DISSEMINATION OF KNOWLEDGE SERIES

ECONOMIC REALITIES
New Emerging Hypotheses

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INDIAN INSTITUTE OF ADVANCED STUDY
RASHTRAPATI NIVAS, SHIMLA

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First Published 2002

Published by the Secretary for
Indian Institute of Advanced Study
Rashtrapati Nivas, Shimla 171005

Typeset at the Indian Institute of Advanced Study, Shimla
and printed at Replika Press Pvt. Ltd., Delhi

Foreword

The Indian Institute of Advanced Study is wedded to the noble task of research on fundamental themes of life relevant to humanity. With this objective in view the Institute organizes intensive research by its resident fellows, lectures and talks by eminent visiting scholars and visiting professors as well as by seminars, conferences, workshops at Shimla and outside through its collaborative institutes and centres. The Institute has a distinguished record of publication of books, monographs, proceedings of seminars, symposiums, etc. It publishes two journals – *Summerhill : IIAS Review* and *Studies in Humanities and Social Sciences*. These publications go a long way in achieving the aims and ideals of the Institute.

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The present paper entitled *Economic Realities: New Emerging Hypothesis* by Professor Vinod Anand brings into focus the shifts in the field of economics. There is no doubt that social sciences including economics originate their mainstream research from their conventional wisdom but suggest new hypothesis in the light of changing needs and aspirations of the society. After brief analysis of radical changes in Keynesian economic theory the paper focuses on the shift in conventional wisdom brought about by waiving the assumption of 'exogeneity' in the sphere of macroeconomics, and replacing it with the assumption of 'endogeneity' The paper looks at the role of the state as an endogeneity as a variable of the New Political economy and brings into prominent relief emerging economic realities. The result is a vicious circle making economic scenario a deplorable affair.

Foreword

I felicitate Professor Vinod Anand for his very illuminating study of new emerging hypothesis in the field of economics It gives me pleasure to present this paper on *Economic Realities* to the interested readers.

28 February 2002

V.C. SRIVASTAVA
Director

ECONOMIC REALITIES: NEW EMERGING HYPOTHESES

VINOD ANAND[1]

There always occur occasional shifts in the conventional wisdom that dominates a given discipline. Economics in no exception (Anand, 1998A).Conventional wisdom is a part of our lives. It is a set of generally accepted customs and standards, based on good sense and judgment, which control both ndividual and social behaviour. It exhibits both intra and inter-regional differentials, and passes informally from one generation to another, providing the guidelines within which families are brought up according to the given traditions. Conventional wisdom also changes with time, and reflects the changing scenario of our life-style with its varied ramifications.

The mainstream research in social sciences emanates from heir conventional wisdom and provides yardsticks, both heoretically and empirically, for verifying the already existing heories and hypotheses, and also suggesting new hypotheses. t is through research, therefore, that conventional wisdom in any discipline undergoes a shift from one set of principles to another. Such shifts are normally gradual, but could be radical having wide and far-reaching effects. This happens when a field of study becomes marked by dissatisfaction and disillusion-nent. For example, conventional wisdom in Economics had undergone a radical change with the advent of the Keynes' Economics during the thirties in the wake of long, wide and unprecedented depression, and there occurred a major shift rom the neoclassical orthodoxy of market system to Keynes' work on economic theory and policy analysis centering around nacro issues involving public works expenditure and other nvestments[2].

Established Keynesian economic doctrines of economic heory and policy of the earlier post-war years also underwent a radical change during the sixties and seventies. Some of the examples are as follows:

a) In the earlier post-war years the conventional wisdom held that a government's primary responsibility was to get the level of total demand right, high enough to ensure something close to full employment, but not so high as to cause inflation. The assumption was that if government got the demand side right, supply would take care of itself. But later, during the sixties, this doctrine was reversed with the new conventional wisdom, holding that if government gets the supply side[3] right, demand will take care of itself. This was in fact a revival of the neoclassical economic principles pursued in West Germany after World War Two.

b) A second change in the conventional wisdom related to the relative importance of Fiscal Policy versus Monetary Policy. The earlier wisdom held that Fiscal Policy was government's most powerful tool and Monetary Policy should be subordinated to it. Conventional wisdom of the sixties asserted the reverse.

c) Another shift affected efforts to stimulate business investment. The earlier wisdom held that investment in capital goods depended on what economists called the 'accelerator", showing a relationship between consumption and the capacity of industry to meet current or expected demands. The new wisdom saw interest- rates as the dominant force and warned that rising rates imperil investment.

A few other prominent shifts had started to emerge around the eighties, which, in recent times, have become the core issues of the present-day economic thinking. The cue of this Paper is taken from the shift in conventional wisdom brought about by waiving the assumption of 'exogeneity' in the sphere of macroeconomics, and replacing it with the assumption of 'endogeneity' (Anand, 1996). 'Exogeneity' refers to exogenous variables, which are determining (explanatory) and, as such, are given, whereas 'endogeneity' refers to endogenous variables, that have to be determined (explained), and, as such, are not given. Conventional wisdom in recent times has moved from 'exogeneity' of certain crucial variables, essentially in the field of macroeconomics, to their 'endogeneity' One such crucial variable is the role of the State, which instead of being regarded as an exogenous variable is now regarded as an endogenous variable.

This development has widened the scope of Economics and has enlarged its frontiers to positively overlap with other disciplines like Political Science, Sociology, and Psychology. The science of Economics has now a multi-disciplinary flavour, and we have an endless vista of interesting and relevant economic issues stretching before us. The mainstream conventional Economics now goes beyond its normal domains, and a number of economic realities have now started emerging essentially because of the failure of the State to perform its given role and to live up to the expectations of the people in terms of basic economic and social provisions. The inclusion of the role of the State as an endogenous variable shifts mainstream conventional Economics to what has now come to be known as the 'New Political Economy' (see Atkinson, 1980; Bagchi, 1993; Irwin, 1991; Anand, 1996), which is the revised version of the historically known 'Political Economy' of the classical period. Unlike standard economic theory, it incorporates government's impact on the economic system and its components, without going into the question of the development of political constitutions and political processes. In fact, it accounts for the behaviour of the electorate, the government (legislature), and the bureaucracy.

In Section I, this Paper briefly looks at the role of the State as an endogenous variable, as understood in the New Political Economy along with its basic assumptions, its genesis, and the resulting fall-outs of the role of the State in terms of 'rent-seeking' and 'directly unproductive profit-seeking' activities and the resulting implications in general, and then in Section II, it focuses particularly on two basic economic realties emerging out of such a shift from mainstream conventional Economics to New Political Economy. These realities are concerned with the failure of the so-called trickle-down effect and its replacement by what we term as the trickle-up effect, and with the newly added dimension of concealed poverty to the already baffling poverty syndrome. The last Section of the Paper briefly sums up the ultimate impact of the two realties, as discussed in Section II, in terms of an acute economy-wide vicious circle emanating basically from the distorted role of the State, as demonstrated by its rent-seeking and related activities, and ending up with a more severe scenario through varied cause and effect linkages.

SECTION I: ROLE OF THE STATE[4]

While examining the role of the State, it is seen that individuals perform three basic roles: as voters, as legislators, and as administrators. These roles are also inter-linked. For example, there is a relationship between voters and legislators on the one hand, and between legislators and bureaucrats on the other. Although these inter-links have different origins and formulations, yet they are based on two common assumptions: (a) conflicting interests and (b) perfect information. The standard economic theory of private economy is devoid of both of these assumptions and it is for this reason that it fails to answer various questions related with the behavior of the State, and its impact on the economic functioning of the system. As a result, much of the analysis on the theory of the State is restricted to qualitative treatment.The genesis of the New Political Economy lies in old ' interest-group' or 'elite theory of politics', which emphasizes the role of group action (especially through differential power, including both differential registration and differential participation of voters) in influencing voter behaviour, in winning over legislators, and in modifying the administration of public policy. Particular attention is also paid to the class interest view of the State

as analysed in the Marxist literature. In its updated-version, the New Political Economy centers around the idea that all political developments result from competition and rivalry among political entrepreneurs who seek to maximize their electoral support and political gain, and thereby their incomes also. They are experts in political survival, and quite often, they strike a trade-off between their survival and national interests, giving priority to the former. It is also maintained that the State exists basically for the politicians and bureaucrats. Whatever the State does is linked directly or indirectly with the vested interests of the politicians, who always strive to raise their electoral support and maintain, and even enhance, their political power. The bureaucrats are in full league with them, and create situations, which, on the one hand, help the politicians to achieve their political motives, and give a dominant position to them (bureaucrats) to exercise massive administrative power, on the other. The two, therefore, strive to exist for each other, and through this process the ideology of public intervention also gets distorted.

With 'endogeneity', therefore, the domains of Economics include a variety of new economic agents other than the conventional ones. Besides having consumers, producers, buyers, sellers, and other conventional agents, we now have agents like political entrepreneurs (both ruling and non-ruling), government officials and bureaucrats, and voters, as important subsets of the macro economic system. It is the sum total of the activities of all these agents that determines the functioning of the economic system. We know that the conventional economic agents are subject to the assumption of rationality: they exhibit maximizing bevaviour, and in that process also add to the overall economic activity of the economic system. We also know that the non-conventional agents (like, political entrepreneurs) also work rationally but essentially for their own vested interests, and in this process they somehow work against the system. Their activities are in fact anti-growth (Murphy et.al., 1993). They also shrink growth and corrode the economy in various ways (Panandiker, 2001). This will be clearly understood if we look at the two fall-outs of the role of the State as linked with the positive side of the New Political Economy (Anand, 1998B). These are briefly described below:

1. *Rent-seeking Activities*: All those re-distributive activities (amounting to transfer), which take up real resources, and do not, in any way, add to growth are termed as rent-seeking

activities. The connotation of the word 'rent' is the same as used by the classical economists to indicate the 'unearned income' accruing to monopolist landlords, but the concept of rent-seeking goes beyond monopoly rent, and covers all kinds of legal and illegal extortion by individuals with or without the support of government and also directly by government itself and its officials in the name of government intervention. Rent seeking, thus, maligns and denigrates all government intervention.

It is also shown that rent seeking activities are subject to natural increasing returns, which means that, as more and more resources move into rent seeking, returns to rent seeking become larger and larger. This also means that an increase in rent seeking lowers the cost of further rent seeking. In essence, therefore, it can be said that very high level of rent seeking may be self-sustaining. There are three ways in which rent seeking exhibits increasing returns:

i) It is self-generating and 'infectious' in the sense that it passes from one person to another. This is so because, in the absence of any protection from the government, one has to protect oneself on his own against the ill effects of rent seeking activities. In other words, one has to have one's own defence, and the best defence is offence itself i.e., getting involved in rent seeking itself.
ii) It depends largely on numbers. 'The more the merrier' describes the success of rent seeking activities. Larger is the number of people getting involved in such activities, higher become their returns.
iii) A time–consuming, inefficient legal system, which denies and delays justice, also helps in encouraging rent seeking activities.

Increasing returns to rent seeking also arise from the interaction of rent seeking and productive activities, as both use and compete for the same given resources. In the case of productive activities, sooner or later, we step into the second stage of production exhibiting falling returns (concavity of the total product curve), but in the case of rent seeking activities, as more and more resources are used, we continue to stay in the first stage of production exhibiting increasing returns (convexity of the total rent seeking). In fact the extent of the stage one of rent seeking has no limits.

In relative terms this implies that, over a certain range, returns to production may fall faster than returns to rent seeking. And hence, rent seeking activities may become more attractive relative to productive activities. There is, therefore, a possibility of multi-equilibria in the economy with both 'bad' and 'good' equilibrium situations, which may either be stable or unstable.

A distinction is also drawn between private and public rent seeking. Private rent seeking amounts to transfers between individuals or private parties. Public rent seeking amounts to transfers either from individuals to the State, or from individuals to the political parties and from individuals to government officials. As already said, rent seeking, in general, adversely affects economic growth, but private rent seeking works more against production, and public rent seeking more against innovation.

2. *Directly Unproductive Profit Seeking Activities:* These are similar to rent seeking activities except for the fact that their direct (immediate) impact is unproductive. Apart from this difference, both lead to 'unearned' income without adding to output. Both use real resources to generate profit (income) without producing an output. In other words, they lead to predation and not to production, and, as such, they do not enter the conventional utility and production functions. In their abbreviated form the directly unproductive profit-seeking activities are termed as DUP or even DUPE activities Even organised religious activities sometimes amount to DUPE activities (Srinivasan, 1991). These activities generally relate to government intervention. They may both be policy-induced (like, illegal trade, smuggling, and black-marketing) and policy influencing (like, tariff-seeking by lobbies). There is a good amount of controversy whether DUPE activities are wasteful in their immediate impact (Bhagwati, 1980 and 1982) or they are ultimately wasteful amounting to 'immiserizing'(Buchanan, 1980).

In winding up this discussion on endogeneity, we can, therefore, say that the endogenous character of the New Political Economy in terms of the inclusion of the role of the State within the broader framework of macroeconomics presents an altogether different and useful (though depressing) scenario as compared to that presented by mainstream conventional Economics. Such a shift in conventional wisdom is most welcome, as it opens up a number of real-life issues that are of crucial importance for a majority of people in any country.

SECTION II

EMERGING ECONOMIC REALITIES

The two major fall-outs (in terms of rent seeking and directly unproductive profit seeking activities of political entrepreneurs and other components of the State) of the given assumption of 'endogeneity', as briefly mentioned in Section I above, have serious repercussions on the functioning of the State in terms of delivering the final outcome to the majority of the people in the shape of economic and social provisions. These fall-outs seriously hinder economic growth and also its trickle down effect. According to one of the case studies on India (Mohammad et.al., 1984) the rent seeking losses to national income amounted to between 30 per cent and 40 per cent of India's GNP in 1980 and 1981. In fact the fall-outs of such activities lead to leakages, which eventually get channeled to the coffers of the major role-players in the whole game, and, thus, lead to further fall-outs, the effects of which are highly immiserising for the country as a whole, and essentially for the its poorer sections. A similar scenario perhaps exists in other countries as well, of course with a difference of degree. The countries, thus, gradually get trapped in an acute vicious circle, which eventually gets translated into a number of depressing economic outcomes, for which the State is fully responsible. We shall briefly look at two of these ultimate fall-outs, and the issues emerging out of them. The first fall-out is the failure of the popularly known trickle down effect, and the other is the emergence of what is called concealed poverty.

A. THE TRICKLE-DOWN EFFECT [5]

The inter-linkages between economic growth and income distribution are crucial for assessing a country's economic performance. For this we have to rely both on macro-economic measures (such as growth rate of Gross National Product) and the micro-economic measures (such as poverty levels, inequality ratios, and unemployment rates). Such a combination of macro and micro measures generates two strategies:

1) emphasising growth but weighing the growth performance by the distributional record.

2) emphasising changing poverty, inequality and unemployment as the principal indicators of development.

The first strategy is subject to the percolation or trickle down effect, according to which 'countries with moderate to rapid rates of aggregate economic growth would succeed in upgrading the economic condition of significant numbers of their people' (Fields, 1980). The experience of different developing countries in respect of the trickle down effect in fact presents a mixed scenario. This theory has been seen to be valid (Fields, 1980), of course due to different reasons in each case, for a number of countries (like, Taiwan, Brazil, Costa Rica, Bangladesh, Pakistan, Pureto Rico, Singapore, Thailand, and Mexico) for given time periods, especially between the fifties and early seventies. At the same time there have been a few exceptions like that of Argentina (1953-1961) with moderate growth, and the Philippines (1961-1971) with rapid growth, where the trickle down theory failed to be true. Apart from this, there have been two other interesting scenarios in this context. One is that of Sri Lanka, where the growth was slow during 1953-1973, and yet there was substantial improvement in poverty levels. The other is that of India, where during 1960-1969 (the Third and the three Annual Plans) there was either no growth, or very low growth, and no trickle down at all (Fields, 1980; Anand, 2001C). In fact the trickle down fails essentially because of the dominance of the rent-seeking and other related activities of the State, and perhaps also because of many other bottlenecks in the whole percolating process such as, the lack of effective bureaucratic control, inefficient implementation of various out-reach programmes, the lack of political will, and the lack of efficient and effective intermediaries.

We shall here attempt to negate, in a highly general way, the trickle down effect of economic growth in its totality, especially in all man-made endeavours including growth, development, and what not, not so much on the basis of any country-wise studies during given periods, as on the grounds of history, philosophy and logic. It would also be interesting to looks at the inverse of the trickle down effect (called the trickle up effect), once again, in a general way, and also analyse its validity, not necessarily in Economics, but in all walks of life. In either case, we bear in mind that there are always exceptions, due to special circumstances, no matter what we say, and what we negate or propagate, and, hence, we do not, in any way, rule out exceptions in the given contexts.

Aiyer (2000) elaborating historically on the invalidity of the trickle down effect maintains that the majority of the poor have never been richer, whereas the minority of the rich has always been richer. According to him, throughout history, especially in feudal societies, which originated initially in Europe in the eighth century, and then spread all over, and flourished especially in closed agricultural economies, and which were based on land tenure and personal relationships in which land (and to a much lesser degree other sources of income) was held in fief (exclusive possession) by vassals from lords to whom they owed specific services and with whom they were bound by personal loyalty (The New Encyclopaedia Britannica, 1991 A), there have always been the highest stratum of a few rich people (the landlords) securing and enjoying the riches at the cost of the poor, and preventing any trickle down to assure that the poor stay to be poor and they (the landlords) become still richer to rule, dictate, and exploit.

He further maintains that beyond Feudalism, even in Capitalism (contemporary and in earlier forms), brought about initially by the French Revolution of 1789, and based on challenging virtues like, enterprise, venturesome ness, acquisitiveness, competitiveness, innovation, individualism, rationality, material progress, and political liberty, to bring about remarkable advances in productivity and material well-being (Grossman, 1974), there was invariably no change in living standards of the poor; and later in the anti-capitalist Marxian systems, as manifested in Socialism and Full Communism, and characterised by the absence of private property, and motivated by class interests, the richer class somehow manipulated to prevent trickle down with the result that poor continued to be poor; and then finally in modern times (beginning from the Keynesian Revolution of the thirties), when the ultimate motto is that of a Welfare State with Keynesian demand-based Economics, protecting the rights of the working class, empowering the poor in various ways, and believing in human resource management, the fate of the poor is just the same as it was centuries ago, and the trickle-down does not work.

We can, therefore, see that throughout history, and more so during the present times, the motivating factor for the failure of the trickle down effect has been the vested interests and the survival instinct of the ruling classes, that always strive to raise their support and maintain and even enhance, their hold, and their political control and power over the masses. The administrators have always been in full league with them (the ruling classes) and create situations which, on the one hand, help the rulers to achieve their motives, and to give a dominant position to them (the administrators) to wield massive administrative power, on the other. In essence, there has always existed a strong nexus between the rulers and the administrators, and both always strive to exist for each other: rulers for their power and hold, and administrators for their supreme administrative authority. All this is, exhibited through what we term as the 'rent-seeking' and 'directly unproductive profit-seeking' activities in the terminology of the 'New Political Economy' These activities seriously hamper the growth process, and especially the trickle down, by dissipating the country's resources and national income (Anand, 1996; Anand1998A, Anand, 1998B).

It is interesting to see that, unlike man-made and man-controlled scenarios and mechanisms, the trickle down effect seems to be highly valid in nature and its mysterious phenomena. Some of the examples supporting this fact are:

> the law of gravitation, as discovered by Isaac Newton in his Principia in 1687 on the basis of the work of Galileo and Johannes Kepler, is the most dominant manifestation of 'the fall of bodies released from a height to the surface of the Earth and the weight of resting bodies at or near the surface' (The New Encyclopaedia Britannica, 1991B).
> Genetics, the study of heredity in general and of genes in particular, as scientifically discovered by Gregor Mendel, maintains that all living creatures, including plants, inherit the hereditary traits (both good and bad) randomly from the parent-body. (The New Encyclopaedia Britannica 1991B).
> 'Blessingway rite', the 'central ritual of a complex system of ceremonies performed by the Navajo Indians to restore equilibrium to the Cosmos' (The New Encyclopaedia Britannica, 1991C), and believed otherwise by the whole humanity throughout ages, both ostentatiously and modestly, is also motivated by the thought that the blessings of the Almighty in all respects follow the downward way and trickle-down to the worshippers.

It is a known fact that through out history, and more so in the present times, man and man-made systems have always worked against Nature and its varied manifestations to achieve their own interests in the name of material progress, resulting in the erosion of natural resources and natural surroundings, to the extreme disadvantage of human existence itself (Anand and Bhatt, 1995). Going against Nature implies, among other things, the complete loss of its modus operandi like, the trickle down effect. What is, therefore, more valid in all man-made systems is not the trickle down effect, but its inverse, the trickle up effect. Apart from this negative logic in support of the trickle-up effect in man-made situations, there are a number of affirmative contexts too that support the theory of trickle up. These are briefly mentioned below:

One of the most important determinants of the rate of economic growth, that works via capital formation (understood in terms of net investment in fixed assets, i.e. additions to the stock of real capital) is domestic saving, which has three basic components: household saving, private corporate saving, and public saving. Household saving is the sum total of financial saving, and saving in the form of physical assets. In Economics, the important feature of household saving (in terms of the theory of circular flow of income) is that it represents money which, having been paid out as income to households (who are also suppliers of resources and inputs) by the business firms and the production sector, is not spent in the present, i.e. it is not returned to the producers *directly* in the form of expenditure on goods and services. In fact, it is returned *indirectly* by the households to the production sector (both private and public) in terms of say, deposits, investments, and physical assets, to secure a better future income for them. The incentives for this indirect return of households present income to the production sector are provided both by themselves (the households) for a better future, and by the private and public sectors in terms of high and attractive future returns, and tax rebates, if applicable. This process of indirect return of households' present income works on a continuous basis, and amounts to nothing else except the trickle up of micro-level household savings to the economic system, enabling it to add to its capital formation, and then to economic growth.

The trickle up effect is also seen to work very well in the industrial sector, essentially manufacturing, that has a long chain of strong backward linkages with other sectors, including the primary sector of an economy. This has been very well exemplified by Aiyar (2000) with the help of an example of textile magnate where, after negating the theory of the trickle down in terms of the failure of the huge profit of the textile magnate trickling down to his workers, cotton-growers and others, he maintains that *'the trickle up theory shows what really happens. First, the cotton* *farmer grows his crop, pays the agricultural labour involved, and then sells the crop at a profit. Note that the agricultural worker gets his money first, the grower second. Next, the cotton moves to a ginning factory to remove the seed. The transporters and ginner make their living in the process. Then the cotton moves to a mill. The staff there is paid their wages and salaries even while processing the cotton, whether or not the mill is profitable. When the cloth is ready, it is sold through agents or traders who also earn commissions or profits. Only at this final point, when the sales are made, does any profit accrue to the textile magnate. At this point, profit trickles up the top.'* It is, thus, seen that the primary agricultural input trickles up to the ultimate user (the textile magnate in the above example) through a number of intermediaries, each one contributing in his own way, to the 'value-added' of the product. This process works on a continuous basis with the help of the market mechanism, where the non-market interventions also play their own roles.

Another context of the trickle up effect is the electoral process in a constitutional democracy, where the power of vote, held by individual voters, eventually trickles up to the winning political entrepreneurs, and gets aggregated to reflect their political hold and influence. It is because of this kind of trickle up that the rival political leaders and contestants always strive to enlarge their vote banks to assure their victory in elections and, thereby, hold massive power of their constituencies.

Lastly, it will not be out of place to mention that the trickle up approach also plays an important role in the strategies of microeconomic development to alleviate poverty too, in terms of linking the poorest families to micro enterprises, essentially run by grassroots NGOs and Government Institutions who have established programmes in the communities (Fairly, 1998). This can be done through various ways like grant of micro credit, provision of business training and support services.

In the light of above discussion, it can, therefore, be concluded that it is not the trickle down but the trickle up, which is the order of the day, especially in man-made systems. The present-day experience has turned the earlier thesis of trickle down on its head, and supports the thesis of trickle up in all man-related contexts. The success of modern economies is in fact the success of trickle-up, where a number of things (both tangible and intangible, visible and invisible) move up the ladder, on a continuous basis, through different mechanisms (both market and non-market) to reach the top.

B. CONCEALED POVERTY[6]

One of the serious outcomes of the failure of the trickle down effect, essentially because of the 'vested' role of the State, as described earlier in this Paper, is concerned with poverty. The extent of poverty, as we know, is both severe and staggering all the world over. Economic literature abounds in a number of studies (Ahluwalia, 1976; Fields, 1980; Midgley, 1988; Hardiman and Midgley, 1989; to name a few) supporting this proposition in their own ways. These Studies report that (a) there exists an overlap between poverty and inequality, and that they are closely related, and (b) incidence of poverty correlates with low levels of health, education, and nutrition, inadequate shelter and other unsatisfactory social conditions. It is also an accepted fact (ILO, 1993) that poverty in most of the developing countries, despite being urbanised, still remains overwhelmingly a rural phenomenon. It is baffling to see (Fields, 1980; Gazette-Canada, 1993) that the poor are not only concentrated in countries with low rates of GNP and per capita GNP levels, but also in fast growing countries with relatively high rates of GNP. There is also a consensus on the suggestions (Economic Times, 1994) that poverty tends to be concentrated in the areas with little or no access to health, education and infra-structural services like transport and communications. Beyond that, research about specific characteristics of the poor (Ravallion, 1992) is limited only to bivariate correlations, and not to joint interrelation-ships with other characteristics of poverty. Based on a few examples (Van de Walle and Ravallion, 1992; House, 1989; Schofield, 1979; Lipton, 1983; Levinson, 1974; Bardhan, 1982; Das Gupta, 1987; Muhuwi and Preston, 1991; Van der Werff, 1995) it is seen that:

larger household size is associated with greater incidence of poverty as measured in terms of household consumption or income per person;
child-adult ratios are larger in poor households;
poor-households are larger and younger, and higher mortality, especially of children, among the poor households, stimulates excess replacement births;
there is a strong association between high fertility and poverty;
there is widespread feminisation of poverty (especially in male-dominated societies) in the sense that young females are more exposed to poverty-induced nutritional and health risks;
poor households depend heavily on unskilled labour income;
poor households often over-exploit their immediate physical environment and the subsequent degradation intensifies poverty;
poor households increasingly lose access in private and common resources; and
poverty in urban areas is often associated with pollution due to the concentration of people, industry and traffic.

The above, and even many other dimensions of poverty as available in literature, constitute what can best be termed as Poverty Syndrome, especially in developing, yet poverty-stricken, economies. The dimension of Poverty that matters in the context of this Paper is what we term as concealed poverty. It is hypothesized that in countries, where poverty-alleviation programmes consistently fail, poverty starts getting 'concealed' or 'disguised' through various legitimate and illegitimate means with the result that poor do not appear to be poor. In essence, there exist an intriguing and also paradoxical situation existing in certain countries where there are high poverty levels based on macro indices and survey data, but where poverty, somehow, is not visible to the casual observer. The dynamics of this process works like this: poverty, amongst other things, leads to loss of self-esteem in the eyes of the richer class. Various manifestations of such marginalisation (also called social apartheid) of the poor by the ricer class become increasingly extreme, especially in the urban areas, thereby challenging the fight against poverty, and even threatening democracy (Sane and Binde,2001).This in turn motivates the poor to protect this loss through borrowing and crime-related activities. Poverty, thus, gets concealed and the pattern of consumption distorted towards visible and conspicuous items to restore their self-esteem at least in an extremely short period and not in a sustained way. Beyond that the fallouts of this dramatized behaviour are highly damaging both for the poor and for the economy as a whole in terms of reduced gross domestic savings, which exercise their adverse impact on investment and growth.

In order to clarify these contentions further we have to get involved, without being biased in any way against the various measurements of poverty (Chaubey, 1995) and all that has been done in that area, in the very semantics of the word poverty. No matter how we define it (say, less comprehensively, in terms of falling short of a reasonable minimum of pre-determined 'basic consumption needs', especially nutrition, or broadly, in terms of other aspects of welfare such as health, longevity, and self esteem), for a layman, it is an accepted fact of life, and no one will ever refute it, that poverty is seen as a curse, and a vice, and poor people (the have nots) are looked down upon with disgrace (which gets accentuated by a number of social factors like racial in South Africa and caste-based in India) by the so-called rich (the haves), who have no real feelings, whatsoever, for the pain and suffering the poor have to go through every moment of their existence. But then, one has to live with whatever it is, given the natural instinct to survive, and that too at a heavy cost of self-esteem, especially in the present-day materialistic and self-centered world. In this kind of a backdrop, any one who is poor naturally has a strong desire to conceal one's poverty, no matter how he does it, to meet his basic survival needs, and also to protect thereby his self-esteem.

The poorer is the person (both absolutely and relatively) stronger becomes such a desire of concealment. This desire, somehow, is also intensified by consumers' tendency to imitate, called the demonstration effect or neighbourhood effect (especially in countries where poverty is compounded by worsening distribution of income), which is highly immiserizing, at least psychologically, for the poor, and victimises them, if not initially then in the long-run, in various ways.

The initial impulse to shed off this mental and physical torture and stress, as caused by the loss of self-esteem, and demonstration effect, is to shift from the consumption of 'inferior' goods to that of 'normal' goods. The idea of this shift to conspicuous consumption places the poor in a state of acute dilemma, where they have to make a difficult choice between two courses of action (namely, staying to be poor and sticking to 'inferior' goods for their subsistence, and moving away, though artificially, from the consumption of 'inferior' goods to that of 'normal' goods) both of which are equally undesirable in their own ways. It is unfortunately the society and its economic and social fabric and also its attitude, that encourages a majority of the poor to get motivated towards the second option of moving away from poverty artificially, and, thereby, publicly concealing it.

There are *two* possibilities (not necessarily mutually exclusive) open for such a course of action, and each one is capable, in its own way, to add to the command or entitlement of the poor, not necessarily over basic consumption needs of 'inferior' goods, but also beyond them over 'normal' goods. The *first* possibility is legitimate, but may be unethical and is concerned not only with spending a major part of one's income on 'normal' goods but also through self-borrowing in the sense of spending one's future income in the present, and this leads to a vicious debt-trap for the poor. The *second* possibility is both illegitimate and unethical, and beyond that it is also immoral and dishonourable, and is concerned with crime and other related activities, which bring in easy and fast money to the stakeholder. In fact, hunger linked with poverty begets crime, and crime begets 'unearned' income. These two possibilities are not only exclusive to the poor, but are also available to the non-poor perhaps to enhance their prosperity with highly disproportionate effort, if any.

The issues that have been raised here may highly be controversial and intricate, and, as such, require to be probed further both qualitatively and quantitatively, and so is the basic hypothesis of concealed poverty (or artificial prosperity) of this Paper. But all that has been said is seen to be true to a large extent in a number of developing countries that are afflicted with abject and low poverty levels accompanied with wide income disparities and high unemployment rates, and where these basic issues are either tackled unsuccessfully at the macro level, or not tackled at all at the micro and grass-root levels. In these countries, the assumptions, as mentioned earlier to motivate the poor to conceal their poverty and helplessness, are valid to a large extent, and poverty is seen not to be truly visible, essentially in terms consumption goods, clothing, personal belongings and the accompanying paraphernalia. If it is at all seen then it is in shelter and housing in terms of highly temporary tin shed shacks located in extremely unhygienic and uninhabitable surroundings. In essence, poverty gets concealed, subject to the given assumptions, only in public life, and not so much within the precincts of poor households.

The most glaring examples (Appleton, 1995, 1998; Dercon and Krishnan, 1998; Bevan and Ssewaya, 1995, African Development Bank, 1998) in this context are from the African continent, where in most of the countries, the link between severe poverty, acute income disparities and high unemployment rates on the one hand, and the severe erosion of poor household budgets and the resulting negligible savings (and, therefore, debt-trap), and involvement in crime, loot and plunder on the other, obtains to a large extent, and this link, in turn, puts a veil on the face of poverty in those countries. Let us focus on such a scenario in the Republic of South Africa, an upper-middle income group country, and the so-called regional power with the largest economy on the continent. In 1993 (the pre-apartheid era), as reported by Hertz (1998), South Africa had an alarming proportion of 53.5 per cent poor people in a population of 40.6 million in terms of household subsistence levels, a Gini-Coefficient of 0.6061 indicating acute income-disparities, and a massive unemployment of 30.6 per cent in the sense that these people were not currently employed, and were looking for work, or had stopped looking for work, or had stopped doing that because no work or job was available. Beyond the post apartheid era, there might have been some improvement in this scenario possibly because of two basic macro-level strategies of the Government namely, Reconstruction and Development Programme (1994) and Growth Employment, and Redistribution: A Macro Economic Strategy (1996), but i) a large number of people still lives in abject poverty, and is subject to periodic malnutrition; ii) the Gini Coefficient is still as high as 0.54 and indicates alarming income inequalities; and iii) unemployment, no matter how it is measured, is still very high (ranging from 24 per cent in urban areas to 41 per cent in rural areas), and none of the sectors are growing adequately to alleviate it (Kingdon and Knight, 1998). Conditions are worse in the backward regions of the country like the North-west Province where 57 per cent of its 3.3 million people live below the poverty line and the unemployment rate is not only high but has been rising over the years: in 1994 it was 34 per cent and in 1996 it rose to 36.4 per cent. In rural areas it has been more than 50 per cent.

This is one side of the story. The other side relates to the high cost of these severe conditions to individuals, especially the poorer lot. They suffer not only from the lack of income, but they are also marginalised by society. This eventually translates into a heavy burden on the social fabric in communities and is extremely damaging for the society as a whole. It gets distinctly exhibited in the loss of income and, therefore, of savings too, resulting eventually in personal debt-traps, and the involvement of the majority of the poor in crime and its related activities.

Economic literature so far does not reveal any quantitative (bi-variate or multi-variate regression or correlation) analysis for any country including South Africa on the link between the two sets of variables as described above.[7] One has, therefore, to rely just on certain scattered and isolated data, if at all available on the relevant variables, and also on qualitative analysis as based on one's observation and perception of the poor people. For example, in South Africa it has been observed that a majority of the poor invariably try to live beyond their means by buying not only essentials but also non-essentials for their living through borrowing and financing that are easily available either at Easy Cash Loan joints or at most of the stores. By doing so, both their present and future income is fully eroded, and they get caught in a vicious debt-trap. Not only this, they also get engaged in making money through illegal activities like theft, larceny, plunder, loot and mugging.

There is some literature on global and country-wise (especially South Africa in the present context) saving patterns (Aron and Muelbauer, 1998A, 1998B, 1999; Blumenfeld, 1998; Prinsloo, 1994) which apply to government, corporate and household sector savings in relation to national saving rate, but they do not, in any way, reflect on the behaviour of poor household savings, if any, and on their consumption profiles. This issue of personal savings in South Africa in general has been tackled (Ebert; Ammet, 1997; Kantoor and Barr, 1990; Mohr) to show, amongst other things, that the change in the composition of personal saving from discretionary to contractual (bound by some form of long-term legal commitment) possibly because of the severe problems of poverty, inequalities and unemployment, indicates a decline in domestic saving[8] and, in turn, an increase in household demand for credit (borrowing) which is provided essentially by non-bank institutions and that too at high rates of interest. Such a decline in personal saving in general is the greatest source of worry for the economy because unlike public dissaving it cannot be directly controlled by monetary authorities. There are possibly many reasons for the decline in household saving, but the most important reason in the present context is concerned with households' efforts to sustain living standards by increasing absolute liabilities, say by mortgaging, amongst other things, their future income to the creditors and finance-providing units that also include shops and showrooms. The problem becomes more serious for the poor, and they eventually get caught in the vicious circle of debt-trap.

The other temptation for the poor, as we have already mentioned, is crime and violence, which begets easy (rather unearned) income and, thus, helps them to get out of the shackles of poverty. This must not be misconstrued to mean that poverty per se is necessarily associated with crime and related activities. But when poverty, including wide disparities and high unemployment rates, gets combined with a perception that the state, on the one hand, does not do much for the poor, and the poor get highly marginalised, isolated and excluded socially, on the other, there emerge very strong incentives that force the disadvantaged poor to crime and violence (Kramer, 2000). It is also true that the less social support there is in a community, the higher the crime rate will be (Cullen, 1994). There is, therefore, a critical link between poverty, inequality, unemployment, exclusion, and violence that stems from the pursuit of monetary success through effective, illegal means. In the South African context (Morris, 1996; Cross et al, 1996; Louw and Bekker, 1996; Louw, 1996A, 1996B, 1996C), all this is very true to a large extent, but combined with it is also its long history of apartheid and multi-racial texture. Despite its relative wealth, solid economic growth in recent years, and won plaudits from the international financial community for its effective budgetary policies, the country faces the serious problems of crime, violence, and corruption of course with inter-province variations which are directly proportionate to the various social indices of poverty, inequality and unemployment.

As compared to Africa, the overall social scenario in Asia is not that depressing. According to Asian Development Bank (2000)

i. the overwhelming majority of the poor in Asia live in South Asia, and the majority of the poor in South Asia live in India, where up to mid-seventies, there was no visible progress in reducing poverty and more than half of all Indians lived below the national poverty line. But since then, however, progress has been made. By the beginning of the nineties about one in three Indians lived below the national-poverty line; and

ii. the Gini coefficient, the standard measure of overall inequality, in Asia is lower than in other parts of developing world. It generally falls in the range of 0.3 to 0.4, and has been fairly stable. In South Asia, the Gini coefficient ranges from a low of 0.30 in India to a high of 0.38 in Sri Lanka.

But the fact remains that India has failed to meet poverty and hunger reduction targets. It has 250 million poor people (below the poverty line), the largest in the world. About 208 million of these are seriously undernourished. However, the percentage of under-nourished population has decreased from 38 per cent in 1979-81 to 26 percent in 1990-92 and 21 per cent in 1996-98. The biggest constraint in poverty reduction is an addition of 16-17 million people to the total population every year. (Singh, 2001).

On the employment front, according to the latest UNDP's Human Development Report (2000), released in June 2000, employment in the formal sector has grown impressively in the past decade with the result that the rate of employment increased 2.4 per cent a year during 1987-1996, outpacing labour force growth of 2.2 per cent. But, according to the results of the latest survey conducted by the National Sample Survey Organisation (NSSO, 2000), employment has declined marginally in both urban and rural areas during 1999-2000. In urban areas, employment for females was lower by more than one percentage point while it remained on the same level for males.

Despite all this, the widespread income poverty and income equality still exists in the country. It becomes worse when we add Amartya Sen's contention to say that poverty is much more than lack of income. It is also lack of voice, it is also lack of empowerment, and it is also lack of good governance. Promoting opportunities for poor is not sufficient. They need to be empowered through elections, decentralisation to the grass roots, responsive administration, an effective judiciary and good governance in general. And, they also need a greater voice in managing their future, and greater inclusion in the decision-making process. India has miserably failed in reducing poverty in terms of such a wider connotation.

But no matter what it is, India is much better placed, and has tackled its problems of poverty, inequality, and unemployment much better and more effectively than many other developing countries not because of trickle down but because of a number of grass-root and micro-level area-specific and people-specific programmes launched by the Government at various times (Anand, 1999). But, despite the fact that the social scene in India, in terms of the given indices, is a lot better in all respects as compared to other South Asian and African countries, the poor in India (of course with the exception of those staying in the metropolitan cities), unlike their counterparts in other countries (like South Africa), invariably still live within their means, save whatever they can by living frugally, go for discretionary rather than contractual savings, do not mortgage their assets or future income, and above all, do not, in any way, try artificially or illegitimately, to make their poverty concealed or disguised. Poverty is still openly seen in India in its crude form, and is very well reflected on the haggard, tired, anxious, stressed, underfed, and famished faces of the poor, through their used, shattered, shabby and torn clothes, and also through the shattered shacks and mud houses in the rural areas and the city slums. Most of these people are both wage and self-employed as vendors, hawkers, labourers, peasants, rickshaw and trolley pullers, and domestic servants. They work hard and live their lives honestly and value their self-esteem more than anything else. Despite living a difficult life, the interesting thing is that they do save money in the high-wage seasons to tide over financial gaps without much dependence on others. They do spend on their own on social occasions and festivals. In order to enhance their income they might favour a large family, and encourage their children to work instead of borrowing and getting caught eventually in debt-trap and perhaps also in illegitimate activities. Of course, there are exceptions which are perhaps more rampant in big cities where the marginalisation of the poor, and even the lower-income class is much more, and the demonstration-effect works faster tempting them to conceal their poverty (both absolute and relative) through the easy means of borrowing and more so by getting involved directly or indirectly in criminal activities. It is for this reason that crime is seen to be more rampant in larger urbanized areas.

What has been said above should not be a cause of being complacent. There is still a long way to go, and much more has to be done to ameliorate the lot of the proletariat keeping in view the wider connotation of poverty as enunciated by Amartya Sen. There is a need to have fresh programme to encourage self esteem and community solidarity, to eliminate discrimination against poor, and to increase the empowerment of the underclass. If all this is not done with strong political and bureaucratic will, the day is not far when India will become another South Africa, or any other such other country that faces the serious problems of an extremely vicious personal debt, and crime situations.

SECTION III

THE RESULTING VICIOUS CIRCLE

We have seen how the inclusion of the role of the State in the conventional framework of Economics brings us to the domains of what is termed as the New Political Economy, the positive side of which very clearly defines the role of the State in terms of rent seeking and directly unproductive profit seeking activities. These activities, in fact, survive on their own and work against the smooth and economically efficient functioning of the economy. Beyond that they lead to many adverse effects offering strong barriers in the way of the trickle down process, thereby setting in motion a highly complicated vicious circle of rent seeking. In other words, these activities amount to leakages in the national income, which not only corrode the whole growth process, but also adversely affect the trickle down process. But even if growth takes place otherwise, its benefits do not reach the masses essentially because of the rent seeking and other vested activities of the State and its components. The rent seeking activities, therefore, provide the initial impulse to the failure of the trickle down effect, which, in turn, accentuates the already existing poverty levels including, unemployment, and income gaps. The more acute is the poverty, more is their marginalisation of the poor, and greater is, thus, the propensity to conceal poverty through various means like, borrowing and crime-related activities, both of which beget easy money to the stake holders. Such impetus to crime strengthens the mafia links and also encourages organized crime, and even extends to the higher strata of society that includes, amongst others, the basic role players in the guise of political entrepreneurs (both ruling and non-ruling) and their supporters (both administrators and voters) in the whole game. Such nexus and linkages give a further boost to rent seeking and other related activities. The circle, thus, gets completed, and rent seeking leads to further rent seeking, and this chain reaction goes on unabated, viciously trapping the economy in a deadlock situation. The diagram on the next Page depicts the operation of such a vicious circle. This complicated vicious circle, apart from being interlocking in itself and leading to further rent seeking through a variety of factors discussed earlier, is also anti-growth, anti-equity, and anti-saving. It goes on unabated and generates, at increasing rates, rent-seeking leakages (essentially, horizontally and diagonally), crime in all its manifestations, private debt trap and mafia nexus/linkages to the advantage of the major role players in the whole game.

Although this is a purely hypothetical scenario devoid so far of any empirical studies in its support, yet it is observed to exist in different countries, though in different degrees. It has also started to emerge in certain other countries, where the trickle down process has utterly failed because of reasons mentioned earlier, and, as a result of this failure nothing positive (in terms of economic and social provisions) ever gets percolated to the masses in general, and the equity considerations, if any, have their focus more at the macro level, and nothing much is done at the grass root levels. The root cause of this depressing

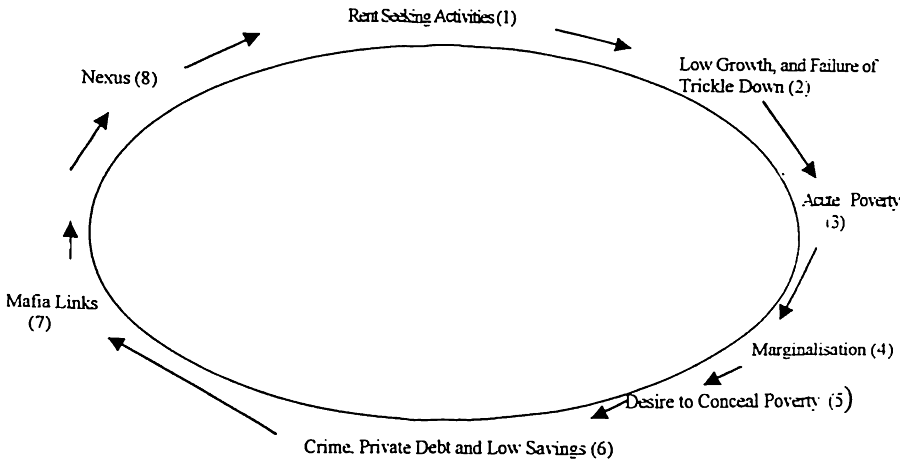

Diagram 1: Showing the Vicious Circle of Rent-Seeking Activities

scenario, as we have said earlier, is the vested interests of the so called political entrepreneurs and their supporters, that get exhibited in the form of rent seeking and other nefarious activities, which are subject to increasing returns because of their self-generating capability, larger involvement of the stake holders, and above all, because of the inefficient legal system. In order to break this vicious circle of rent seeking the very best way out is to minimize or eliminate, if possible, such activities of the political entrepreneurs and their supporters. But the political experience of countries completely negates such a solution. We have, therefore, to depend on the *second best solution* that relates to the efficacy of the legal system. The basic rules of jurisprudence to tackle such situations are always available in almost all the countries, but the reality is that these rules are not effectively and timely used by the concerned authorities to curb the given situation and the role players, thus, keep on playing their game of manipulation and manoeuvre for their own benefit (in terms of enhancing their electoral support, and reaping political mileage to the detriment of the whole economy. The judiciary should, in fact, take matters in hand and ensure that the major role players of the State do not resort to their clever stratagems. This perhaps is the only effective way to break the given vicious circle of rent seeking, and bring back the economy to its normal functioning. There is also a *third best solution* that can perhaps reduce both the extent and intensity of marginalisation of the poor by the richer sections of the society which, as we have seen, is a crucial link in the operation of the said vicious circle. This solution relates to well focused urban policies. It is seen that marginalisation in urban areas (or urban apartheid) has become increasingly extreme in most of the countries, and challenges the fight against poverty (Sane and Binde, 2001). Urban policies, therefore, have to be tuned to ensure, apart from other things, the common social ethos of the rich and poor, so that income-based, caste-based, class-based, and even racial-based discrimination and intolerance is at least reduced, if not completely eliminated from the urban areas, thereby weakening the operation and the impact of the vicious circle of rent seeking.

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NOTES

[1] The author is a Fellow at the Indian Institute of Advanced Study, Shimla. Prior to that he was Professor and Head of Economics at the University of Allahabad, India and also at the University of North West in the Republic of South Africa.

[2] As compared to Keynes' work on economic theory and policy analysis, his work on methodology, " *such as the role of institutions, the use of econometrics for testing theories, the value of prediction, the nature of animal spirits, and the importance of persuasion in the conduct of economic policy*" was highly significant, but it was generally neglected initially being overshadowed by his other work on former issues (see Lawson and Pesaran, 1989)

[3] The extreme side of supply-side economics is associated with the name of Arthur Laffer.

[4] For this Section See Anand, 1996

[5] Trickle-down effect is understood here in a completely positive sense. If considered negatively, it does work very effectively, without any barriers whatsoever, in all man-made systems, percolating all kinds of immoral vices and ill practices like indiscipline, inefficiency, and corruption in all its facets, from top to bottom. For this Part see Anand, 2001A.

[6] Based on Anand 2001B

[7] There are, however, models describing household behaviour and the consequences of poverty (Muller, 1998), which provide both theoretical and empirical analysis of permanent and seasonal interactions between consumption, production, labour, health and nutrition of households, and of their consequences on welfare analysis.

[8] According to South African Reserve Bank Quarterly Bulletin, the trend in net personal saving (NPS) fell on an average from 5.2 per cent of GDP for 1975-1979 to 1.3 per cent for 1995-1996.

Dr. Vinod Anand has been Professor and Head of Economics at the University of Allahabad and he has served as Professor at many universities in South Africa also. He has written a number of books and contributed several articles in national and international journals. Presently, he is a Fellow at the Indian Institute of Advanced Study, Shimla.

ISBN: 81-7986-013-2

Rs. 60