Subsidies must give way to a universal basic income: Pranab Bardhan

The development economist on the Modi government’s initiatives and his stand on them, and MGNREGS

Mumbai: The Narendra Modi-led government should consider replacing inefficient subsidies with a basic monthly income for all citizens, says Pranab Bardhan, emeritus professor of economics at the University of California at Berkeley. Bardhan, who recently sparred with economists Jagdish Bhagwati and Arvind Panagariya in a debate over the Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS), says the programme is better targeted towards the poor than many other government welfare programmes.

Among the foremost development economists of the world, the 75-year-old studied at the University of Calcutta before doing his Ph.d at Cambridge. Bardhan’s 1984 book on the political economy of India is considered a classic text. Bardhan, who was in Mumbai to attend a conference organized by the Indira Gandhi Institute of Development Research, spoke exclusively in an interview on the Modi government’s initiatives, and his stand on them. Edited excerpts:

What do you make of the policies of the new Indian government so far? Do you see more continuity or change?

As in most things, I see both continuity and change. In fact, some of the announcements that have been made are continuation of earlier policies. The Swachh Bharat Abhiyan, announced with much fanfare and broom-wielding by politicians stepping out of their limousines, for instance, is largely the same as the Nirmal Bharat Abhiyan the earlier government had launched. This government has probably more energy and will probably do more, but one has to understand issues such as why toilets built in the earlier programme did not get used. One obvious reason is the absence of regular water supply to keep toilets usable. Even without that problem, there are several social and cultural issues that come up, which cannot be solved merely by bureaucratic fiat.

For instance, why is it that the toilet programme has succeeded much more in Bangladesh, a poorer country, than in India? One does not really know, but a part of the answer may be that as in other social programmes in Bangladesh these are not just sarkari (government) programmes foisted from above. Non-government organizations (NGOs) got involved in working with the common people on these projects. Another answer that has been given by some, and which we should discuss and find out more about, is that Hindu culture instills some aversion to cleaning toilets. For centuries, our toilets have been cleaned by people who have occupied the lowest and most degraded rungs of the social hierarchy.

So, even if you give people toilets but they are not willing to clean it, they will remain unused. This is less true of primarily non-Hindu societies like Bangladesh. The new government’s energy to solve this issue is welcome but they must understand (and that's where the continuity part comes in) why the earlier programme did not work.

Similarly, one programme that the government has announced, and which I am generally in favour of, is the Jan-Dhan Yojana. But here, too, the government must understand why more than 40% of households have so far lacked banking access. It is difficult to reach out to remote areas of the country. The idea of bank accounts with overdrafts for everybody is also problematic. This will amount to loan waivers which will weaken the banks. If you want to help the poor, give them unconditional transfers out of public revenues, if you like, but not at the expense of the public sector banks’ viability.

There are some who say that no-frills accounts for the poor can become viable if there is a move towards direct cash transfers. The earlier government tried but gave up on it. Do you think this is something the new government should push aggressively?
We must distinguish between two kinds of cash transfers: transfers to producers and transfers to consumers or citizens. I think producer subsidies such as fertilizer subsidies should be transferred as cash directly to producers. Today, fertilizer subsidies are both regressive, benefiting richer farmers more than the poor, and inefficient, with a part of the subsidy going to inefficient fertilizer firms.

There will be opposition if you try to reduce such subsidies. So as a first step, the subsidies must be converted to cash transfers, which is somewhat politically easier, and which will make the subsidy transparent. If I may be flippant, even the perks and allowances which ministers and their families receive, such as free flights and free medical treatment, should all be given in cash, so that you and I know how much each minister costs the country. Transparency will make it easier to reduce such subsidies over time. Even consumer subsidies such as those on LPG (liquefied petroleum gas) cylinders, which benefit mostly the richer sections, should be eliminated.

Instead, I would favour some kind of universal citizen transfers. Estimates show that total non-merit subsidies funded by both states and the Centre amount to roughly 9% of India’s gross domestic product (GDP), which largely benefit the better off—the dole for the rich and middle classes. So, I have advocated the following kind of deal: if we can persuade the better-off people to give up only one-third of these subsidies, calculations show it is possible to provide each household more than 1,000 per month. And you won’t even need to raise fresh taxes.

So you favour something like a universal basic income?

Yes. This is the idea of a universal basic income, and it was originally suggested by some French thinkers in the nineteenth century. This is very much on the agenda of green parties in Europe today. This is even more important in India because we mess up on distinguishing the poor from others. Below poverty line (BPL) lists in most states exclude many poor people while many well-off families manage to bribe their way in. Even the Aadhaar programme, which I am in favour of, will not solve the problem because the Aadhaar card won’t tell you if the person is rich or poor. But if you move towards universal transfers, you can avoid the inefficiency and corruption in classifications such as BPL. Of course, mere cash transfers are highly unsatisfactory in case of healthcare. The universal programme I am in favour of in that sector is that of a single-payer universal healthcare system.

You have been involved in a debate on the MGNREGS. Why do you think the programme should be retained despite leakages?

Those of us who support MGNREGS are not saying that there are no problems. Many problems such as delay in payments, corruption, irregularities in materials, etc., persist, though there is some evidence that these problems are declining over time in many parts of the country. But despite its problems, it is an effective conditional cash transfer programme when you come to think of it. The condition is that you have to work manually, which immediately excludes the middle class and the rich. And it acts as a safety net for the rural poor who find it difficult to get work in the lean season. The sheer existence of an alternative improves the bargaining power of landless labourers.

There are leakages, and the programme needs to be improved. But the leakages are very small compared with the subsidies to the rich. The entire programme costs only 0.4% of GDP. Even if you assume that half of it is stolen, which I don’t think is true, it still costs only a tiny fraction of the subsidies spent annually on the rich. So I think there should be some sense of proportion, which people tend to lose, in this debate.

There are also those who oppose MGNREGS because they believe it is raising wages but I tell them that any poverty eradication measure will raise the bargaining power of the poor, and hence their wages. If you are against MGNREGS raising wages, you must be consistent and oppose any poverty eradication effort!

So, I am a bit worried about the government’s attempts to dilute MGNREGS provisions surreptitiously rather than through openly debated amendments to laws that were passed with the BJP’s (Bharatiya Janata Party’s) support earlier. The same kind of changes by means of various notifications, a form of reform by stealth, are happening in case of environmental clearances and the legislated need for consent of local people.

What do you think of the Make in India campaign? Do you think India has already missed the manufacturing bus, given that economists such as Dani Rodrik seem to suggest that the days of manufacturing are over?

I hope Make in India is not what the Swadeshi Jagran Manch used to ask for. If it is about swadeshi in another incarnation, then it goes against trade liberalization. Before trade liberalization, Indian producers had to use domestically made intermediate goods, which were inefficient, rendering finished products costly and uncompetitive. One of the ways in which trade liberalization improved productivity was that it allowed producers to use more efficient imported materials and components.

As long as they are in favour of trade liberalization, I welcome efforts to boost manufacturing. I don’t completely agree with the reported view of Dani Rodrik that the days of manufacturing are over. Yes, there are some countries where manufacturing has peaked. But for countries such as India, China, and Indonesia with large domestic markets, there is still a huge scope for manufacturing. Think of the huge increase in demand for light manufactured items when living standards in the rural areas of states such as Odisha, Bihar, UP, and Madhya Pradesh improves. What is disconcerting is that India is not able to get into manufacturing products in the global value chain that China is getting out of.
Countries such as Bangladesh, Vietnam, and Indonesia are ahead of us in making those products.

Are our labour laws to blame for this?

The labour regime is a constraint but as I have written earlier, it may not be the binding constraint. I looked at the data on a very labour-intensive industry: garments. Now, if labour laws are the binding constraint, you will expect to find many firms just below the threshold level of 100 workers beyond which stringent labour regulations kick in. But the data do not show that. There is instead bunching at a very low level: at around the eight-employee mark. So, the question really is what prevents an eight-employee firm from becoming an 80-employee firm.

If you ask an eight-employee firm’s owner what prevents him from expanding, he is likely to tell you that if he were to expand, and invest in better machines, he will need to assure himself of regular power supply. So, the binding constraint, in my view, may well lie in the poor quality of infrastructure in India, whether it be power, roads, or ports.

China’s success in manufacturing is a classic example of infrastructure-led growth. Most people don’t know that long before China initiated economic reforms, it had already created the base for an industrial boom by investing heavily in the power sector. Under Mao, China carried out a lot of rural electrification, whereas even today, half of the households in our villages don’t use electricity. Of course, China also invested heavily in health and education and that created a much more productive workforce. But even in infrastructure, China had already solved its problems much earlier, in the Maoist period.