drishti

Distance Learning Programme

UPSC Mains

Indian Economy – I

INDIAN ECONOMY - I

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Resource Mobilization

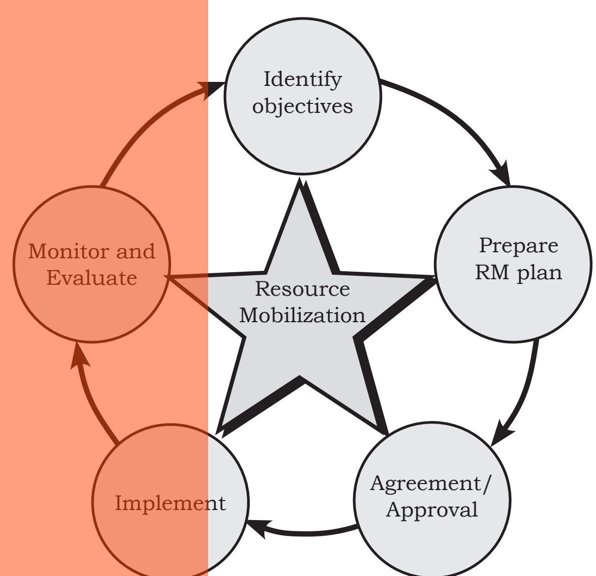
Chapter 5

Mobilizing is the process of assembling and organizing things for ready use or achieving a collective goal. Mobilization of resources should also be seen in the same context. Mobilization of resources means freeing up of locked resources. Every country has the economic resources within its territory not be available for collective use. The percentage of resources used when compared to the potential is often very low. For a country to grow, identification and mobilization of its resources is necessary. It should be available for easy use and for central and state level planning.

Resource mobilization is a process, which will identify the resources essential for the development, implementation and continuation of work for achieving the national mission. In real terms, Resource mobilization means expansion of relations with the resource providers, the skills, knowledge and capacity of proper use of resources.

Why Should We Study Resource Mobilization?

The resource is anything which has some value and is required to accomplish some desired objective. For life on earth sunlight is the supreme resource. It gave birth to all other current form of resources such as fuel and food. Human beings (and every creature) constantly struggle and arrange for or mobilize resources they need. Over thousands of years we have built evolutionary societies in which resource mobilization, its means and methods have also evolved. Ancient barter trade was a system of resource mobilization, and later currencies developed to facilitate it. For a currency to be acceptable to all, it needs a strong legitimacy. In ancient times this legitimacy was provided by monarchies and now it is done by numerous form of governments.



Central thing to the concept of laissez faire was the concept of resource mobilization only. When East India Company colluded with British Empire to get the exclusive rights to trade in the east, it created resentment in newly emerged capitalist class. As we know, it was around this time that Adam Smith in his book 'Wealth of Nations' strongly pitched for free markets. This theory propagated that ruling regimes should let resources be distributed as per principles of demand and supply, without any intervention. Prices of the different commodities or services will send signals to buyers and suppliers as to what to consume and manufacture, respectively. The shortage will shoot up prices attracting more investment in production and reverse will happen in case of abundance. This is what he called 'free hand of markets'.

This free hand or Capitalism went on undeterred for almost two centuries, when finally in late 1920's west experienced the 'Great economic Depression'. Just before this, in 1919**,** Russian revolution yielded a new alternative ideology of resource mobilization, to be called socialism and communism. Great depression dismantled the concept of free markets. British Economist John Keynes demonstrated that markets were amenable to a failure and since then term 'market failure' came in vogue. He professed that government's task in times of market failure should be to incur 'Fiscal Deficit' so that demand in the economy is increased. Fiscal Deficit (in short) is expenditure by government over and above its (revenue) earning. So traditionally, the government taxed citizens to fulfil its commitments, but now the government will be a 'net giver' as expenditure will be more than its income. So this unfolded a new chapter in resource mobilization, and fiscal deficit became an all pervasive mean to cause changes in resource distribution toward weak and vulnerable.

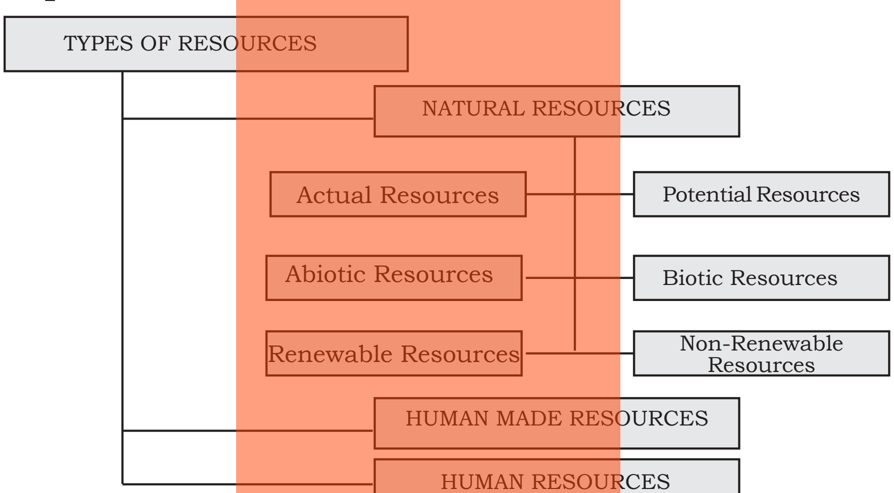
By this time Banking System was highly evolved. Capital or debt markets, primary and secondary markets, which are used as a potential source of investment and resource appropriation also emerged. Topic of resource mobilization is so central to subject of economics that everything, be it budgeting, taxation, stock markets, self-help groups, APMCs, financial inclusion and many more, are nothing but related means or issues. So, every topic should be read keeping this thing in mind.

It should be noted that in modern societies all factors of production, trade or service like natural resources, human resources, energy resources etc. and their value is represented by currency/money. So learning about the distribution of money in market subsumes all other types of resource distribution under it.

So the institutions which basically facilitate resource mobilization are called 'financial intermediaries' (FI). The effective resource mobilization will aim at channelizing resources toward most productive sectors and avenues, which yield maximum good for least advantaged people. It is precisely here that debate of Growth vs. Development also becomes quite relevant.

Types of Resources

Physical Capital



Natural Resources are naturally occurring substances that have considered valuable in their natural form. Its value rests in the amount available and demands for it. Examples are land, water, sunlight, wind, minerals, etc.

Natural resources can be classified into different categories depending based on various factors such as:

- Resources that need development and value addition.
- Resources based on origin
- Availability and Distribution of Resources

Natural resources that need development can further be divided into:

- Actual resources are those that have been surveyed, their quantity and quality determined, and are being used in present times. For example, petroleum and natural gas is actively being obtained from the Mumbai High Fields. The development of an actual resource, such as wood processing, depends upon the technology available and the cost involved. That part of the actual resource that can be developed profitably with available technology is called a reserve resource, while that part that cannot be developed profitably because of lack of technology is called a stock resource.
- Potential resources are known to exist and may be used in the future. For example, petroleum may exist in many parts of India and West Asia/Middle East that have sedimentary rocks, but until the time it is actually drilled out and put into use, it remains a potential resource.

Natural resources based on the origin can be divided into:

- Abiotic resources comprise of non-living things like land, water, air, gold, silver, diamond, etc.
- Biotic resources are the ones which are obtained from the biosphere e.g. forest and their products, marine life etc.

Natural resources based on availability can be divided into:

- Renewable resources, such as forests and fisheries, can be replenished or reproduced relatively quickly. The highest rate at which a resource can be used sustainably is the sustainable yield. Some resources, like sunlight, air, and wind, are called perpetual resources because they are available continuously, though at a limited rate. Their quantity is not affected by human consumption. Many renewable resources can be depleted by human use, but may also be replenished, thus maintaining a flow. Some of these, like agricultural crops, take a short time for renewal; others, like water, take a comparatively longer time, while still others, like forests, take even longer.
- Non-renewable resource (also called a finite resource) is a resource that does not renew itself at a sufficient rate for sustainable economic extraction in meaningful human time-frames. An example is carbon-based, organically-derived fuel. The original organic material, with the aid of heat and pressure, becomes a fuel such as oil or gas. Earth minerals and metal ores, fossil fuels (coal, petroleum, natural gas) and groundwater in certain aquifers are all considered non-renewable resources, though individual elements are almost always conserved.
- Human made resources are the resources made by mankind by using natural resources for their needs like paper, clothes, books, plates or wallpaper. High-tech products typically feature components that are man-made resources, such as wires, television, computer and mobile phones other electronic products. They provide comfort and smoothness to our lives.

- **Human Resources:** Humans are considered to be resources because of its ability to transform original resources of nature into a valuable resource. This is done with the help of skills, knowledge and technology.

Human resources are the people who make up the workforce of an organization, business sector, or economy. "Human capital" is sometimes used synonymously with "human resources", although human capital typically refers to a narrower view (i.e., the knowledge the individuals embody and economic growth). Likewise, other terms sometimes used include "manpower", "talent", "labour", "personnel", or simply "people".

Human capital is a similar concept built upon the notion of human ability to appropriate available resources in a sustainable manner. Here skills, education, health, etc., are identified as capital in itself. Human capital formation can be subdivided into tangible and intangible. Intangible can be simply referred as the energy a human being invests in the work, his integrity, truthfulness, knowledge, etc.

Financial Capital

Financial capital is any economic resource measured in terms of money used by entrepreneurs and businesses to buy what they need to make their products or to provide their services to the sector of the economy upon which their operation is based, i.e. retail, corporate, investment, banking etc.

This can be classified into:

- **Debt Instruments:** Debt capital refers to borrowed funds that must be repaid at a later date, usually with interest. Examples are bank loans, personal loans, overdraft agreements and credit card debt.
- **Equity Instruments:** Equity capital refers to funds generated by the sale of stock, either common or preferred shares. While these funds need not be repaid, investors expect a certain rate of return.
- **Grants/Subsidies:** These are the capital provided by government or foreign aid agencies.

Need for Resource Mobilization

Resources are needed for every type of economy, whether it is a police state or a democratic welfare state. Every economy strives to fulfil some basic needs and aspirations of its citizen and for that it does following works:

- Diversifies and expand resources
- Formulates an independent budget (fund)
- Allows spending and utilization of resources
- Minimize dependency on others
- Sustains the nation and its policies
- Maximize use of domestic capital and skills
- Expand relations
- Fulfil responsibility

In Police state, resources are also mobilized to fulfil some functions such as:

- The state is usually run by single party which needs huge resources to maintain itself.
- There is a greater role of the military in the police state and to maintain large military resource mobilization is must.

- There should be total control of communication which requires resource mobilization.
- Resources are also required to induce and maintain terror in the minds of citizens

In democratic welfare state along with the common functions of state, resource mobilization is required for:

- A welfare state ensures social security. The government plays a dominant role in controlling the economic activities and in the social welfare of the people, which requires resource mobilization.
- A welfare state is socialistic in nature. It is based on the principles of equality and is keen to provide equal opportunity to all. It also aims to ensure equitable distribution of wealth.
- It exercises control over all the economic activities. In a welfare state, all the private enterprises are regulated by the government.
- It provides even the basic facilities to its citizens. Furnishing services to each and every individual is its duty. A welfare government is keen in providing economic and social services such as general education, public health, public transport, housing, and other financial assistance to its people.
- It undertakes and runs various enterprises. Ownership and operation of industrial enterprises, business and other commercial activities are also done by welfare governments.
- It ensures justice for all. In a welfare state, common man has to deal with the authorities for many of their needs. For example; administrative officers, controlling officers, sanctioning authorities, officers of social services, executives of public sector undertakings etc. In all such dealings, a welfare state has the responsibility to ensure justice and fulfilment of their requirements.
- It is the function of a welfare state to regulate and control all private enterprises engaged in economic activities. Such control includes registration, licensing, taxation etc.
- The welfare of labourers also comes under the purview of the duties of welfare state. They are bound to make legislations to prevent exploitation of workers, and to ensure the security and welfare of those who work in industrial enterprises, factories, companies and all other sectors of employment.

All of the above aspects are directly or indirectly pertains to the issue of resources and its mobilization. Hence the need of resource mobilization is vital in any welfare state.

Sources of Resource Mobilization

Private Sector and Public Sector

Private sector resource mobilisation is done via:

- Cooperatives, which are an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise.
- Credit union, which is a member-owned financial cooperative, democratically controlled by its members, and operated for the purpose of promoting thrift credit at competitive rates, and providing other financial services to its members.

- Finance and Leasing Association (FLA) which is the trade association for the consumer credit, finance and asset finance sectors. Members of FLA include: banks, subsidiaries of banks and building societies, the finance arms of retailers and manufacturing companies as well as independent firms.
- Bank which is a financial institution that accepts deposits from the public and creates credit. Banks are the perhaps prime Financial Institutional source of resource mobilization.
- Angel investors who invest in small startups or entrepreneurs are another important source of resource mobilization in an economy. Often, angel investors are among an entrepreneur's family and friends. The capital angel investors provide may be a one-time investment to help the business propel or an ongoing injection of money to support and carry the company through its difficult early stages.
- Innovation funding like India Innovation Fund, which is a SEBI registered venture capital fund that invests in innovation led, early stage Indian firms. The focus areas include Information and Communication Technologies and Life Sciences.
- Venture Capital (VC) which is a type of private equity, a form of financing that is provided by firms or funds to small, early-stage, emerging firms that are deemed to have high growth potential, or which have demonstrated high growth (in terms of number of employees, annual revenue, or both). Venture capital firms or funds invest in these early-stage companies in exchange for equity, or an ownership stake, in the companies they invest in. Venture capitalists take on the risk of financing risky startups in the hopes that some of the firms they support will become successful. Thus VC are another important source of resource mobilization in an economy.
- Capital network which covers all aspects of fund raising: finding investors, pitching, due diligence, term sheets, exits and more.
- Merchant bank, which is a company that deals mostly in international finance, business loans for companies and underwriting. These banks are experts in international trade, which makes them specialists in dealing with multinational corporations. A merchant bank may perform some of the same services as an investment bank, but it does not provide regular banking services to the general public.
- International trade financing companies are another source of resource mobilization. These companies provide services which include such activities as lending, issuing letters of credit, factoring, export credit and insurance. Companies involved with trade finance include importers and exporters, banks and financiers, insurers and export credit agencies, and other service providers.
- Specialized financial institutions which are banks, which concentrate mainly on financing specialized economic and social activities. Specialized activities may be:
  - small and cottage industries financing
  - insurance companies
  - commercial mortgage lenders
  - specialty equipment financing organizations

  In India these institutions mainly include, Export-Import Bank Of India, Board for Industrial and Financial Reconstruction, Small Industries Development Bank of India, National Housing Bank. They are government undertakings established with a view to offer financial as well as technical assistance to the Indian industries.

Sources of Resource Mobilization Belonging to the Public Sector

Tax Resources

- Direct taxes, i.e., taxes paid by households and companies to the government or other public agencies. This includes income tax, payroll tax (including mandatory social health insurance contributions) and corporate or profit tax.
- Indirect taxes, i.e., taxes paid to the government or other public agency via a third party (retailer or supplier). The tax is based on what a household or company spends and includes value-added tax, sales tax, excise tax on alcohol and tobacco and import duties. Now, as many of the indirect taxes have been subsumed in single tax, i.e., GST so now onwards GST becomes an important source of resource mobilization.
- Non-tax revenues (from state-owned companies, including natural resource revenues such as oil and gas).
- Financing from external (foreign) sources is considered 'public' when the funds flow through recipient governments.
- Savings and investments are another important way of understanding the sources of resource mobilization.

Role of Fiscal Policy in Resource Mobilization

In a democratic society, there is an inherent dislike for direct (physical) controls and regulation by the state. The entrepreneurs would not like to be ordered about to produce this or that, how much to produce or where to produce. Fiscal incentives in the form of tax concessions, rebates or subsidies are, therefore, preferable.

Similarly, the consumers would not like to be told directly to curtail their consumption or to consume this and not to consume that. Taxation of commodities and services whose consumption is to be discouraged is therefore preferable for e.g-Sin tax is being levied on tobacco products. Hence, a democratic state must rely on indirect methods of control and regulation and this is done through fiscal and monetary policies. Thus, in democratic countries, fiscal policy is a powerful and desirable weapon on which government can rely for promoting economic growth.

Resource mobilization is of strategic importance for bringing about rapid economic growth. It is, therefore, necessary to achieve a higher ratio of savings to national income. Taxation can be used to raise collective savings for public investment and also at the same time to promote private investment. A well-conceived scheme of taxation is an important way of raising the ratio of savings to national income which is one of the crucial determinants of the rate of economic growth.

However, in a liberal mixed economy, such as ours the task of fiscal policy is not only to raise saving ratio for acceleration of growth, but also to improve investment in the private sector so that higher rate of investment be achieved. Public finance assumes a new significance in the face of the problem of resource mobilization in underdeveloped countries.

On the expenditure side, there is a positive need for public investment, especially in those spheres of economic activity where the private investments are not easily attracted, for example, the development of power resources, roads and highway, ports and airports, means of transport and communications, basic heavy industries, social infrastructure such as education and research, public health etc. Such investments are very often the very foundations of rapid economic advance. Thus, fiscal policy is of crucial importance in accelerating the pace of economic growth in developing countries.

Fiscal policy, if properly designed, is an efficient and equitable way of mobilizing resources for augmenting public investment. Through it not only that collective public savings can be raised for financing public investment, but also at the same time private savings and investment can be encouraged.

In other words, Fiscal policy allows the government to mobilize resources for public expenditure and development. There are three ways of resource mobilization viz., taxation, public savings and private savings through issue of bonds and securities.

In fact, taxation may be the most effective means of increasing the total volume of savings and investments in an economy where the propensity to consume is normally high. Further, the fiscal policy can be so devised that not only the objective of rapid capital accumulation or growth, but also other objectives of economic policy, such as equitable distribution of income and wealth, price stability and promotion of employment opportunities can be achieved.

It has been suggested that an appropriate tax, which would mobilize resources or mop up economic surplus is the progressive income tax. Income tax is imposed not only on the incomes of individuals, but also on the profits of the corporate companies.

Thus, there is personal income tax and corporate income tax (that is, tax on net profits earned by corporate companies). In India and the other developing countries, income has been regarded as a good base for direct taxation. And the imposition of highly progressive income tax, not only mops up relatively greater amount of resources, but also tend to reduce inequalities of income.

However, a progressive income tax with a high marginal rates of taxes adversely affects private saving and investment and also raises the propensity to evade the tax. In view of this, two proposals have been put forward to make the income tax both as an effective instrument of resource mobilisation for the public sector and of providing incentives to save and invest.

First, Prof. Kaldor of Cambridge University, who in 1956 was invited by the Government of India to suggest reforms in the Indian tax system for mobilizing resources for development, suggested that whereas the marginal rate of income tax be reduced to, say, 45 to 50 per cent, expenditure tax be levied to discourage the people belonging to upper income brackets from dissipating their income in conspicuous consumption.

According to him, this will also reduce the tendency to evade income tax on the one hand and promote private savings on the other. The second proposal to reform the income tax put forward by others is that whereas marginal rates of income tax be kept high, but some exemptions for approved forms of saving and investment be allowed to the individuals. This will channel individual savings along desired lines and at the same time mobilize resources for development.

Apart from the income tax on individuals and companies, the imposition of other direct taxes such as capital gains tax, wealth tax, gift tax, and estate duty are also needed to mobilize sufficient resources for capital formation. Unlike income tax, these capital taxes do not have any adverse effects on incentives to save and invest.

They are also important instruments for reducing inequalities of income and wealth. Because of these advantages, Professor Kaldor in his report of taxation reforms in India recommended the imposition of these capital taxes and this recommendation was accepted