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SAVINGS IN INDIA: SOME BROAD REFLECTIONS

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1. Accuracy of Savings Estimates

IN recent years, it may be stated, our estimates of saving (at current prices) are perhaps more accurate than any other macro-economic magnitude. The reason is that with increasing monetisation of the economy, the element of direct labour (or material) input for capital formation—which is, of course, subject to unknown error because of the absence of cross-checks—is now a relatively small proportion of total saving/capital formation.

There are, of course, several possibilities of error in the estimates of saving. To understand the degree of error in the estimate of saving, one has to examine the source material for the three sectors: government, corporate sector and households (including unincorporated enterprises).

One may expect the estimate for the government sector to be reasonably accurate except that the availability of accounts of local authorities is not adequate. Indeed, increasingly, one should take note of the functioning of the 'panchayats', which should be treated as part of the government sector. However, the panchayats do not so far have any significant taxation powers, and hence have no saving; municipalities have, if anything, negative savings made good by subventions from State Governments. In practice, no deduction is made for the possible negative savings of municipalities, and to that extent there may be a slight exaggeration in the estimate of government saving.

On the other hand, there are increasingly new types of government expenditure under the Rural Development Department of the Ministry of Agriculture, which are really of the nature of capital expenditures but may not be treated as such in the national income accounts. To the extent that funds under the RLEGP/NREP/DPAP and similar programmes lead to payments for direct capital formation in the rural areas, such expenditures from the Revenue Budget should be treated as 'saving' by government, spent for capital formation in the rural areas. I am not sure whether and to what extent this is already being done; there is a possibility of such expenditures being treated as 'transfer payment', since they are popularly known as 'subsidies' for the poor. Incidentally, such capital formation—e.g., by way of kutcha roads—may have a high rate of obsolescence, but that is another matter. The gross and net investment figures, as well as savings, would presumably need to be improved in this context.

Next, we come to the estimate for the corporate sector which is derived by blowing up an estimate of corporate saving obtained from a sample analysis of balance sheets of approximately 2000 large and medium companies. The problems here are several. The accounting years of the companies vary. So do accounting practices; and several procedures such as writing back depreciation provision made in the past into current profit and loss accounts can introduce errors in the estimates. Hence, much more than the problem of the procedure adopted for blowing up the sample estimates (by the amount of paid-up capital of companies analysed in relation to total paid-up capital). the varying accounting years as well as varying accounting practices adopted by companies can distort the estimate of corporate saving. The Reserve Bank of India has lately been attempting to introduce corrections for changes in accounting practices from year to year, and thereby reduce the possibility of error therefrom. Nonetheless, the estimates of corporate saving remain subject to an unknown margin of error.

The direction of error in the RBI estimates cannot be assessed. However, to the extent that corporate savings are a small proportion of total savings, the error involved in the estimate of total saving may not be very large.

In regard to household saving, the estimates are derived largely from the totality of financial savings in the community from year to year (including savings in the form of currency) adjusted for an estimate of such financial instruments of saving acquired by the 'government' sector or by the corporate sector, *and* direct saving in the form of physical assets, by households. The latter form of saving occurs primarily in the rural areas, though direct investment by unincorporated enterprises on plant and machinery, etc., without recourse to financial intermediation, would also be part of such saving. These savings invested directly in physical assets (as a percentage of total savings) have been declining lately. As stated earlier, this lends greater assurance to the over-all estimate of saving, because the data on financial instruments are reasonably firm.

The derivation of estimates of saving by households, in the form of financial instruments of saving, is subject to error because the holding of currency as well as diverse financial instruments by both 'government' and by the corporate sector is only roughly estimated, the balance of the incremental amount of all such savings instruments being treated as household saving. (For instance, even the ownership of time deposits with banks is imperfectly known, there being a large chunk of 'unclassified' owners. These could be non-profit-making institutions—treated as part of the household sector—or municipalities, or even other financial institutions).

However, once again, the error likely to arise herein may not be significant, though unfortunately the non-formal financial intermediates have a very shaky base in our national accounts. In fact, we do not know even whether the actual size of the non-formal financial intermediaries sector is close to what is being estimated.

There is, of course, a strong possibility that both the income originating in and the savings of the unincorporated enterprises sector may be grossly under-estimated of late. There is evidence that a modern small sector is fast emerging in many parts of the country. Much of the output of this sector is not recorded in official statistics, and it is possible that the savings of this sector also—directly invested into the same or similar enterprises—are not fully recorded. There is some possibility, there fore, that both output and savings of unincorporated enterprises are not fully reflected in official statistics. Efforts need to be made to catch this element through special surveys, in areas of concentration of the modern small-scale industry. These are fairly well known and are capable of identification.

There are two further problems which arise. In the first place, our savings estimate includes savings arising from remittances from expatriate Indians working abroad. *These are not part of domestic savings*, though they may still be deemed to be national saving (or the saving of Indian nationals abroad). There are no means available at present of precisely determining the extent of such saving. Since remittances from expatriates are sizeable, we need to take note of this point, because *our domestic savings are to that extent less.*

The second problem arises from the possibility of unrecorded (black) incomes and savings therefrom. Two issues arise herein. To the extent that unrecorded or black incomes are saved in the form of currency—or in the form of bearer bonds like the Indira Vikas Patra—they get covered in our estimate of saving. To the extent that such savings are kept in the form of smuggled gold or jewellery made therefrom, our savings are underestimated (except that acquisition of jewellery may be deemed to be consumption rather than saving). Smuggled gold could be treated as a hoard, but in fact, it leads to the generation of further black income. The considerable income—and consumption—from activities like smuggling are in any case missed out from our national accounts.

Finally, we do not have any estimate of the flight of capital from the country, for which diverse estimates are available. In technical parlance, such export of capital should be treated as such; however, to the extent that such capital may never come back, the income accruing from that capital being spent abroad, we may have to ignore this magnitude and not treat it as saving invested abroad. The large 'errors and omissions' in the balance of payments statistics are, however, *not* connected with capital flight. The usual technique for the siphoning off and the stashing of funds abroad are under-invoicing of exports and over-invoicing of imports (Cuts or commissions on purchases abroad may be lumped with over-invoicing of imports.)

With all these defects, it may still be reasonable to assert that our savings estimate is more accurate than our estimates of capital formation which depends on diverse proportionalities for classification of certain products as meant for final consumption or capital formation (e.g., vehicles, typewriters, air-conditioners, other office equipment which could also be used for household consumption).

2. Saving in Real Terms

In macro terms I=S. Hence, the deflator for investment becomes, in effect, the deflator for saving. The only problem herein is that in India

$$I = Sd + Si$$

where Sd = domestic saving
Si = imported saving

Over some years past, Si has been 1.5 to 2 per cent of the GDP where Sd has been around 22 per cent of the GDP. That is, Si is less than 10 per cent of Sd. Hence, unless we have reason to believe that the prices of capital goods abroad and in India are moving in different directions—and there is no reason for this belief—the deflator for capital formation would be a reasonably good deflator for domestic saving. One would also need to think over the "terms of trade" effect—in the matter of debt repayment—on imported saving. But that concept may be equally, indeed more, relevant for over-all GDP than merely for the estimate of saving.

There is, in theory, no other satisfactory way of deriving a deflator for domestic saving. There are those who argue that the deflator for Gross Domestic Expenditure would give a better deflator for saving than the deflator for "investment" (again as a deflator for saving), but the former would not give the *ex-post* identity of I = S. Hence, the series of domestic saving in real terms can in practice be derived from the series of domestic capital formation in real terms.

3. Behaviour of Savings and Some Reflections Thereon

Savings increased rapidly during the seventies, but have stagnated thereafter. (Part of the rapid increase may also be ascribed to the rapid increase in remittances from expatriate Indians during the seventies). There is also some evidence that the distribution of income has been getting to be increasingly skewed. Is it possible that the increase in savings (since the seventies) is linked to the increasing inequality in the distribution of income?

There are certain flaws in the above hypothesis. Presumably, the distribution of income has been getting to be increasingly more uneven during both the seventies and the eighties. The savings rate showed an increase during the seventies but stagnation (even some decline) during the eighties. So, one needs to do more empirical research on the sources of savings before coming to any conclusion. Is it possible that the increasing proportion of saving in the form of financial assets in the eighties is a reflection of (*a*) the increasing role of black money (mainly in the urban areas) in the economy, (*b*) increasing inequality in the distribution of income—or is that not even proved?—and (*c*) declining growth of as well as declining return from investment in agriculture?

We need more detailed data on the ownership of financial assets to be able to come to any judgement on the subject. (We are discussing only the sources of saving and their causal relationships; we are not concerned with any value judgement on the fact of inequality here). It does mean that we should attempt, first, an urban/rural break-up of savings and investment, and a source-wise classification of household saving (which includes the savings of unincorporated enterprises).

For an analysis of savings, therefore, we first need to look into the savings behaviour of different sectors. In this context, we need to note the following: (*a*) there has lately been a steep decline in the rate of government saving, particularly in the eighties; (*b*) corporate saving has stagnated at a low level all along and in fact has been declining of late; and (*c*) household saving has shown an increase over time. Since farm output has stagnated lately, it is possible that household savings have come in the main either from the unregistered manufacturing sector or the services sector (including trading activity), and not from the farm sector. This last hypothesis is confirmed by the steep decline observed in 'rural investment' without any financial or monetary counterpart, indicating the possibility of a decline in investment in the rural areas generally. The above implications may be hypothesised as follows : (*i*) there is increasing stagnation—possibily a decline—in savings in the rural areas;

(*ii*) there has been a marked increase in savings by the urban middle (and richer) classes; and (*iii*) the above developments have been reflected in a spectacular increase in saving in the form of financial assets by households. Again, this last development reflects an increase in the savings of the urban classes over a wide range of households and not merely the traditionally rich and well to do.

While the increase in financial asset holding by households has increased both in absolute magnitude and as a proportion of total saving in recent years, some recent surveys (e.g., by the NCAER) have indicated a decline in farm investment in Punjab in recent years. The shift from farm investment to the holding of bank deposits and other form of financial assets (in Punjab) has been hailed as signifying increased monetisation in the economy, in some quarters. In fact, it is perhaps a retrograde step, because it is likely to slow down the growth of farm output. This decline also explains the decline in "real investment" and increase in the holding of financial assets by the household sector.

To conclude, then, the following *possibilities* need to be investigated:

(*a*) Despite increases in the GDP, the rate of saving has stagnated. The increases in GDP have occurred mainly in the tertiary sector. Real output of agriculture has increased relatively slowly. The rate of saving has also stagnated. Is there a link between the two? One has, of course, to attempt a break-up of savings into those by different segments of the population, which is necessary before one can come to any conclusion on this subject. A break-up of savings by different sectors has been briefly indicated earlier, with certain implications which have been noted already.

(*b*) There is evidence of an increase in untaxed incomes. How much of it arises in the modern small-scale manufacturing sector and how much in services? There seems to be some link between increased deployment of saving and increased output in the modern small-scale sector. But where do the savings of the services sector get invested? Inventory holding is one possibility. But what about the cash savings of this sector? Are these going primarily into increased holding of financial instruments of saving?

(*c*) To get an answer to some of these questions, we need an analysis of the holders of financial instruments of saving. What is the best way of proceeding in this type of study? The RBI data pertain to earlier years and relate only to bank deposits. What about the ownership of other forms of financial assets?

(*d*) Can we get the banking sector to segregate the savings from remittances from expatriates (and their investment)?

(*e*) The stagnation of the savings rate is a worrying factor, especially because we need an increasingly higher rate of saving to allow for an increasingly higher rate of obsolescence. Hence, we need a better analysis of incomewise distribution of savings. Is it possible, for instance, that the higher rate of return on financial instruments has had the effect of merely shifting savings from, say, farm investments to financial instruments? That may not be such a good thing, though it may help to reduce the immediate problems of the government.

(*f*) In order to give a boost to investment (and real saving) by small and marginal farmers—which would help to raise output as well as employment, and also improve the distribution of income—do we need to pursue a wholly different policy for the agriculture sector? There is a possibility that a well-conceived policy in this regard may help to increase the generation of savings for investment on the farm directly. The focus has to shift to decentralised decision-making by the panchayats which can become the instruments of micro planning in rural areas. Is there any study which can be quickly undertaken to examine this hypothesis? A change of focus in investment planning may then help to increase the effective rate of saving, and help to raise rural incomes.

(*g*) Finally, as indicated earlier, a major factor in the stagnation of the over-all rate of savings of late is the decline in government saving. In fact, government saving (i.e., saving of government administration) is now negative. The revenue deficit of the Government of India in 1986-87 was approximately 2 per cent of the GDP (at market prices). So the questions to be asked are:

(*i*) To what extent is it possible to hold government consumption expenditure?

(*ii*) To what extent have the tax concessions to industry helped to increase corporate saving and investment, if at all? In fact, corporate saving has taken a worse dive as a proportion of total saving.

(*iii*) To what extent has the higher rate of interest on personal savings helped to increase personal savings, and to what extent has there been merely a shift in the pattern of investment of these savings by the households?—And *inter alia* led to larger interest payments (and a negative saving) by Government.

Depending on the answers to the above questions, the whole set of policies of the government in regard to financial instruments of saving would need to be overhauled. Since there is no visible decline in saving in financial assets, in fact, a steady increase even in a difficult year, after the reduction of the rate of interest of NSCs (from 12 per cent to 11 per cent), this is one subject which needs careful study.