with direct reference to the conditions of India, and the case for protection in India can hardly be stated better. India is an agricultural country which possesses undoubted natural advantages for manufacturing. She produces an abundance of raw materials, she has an ample potential supply of cheap labour and adequate sources of power; and the establishment of two great manufacturing industries shows that she is capable of turning these natural advantages to use. We have been told by many witnesses that the chief obstacle to a more rapid development of industries in India is a certain want of confidence among the owners of capital. The practical protection afforded by the war had a stimulating effect on many Indian industries. But this protection, and such incidental protection as is yielded by high revenue duties, lacks the assurance of permanence, and fails to give the sense of security which arises from the

deliberate adoption of a policy of protection. This point of view was perhaps expressed most clearly by Mr. Shakespear giving evidence on behalf of the Indian Sugar Producers' Association. He said, "My personal view is that it is the principle of the thing which we, as an industry, would like to see far more than an actual duty of 15, 20 or 25 per cent. If the principle of protecting the industry is accepted, that is what is going to be of value to us in developing the industry." Again Captain E. V. Sassoon, one of the leading Bombay industrialists, after stating that Indian capital was "shy of anything new in the way of industrial enterprise" said, "what is wanted is confidence, and a policy of protection would help to secure that at once."

75. We have now shown that India will derive very great advantages from industrial development, that the conditions for a rapid advance are suitable, and that without the stimulus of protective duties the advance will not be sufficiently rapid. All these considerations lead us to the conclusion that protection will bring a very material gain to the country.

Necessity of deriving a high revenue tariff

76. A further consideration pointing to the same conclusion will be found in the present tariff position in India. We have referred in Chapter II to the increasing proportion which customs revenue bears to the total Imperial revenue, and we have now to consider whether this tendency is likely to be permanent. We received a considerable amount of evidence regarding the respective merits of direct and indirect taxation. We do not propose to recapitulate the well-worn arguments of the economists on this subject, but we are bound to take note of the fact that the general sentiment of Indian witnesses was strongly opposed to direct taxation, and that the collection of income-tax in India presents peculiar difficulties. Direct taxes in India are confined practically to income-tax and land revenue. With the latter, which is a provincial receipt, we are not concerned. The income-tax rates have been raised largely since 1915-16, and the yield has risen from 3 to 20 crores of rupees. High taxes on income are undoubtedly a handicap to industrial development, and there are many who hold that the rates ruling at the present moment are distinctly too high for the interests of industries and the general prosperity of the country. The witnesses whom we examined on this point were almost unanimous in the opinion that direct taxation has reached its limit under present conditions, and in view of the general feeling in the country we do not think that any material increase in this form of taxation is feasible. If, therefore, any further

increase in taxation becomes necessary, it will have to take the form of indirect taxation. If, on the other hand, a decrease in taxation became possible, we think that it should take the form of a *puri passu* reduction in direct and indirect taxation. In view of these conclusions we cannot anticipate for many years to come any appreciable reduction in the revenue which it is necessary to derive from the customs. This means that import duties must continue high, and that, whether intended or not, protection will be given.

77. But a high revenue tariff such as that now in force in India is open to great objection. A revenue tariff based on free trade principles is one that is imposed on goods that cannot be produced in the country ; or, if this condition cannot be observed, it must be kept at a very low rate on goods produced in the country, or countervailing excises must be imposed, so that no protection is afforded to local industries. Until the year 1916 the Indian tariff might be said to have fulfilled these conditions. But since 1916 the tariff has become less and less consistent with purely free trade principles. It gives protection, but it gives it in the least convenient and the least beneficial way. The protection is not calculated on the needs of the industry, nor does it carry any assurance of a permanent policy. It is casual and haphazard. Moreover, it may actually impede the industrial development by taxing raw materials and semi-manufactured articles. It appears to us therefore that the necessity for raising a large revenue from customs duties and the obvious inexpediency of ignoring the effect of those duties on the industries of the country must inevitably lead India to the adoption of a policy of protection, as they led Germany in 1879.

The loss protection will involve.

78. We turn now to the loss that must be set against the gain to India from protection to which we have referred in paragraph 75. The most important item is the burden of increased prices that protective duties will impose on the people. We have explained the nature of these burden in paragraph 68 above, and we proceed to consider whether it will be so great as to outweigh the advantages which we anticipate from the adoption of a protective policy.

79. As import duties have a tendency in some degree to extend their influence beyond the particular commodities on which they are imposed, it is necessary to treat with caution the argument that some article is not consumed by the poorer classes and that therefore a protective duty on it can do them no harm. A further limitation of this argument is to be found in the fact that there are frequently partial substitutes for imported articles, which are manufactured and consumed locally, and that any cause which

raises the price of the imported article raises the price also of the locally produced substitutes. An obvious instance of such a case is seen in cotton cloth. Experience, as well as theoretical reasoning, shows that the price of Indian manufactured cloth is influenced by the price of imported cloth, even when the two classes are not in direct competition. In estimating therefore the extent to which the poorer classes will be affected by protection, it is not safe merely to ask what proportion of their income is spent on imported goods. We have received various estimates on this point, and all agree that the actual quantity of imported goods purchased by the masses of India is small. But this is no final criterion of the degree to which protection will affect them, though there is no reason to suppose that, under the system we recommend, the indirect burden will be considerable.

Effect of Protection. —(1) On the Agricultural classes.

80. There are however two classes of the population whose interests as affected by protection it is particularly important to consider, the agricultural and middle classes. Agriculture is, and must remain, the foundation of the economic life of India, and this not merely because it furnishes the livelihood of three-quarters of the population. Indian industries cannot flourish without a prosperous Indian agriculture. Agriculture is largely the provider of the raw materials for industry, and the Indian agriculturist will offer the main market for the products of Indian industries. Any form of protection therefore which would seriously affect the interests of agriculture would go far to defeat its own object. We have already explained in what ways we think that industrial development may be of advantage to the agricultural community, in some cases through a sympathetic rise in wages, in others through the wages of industrial workers being made available for expenditure in the villages, in others through a reduction in the number dependent on the produce of the land. But while a policy of protection of industries may not injure the agricultural wage earner, who may be able to secure a rise in wages equal to, and in some cases greater than, the rise in the cost of living, there can be little doubt that the agricultural producer, the man who either works the land himself or employs hired labour, must suffer to some extent. Protection must mean to him a higher cost of production, arising partly from the higher cost of the implement that he uses, partly from the higher wages that he will have to pay and partly from the general rise in the cost of living. As a set off against this higher cost of production it is probable that in the neighbourhood of industrial centres the demand for agricultural produce will raise the price. But, in general, one of two results seems

likely to follow. Either the agricultural producer, will not receive for his produce an increased price which will fully compensate him for the increased cost of production, in which case agricultural interests would suffer and there would be a tendency for marginal land to go out of cultivation ; or the price of agricultural produce will be raised generally to cover the increased cost of production with injurious effects on the mass of the population. Provided however protection is applied with discrimination, we do not think that the burden imposed, either on the agricultural producer or, through a rise in the prices of agricultural produce, on the consumer in general, need be sufficient to make us hesitate regarding the net advantages of the policy we recommend.

(II) on the middle classes

81. With regard to the middle classes, by which we mean mainly the professional, clerical and petty trading classes, there is no doubt that they will be more adversely affected than any others by a policy of protection. The middle classes have a certain standard of living which entails expenditure on imported goods. Their cost of living will undoubtedly rise. The possibilities of equivalent, or at any rate timely, expansion in their incomes, however, are limited. It is probable therefore that for some period they will feel the effects of protection more than any other class of the population. But in virtue of their education they, more than other classes, are in a position to estimate the value to the country as a whole of the developments which we believe our policy will produce, and so far as we have been able to judge from those witnesses who have given evidence before us, the middle classes are prepared to merge what might be regarded as their own immediate interests in the wider interests of the country.

82. In estimating the burden of protection we have to anticipate the arguments given in the next chapter, in which we show that any type of indiscriminate protection would entail a sacrifice out of proportion to the results. We explain in that chapter the limitations that we propose with a view to restricting the immediate loss as far as possible without reducing the gain that is to be anticipated from protection. If those limitations are observed, we consider that the burden will be one which it is reasonable to ask the country to bear in order to secure the great benefits anticipated.

83. Before coming to our final conclusion we must refer to certain disadvantages which are inherent in any system of protection, namely, the risk of encouraging inefficient methods of production, the danger of political corruption and the possibility of combinations of manufacturers. We have borne these points in mind in formulating our scheme of protection and in devising the

constitution of the Tariff Board. We explain in detail in Chapter VI to what extent we think these dangers will be mitigated by our proposals, and it is enough to say here that we do not consider them sufficiently serious to affect our main conclusion.

The balance of advantage

84. We have now set forth, as impartially as possible, the arguments for and against the adoption of a policy of protection in India. In Chapter IV we have shown the great benefits that will accrue to India from industrial development, and in the present chapter we have explained the necessity of the stimulus of protection to secure rapid progress in this direction. We have also shown that the necessity of a high customs revenue is inevitably leading India towards protection. On the other side we have shown that the immediate loss to be apprehended from protection, and the dangers inherent in it, will be mitigated by the system of discrimination which we recommend and by the constant supervision of our proposed Tariff Board. We have carefully considered the weight of the arguments on both sides, and apart from the strong Indian sentiment in favour of protection, to which we have referred above, we are satisfied, on economic grounds, that the temporary loss involved will be more than made good by the ultimate gain, and that the balance of advantage is heavily on the side of the recommendation made in the opening paragraph of this chapter *viz.*, the adoption of a policy of protection to be applied with discrimination along the lines indicated in this report.

Imperial Preference

(1) History and Meaning

214. The question of Imperial Preference in the British Empire first took practical shape in 1897, when Canada, partly in pursuance of a more liberal tariff policy, reduced her duties on British goods. Owing to the existence of certain commercial treaties the benefits intended for Great Britain had to be conferred temporarily on some other countries, but the hampering treaties were denounced in 1898, and from that time the preference, which was fixed at one-fourth of the duty, was confined to the United Kingdom and such British colonies as gave Canada favourable treatment. In 1900 the preference was raised to one-third.

215. The subject of Imperial Preference came before the Colonial Conference of 1902, and on this occasion the principle was for the first time authoritatively recognised as one of general application. The resolution passed by the Conference was as follows :—

"1. That this Conference recognises that the principle of preferential trade between the United Kingdom and His Majesty's Dominions beyond the seas would stimulate and facilitate mutual commercial intercourse, and would, by promoting the development of the resources and industries of the several parts, strengthen the Empire.

"2. That this Conference recognises that, in the present circumstances of the Colonies, it is not practicable to adopt a general system of free trade as between the mother country and the British Dominions beyond the seas.

"3. That with a view, however, to promoting the increase of trade within the Empire, it is desirable that those Colonies which have not already adopted such a policy should, as far as their circumstances permit, give substantial preferential treatment to the products and manufactures of the United Kingdom.

"4. That the Prime Minister of the Colonies respectfully urge on His Majesty's Government the expediency of granting in the United Kingdom preferential treatment to the products and manufactures of the Colonies either by exemption from or reduction of duties now or hereafter imposed.

"5. That the Prime Ministers present at the Conference undertake to submit to their respective Governments at the earliest opportunity the principle of the resolution, and to request them to take such measures as may be necessary to give effect to it."

The principles of Imperial preference

216. The points of chief importance which emerge from this resolution are :—

(1) That the stimulation of commercial intercourse between the different parts of the Empire was in the interests of the Empire ;

(2) that the policy of preference would develop the resources of the several parts of the Empire and thus strengthen the whole ;

(3) that there was no question of the Dominions abating their protectionist policy, and no idea of establishing free trade within the Empire ;

(4) that the preference given should be wholly voluntary, and should not go beyond what the circumstances of each unit might reasonably permit ;

(5) that the United Kingdom should, if possible, grant certain preferences in return.

Its extension

217. In pursuance of this resolution preferential duties were introduced by New Zealand and South Africa in 1903 and by Australia in 1907, but the United Kingdom decisively rejected the policy of taxation of food, through which alone any effective response could have been made to the preferences granted by the Dominions. At the Colonial Conference of 1907 the question was once more raised prominently. The representatives of the Dominions showed the importance they attached to the development of the system and to some response on the part of the United Kingdom, but the British Government explained without disguise that in their opinion the circumstances of the United Kingdom made this impossible. The resolutions of 1902 were reaffirmed with a reservation by the British Government that they could not assent that it was necessary or expedient to alter the fiscal system of the United Kingdom.

The Position of India in relation to Imperial Preference.

218. In the meantime the Government of India had been consulted in 1903 on the question of Imperial Preference from the standpoint of the interests of India. After reviewing the position of India, the nature of her trade and tariff, and her commercial relations with the Empire and other countries, their general conclusion was that from an economic standpoint India had something, but not perhaps very much, to offer to the Empire, that she had very little to gain in return, and that she had a great deal to lose or to risk.

219. Up to the time of the war therefore the position was that the self-governing Dominions all gave preferences at such rates as they considered advisable to certain products of the United Kingdom, and in some cases to the products of other parts of the Empire; that India and the majority of the Crown Colonies had not adopted the principle; and that the British Government had definitely stated that it did not see its way to grant preference in the United Kingdom. The preferences granted by the Dominions were intended primarily for the benefit of the United Kingdom, but New Zealand extended her concessions to the whole Empire, and Canada has voluntarily granted her preferences to New Zealand, India and most of the Crown Colonies. Canada has also entered into special agreements with the West Indies. Australia and South Africa adopted the principle of confining their preferences primarily to the United Kingdom and only extending them to other parts of the Empire as the result of negotiations. South Africa has negotiated agreements with Canada, New Zealand and Australia. Australia has made an agreement only with South Africa, but it is stated that negotiations for an agreement with New Zealand are at present in progress. In Canada, Australia and New Zealand the preferential duties are usually about two-thirds of the full duty, though the fraction varies considerably both above and below this figure. The South African preference is a small one and is usually only a rebate of 3 per cent. *ad valorem*. In a number of cases when the general duty is only 3 per cent British goods are admitted free, and in the other Dominions in the same way British goods are sometimes admitted free, when the general duty is at a low rate. It must be remembered that in no case do the Dominions allow these preferences to interfere with the degree of protection which they consider necessary for their own industries.

The effects of the War.

220. The war gave a great impetus to the policy of consolidating the Empire, and in the light of the ideas engendered by the war the

question of Imperial Preference began to be re-examined. The Economic Conference at Paris in 1916 passed a resolution recommending the Allies to take the necessary steps without delay to render themselves independent of the enemy countries as regards the raw materials and manufactured articles essential to the development of their economic activities. This resolution raised the whole question of the organization of the Empire as an independent economic unit, and it was proposed to convene a conference of the Dominions and India to consider the commercial policy to be adopted after the war. Ideas at this time were perhaps coloured unduly by war conditions, and more stress seems to have been laid on the desirability of making the Empire self-contained in the matter of food supplies, raw materials and manufactures, and evolving a unified policy, than on the mere development of the interchange of products between the various parts.

Further preferences. The United Kingdom adopts the policy

221. The projected conference was never held in the form which was apparently contemplated. But the Imperial War Conference, 1917, passed the following resolution:—

"The time has arrived when all possible encouragement should be given to the development of Imperial resources, and especially to making the Empire independent of other countries in respect of food supplies, raw materials, and essential industries. With these objects in view this Conference expresses itself in favour of:—

(1) The principle that each part of the Empire, having due regard to the interests of our Allies, shall give specially favourable treatment and facilities to the produce and manufactures of other parts of the Empire.

(2) Arrangements by which intending emigrants from the United Kingdom may be induced to settle in countries under the British flag "

222. The movement towards a strengthening of the links of Empire found expression in independent action taken by many of the members. The most important event was the adoption by the United Kingdom in 1919 of the policy of preference, thus reversing the attitude taken in 1907. It had always been recognised that preferences given by the United Kingdom, unless accompanied by considerable departures in fiscal policy would not have any great practical effect. But in 1919 the United Kingdom without altering its general tariff policy granted to the whole Empire preferential rates, which were usually five-sixths or two-thirds of the full rate, on nearly all articles on which import duties were levied. At the same time many of the Crown Colonies took up the question of Imperial Preference, some of them have already introduced preferential rates, while it is believed that others have them under consideration. Australia and New Zealand have also within the last two years revised and increased their preferences.

223. It was not possible for India to ignore a general movement of this nature, and from 1917 onwards the question of Imperial Preference has in one form or another been before the Government of India. We have already explained how the resolution moved by Sir George Barnes in February 1920 in the Imperial Legislative Council for the appointment of a committee to report "whether or not it is advisable to apply to the Indian Customs Tariff a system of preference in favour of goods of Empire origin," led directly to the enquiry which we have been conducting.

(ii) Economic Principles

224. As a preliminary to considering the adoption of a policy of Imperial Preference by India it is important to obtain a clear idea of the economic effects of preferential duties. Preference means that goods from one or more favoured countries pay duty at a rate lower than the general rate. Whether the preferential rate is a real reduction in duty or whether the general rate has been arrived at by making an addition to what is considered the minimum duty, which thus becomes the preferential rate, is, in considering the economic effect, immaterial. For our present purpose the preference may be treated as a reduction of duty in comparison with the rate imposed on foreign countries in general. The effect of such a reduction is clearly expressed in the following passage from the Report on Reciprocity and Commercial Treaties prepared by the United States Tariff Commission in 1918 :—

"As regards economic effect, reductions of duty under the concessional method have different consequences under varying conditions of supply as regards the article affected. Where a reduction of duty affects only a fraction of the imports of a particular article, and the major portion of the imports of that article is still left subject to the main, or non-concessional duty, the result is not only a loss of revenue to the Treasury, because of the lower rates of duty, but absence of any gain to consumers. The reduction of duty redounds only to the advantage of the foreign producer. This situation was exemplified by our experience with Hawaii, as detailed in this report, under the reciprocity treaty of 1875. That experience was not indeed part of a general concessional policy; but it, nevertheless, supplies an example of the working of a limited concession. If, on the other hand, virtually the entire imported supply of a given article is admitted at the lowered concessional rates, the effect is that of a general reduction of duty. Such a result ensued, at least in the more recent years of the operation of the reciprocity treaty with Cuba, as a consequence of our concession of a reduced duty upon Cuban sugar. As shown in the discussion of Cuban relations, this concession resulted in a gain to the Cuban sugar producer during the first years after the reciprocity arrangement went into effect, but had come to redound, during the years immediately preceding the European war, mainly to the advantage of the domestic consumer."

Effect depends on the relative importance of the sources of supply

225. We take it that this passage expresses accurately the

economic effect of a preferential duty. So long as a substantial quantity of the commodity continues to be imported from countries to which the preferential rate is not extended, the price of the commodity will be regulated by the higher duty. The consumer will thus pay the higher price on the whole supply, and the differences between the two rates of duty will be equivalent to a bounty to the manufacturer in the country receiving the preference. When on the other hand the country receiving the preference supplies practically the whole market, then the price to the consumer will be regulated by the lower rate. The bounty to the foreign manufacturer will cease, and the consumer will get the benefit of the lower rate. The question therefore whether the consumer is or is not penalised for the benefit of the foreign manufacturer depends on the relative importance of the sources of supply. If the portion of the market supplied by the favoured country is large, the burden on the consumer will be small, or possibly there will be no burden at all. So long, however, as the supply from the favoured country is small relative to the total supply, the consumer will suffer.

226. It may be thought that, unless the consumer suffers, the foreign manufacturer cannot benefit; that is to say, unless the foreign manufacturer is able to annex for himself some of the difference between the two rates of duty, he will not be receiving any benefit. This however is not a fair statement of the case. To take an illustration, we may assume that the favoured country is, before the grant of preference, supplying three-quarters of the market. After the preference is given, the price to the consumer for a time may be regulated by the higher rate of duty, and the manufacturers of the favoured country will receive, as has been already explained, a bonus of the difference between the two rates. The effect of this bonus is to stimulate the trade of the manufacturers of the country receiving the preference, and in a short time they may secure for themselves the whole market, driving out altogether the non-preferred manufacturers. The price to the consumer will then be regulated by the lower or preferential rate of duty, and the favoured manufacturers will find that the price falls to the true competitive level. But they have not thereby lost the whole benefit of the preference. Their gain is represented by the additional quarter of the market which they have secured for themselves at the expense of their non-preferred rivals. Thus they benefit even when the consumer has ceased to suffer.

227. It will be apparent from the considerations stated above that the arguments in favour of preferential duties are very similar

to those in favour of protective duties. In both cases the consumer is invited to suffer a temporary loss. In both cases he is given the hope that when the policy succeeds the loss will terminate. In the one case, however, the advantage for which he is invited to suffer his temporary loss will accrue to the industries of his own country ; whereas in the case of preference it will accrue to the industries of the country to which preference is given.

228. The analogy may be traced further. It is an essential part of the scheme of protection which we have advocated that protection should be given only to such industries as may be regarded as possessing a comparative advantage, and which are therefore likely with the aid of the protection given to be able eventually to supply the needs of the country as cheaply as foreign industries. The same principle should be applied in the grant of preference. If a preference is given to an inefficient industry or to an industry which with the preference is not likely to be able to supply eventually the whole market, the preference will constitute a permanent burden on the consumer, and will therefore from an economic point of view be unjustifiable.

The revenue aspect

229. The economic effect of a preferential duty has two aspects. Hitherto we have been considering the duty merely as it affects the consumer. But the duty may also affect the Government revenue. If the preferential rate is a true reduction from the general rate, it is clear that the country granting the preferential rate is sacrificing revenue. As we have indicated above, however, preferential rates are frequently not real reductions. Preference often takes the form of raising the duties against the non-favoured countries instead of lowering them for the benefit of the favoured countries. In such cases it may be argued that the State sacrifices no revenue. Indeed it may receive in view of the higher rates imposed on the non-favoured countries a slightly higher revenue. But for the true economic effect we have to look below the surface. The best tax from the economic point of view is that which brings to the public exchequer all the money extracted from the pocket of the tax-payer. An import duty operates to raise the price of the whole of the commodity sold in the country, whether imported or produced locally. Consequently the best economic import duty is one imposed on a commodity none of which is produced within the country. In this case the whole extra price paid by the consumer is levied in the form of import duty and reaches the public exchequer. The smaller the amount imported as compared with the amount produced locally, the smaller is the revenue in proportion to the tax on the consumer. It is to meet these conditions that those

countries which regulate their tariffs purely for purposes of revenue impose excise duties on the home production of goods on which import duties are imposed. Exactly the same considerations arise in the case of preferential duties. We may for purposes of this argument concentrate our attention solely on the goods imported, and may ignore the home production, if any. It is clear that if a single rate of duty is imposed, the State will secure as revenue the whole amount paid by the consumer. But if two rates are imposed and the consumer pays a price based on the higher of these two rates, the State does not secure as revenue the full amount taken from the pocket of the consumer. The tax therefore to this extent is not sound economically, and this unsound economic effect may be represented by saying that the Government loses revenue—not possibly actual revenue, but relative to the amount which it should receive in virtue of the burden which it is placing on the consumer.

230. A preferential duty, when it takes the form of raising the rate against non-preferred countries, may sometimes receive the support of the home industry because it increases the protection which that industry enjoys. But this is by no means a sound argument for granting such preference. It must be assumed under our scheme that the industry is already enjoying the protection which it needs. If, then, this protection is increased by means of a preferential duty, the result merely is that the consumer is being penalised to an unreasonable and unnecessary extent, and that the industry is receiving a larger measure of protection than it requires.

231. There is one indirect effect of preferential treatment which is perhaps worth mention. The effect of preference will be to stimulate imports from the country which receives favourable treatment. If the preferences are important, this will tend to build up direct shipping connections between the two countries, and as a consequence will give the exporters of the country granting the preference some advantage in market of the country receiving the preference. In other words, if imports are attracted from a particular country, there will be a tendency for exports to be attracted to that country. Thus to some extent it may be the case that the grant of a preference may bring some indirect compensating advantage to the country which grants it, provided its exports are competing with the exports of other countries in the market of the country to which the preference is granted.

(iii) The economic limitations of preference in India

232. We have explained in general what we conceive to be the normal economic effects of preferential duties, both on the producer in the country receiving the preference, and on the consumer in the

country giving it. We now have to consider the probable results of a policy of preference in India, in view of the special features of her economic position. This aspect of the question was examined with great care by the Government of Lord Curzon, and their conclusions were stated in their despatch to the Secretary of State, dated the 22nd October 1903. In its general features the analysis of the situation then made holds good. The Government of India in 1903 found that about three-fourths of the total imports into India came from the British Empire. Indian exports on the other hand went preponderately to foreign countries. The situation still is in broad outline the same, though such change as has taken place has been to the disadvantage of the British Empire. The figures given in Appendix D show that the imports from the British Empire, which were estimated at about 75 per cent in 1903, averaged in the five years immediately preceding the war only 69·8 per cent, and in 1921-22 stood at 66·6 per cent. The percentage of India's exports going to the British Empire has followed a similar course of gradual diminution. In 1903 approximately 47 per cent of Indian exports went to the British Empire, including exports to Hongkong and the Straits Settlements, which were, however, destined very largely for China and Japan. The corresponding figures for the years preceding the war show a percentage of 41·9, and in 1920-21 of 43, which in 1921-22 fell abruptly to 37·3. Turning to exports from India to the United Kingdom, these represented in 1903 about 25 per cent of the total exports, in the five years preceding the war the average percentage was the same, in 1920-21 it stood at 21·9 per cent, and in 1921-22 it had fallen to 19·7. Conditions have not completely readjusted themselves after the war, but the figures seem to indicate, for exports as for imports, some degree of relative decline of the importance of the British Empire in the trade of India. The present position is that India receives about two-thirds of her total imports from the British Empire, and sends to the British empire, after deducting exports to Hongkong and the Straits Settlements which are destined for China and Japan, something over one-third of her exports.

Indian exports not of a kind to benefit appreciably from preference

233. We have shown in Chapter III that between 70 and 80 per cent. of the imports into India come under the class of articles wholly or mainly manufactured. On the other hand the exports of manufactures from India amount to only some 30 per cent of the total exports, the remainder consisting to the extent of 40 to 50 per cent of raw materials, and the balance of articles classified under the head of "food, drink and tobacco." Broadly speaking, therefore, India may be said to import manufactures and to export

raw materials and foodstuffs. This fact is of great significance in considering the probable results of a system of preference. The economic advantage derived from a preference tends to be more important in the case of manufactured goods than in the case of raw materials. Manufactures nearly always meet with keen competition in foreign markets, and therefore a preference on manufactures is nearly always of value. The position in regard to raw materials is different. In the first place they are usually admitted free into foreign markets, so that the possibility of a preference does not arise; in the second place it is an obvious fact that to a large extent they find their markets ready made, whereas the market for manufactures has to be developed and carefully nursed. With a comparatively small degree of competition to meet, it is clear that raw materials stand very much less in need of preference than do manufactures, and that the gain to them by preference is likely to be correspondingly smaller. With regard to foodstuffs the general tendency in most countries is to admit them free, and the possibilities of preference are limited.

Indian exports receiving preference in the United Kingdom

234. These general considerations are corroborated by an examination of Indian exports and the possible advantage they could derive from a system of preference. Lord Curzon's Government in 1903 considered the possible commodities to which preference might be extended by the United Kingdom, and found that few, if any, were likely to receive any appreciable benefit. We are now able to deal with the matter on a more practical basis, for, as we have explained above, the United Kingdom granted to the whole Empire in 1919 such preferences as were found to be consistent with the tariff policy. The only preferences of interest to India are those on tea, tobacco and coffee. In each of these cases the preference took the form of a reduction of one-sixth of the duty. The preference was a genuine reduction from the general rate of duty, and was not created by maintaining the existing rate for British products and enhancing it for foreign products. The amount of the preference was reasonable. The United Kingdom early went as far as could be expected consistently with a regard for her own interests. We have to see what benefit within those limitations has been conferred on Indian producers.

Tea.

235. In the case of tea the value of the preference granted to India is discounted by the fact that her chief competitor, Ceylon, enjoys an equal preference. Between them these two countries provided 86 per cent. of the tea entered for home consumption in the United Kingdom in the year 1913; and in 1920 they provided 90 per cent. When such a large percentage of the total

supply is entitled to the preferential rate, it may be assumed in accordance with the general economic principles which we have stated above that the price to the British consumer will be regulated by the preferential, and not by the general, rate of duty. No direct bonus therefore is likely to accrue to the Empire producers of tea from the British preference. The advantage which they may be expected to derive consists in the increased demand which the reduction in price may cause, and in the possibility of securing for themselves the remaining 10 per cent. of the British market. But in this particular case it is not entirely clear that the capture of the remaining 10 per cent. of the British market will be of any great advantage to the Empire tea producers. When the question of introducing preferential rates in the United Kingdom tariff was under consideration in 1919, the Indian Tea Association expressed some doubt as to the value to them of the suggested preference. They thought that it would have the effect of driving Java and inferior China tea out of the English market altogether, that the result would be that these teas would compete keenly in American and other foreign markets with British tea, and that the British tea exporters might possibly lose those markets and would therefore gain nothing by the preference. These views, however, are not those now held by the Indian Tea Association. In 1919 the Association made a special request that India should be granted preference in the Canadian market where Java tea was obtaining a serious hold, a request which was granted by the Canadian Government, and it expressed itself to us as believing in the advantage of preference to the tea trade, and as anticipating good results if a preference were granted by Australia. We do not therefore endorse the views expressed before the grant of the preference on tea in the United Kingdom as to its possible inutility. But we do not think that the preference on Indian tea is only of indirect advantage to the Indian tea producers by way of a possible extension of their market, and that it does not operate to increase their profits per pound of tea sold.

Coffee.

236. The Indian coffee planters are probably in a better position to benefit by the British preference than the tea planters, and they have consistently supported the concession. The proportion which the Indian supply of coffee bears to the total supply in the United Kingdom is comparatively small, and it is possible therefore that the Indian coffee planters receive something in the nature of a direct bonus. The Indian coffee trade is however small compared to the tea trade, and it is not clear whether there is any large scope for increased production in India.

Tobacco.

237. In the case of tobacco, which however also occupies but a minor position among Indian exports, it would seem likely at first sight that the preference would be of substantial advantage to the trade. But, as was pointed out in 1903, the system of laying the duty in the United Kingdom creates a discrimination against Indian tobacco. The duty on tobacco in England is charged by weight and not by value. Consequently the cheaper article is taxed more severely in proportion to its value than the more expensive, and the cheap Indian tobacco pays a duty which is particularly heavy. Even with the preference Indian tobacco remains at a disadvantage in the English market. This is a case in which a higher degree of preference or a change in the system of assessing the duty might be expected to give a real stimulus to the Indian trade.

Actual and Possible Gain to India from Preference is Small

238. The above examination of the existing preferences granted to Indian products in the United Kingdom bears out our general

proposition that Indian exports on the whole are not of a nature capable of benefiting to any great extent by preferential rates, freely recognise that except perhaps in the case of tobacco, the British Government has done what it can within its existing tariff system. But only one of the major exports of India receives a preference, and even if the tariff policy of Great Britain were to be modified, as was proposed in 1904, with a view to extending the field of preference, we do not think that the gain to India would be great.

239. On the other hand it would no doubt be possible for India to confer substantial advantages on British products by the grant of preferences in her market. The nature of the British imports, which are nearly all manufactures, makes this clear. But we do not think that India could grant anything of great value without imposing a serious burden on herself, and it would not be reasonable for India to incur such a burden.

Indian fear that preference must diminish protection not justified.

240. Before dealing with what we take to be the real objection to the grant of any extensive system of preferences by India, we wish to mention two points in respect of which apprehension is generally expressed by Indian witnesses, but which do not seem to us to justify an adverse verdict from the economic point of view. In the first place many witnesses have expressed the fear that a policy of preference would be equivalent to weakening the policy of protection, that the grant of preference to British manufactures in the Indian market would mean that Indian industries would not receive the full protection which require for their development. We need hardly say that, if such were the probable consequences of a policy of preference, we should, as strongly and unreservedly as the witnesses to whom we have referred, pronounce our condemnation. But we have explained above that Imperial Preference involves no question of abatement of a protectionist policy, and implies no idea of free trade within the Empire. The Dominions, which have freely granted preferences to the United Kingdom, have all adopted a pronounced protectionist policy, and they have in every case taken care that the preferences granted by them to the United Kingdom in no way interfered with the protection which they considered their own industries required. We wish to make it perfectly clear that it is essential that, if any preference is granted by India, it should not be allowed in any way to diminish the full protection which it may be decided any Indian industry requires.

Apprehensions of loss through relation by foreign countries exaggerated.

241. The second apprehension of economic loss which we do not

consider to be justified is that foreign countries will take retaliatory measures against India, if India excludes them partially from her mistakes by a system of preference. This was an argument to which Lord Curzon's Government in 1903 attached great importance. They realised the strength of India's position as an exporter of raw materials which foreign countries were interested in obtaining at the cheapest rates. But they could not exclude the possibility that in the case of some countries and in the case of certain articles India might be open to attack. The position was re-examined by the Government of India in 1917, and they come to the conclusion that the dangers apprehended by Lord Curzon's Government on this account were not serious. They thought that the strength of India's position as a supplier of raw materials, many of which were monopolies or partial monopolies, had been under-estimated, and that the Indian export trade was not likely to be seriously prejudiced by any retaliatory action taken by foreign countries. The position was examined once more by the Committee of the Imperial Legislative Council which was appointed in 1920 to consider the subject of Imperial Preference. Their conclusion on this point is stated in the following words :—

"We first considered the question whether the application to the Indian Customs Tariff of a system of preference in favour of goods of Empire origin would be likely to involve any danger of retaliation by countries outside the Empire in respect of our export trade. So far as we are able to judge, we are unanimously of opinion that in view of the demand for our raw materials, there is no danger to be feared on this score, [and that the apprehensions of Lord Curzon's Government in respect of this particular aspect of the question would in present circumstances be unreal."

242. The consideration which we have been able to give to the matter leads us to the same conclusions as were reached by the Government of India in 1917 and the Committee of the Imperial Legislative Council in 1920. While it is impossible to say that no country would take retaliatory measures against India in the event of the adoption of a policy of preference, we do not think that any country is likely to be able to embark on such action with any prospect of economic advantage to itself.

243. We have dealt with two aspects of this question in regard to which we believe that popular opinion is mistaken in anticipating economic loss to India from the adoption of a policy of preference. But we have shown, in analysing the effect of preferential rates, that they are likely in many instances to penalise the consumer in the country granting the preference, and it is in this respect that we anticipate that any considerable application of a policy of preference would cause distinct economic loss to India. The great mass of the

people in India, it must be remembered, are poor. We have throughout our enquiry borne this consideration in mind. Our general recommendations have been framed with a view to confining the sacrifice which must be demanded of the Indian consumer within the narrowest possible limits. It would not be consistent with our general view of the situation to ask the Indian consumer to bear an appreciable burden for the benefit of British manufacturers. Such burden as appears to us inevitable in the pursuit of a policy of more rapid industrial development the Indian consumer must be asked to bear. But he should not be called upon to bear an additional burden on top of this for the furtherance of interests which are not primarily Indian.

244. In this connection a suggestion has been made that preference should never be given in the case of an industry which is protected in India. This suggestion is not dictated by any fear that the preference might weaken the protection granted to the Indian industry, but by the consideration that the protection of the Indian industry already imposes a burden on the Indian consumer, and that, therefore, it is not desirable that a further burden should be imposed on him by a preferential rate, which would undoubtedly take the form of raising the general rate above the level which is required for purposes of protection. We do not think that it would be reasonable to lay down any absolute rule to this effect, but we consider that in selecting articles for preference the extent of the burden already imposed on the consumer in respect of those particular articles should not be ignored.

Conditions in which the grant of preference might be justifiable.

245. In our view it is clear that if preference is to be given it must be confined to comparatively few commodities and cannot take the form of a general preferential tariff. The commodities selected must be as far as possible those in which British manufacturers already hold an important part of the market, and in which the grant of preference is likely to develop rapidly the portion of the market which they will command, so that the burden on the consumer, if any, will be removed at an early date. We have to recognise however that there may be few industries which fulfil the requirements we have laid down. A British industry which is thoroughly efficient and already commands a large part of the Indian market is not perhaps likely to stand in need of the impetus that preference would give. The industries which would be likely to place their faith in preference are precisely those which are less efficient, and the grant of preference to them might impose a permanent burden on the Indian consumer. Nevertheless we recognise that there may be cases, particularly arising out of special and

temporary conditions, in which India might be in a position to give assistance to British industries without appreciable economic loss to herself.

Nature of foreign competition in the Indian market.

246. Looking broadly at the competition of foreign countries in the Indian market, we see that out of 34 per cent. of imports derived from countries outside the British Empire about 18 per cent. in 1920-21 and 13 per cent. in 1921-22 came from the United States and Japan. After these two comes Java, the imports from which, however, consist of sugar, and therefore do not compete with imports from the United Kingdom. The most serious general competitors of British manufacturers therefore at the present moment are America and Japan. German competition in the matter of dyes is an important factor; and both Germany and Belgium are competitors of whom account must be taken in the imports of iron and steel. It must also be remembered that before the war German imports into India exceeded those of any other foreign country, and that there are signs that Germany is gradually working up this trade again. Japanese competition is mainly confined to cotton yarn and piece-goods. The United States sends large quantities of iron and steel, machinery, hardware and cutlery, instruments, apparatus and appliances, motor cars and tobacco, which may be considered in varying degrees to be in competition with British imports. These are the main heads under which we might expect British manufacturers to anticipate advantage to themselves from the grant of preferences in the Indian market.

247. We have received a certain number of applications from British manufacturing interests for the grant of preference. Representations have been made in respect of dyes, motor cars, electrical apparatus, tobacco, drugs and rubber tyres, while a general appeal was received from the British Empire Producers Organisation impressing upon us the importance of the adoption of the principle of Imperial Preference. We are not in a position to make any definite recommendations in regard to the merits of these various applications. But we think it desirable to point out certain aspects of some of them which have come under our consideration.

Dyes

248. The application which is probably of the most importance and which has been most earnestly pressed on our attention is that on behalf of British dyes. It was pointed out that the manufacture of dyes has been recognised in the United Kingdom as an industry of imperial importance, and that in consequence it has received a very special measure of protection in the market of the mother country. The considerations, it is urged, which have led the United Kingdom to give special treatment to the dye industry should lead other parts of the Empire

to do what they can to assist the development of British dyes. It is not only that in time of war the Empire should not be exposed to the risk of finding its supplies of dyestuffs entirely cut off. The dye industry has a much closer and more direct relation to the interests, and even the safety, of the Empire in the event of war. It is recognised that an efficient dyestuff industry is of the utmost importance to the national security, as in its absence serious difficulty must be experienced in turning out rapidly the explosives and chemicals required for war. From this point of view therefore the establishment of a large scale dyestuff industry is of supreme importance to all parts of the Empire. It is admitted that under present conditions there is no possibility of starting such an industry in India. India, therefore, in time of war must be dependent on the dyestuff industry of the United Kingdom; and from the point of view of Indian interests it might be thought that some help could reasonably be extended by India to the British industry. The Indian market is of great importance, and the British industry is at present apprehensive that it may lose this market and thereby suffer a severe blow. The competition is mainly with Germany which before the war was unchallenged in the production of dyestuffs. It is urged that the German industry, which is a well-organised monopoly, would be prepared to sell even at a loss in order to drive the British industry out of the Indian market, and that in any case the present depreciation of the mark gives the Germans an enormous temporary advantage in competition with the British product. For these reasons, and because the British industry is still to some extent in its infancy and has not yet reached the stage of full efficiency, the British companies ask for a preference in the Indian market.

249. We recognise the strength of the considerations put forward, but we realise also that there are important arguments on the other side. We understand that in many cases the British dyes are not considered equal in quality to the German dyes, and that therefore by preferring the former India would be imposing a handicap not only of price, but of quality, on her manufacturers. The competition of the Indian mills with Japan in piece-goods is at the present time so keen that India might well hesitate to handicap her own manufacturers by forcing them to use dearer and inferior dyes. So far as the Indian market is concerned this handicap might be neutralised by increasing the duty on imported piece-goods, but such a course would have the effect of penalising the Indian consumer. In any case, the handicap could not be removed in the case of competition with Japan in foreign markets.

250. We have stated as impartially as we can the arguments which have been used on both sides; and we feel that, in accordance with the principle we have adopted throughout this report, we cannot go any further and on the limited information available to us make any definite recommendation. We think that, if the principle of Imperial Preference is adopted, the question of a preference on dyes as affecting all interests might be examined by the Tariff Board.

Motor cars.

251. The case for a preference on British motor cars was put before us in writing by the Association of British Motor Manufacturers Limited, and orally by the Motor Trades Association in Calcutta. The case of motor cars is somewhat peculiar. The main source of supply is the United States which in 1920-21 sent motor cars to the value of £4,506,399, while the value of cars imported from the United Kingdom was only £2,133,987. The class of cars supplied by the United States and by the United Kingdom is different. The American cars make their appeal to the Indian market in virtue of their cheapness, and the enormous increase in the import of American cars recently shows that this is a factor which is of the utmost importance in India. We understand that efforts

are being made in the United Kingdom to produce cars which would compete with the cheap American cars, and a preference in the Indian market might give a decided stimulus to this movement.

Machinery

252. With regard to machinery we have stated that it is desirable that it should be admitted free. But we would not exclude an examination by the Tariff Board as to the effect of imposing a low import duty on foreign machinery while admitting British machinery free.

Cigarettes

253. The feasibility of a preference on cigarettes might also be examined. In 1920-21 the import trade was divided almost equally between the United Kingdom and the United States, the latter having a slight advantage. The figures of recent years show that the imports from the United States have been increasing very largely, and it is possible that a case for preference might be made out.

254. So far we have shown that in the nature of things any preferences granted to India are likely to be of considerably less value than the preferences which India might grant to the Empire; and that consequently in any balance of economic loss or gain India would under any general system of preference be a decided loser. We do not however wish to lay too much stress on this aspect of the matter. We realise that Imperial Preference as between the Dominions and the mother country has not hitherto been a matter of bargain. The Dominions from the first gave such preferences to the mother country as they felt were consistent with their own policy and were not injurious to themselves. Though they made it clear that they would welcome any response on the part of the United Kingdom, they did not make the grant of their preferences conditional on such a response. From 1897 to 1919 no response in fact was made. When in 1919 Great Britain decided to follow the example of the Dominions and introduced a preferential system, she gave freely such preferences as she felt could be granted consistently with the interests of her own people and the requirements of her own tariff policy. In the same way, if India is to adopt the principle of Imperial Preference, she must adopt it freely to the extent to which she feels she can do so without detriment to the paramount interests of her own people. She receives already certain preferences from the United Kingdom. She recognises with gratitude the spirit in which they are given. She will not wish to look too narrowly to the actual economic advantage of these preferences, and in turn she would expect that any preferences which she finds herself in a position to grant without serious detriment to her own interests should be received in the same spirit, and should be regarded as a voluntary gift and not as part of a bargain.

(iv) Conclusions.

Causes of Indian Hostility to Preference

255. We have been impressed throughout our enquiry by the almost complete unanimity with which Indian witnesses opposed the principle of Imperial Preference; and it is important to explain the causes which in our view underlie this antagonism.

(1) Fear that it may Diminish Protection

256. We have already referred to the belief entertained by

many witnesses that preference would operate to weaken the protection granted to Indian industries. This apprehension can be met by laying down definitely the principle that under no circumstances should preference be allowed to diminish the protection which it may be decided that an Indian industry requires.

(ii) **Burden on Indian Consumer**

257. A second argument which has weighed with many witnesses is that preference is equivalent to the grant of a bounty to the British manufacturer at the expense of the Indian consumer, that India is poor while Britain is rich, and that it is not reasonable to expect the poor country to make a gift to the rich one. We have explained that in our opinion this view of the question is not unreasonable, and that any general system of preference would undoubtedly impose an appreciable burden on the Indian consumer, which we do not think it fair that he should be called upon to bear. This argument may be met by the assertion of a second principle, namely, that Imperial Preference should not involve any appreciable economic loss to India. In estimating the economic loss it would be reasonable to take into account any economic gain which India receives from the preferences granted by the United Kingdom; and in case any should be tempted to look too narrowly at the balance of loss and gain, it is well to remember that India at present enjoys the protection of the British Navy in return for a merely nominal contribution.

(iii) **Fear that it will affect India's Fiscal Autonomy**

258. The main cause however of the general hostility displayed by Indian witnesses to the idea of Imperial Preference is, we think, political. It is based on a feeling of suspicion. There is a fear that if India accepted the principle of Imperial Preference she would find that she had parted with the newly won privilege of fiscal autonomy, that in the name of Imperial Preference the tariff policy of India would be directed not in her own interests but in the interests of other parts of the Empire, that if India signified her acceptance of the principle the details would be dictated to her regardless of her own interests and wishes. We think that these fears are based on a misunderstanding of the true position. Many regard Imperial Preference as meaning a unified tariff policy for the whole Empire, dictated, if not by the mother country, at least by binding resolutions passed at periodical Imperial Conferences. This is a complete misunderstanding of the real principles which underlie Imperial Preference. We have shown above that Imperial Preference implies no kind of interference in the tariff policy which the various Dominions have chosen for themselves, and no idea of a system of free trade

within the Empire or any uniform tariff policy. It is true that as a result of the Paris Economic Conference of 1916 already referred to, the question of the organisation of the Empire as an independent economic unit seemed for a time to be coming into practical consideration. But the ideas to which the crisis of the war gave rise did not long survive its termination, and the policy of Imperial Preference developed on its original lines. Each part of the Empire took such steps as it felt could reasonably be taken consistently with its own interests to promote inter-imperial trade and the manufactures of the mother country. This is the meaning which we attach to the policy of Imperial Preference, and all our recommendations must be read as referring to such a policy, and not to any idea of a joint tariff policy for the Empire imposed on the various component parts.

The assurance of the British Government regarding fiscal autonomy.

259. But the doubters think that, whatever may be the policy in regard to the Dominions, India stands in a different relation, and that the principle of Imperial Preference may be utilised against India to interfere with her fiscal autonomy. We would remind them that the principle of permitting India to decide her own fiscal policy has been stated in the most explicit terms. We quote once more the recommendation made by the Joint Select Committee on the Government of India Bill in their report on clause 33 :—

“ Whatever be the right fiscal policy for India, for the needs of her consumers as well as for her manufacturers, it is quite clear that she should have the same liberty to consider her interests as Great Britain, Australia, New Zealand, Canada and South Africa. In the opinion of the Committee, therefore, the Secretary of State should as far as possible avoid interference on this subject when the Government of India and its Legislature are in agreement, and they think that his intervention, when it does take place, should be limited to safeguarding the international obligations of the Empire or any fiscal arrangements within the Empire to which His Majesty's Government is a party.”

In his despatch of the 30th June 1921 the Secretary of State said that on behalf of His Majesty's Government he had accepted the principle recommended by the Joint Committee in this passage. It is true that some doubt may be aroused by the words “ any fiscal arrangements within the Empire to which His Majesty's Government is a party.” But we have explained that Imperial Preference, as hitherto practised and as understood by us, cannot involve any dictation by His Majesty's Government to any portion of the Empire. The convention which the Secretary of State has undertaken to establish gives, it is true, no assurance that a policy favoured by the Indian Legislature will necessarily be adopted. But it does, we think, give a practical assurance that no fiscal measures which the Indian Legislature does not approve will be adopted in India. Any fear therefore that particular applications of a policy of preference

can be made contrary to the wishes of the Legislature appears to us to be illusory. Nevertheless we would put the matter beyond all possible doubt by asserting as our third principle that no preference should be granted on any commodity without the explicit approval of the Indian Legislature.

The Imperial aspect

260. Hitherto we have discussed this question purely from the point of view of India's interests and India's feelings. But we are not blind, and we do not believe that Indian opinion will be blind, to the larger Imperial aspect. In discussing the advantages that Great Britain might derive from a preference in the Indian market we have hitherto treated that advantage solely from the narrow economic aspect, and it has presented itself as an advantage to be derived by particular industries or particular manufacturers. But even on the material and strictly economic side the interests involved are far wider than those of the prosperity of particular industries. We do not forget that the United Kingdom is the heart of the Empire, that on its strength depends the strength and cohesion of the empire, and that its strength is bound up with the prosperity of its export trade, which has enabled a small island to find the resources which bind together and uphold the great Commonwealth of Nations known as the British Empire. Unless the United Kingdom maintains its export trade the heart of the Empire will weaken, and this is a contingency to which no part of the Empire can be indifferent. Nor again do we forget that the communications of the Empire are guarded by the British Navy, and that the burden of maintaining that essential service falls almost entirely on the people of the United Kingdom.

The sentiment of Empire

261. While however we do not ignore the material side of the policy of Imperial Preference, we believe that the sentiment with which it is associated is even more important. Imperial Preference is regarded throughout the Empire as a means of strengthening the ties which bind together its scattered units. Adhesion to the policy of Imperial Preference is thus coming to be regarded as a test of loyalty to the Empire, as a proof that the various parts of the Empire look beyond their own immediate interests and recognise their position as parts of a greater whole. From this point of view we firmly believed that India should not turn her back on the principles which have been adopted in the greater part of the Empire and are rapidly being extended to the remainder. We would not have India standing in a position of moral isolation within the Empire. The view has been expressed that in consequence of India's special

economic situation, which we have explained in detail above, and her consequent inability to grant preferences which are likely to be of serious economic value, such a gift as she might make would be regarded as valueless. We are convinced that such a view is wholly mistaken, and that on the contrary a free gift from India, however small, would be welcomed by the United Kingdom as a gesture of friendship and as a proof that India realised her position as a member of the Empire.

Decision must rest with the Legislature.

262. We recognise that the question of Imperial Preference is one which can only be determined in accordance with Indian opinion; and that the Indian view can be best ascertained by reference to the Council of State and the Legislative Assembly, without whose free consent no such policy can be adopted. We feel confident that the Indian Legislature will consider the obligations of India in this matter as a component part of the Empire. We have endeavoured to indicate certain principles which should govern the application of the policy, if adopted. We repeat them once more. In the first place, no preference should be granted on any article without the approval of the Indian Legislature. Secondly, no preference given should in any way diminish the protection required by Indian industries. Thirdly the preference should not involve any appreciable economic loss to India after taking into account the economic gain which India derives from the preference granted her by the United Kingdom.

Suggested enquiry by Tariff Board.

263. It is evident that the Legislature can hardly be asked to pronounce an opinion on the policy until it has some idea of the extent to which its application is feasible. We must therefore recommend that, as a preliminary to any consideration of the desirability of India adopting the policy of Imperial Preference, an examination should be made by the Tariff Board to determine whether there are any commodities on which preference might be given in accordance with the principles which we have laid down, to the benefit of the Empire and without detriment to Indian interests.

Policy to be adopted towards the Dominions and Colonies.

264. Hitherto in discussing the question of Imperial Preference we have confined our consideration to preferences granted to the mother country. With regard to other parts of the Empire we would recommend a different policy. We suggest that to the United Kingdom should be offered such preferences as India may find she is able to offer without appreciable injury to herself. With regard

to other parts of the Empire; we recommend a policy of reciprocity such as is already adopted by more than one Dominion for inter-dominion trade relations; that is to say, preference should be granted only as the result of agreements which might prove to the mutual advantage of both parties. In this connection India would doubtless not be unmindful of the fact that she already enjoys the benefit of certain concessions granted by Canada and New Zealand. The agreements which we contemplate would be purely voluntary; there would be no kind of obligation on India to enter into them unless her own interests appeared to demand it; and it is evident that political considerations could not be excluded in determining whether it was desirable for India to enter into an economic agreement or not.

The question—a practical one

265. We think it is necessary that there should be laid down for India some policy of the nature outlined above in regard to trade relations with other parts of the Empire. We have already mentioned that India receives preferences from Canada and New Zealand. We understand that proposals for reciprocity were received in 1919 from one of the Dominions. We have recently been informed by the Canadian Government Trade Commissioner to India that a preference on motor cars granted to Canada would stimulate the present tendency for the well known makes of American cars destined for the Indian market to be made in Canada, and would be regarded as a graceful reciprocal act of the part of India. It seems probable that this benefit could be conferred on Canada without any appreciable loss to India. We have also received strong representations from the Govt. of Mauritius and the Mauritius Chambers of Commerce and Agriculture requesting that preference may be given to Mauritius sugar in the Indian market. We realise that, judged by ordinary economic principles, the case for a preference on Mauritius sugar is not strong. The proportion of Mauritius sugar to the total imports of sugar into India is small, and there appears to be little probability that Mauritius will ever be able to supply the whole Indian market. Nor does it seem that Mauritius, though willing to grant India reciprocal benefits, would be able to offer anything which would be of material advantage. At the same time it has been urged that the majority of the population of Mauritius is Indian, that Mauritius sugar is grown entirely by Indian labour and that a large proportion of it is owned by Indian proprietors. A case like this is, we consider, suitable for examination by the Tariff Board; and the Legislature should then decide after balancing the advantage and disadvantages whether it would be to the interests of India to enter into a reciprocal agreement with Mauritius.

The Minute of Dissent

of the President and the Indian Members.

The reasons which have moved us to write a dissenting minute may be stated in a few words :

- (A) The main recommendation has been hedged in by conditions and provisos which are calculated to impair its utility.
- (B) In places, the language employed is half-hearted and apologetic.
- (C) We are unable to agree with the views of our colleagues on Excise, Foreign Capital, Imperial Preference and the continuation of the Tariff Board.

2. Our first objection is to the statement in the Report that "we recommend a policy of protection to be applied with discrimination along the lines of the Report." To formulate a policy in these words is open to objection because

- (I) In the first place, it mixes up policy with procedure.
- (II) In the second place, by emphasising the method of carrying out the policy the vital issue of the problem is obscured.
- (III) In the third place, it ignores the fact that every country applies PROTECTION with discrimination suited to its own conditions.
- (IV) Fourthly, in our opinion, the outlook of our colleagues is different from ours. We do not, therefore, feel justified in subscribing to the view that Protection should be applied with discrimination "along the lines of the Report."

In our opinion, there should be an unqualified pronouncement that **the fiscal policy best suited for India is Protection.**

3. The manifold advantages which a policy of intense industrialisation will secure to India are undisputed and our unanimous conclusion is embodied in paragraph 54 which may be quoted here :

"We have considered generally the advantages and the possible disadvantages which would attach to a considerable development of Indian industries. We have no hesitation in holding that such a development would be very much to the advantage of the country as a whole, creating new sources of wealth, encouraging the accumulation of capital, enlarging the public revenues, providing more profitable employment for labour, reducing the excessive dependence of the country on the unstable profits of agriculture, and finally stimulating the national life and developing the national character."

4. We would, however, place before the country the goal to be aimed at, namely, that India should attain a position of one of the foremost industrial nations in the world, that instead of being a large importer of manufactured goods and exporter mainly of raw materials, she should so develop her industries as to enable her within a reasonable period of time, in addition to supplying her own needs, to export her surplus manufactured goods. With

the natural advantages which India possess it is by no means difficult to reach this goal at an early date. India has an abundant supply of raw materials, a plentiful supply of labour, adequate capital and a large home market. All the requisites for industrial growth and development are thus present much more so than in many countries which have, without such advantages, attained a commanding position in the industrial world. There appears to be no reason why India should not reach a similar, if not a higher, position. This goal can only be reached by a whole-hearted co-operation of the State and of the people. As pointed out in paragraph 58 of the Report, the tariff systems prevailing generally throughout the world are based on the principle of protection. The State and the people co-operate and the result is great economic prosperity. Until recently, the Government of India were unable to frame a tariff policy which would have been in the best interests of India. That position has now changed. In the first chapter of the Report it has been pointed out how India has now attained fiscal autonomy. The Government of India is, therefore, free to adopt, in co-operation with the Indian Legislature, such measures as may appear to them necessary for promoting the industrial development of India and the consequent economic prosperity of this country. The appointment of this Commission is the result of such freedom conceded to the Government of India under the Reform Scheme.

5. We are unanimous in recommending that a policy of protection should be adopted. Our disagreement arises from the fact that the policy of protection recommended by our colleagues is qualified by the words "to be applied with discrimination along the lines of the Report." We do not know of any other country in the world, including the British Dominions, which have so qualified the policy of protection. While it is perfectly relevant for the Commission to indicate the lines on which protection may be worked in the initial stages, the recommendation of the policy should be clear and unequivocal. While our colleagues recommend "a policy of protection to be applied with discrimination along the lines of the Report," our recommendation is that a "policy of protection" should be adopted in the best interests of India. The policy has not only the unanimous support of the people of India, but is on the same lines as it prevails in all other protectionist countries of the world.

6. While we agree that the policy of protection should be applied with discrimination, we do not think that any qualifications or limitations should be made a condition precedent to its adoption. We recognise that in the efforts to attain a prominent position in the industrial world, India will have to pay a price. The economic well-being of India which we aim at in the tariff policy which we

recommend cannot be obtained without making a sacrifice. It is for this reason that we agree that the policy should be applied with discrimination. The discrimination with which we agree is intended to minimise such sacrifice as far as possible consistently with reaching the goal which we are putting before the country. We do not subscribe to the condition that such discrimination should be "along the lines of the Report." The conditions laid down in Chapter VII appear to us to be stringent, and will entail considerable delay in giving effect to the policy which we have unanimously recommended and will not produce adequate results. We share the concern shown in the Report for the interests of the consumers, and we agree that the policy should be applied in such a manner as to reduce the burden on the consumer to the minimum necessary for the purpose of carrying out the object in view. In the present economic condition of India, limitations in the interest of the consumers are necessary, but we anticipate that if immediate effect is given to the policy we recommend, India will begin to grow economically prosperous within a reasonable period of time. It is, therefore, necessary to make it clear that while the policy of protection should endure till the goal is reached, discrimination must vary according to the circumstances for the time being and should not be applied rigidly along the lines indicated in the Report. We may point out here that while we want India to rise to a commanding position in the matter of her industrial development under the policy of protection, our colleagues anticipate as a result of the qualified policy which they recommend that "India for many years to come is likely to concentrate on the simpler forms of manufactured goods" (paragraph 310). A policy which is likely only to lead to this result for many years to come is not and cannot be acceptable to the people of India. In all protectionist countries, the Government and the Legislature as representing the people regulate the application of the policy of protection in a manner most suitable to local conditions and circumstances, and there appears to us no reason why the discretion of the Government of India and the Indian Legislature should be fettered in any way. The records of the Provincial and Central Legislatures conclusively show that non-official members have vied with one another in pressing on the attention of Government the interests of the masses. We can, therefore, confidently leave the interests of the consumers in the hands of the non-official members of the Indian Legislature who are representative of large and varied interests. We should, therefore, recommend that the application of the policy of protection should be regulated from time to time by such discrimination as may be considered necessary by the Government of India and the Indian Legislature.

7. While recognising the necessity of caution in the application of the principle of protection in the interests of the masses we do not think it would be right to hedge the policy in such a manner as to lead to inadequate results. We may, therefore, emphasise the fact that we desire immediate effect to be given to the policy recommended by us in order to achieve the object in view as early as possible. India's dependence upon agriculture has found her in serious economic difficulties. Through the operation of world causes, the cost of living has enormously increased during recent times and there is a great amount of misery prevailing in the land. The revenue needs of the country have enormously increased and taxation has been raised to an unbearable level. It is, therefore, essentially necessary that immediate steps should be taken to adopt an intense policy of industrialisation to ensure the creation of new sources of wealth, encouragement for the accumulation of new capital, enlargement of public revenues and providing more profitable employment for labour.

8. We regret that our colleagues should have thought it necessary to justify the fiscal policy hitherto pursued; there is considerable difference of opinion as to its wisdom or suitability. We are not, therefore, prepared to accept that portion of the Report dealing with the subject. We would, however, point out that all the necessary requisites for industrialisation have existed in India for a long time and if a policy of protection had been adopted, say at least a generation ago, if the same freedom to regulate her fiscal policy had been conceded to India as was conceded to the Self-Governing Dominions, India would have made by this time great progress in the direction of industrialisation and would not have been found in the state of economic backwardness in which we now find her.

9. The Industrial Commission has placed on record the policy pursued in India in the following words:

"The commercial instincts of the East India Company had from its earliest days in this country led it to make various attempts to improve those Indian industries from which its export trade was largely drawn, as for example, by organising and financing the manufacture of cotton and silk piece-goods and silk yarn, although this policy met with opposition from vested interests in England, which were at one time sufficiently powerful to insist that it should be suspended and that the Company should instead concentrate on the export from India of the raw material necessary for manufactures in England. The effect of this traditional policy continued for some time after the Company had ceased to be a trading body and even after it had been replaced by the direct rule of the Crown, and doubtless moulded such subsequent efforts as were made in the same direction by Government. But as laissez-faire views gradually gained increasing acceptance both in England and in India, these spasmodic efforts became less frequent and the first effort at a general policy of industrial development took only two forms—a very imperfect provision of technical and

industrial education, and the collection and dissemination of commercial and industrial information."

10. As admitted in the Report, in view of her past achievements India's capacity to be an industrial country cannot be doubted. The Industrial Commission found that "the industrial system is unevenly and in most cases inadequately developed and the capitalists of the country with a few notable exceptions have till now left to other countries the work of and the profit from manufacturing her valuable raw materials or have allowed them to remain unutilized." If the Industrial Commission had not been debarred from considering the question of Indian fiscal policy, we venture to think that they would have come to the same conclusion as is held by the people of India that this result was to the policy of free trade imposed upon India. If a policy due to

"vested interests in England which were at one time sufficiently powerful to insist that.....the (East India) Company should concentrate on the export of raw materials necessary for manufactures in England" (Industrial Commission Report).

had not been adopted, the Indian artisans, whose skill was recognised throughout the world, could have easily adapted themselves to conditions produced by the advent of machinery, and the economic history of India would have been differently written. We believe that the industrial backwardness of India is in no way due to any inherent defects amongst the people of India but that it was artificially created by a continuous process of stifling, by means of a forced tariff policy, the inborn industrial genius of the people. In paragraph 57, doubts have been cast on the view of the Indian people that India was a country of great wealth which attracted foreign invasions and drew to its shores adventurous spirits from European countries. We would fain have left the past alone as no useful purpose can be served by raking up historical facts which can have no direct bearing on the tariff policy which is best suited to the conditions of India. We are, however, constrained to refer to the position in view of the remarks which our colleagues have considered it necessary to make for arriving at a conclusion on the subject. The works of eminent writers such as Meadows Taylor, Lecky, Romesh Chandra Dutt, Wilson and Professors Hamilton and Jadunath Sircar show how great India's economic and industrial position was in the past. A few extracts from these authors will be found in the Appendix.

Excise Policy.

11. We must record our dissent from the policy recommended by our colleagues in regard to excise duties. It may be pointed out

that towards the close of the Middle Ages internal duties formed a substantial part of revenue resources ; but even in those days, they were regarded as an obnoxious method of taxation. The more enlightened policy of the modern age has gradually swept away all internal duties which hampered trade and industry and excise on all articles excepting those which are injurious to public health and on a few luxuries. Our colleagues have in paragraph 143 referred to the excise policy of various countries from which it is evident that in most civilized countries such duties are restricted to alcohol and tobacco. They state :—

" In the British Colonies and the United States of America excise taxation has gradually been confined to these articles. But on the continent of Europe many countries have applied the excise system to other commodities, such as sugar and salt, while France employs not only a comparatively wide range of excise duties, but also a system of State monopolies under which the whole profits from the manufacture of excisable articles, such as tobacco and matches, are secured to the State. In Egypt after the establishment of two cotton mills in 1901 the Government subjected their product to a consumption tax of 8 per cent. as compensation for the loss of customs revenue. In Japan cotton cloth is subject to a consumption tax which comprises both an excise duty on home production and a surcharge on the customs duty on the imported articles. A rebate is allowed if the cloth is exported. Japan also levies a consumption tax on kerosene and an excise duty on sugar."

12 We will state at once that in our view excise duties should be restricted to such articles as alcohol and tobacco which are regarded as injurious to public health or to public morality and the consumption of which it is desirable to check and to a few luxuries. This is the policy which is at present adopted by the United States of America and the British Colonies. It has the support of Professor Plehn who argues that excise is a justifiable source of revenue when it is levied on articles such as wines, tobacco, etc., whose consumption it is desirable to check in the interests of the community and that if more revenue is required it may be justifiable to impose excise on articles of luxury produced in the country.

13. As regards the instances of European countries quoted by our colleagues, *viz.*, excise on sugar and salt, it may be pointed out that sugar may well be regarded as a luxury and the question of duty on salt which India also levies had led to considerable differences of opinion and cannot, therefore, be regarded as a precedent for a general excise policy. The case of France and Japan is different. France has adopted a policy of State Monopolies under which the whole profit from the manufacture of articles is secured to the State. A policy of this kind which a State works as a monopoly cannot be regarded as a guide for a correct policy on excise matters. The consumption tax on cloth manufactured in Japan cannot be held to provide any precedent for the purpose of a similar policy in India.

This tax is levied in Japan with the specific object of encouraging the export of cloth and to economise home consumption. Such a policy may be justifiable in Japan because she has developed her industries under a system of high protection and is able to manufacture for the purposes of export. This condition does not apply to India which is hardly able to supply 50 per cent. of her own requirements. We have dealt with the excise duty on sugar which we regard as coming within the category of luxury. We are not aware of the facts in regard to the excise duty levied by Japan on kerosene, but one instance in one country cannot justify the laying down of an excise policy for India. The best principle to follow appears to be that of the British Dominions and this supports the view we are recommending. The only other case which remains to be dealt with is that of Egypt. It is stated that "in Egypt after the establishment of two cotton mills in 1901 the Government subjected their product to a consumption tax of 8 per cent. as compensation for the loss of customs revenue." We wish our colleagues had not quoted the case of Egypt. In view of the political control which England exercised over Egypt and the history of cotton excise duty in India embodied in Chapter 10 of the Report, the conclusion appears irresistible that the excise duty on cotton piece-goods in Egypt was due more to Lancashire influence than to any idea of compensation for the loss of customs revenue.

14. Our colleagues recommend the imposition of excise duties on certain principles noted in paragraph 151 of the Report. The reasons why we do not agree with them have been stated. We may emphasise the fact that excise duties hamper industries and lead to undue interference with local manufacture, and it is for this, amongst other reasons, that excise duties are restricted in almost all civilized countries to the articles the consumption of which it is necessary to check in the public interest and to a few luxuries.

15. We may point out that during the period of the war every belligerent country was hard pressed to obtain revenue from every possible source. In spite of such over-powering needs for revenue to carry on the war, none of them resorted to excise duties of the kind which our colleagues have recommended as a general policy to be adopted in India. An effort is made to meet this point in paragraph 146 of the Report, but we do not regard it as in any way convincing. The United States of America has gone dry and still no excise duties of the kind recommended have been imposed. Even if a large portion of the people of India abstains from indulging in intoxicating drinks, as is implied in the statement in the report "we have pointed out above that the British Treasury is able to tax the general population by means of heavy excise duties on

alcohol, and that this excise does not have the same wide incidence in India," it can hardly be regarded as any reason for imposing excise duties on the lines recommended. It cannot be contended that the needs of the Indian exchequer can possibly compare with the needs of the belligerent countries during the war, and it must be obvious that when none of them resorted to this form of taxation, it cannot be justified in India as a general policy. In this connection, we would invite attention to the case of England herself. England raised revenue several times larger than the amount she collected before the war. She imposed a duty of 33 and one-third per cent on imported motor cars but did not put any countervailing excise duty on locally manufactured cars. England has been a free trade country and the principles of that policy coupled with the over-powering needs for revenue would have justified the imposition of countervailing excise duties on locally manufactured cars. The fact, however, remains that she did not put any excise duty on cars manufactured in England. This instance alone is, in our opinion, sufficiently conclusive to show that the excise policy recommended by our colleagues in regard to local manufactures cannot be justified.

16. We share with our colleagues the concern for the interests of the consumers in regard to the application of a policy of protection. We should like, however, to ask how this concern is consistent with the excise policy which they have recommended. They propose that—

"when an industry requires protection, any further necessary taxation on its products may, if other conditions are fulfilled, take the form of an excise duty PLUS an additional import duty. The latter should fully counterbalance the former and may be pitched at a little higher rate."

One of the conditions referred to is that "excise duties should ordinarily be confined to industries which are concentrated in large factories or small areas." Coupled with this condition is the recommendation in paragraph 170, *viz.*, "if, on the other hand, Government hold that their revenue requirements make it obligatory to levy taxation on cotton cloth in excess of this amount, it will be necessary for them to formulate proposals in accordance with the principles we have explained, and to lay these proposals before the Legislature." The effect of these recommendations with regard to an excise duty on cotton piece-goods is as follows:—

17. Assuming that the Tariff Board decides that a protective duty of 10 per cent. is required for the textile industry and the revenue requirements of Government make it obligatory to levy excise taxation on cotton cloth to the extent of 5 per cent., the import duty will have to be raised to approximately 17 per cent.

The price of cloth will thus rise to a parity of 17 per cent. The economic condition of India is admitted to be such that a large part of the population is under-clothed and under-fed. It is a well-known fact that prices of cotton piece-goods have considerably risen during recent years and the effect of it on this article of necessity may be judged from the speech of our colleague, Mr. C. W. Rhodes in the Legislative Assembly. He pointed out that the average consumption of cloth in India before the war was 18 yards per head, while in 1920-21 it had gone down to 10 yards. The consumers in India will have to bear the necessary burden in the wider interests of the country, as a result of the protective policy which the Commission has recommended. To suggest that further burdens should be imposed upon them by increased import duties for the purpose of countervailing excise duties is hardly consistent with the interests of the consumers, many of whom have to be content with insufficient clothing.

18. Our colleagues have referred to the power which the Central Legislature exercises under the Reforms and have stated that the question of cotton excise duties should be left to the decision of Government and the Legislature. We have already recorded our confidence in the Central Legislature in regulating the policy of protection and we would have unhesitatingly accepted their recommendation if the policy of excise duties, as recommended by our colleagues, was sound in principle. The exercise of discretion is only possible in matters which are sound in principle. We have shown that the excise policy as recommended by our colleagues is unsound in principle, and the question of the direction of the Legislature cannot therefore arise. As, however, the constitutional question has been raised by our colleagues, it is necessary to note what the actual position is. In all countries enjoying responsible government the Legislature is wholly elected and the executive government is responsible to the Legislature. During the transitional period the position in India is different. The Government is not responsible to the Legislature, and that body is not wholly elected. The budget estimates are prepared by the Executive Government and important items are non-votable. Even in regard to the items which are subject to the vote of the Legislature the power of reinstatement vests in the Governor-General. The constitution of the Legislature also requires examination. There are 143 members in the Legislative Assembly. Assuming that every member is present—experience has shown that this has not been so in practice—47 non-official members can, with the help of the official vote, out-vote 71 non-official members. It must be obvious therefore that the result of a vote in the Legislative Assembly, unless there is

a clear majority of non-official members, cannot be regarded as representing the views of the country. If the policy of excise duties, as recommended by our colleagues, was sound in principle and the vote of the non-official members of the Assembly had a binding effect we would have no hesitation in accepting the recommendation to leave the decision to such vote. We, however, hold that excise duties beyond the limitation indicated by us are not sound in principle. We, therefore, reiterate our conclusion that excise duties in India should be restricted to alcohol, tobacco, and such other articles, the consumption of which it is desirable to check in the interests of the community, and to a few articles of luxury.

Cotton Excise

19. We have nothing to add to the history of the cotton excise duties contained in the Report, but we do not agree with the conclusion arrived at. Our colleagues provide for a possibility of excise duties being levied on cotton piece-goods and other articles of local manufacture which is opposed to the policy generally adopted by the civilised world and is contrary to the conclusion which we have come to in regard to the general policy of excise duties.

20. The Indian point of view is conclusively shown by the evidence of witnesses who appeared before us. It is that the people of India are opposed to the levy of cotton excise duties either to countervail the import duty or for revenue purposes. Questions were asked by members of the Commission as to whether they would agree to the imposition of an excise duty on cotton piece-goods for revenue purposes, and the answer was mostly an emphatic negative. The debates in the Indian Legislature have proved beyond doubt that the sentiment of the people of India is opposed to this form of taxation. It has been admitted in the report that excise duty on cotton piece-goods is no longer fully countervailing and that in spite of this fact "*the great majority (of witnesses) both Indian and European have demanded its abolition.*"

21. We have pointed out in the previous chapter what in our opinion should be the policy in regard to excise duties and we believe that correctly represents the Indian view. We cannot understand why our colleagues have recommended that—

"the British Government should announce its intention of allowing the Government of India to decide the question in agreement with the Indian Legislature."

This recommendation casts a doubt upon the fiscal freedom which India has already attained. The recommendation made by our colleagues is in contradiction of the history embodied in Chapter I of the Report showing how India has now become fiscally free. In paragraph 4 of the Report, reference is made to the Despatch of the

Secretary of State dated the 30th June 1921 in which he says that he has accepted *on behalf of His Majesty's Government* the principle recommended by the Joint Committee in their Report on clause 33 of the Government of India Bill. India is, therefore, entitled to regulate her customs tariffs as is most suitable to herself and it appears to us highly prejudicial to the interests of this country for a Commission like this to suggest that any such announcement is necessary before action can be taken in the matter of cotton excise duties.

22. Our colleagues proceed to point out the financial difficulties of the Government of India. We concede that such difficulties do exist, but it is necessary to point out that the cotton excise duty was not imposed for revenue purposes, that it was levied purely to propitiate Lancashire and that the amount of revenue received has substantially increased during recent years in consequence of higher prices of piece-goods as the result of war conditions. It may be of interest to note that the average annual revenue from cotton excise duty for five years preceding the war was only Rs. 48,44,100. In other parts of the Report, recommendations have been made to abolish certain duties which were levied expressly for revenue purposes, and the following statement shows the effect of such recommendations on the revenues of the Government of India.

Abolition of export duty on tea	...	...	60 lakhs.
Abolition of import duty on machinery	...	...	105 lakhs.
Abolition of import duty on raw materials	...	...	61 lakhs.
Abolition of import duty on coal	...	...	5 lakhs.
Abolition of import duty on hides and skins	...	...	62 lakhs.
			<hr/>
			293 lakhs.
			<hr/>

A further recommendation is that semi-manufactured goods used in Indian industries should be taxed as lightly as possible. The estimated income from articles wholly or mainly manufactured is Rs. 4,77,00,000 which will, if the recommendation is accepted, be reduced by an amount which can hardly be negligible.

24. It will be observed that revenue considerations have not deterred our colleagues from recommending the abolition and reduction of those duties which have been specifically imposed for revenue purposes, nor have they prevented them from recommending payment of bounties and subsidies. It is only when the question of abolishing the cotton excise duty is concerned, that their keen solicitude for Government revenues manifests itself. It has already been pointed out that cotton excise duty is not levied for revenue purposes, that there is an overwhelming feeling amongst the Indian

public to abolish this duty and that the Government of India have already declared their intention of removing it. It has been unanimously decided that the Commission is not in a position to determine what amount of protective duty is necessary in regard to any article and the duty of enquiring into and making recommendations on the subject has been left to the Tariff Board. The whole case for excise duties has been based on the revenue requirements of the Government of India. It appears to us that the real remedy to put Imperial finance on a sound basis is to take immediate measures to fill the reservoir of India's national wealth from which State revenue can be easily drawn. The best way to replenish the reservoir is to stimulate industrial development by a policy of protection. We may quote in this connection the case of the United States of America and Japan.

The following statement furnishes the growth of state revenues in those countries.

UNITED STATES OF AMERICA		JAPAN	
Year	Duties Collected	Year	Duties Collected
	Millions of dollars		Thousands of Yen
1870	191.5	1916	33,822
1875	154.5	1917	33,019
1880	182.7	1918	61,696
1885	178.1	1919	69,435
1890	226.5	1920	74,414
1895	129.6		
1900	229.4		
1905	287.1		
1910	326.3		
1920	308.0		
1921	275.0		
1922	330.0		

The above figures speak for themselves. In our opinion, therefore, the real remedy is to improve the economic condition of India by promoting its industrial advancement and not by imposing excise duties on local manufactures.

25. The revenue duties—and 11 per cent on textiles is a revenue duty—have been imposed without reference to their protective effect and such duties have been levied irrespective of their effect on local manufactured goods. A duty of 15 per cent is

imposed on articles wholly or mainly manufactured, 25 per cent on sugar and 30 per cent on silk piece-goods. Though sugar may well be regarded as an article of luxury and on which excise duties are levied in some countries and silk piece-goods are classified amongst articles of luxury, no excise duty is levied on any of these articles. It is difficult to understand why our colleagues have shown in view of all these facts so much concern about cotton excise duty which was admittedly imposed not for revenue purposes but for other well-known reasons.

26. As already pointed out, the British Government has not imposed any excise duty on such an article of luxury as motor cars when she levied so high a duty as 33 and one-third per cent on their import. If the Government of India desire to maintain an import duty of 11 per cent on textiles for the same reasons as they levy import duties on other articles they may retain it at that figure. If they consider that they can reduce it to 7·5 per cent or any other figure, they are perfectly free to do so ; but we hold the emphatic view that for maintaining India's self-respect it is necessary to abolish the cotton excise duty.

27. Our colleagues subscribe to the suggestion of a clean slate. If that is so, then the conclusion is inevitable that the cotton excise duty must go. This is the unanimous sentiment of the people of India and should, we think, be given effect to immediately. Whether anything should be written in the slate again after it has been wiped clean must depend upon the policy of excise duties laid down for this country and in regard to which we have expressed our views in the previous chapter.

28. There is one aspect of the question to which special attention should be drawn. When, in consequence of the first gift of £100 millions which India contributed for the prosecution of the war, India was allowed to raise the import duty on cotton textiles to 7·5 per cent without raising the excise duty on cotton piece-goods manufactured in India, a storm of protest was raised by the Lancashire interest in Parliament which led to much embitterment of feeling in India. Again, in 1921, the needs of revenue became insistent probably owing to the loss sustained by the policy of Reverse Councils and the import duty on cotton textiles was raised to 11 per cent. The agitation which was carried on in England is well-known. The Report records the facts in the following words :—

"The whole question is permeated with suspicion and resentment ; and these feelings have been kept alive by the action taken by the representatives of the Lancashire cotton industry in 1917, in 1921 and again within the last few months, the system which their influence had for so many years imposed upon India."

29. We should like to invite attention to the political effects in India of such agitation by Lancashire representatives. It is, in our opinion, essentially necessary that cordial relations should subsist between India and England. The imposition of cotton excise duties is one of the principal causes of estrangement between the two countries. Far-sighted statesmanship demands that this cause should be removed. The Indian sentiment on the question is decisive. The evidence placed before us conclusively proved this. It would be unwise to deal with the question by resorting to expedients which will not be acceptable to the Indian people. The best mode of promoting cordial relations and better understanding between the people of the two countries is boldly to face the problem and in a spirit of political sagacity to abolish the cotton excise duty at once. It is needless to point out that unless this course is adopted, Lancashire will not cease to agitate on the subject and such agitation will be a constant source of ill-feeling between the two countries.

Imperial Preference.

30. We recognise that Imperial Preference is a means of strengthening the ties amongst a Commonwealth of Free Nations. The exchange of trade amenities, not in a spirit of bargain, but as a free gift, has the effect of cementing the bond amongst free nations forming a Commonwealth. It may be pointed out in this connection that the Dominions conceded the principle of preference after they had attained full responsible government "*consistent with their own interests and not injurious to themselves.*" Great Britain followed in 1919 and "*introduced a preferential system. She gave freely such preferences as she felt could be granted consistently with the interests of her own people and the requirement of her own fiscal policy.*" Great Britain and the Dominions are able to regulate the policy of Imperial Preference on these lines because they are politically and fiscally free. The principle of Imperial Preference implies the uncontrolled power of initiating, granting, varying and withdrawing preference from time to time consistently with each country's interest and on lines which are not injurious to itself. India must therefore possess the same supreme powers as are enjoyed by the Dominions before Imperial Preference can become for her a matter of practical politics. India has not yet reached Dominion status. She is in a transitional stage; her Government is not responsible to her Legislature but to the British Parliament. Any acceptance in practice of the principle of Imperial Preference would make her liable to measures of preference at a time when she is not entitled to determine them

by the vote of a wholly elected Legislature with her Government responsible to such Legislature as is the case in all the Dominions.

31. It is an admitted fact that the Dominions have regulated preference as it has suited them from time to time. The British policy in regard to the grant of preference to Indian tea has been on the same lines. We do not wish to enter into the controversy as to whether reduced import duty on Indian tea is real preference or not. In 1915, a resolution was moved in Parliament asking for a reduction of import duty on Indian tea. The mover clearly disclaimed any idea of basing it on Imperial Preference, but urged the reduction on the ground that as the Indian tea was consumed by the poorer classes, it would be a relief to them. Mr. Lloyd George, who was then the Chancellor of the Exchequer, opposed the resolution on the ground that it would be construed as preference and might lead to retaliation by China which was a large buyer of Lancashire goods. The point to which we wish to draw special attention is that while a preference of 2d. per pound was granted in 1920-21, the budget estimates for 1921-22 reduced it to 1 and half pence. We mention this in order to confirm the principle underlying Imperial Preference that the country granting it has full power of initiating, granting, varying and withdrawing preference as it suits the interests of its own people. Such power India does not possess at present. It does not enjoy the powers which a member of the Commonwealth possessing Dominion status does. The logical conclusion, therefore, is that India cannot accept the principle of Imperial Preference until she has attained responsible government, and is able to regulate her fiscal policy by the vote of a wholly elected legislature.

32. The Report summarises the present economic condition of India, and the conclusion arrived at is embodied in paragraph 257. After recording the fact that most of the witnesses expressed themselves against the principle of Imperial Preference, it states that

"a second argument which has weighed with many witnesses is that preference is equivalent to the grant of a bounty to the British manufacturer at the expense of the Indian consumer, that India is poor while British is rich, and that it is not reasonable to expect the poor country to make a gift to the rich one. We have explained that in our opinion this view of the question is not unreasonable, and that any general system of preference would undoubtedly impose an additional burden on the Indian consumer, which we do not think it fair that he should be called upon to bear. This argument might be met by the assertion of a second principle, namely, that Imperial Preference should not involve any appreciable loss to India."

33. India cannot be called upon at present to suffer any economic loss as she is poor and as the consumers will have to bear a certain amount of burden in the larger interests of the country under

a policy of protection which we are recommending. If this policy is given effect to immediately, it is likely to become fruitful within the next few years and the economic condition of the people will improve. India by that time will have attained responsible government, which has been promised to her; then as a Self-Governing Member of the Commonwealth she will, we feel confident, be ready to adopt a policy of Imperial Preference.

34. Paragraph 255 of the Report records the fact of the

"almost complete unanimity with which Indian witnesses opposed the principle of Imperial Preference."

One of the principal reasons for this opposition is, in our opinion, the fact that India is not free, *i.e.*, does not enjoy Dominion status in the Empire. The Hon'ble Lala Harkishen Lal pointed this out in his evidence. He expressed himself in favour of the principle of Imperial Preference on the distinct condition that the political status of India should be the same as that of the other partners in the Empire. Captain Sassoon also favoured the principle but conditionally upon the right of India to withdraw such preferences when her interests required her to do so. It will be obvious that Indian sentiment is practically unanimous against Imperial Preference in view of India's present political status in the Empire. The conclusion is therefore inevitable that this question can only become a matter of practical politics when the promised goal of responsible government is reached.

35. It may well be argued that while subscribing to the principle of Imperial Preference our conclusion leads to the postponement of its application to the time when India attains her full status in the Commonwealth. This is practically the unanimous view of the people of India. We are, however, of opinion that the Indian view would be favourably inclined to accept the immediate application of the principle provided conditions are created to place India at once on the same footing as the Self-Governing Dominions in this matter. It may be pointed out that in 1918 when the Government of India proposed a further gift of about £45 millions to Great Britain for the prosecution of the war, they left the decision to the vote of the non-official members of the Imperial Legislative Council. It is therefore possible even under the political status which India now enjoys to so arrange matters as to bring about in practice the position which the Dominions occupy. We will therefore recommend that the power of initiating, granting, varying and withdrawing Imperial Preference in regard to every article should vest by legislation or other equally effective means in the non-official members of the Legislative Assembly. They will thus be empowered by non-official vote to regulate the policy of Imperial Preference with

perfect freedom on the same lines as those enjoyed by the Self-Governing Dominions.

36. In paragraph 225 of the Report, it is stated

"when the country receiving the preference supplies practically the whole market, then the price to the consumer will be regulated by the lower rate. The bounty to the foreign manufacturer will cease and the consumer will get the benefit of the lower rate."

In paragraph 226 it is stated that

"after the preference is given, the price to the consumer for a time may be regulated by the higher rate of duty and the manufacturers of the favoured country will receive, as has been already explained, a bonus of the difference between the two rates. The effect of this bonus is to stimulate the trade of the manufacturers of the country receiving the preference and in a short time they may secure for themselves the whole market, driving out altogether the non-preferred manufacturers. The price to the consumer will then be regulated by the lower or preferential rate of duty, and the favoured manufacturers will find the price falls to the true competitive level. But they have not thereby lost the whole benefit of the preference. Their gain is represented by the additional quarter of the market which they have secured for themselves at the expense of their non-preferred rivals. Thus they benefit even when the consumer has ceased to suffer."

37. It is contended that when the whole supply arrives from the preferred country the consumer will cease to suffer. This is contingent upon there being in the preferred country sufficient internal competition to regulate the price on a competitive basis. In dealing with the policy of protection attention has been drawn to the danger of a possible combination of manufacturers for the purpose of exploiting the domestic consumer. It is further stated (paragraph 86) that a protectionist system certainly gives an opportunity for undesirable forms of combination.

"In a free trade country no combination of manufacturers is able to keep price of a commodity above the world price. If all the manufacturers of a particular country agreed not to sell below a certain price the only effect would be that their home market would be captured by the foreign manufacturers selling at the world price. The case of the protectionist countries is different. Here we have a tariff wall affording, when the foreign manufacturers have been partly or wholly excluded, a certain latitude of price to the home manufacturers. If the latter do not combine, the home price will be regulated by the ordinary conditions of internal competition. But by means of combinations, it is possible for the home manufacturers to keep the price distinctly above the true competitive level without inviting foreign competition."

The Report points out various remedies to be applied in the event of such a combination materialising in India. Under Indian conditions such combinations are a remote contingency but in advanced countries they are far more possible. Applying this analogy to preferred countries the Indian consumer is likely to suffer heavily when by means of preference the competitive foreign manufacturers have been excluded and the prices are maintained

at a high level. The case of the monopoly in "shipping" is a clear instance in point. The Indian people have to pay comparatively higher rates of freight because competition has been eliminated and a practical monopoly has been created. Combinations of manufacturers in India would be easily known and the Indian Government can devise adequate measures to counteract their evil effects on the consumer. When, however, competitive foreign manufacturers have been eliminated and the whole Indian market becomes the monopoly of the manufacturers of a preferred country, the consumers may be penalised to a heavy extent and the Government of India may be powerless to take immediate and effective measures to counteract the evil. The remedy would of course be to withdraw preference, but the foreign manufacturers having lost the important Indian market may have reduced production and may not find themselves in a position to re-enter the market to the benefit of the Indian consumer. There is, therefore, clear danger in the grant of preference and the loss to the consumer in India may not prove to be temporary as stated in paragraph 227.

38. In paragraph 231, attention is drawn to a possible advantage to India in the matter of her export trade. It is stated that

"if the preferences are important, this will tend to build up direct shipping connections between the two countries, and as a consequence will give the exporters of the country granting the preference some advantage in the market of the country receiving the preference. In other words, if imports are attracted from a particular country, they will be a tendency for exports to be attracted to that country."

We are not satisfied whether in view of the actual trade between India and England any such advantage will accrue. There is a danger that such a policy may penalise the Indian producer, by reducing the number of buyers, competition amongst whom maintains a standard of world prices for Indian produce. It may also be remarked that there is a very strong feeling amongst the Indian people in favour of an Indian mercantile marine. Reference has been made in the Report in paragraph 131 to this feeling and recently it found expression in the Central Legislature. Nothing should in our opinion be done which will have the effect of retarding the establishment of a mercantile marine in India, or of making its success doubtful.

39. We regret that our colleagues should have pleaded for Imperial Preference on the ground amongst others of maintaining the British Navy. We feel that the question of naval defence of the Empire stands on an entirely different footing, and ought not to have been brought forward in this connection. It might have the effect of reviving a political controversy which is best avoided at the

present juncture. In our opinion the question stands on Imperial sentiment alone and should be examined from that point of view. The defence of the Empire depends upon various other standpoints, and the maintenance of the Indian Army which has served the interests of the Empire in the various parts of the world will have a pronounced bearing on the issue. As the question has been raised we will content ourselves by remarking that the economic prosperity which we anticipate as the result of extensive industrialisation will in course of time enable India to maintain in Indian waters a navy sufficient for the defence of India, officered and manned by Indians. It will also prove a valuable Imperial asset.

40. Having drawn attention to the possibilities which a policy of Imperial Preference may lead to, we leave the matter with full confidence in the hands of the non-official members of the Legislative Assembly in the conviction that as representatives of the people of India and fully conversant with Indian sentiment they will give effect to it in a manner consistent with Indian interest in all its aspects.

41. We wish to make it perfectly clear that we have dealt with the question of Imperial Preference as between England and India and not as affecting the British Dominions and Colonies. We are unanimous in thinking that a different policy should be adopted in regard to trade relations with other parts of the British Empire.

Our colleagues recommend in paragraph 264 that

"Hitherto, in discussing the question of Imperial Preference we have confined our consideration to preferences granted to the mother country. With regard to other parts of the Empire, we would recommend a different policy. We suggest that to the United Kingdom should be offered such preferences as India may find she is able to offer without appreciable injury to herself. With regard to other parts of the Empire, we recommend a policy of reciprocity such as is already adopted by more than one Dominion for inter-Dominion trade relations; that is to say, preferences should be granted only as the result of agreements which might prove to the mutual advantage of both parties. In this connection, India would doubtless not be unmindful of the fact that she already enjoys the benefit of certain concessions granted by Canada and New Zealand. The agreements which we contemplate would be purely voluntary; there would be no kind of obligation on India to enter into them unless her own interests appeared to demand it; and it is evident that political considerations could not be excluded in determining whether it was desirable for India to enter into an economic agreement or not."

In the next paragraph 265, it is stated that:

"We think it is necessary that there should be laid down for India some policy of the nature outlined above in regard to trade relations with other parts of the Empire. We have already mentioned that India receives preferences from Canada and New Zealand. We understand that proposals for reciprocity were received in 1919 from one of the Dominions. We have been recently informed by the Canadian Government Trade Commissioner to India that a preference on motor cars granted to Canada would stimulate the present tendency for the well-known makes of American cars destined for the Indian market to be made in

Canada and would be regarded as a graceful reciprocal act on the part of India. It seems probable that this benefit could be conferred on Canada without any appreciable loss to India."

42. We cannot agree to any trade agreements being entered into with any Dominion which discriminates against the people of this country. We believe we are voicing the unanimous opinion of the people of India when we say that no agreements based even on reciprocity in trade matters should be entered into with any Dominion which has on its statute book any anti-Asiatic legislation applying to the Indian people. Our colleagues point out the fact that Canada and New Zealand have conferred certain preferences on India. To the Indian people their self-respect is of far more importance than any economic advantage which any Dominion may choose to confer by means of preferential treatment. We may confidently state that the people of India would much prefer the withdrawal of such preference as they would not care to be economically indebted to any Dominion which does not treat them as equal members of the British Empire having equal rights of citizenship.

43. We are not opposed to negotiations being opened for trade agreements on a reciprocal basis, but the condition precedent must be the recognition of the right of Indians to equality of status. The first principle of Imperial solidarity must, in our opinion, be equal treatment of all nations forming part of the Empire. The facts as regards the treatment meted out to Indians are too well-known to be mentioned here. We will therefore content ourselves with recording our emphatic view which we think reflects the feeling of the whole country that no trade agreement should be entered into with any Dominions unless it agrees to treat the Indian people on a footing of equality and to repeal all anti-Asiatic legislation in so far as it applies to the people of this country.

44. We will now summarise our conclusions in regard to Imperial Preference :

(i) We are in favour of the principle of Imperial Preference on the distinct condition that India should in this matter be put on the same footing of freedom as is enjoyed by the Self-Governing Dominions, and that the non-official members of the Legislative Assembly should be given power by legislation or other equally effective means to initiate, grant, vary and withdraw preference as may be necessary in the interest of India in all its aspects.

(ii) That the condition precedent to any agreement with a British Dominion in trade matters on the basis of reciprocity should be the recognition of the right of the Indian people to a status of complete equality and the repeal of all anti-Asiatic laws so far as they apply to the people of India.

Foreign Capital

45. The only exception which our colleagues make in recommending free and unconditional introduction of foreign capital

after the policy of protection is adopted and a tariff wall is erected is contained in paragraph 292 which reads as follows :—

"We think, however, that where Government grants anything in the nature of a monopoly or concession, where public money is given to a company in the form of any kind of subsidy or bounty, or where a license is granted to act as a public utility company, it is reasonable that Government should make certain stipulations. Where the Indian Government is granting concessions or where the Indian tax-payers' money is being devoted to the stimulation of an enterprise, it is reasonable that special stress should be laid on the Indian character of the companies thus favoured. In all such cases we think it would be reasonable to insist that companies enjoying such concessions should be incorporated and registered in India with rupee capital, that there should be a reasonable proportion of Indian Directors on the Board and reasonable facilities should be offered for the training of Indian apprentices at Government expense."

46. We are unable to appreciate the distinction drawn between companies getting Government concessions and companies establishing themselves behind the tariff wall erected under the policy of protection. We can understand such a distinction under a policy of free trade. The Government of India have, as pointed out in the Report, laid down the following policy under the free trade conditions :—

"The settled policy of the Government of India is that no concession should be given to any firms in regard to industries in India unless such firms have a rupee capital, unless such firms have a proportion, at any rate, of Indian Directors, and unless such firms allow facilities for Indian apprentices to be trained in their works."

47. The distinction to be drawn on the question under a policy, of free trade and that of protection is obvious. In the former case the grant of concession is a favour justifying the laying down of special conditions. This was done by the Government of India. Under a policy of protection, the right to establish an industrial enterprise behind the tariff wall is a concession in itself. There is really no distinction between Government granting subsidies or bounties out of money collected by them by way of taxation and allowing an industry to tax the people directly by means of higher prices resulting from protective duties. In both cases, it is the people of India who have to pay the price either as tax-payers or as consumers. Industrial concerns benefit either directly from Government subsidies or bounties or indirectly by higher prices due to protective duties. If the imposition of conditions is justifiable in the one case, it is equally justifiable in the other. Our conclusion therefore is that every company desiring to establish an industry after the policy of protection has been adopted in India should be subject to the same conditions which are recommended by our colleagues, *viz.*, that all such companies should be

incorporated and registered in India with rupee capital, that there should be a reasonable proportion of Indian Directors on the Board and that reasonable facilities should be given for the training of Indian apprentices.

48. There are special reasons why all industrial companies should be incorporated and registered in India with a rupee capital. In this connection, we should like to quote Sir Frederick Nicholson. He says :—

"I beg to record my strong opinion that in the matter of Indian industries, we are bound to consider Indian interests firstly, secondly, and thirdly I mean by firstly, that the local raw products should be utilised, by secondly, that industries should be introduced, and by thirdly, that the profits of such industries should remain in the country."

Our colleagues have stated in paragraph 293 that in their opinion "whether the immediate profit goes to a foreign or an Indian capitalist, the main and ultimate end, namely, the enrichment of the country will be attained." We may point out the fallacy underlying this argument. The enrichment of the country depends, in the words of Sir Frederick Nicholson, upon the profits of the industry remaining in the country. National wealth can thus be increased in a shorter period of time than by the taking away of industrial profit to foreign countries.

49. It appears to us that there is some confusion in the treatment of considerations relating to capital contained in the Report. Loan capital and ordinary capital are mixed up. It is only in regard to this latter form of investment that there can be room for difference of opinion, and the balance of advantage has to be ascertained. Our colleagues point out the advantages of a rapid development of industries as conducing to the relief of consumers. We are unanimous in thinking that in the interests not only of the consumers but of the economic advancement of the country, it is essentially necessary that industrialisation should proceed at a rapid pace. It is because we apprehend that the progress will be slow that we have demurred to the stringent conditions which our colleagues have attached to the policy of protection and the qualifications with which they have circumscribed it. We will, therefore, state at once that we would raise no objection to foreign capital in India obtaining the benefit of the protective policy provided suitable conditions are laid down to safe-guard the essential interests of India.

50. We must not be understood as subscribing to the reasoning adopted by our colleagues in agreeing to the introduction of foreign capital in India behind the tariff wall. We should like to draw attention to the following extract from paragraph 289 of the Report :—