UBI: Policy Brief

In this brief, we contest the proposal that the Universal Basic Income (UBI) in India will secure more egalitarian economic outcomes. We first review the different strands of argument in favour of a UBI. We argue that in one important case, the theoretical framework does not argue for a UBI but for a non-universal re-distribution of income. This argument is supported, either on grounds of greater instrumental efficiency, or by postulating that a restricted UBI is affordable, and therefore desirable. We argue that the proponents of a genuine UBI are in fact implicitly making a disturbing admission: that India's growth strategy is, and will continue to be, highly exclusive and it is therefore necessary to correct for this by invoking some form of ex-post Kaldor-hicks re-distribution, cast in UBI language, that is based, in effect, on the invocation of second theorem of welfare economics.

Chapter 9 of the *Economic Survey 2016-17* presents arguments for UBI, and the conceptual case against UBI. The survey acknowledges that UBI is unconditional and universal but the unconditionally and universality is interpreted as every person having "a right to a basic income to cover their basic needs". It does not advocate an *actual* basic income for all citizens and argues that it should be "de-facto quasi-universal and gradual". To this end, it proposes a UBI for a particular demographic (women, pregnant mothers, widows or for urban citizens). Thus, what this, in effect, proposes is not a UBI but a targeted scheme inspired by universalization which is to be attained at some future undefined point. The rest of the chapter is, in effect, an argument existing forms of targeting, particularly exclusion errors in such targeting, and positive externalities to the socio-economy generally from instituting a quasi-UBI. These include insurance against risk, psychological benefits, improved bank profitability etc.

Pranab Bardhan and Vijay Joshi are perhaps the most eminent economists who have advocated the UBI. Unlike the economic survey, Bardhan advocates a genuine UBI and clarifies that the goal of UBI is to provide minimum economic security for all citizens and not to eradicate poverty. He argues that the UBI should be additional to existing welfare programs and should be financed by ending "non-merit subsidies-which are subsidised that mainly benefit the better-off-reducing tax concession to companies and raising the tax-GDP ratio". Collectively he expects that this would raise an additional 10% of GDP in public resources which could be used to fund a genuine UBI.

Vijay Joshi also argues for a universal UBI equal to Rs. 3500 per head per year at 2014-15 prices. His main argument for a UBI is that universality addresses a major development problem in India, which is that "there is a huge bunching of people around poverty line". The UBI would improve the economic security of several hundred million people and would also cushion them against the shocks that will come from deep fiscal adjustments which he considers necessary for improved policy effectiveness. These include all forms of subsidy that do not have to do with social expenditures as-well-as ineffective expenditures on poverty programs. Like Bardhan, he estimates that this, along with a more aggressive privatisation program, would free up public resources equivalent to 10% of GDP. However, he only proposes to use 3.5% of GDP for the UBI, the rest is going to increase public investment and social expenditures.

The details of these proposals have been critiqued by many economists (Dreze 2017, Saith 2017, Aiyar 2017, Shah 2017, Mahendra Dev 2017). These critiques have mainly focussed on affordability of UBI, its money metric approach and a critique of pilots and fieldwork used to justify the UBI.

Thus, of the three major arguments in the favour of UBI, one doesn't argue for a Universal Basic Income at all. The other two that do justify the UBI either instrumentally (Bardhan) or to protect the poor and vulnerable from the costs of a "deep fiscal adjustments" that is pre-requisite for inclusive growth. In policy terms the argument for UBI seems to have been made by highlighting its superiority as a measure to reduce poverty and vulnerability. This superiority is also sought to be established by showing how a UBI could be financed by reducing these subsidies.

The argument over whether UBI could be financed by ending all other forms of transfer and subsidies is a facile one. India's price subsidies are dysfunctional because they do not meet their intended objectives. But they do not have ending poverty as a common objective, though it is politically convenient to argue that they are pro-poor. Food and fertilizer subsidies are meant to benefit incomes of farmers and provide limited cheap food to all those who want it. Both may help the poor, but no sane person would argue that they would end poverty. Most other subsidies, tax exemptions, etc. are meant to stimulate growth or exports or effect structural change, not end poverty. Even the MGNREGA is confused in its objectives; the intention appears to provide employment in public works to those who want it with an added aspiration that such employment would create capital assets. If the objective were to merely compensate for lack of employment opportunity then the simplest thing to do would be to transfer income worth a 100 days minimum wage to those unable to find work for that period. The latter may be poverty reducing; the former cannot be justified on poverty alleviation grounds.

UBI is nothing if it is not universal. Hence, those who argue for a targeted basic income as an instrument of poverty alleviation, are not talking about UBI, but about an income subsidy to the poor. Development economics has acknowledged for some time now that handouts to the poor are not a solution to the problem of poverty, but merely an instrument to alleviate it, when economic growth does not do so. Participation in growth is what ends poverty, handouts are invoked when this does not happen. This important insight has been bypassed, if not entirely missed by both the proponents and the critics of UBI. In what follows we shall show why this is important as it conceals a disturbing implicit assumption about our aspirations and expectations from the process of India's economic development.

The relationship between Equity, inclusion and growth: an exposition by example

It is a *non sequitur* that equity is an important consideration in securing a country' development transformation. However, equity is not the same thing as inclusion. It is perfectly possible to secure an equitable society that is not inclusive. Equity is about how the benefits of growth, once secured, are distributed. Inclusion is about how people participate in the process of increasing levels of output, and income. The greater the number of people that participate in delivering increased output and income, the more inclusive is growth. And the greater the contribution of each and every citizen to delivering increasing levels of output and income, the more inclusive is the growth process. As a development strategy, inclusive growth is therefore about securing the productive inclusion of the maximum number of people in delivering growth, while growth with equity is about distributing the benefits of growth, by redistributing its benefits from those who disproportionally gain from it, to those who disproportionally lose. It is a process that kicks in, after growth has happened, rather than when growth is happening.

To see this, consider the following numerical example. Let us say that India is able to achieve 10 per cent growth by adopting a particular strategy. This means that total output increases by 10 per cent in a given year. Since increases in output must exactly equal increases in income, if the income of each and every Indian household increased by exactly 10 per cent *without anygovernment redistributive intervention* then this would mean that each and every Indian hasproductively contributed equally to growth. Each and every Indian household would see an equal percentage increase in their income which they would then use to increase their welfare by consuming and saving (in some combination) 10 per cent more. Now consider a situation where the bottom fifty percent (measured in terms of household income) of Indians households increase their contribution to output (and therefore income) by 20 per cent, while the top fifty percent see it increase by 5 per cent. The latter case is *more* inclusive and therefore *more* equitable than the former case. Conversely if the contribution to output of the top fifty per cent households was double that of the bottom fifty per cent then growth would be *less* inclusive and less equitable than the first two cases.

The choice of the 50 per cent threshold is to keep the example simple and to illustrate the difference between inclusion and equity. One could equally ask the following question: If output in India grows by 10 per cent then what was the contribution of the bottom 10 (or 20 or 30) per cent of households to this 10 per cent growth. The higher the number, the more inclusive *and equitable* is the growth process. If a country grows at 2 per cent then an alternative pathof 10 per cent growth would have to be very exclusive to be less equitable than the former. In this example, even if the entire 2 per cent growth was due to the contribution of the bottom fifty per cent, even a highly exclusive strategy that delivered overall growth of 10 per cent but in which the bottom 50 per cent contributed anything more than 2 per cent would be more equitable.

The intention of the above illustrative example is not to argue for trickle down growth or for ignoring equity. The intention is to (a) show that growth and inclusion are not the same thing (b) the link between equity, inclusion and improvements in the welfare of the relatively worse off is more complex than simply a trade-off between higher and lower levels of equity for the same rate of growth.

That being said, the above example illustrates quite simply that for a given rate of growth the greater the inclusion the more equitable it is. This has important implications for our understanding of the analytical framework within which universal basic income is advocated

Universal Basic Income: a disturbing admission

The Economic Survey correctly points to the support for UBI from all ends of the ideological spectrum. But as we will show using the illustrative example above, there is a gloomy assumption regarding the future of Indian political economy underlying this consensus that votaries and opponents of UBI have ignored, or avoided.

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In its simplest form, UBI is a negative income tax. Imagine that every adult Indian has a PAN number. Every month some Indians pay taxes, and some Indians receive a credit of money from the government into a bank account to which their PAN is linked. This neatly captures the essence of UBI- to use taxation to alter the income distribution created by market forces such that those getting less from engaging in economic activity are given some income which is taken from those getting more. This intervention by the State reduces income inequality. But it does make growth more inclusive.

The idea behind this is encapsulated in the second theorem of welfare economics: when an economy reaches its "steady state" i.e. the growth rate at which labour and capital are fully utilised, governments can use fiscal policy to change the income distribution by taxing the rich to give to the non-rich without compromising on growth. This recognizes that markets may fail to secure a desired income distribution even when resources are fully employed, so the State must intervene to correct this. In terms of our example, this is akin to attaining a rate of growth of 10 per cent which is not as inclusive as desired (because, for example, the bottom half of Indian households are only contributing seven per cent to such growth). A UBI then corrects for this by using taxation to reduce the disposable incomes of the rich to increase the disposable income of the poor. Thus, the UBI is only an application of the second theorem, of welfare economics, by which growth is first maximised and then the proceeds are reallocated so as to attain a desired income distribution. It is a *compensatory* device to address the failure of the growth process to be sufficiently inclusive and therefore less equitable than society desires. It does not address the driving cause of such inequity which is that *inclusion* in producing the growth is lower than the level needed to attain the desired income distribution.

The second theorem of welfare economics applies when resources are *fully employe*d. This is deemed to be so when the economy is at *steady* state, namely when everyone is contributing to the production of output at their full potential and, therefore, only improvements in technology, productivity or an increase in the stock of productive assets (land, labour, capital equipment) can raise the growth rate. In such a circumstance, if the income distribution is not as equitable as desired, then the second theorem of welfare economics is invoked to collect taxes from everyone (called a lump sum tax) and give the proceeds of those taxes to those whose incomes are lower than deemed acceptable. Alternatively (and as the negative income tax construct shows,i this is the same thing) to give everyone a minimum level of income financed by taxing those who earn some multiple of this income such that the desired income distribution is attained. The latter variant is what a UBI does.

But developing and emerging economies like India, are so called because they are *not* in the steady state. Hence the focus on steady, high growth- incomes rise as economic activity increases, productivity rises and wages and profits both increase. The benefits of growth ensure an increase in everyone's income and living standards. This has been the case with every historically successful development transformation. Thus, if India grows at 8 per cent a year in real terms and incomes of all rise by at least 6 per cent a year, then the real incomes of *all* Indians would *at least triple* by 2035. And India will still not be in steady state, unless the middle income trap, by 2035.

As the process unfolds, Government intervenes in income distribution only to provide social safety nets for a small minority that is unable to participate in growth and therefore, reap its benefits. Taxes are used to provide "merit goods" (say, health and education) that society judges can be more equitably provided by government than by the private sector, and "public goods" that are produced for national benefit, like defence and justice. Thus, measures like the UBI are only invoked if the growth process is so inequitable that a majority of the population, or even a large plurality, fail to participate in, and therefore benefit from, growth.

The political consensus around UBI thus reflects a disturbing admission; India will triple its GDP in 15 years, but there is no expectation that this will lift all boats. Growth is expected to hugely benefit the minority who possess the human and financial capital to produce it and earn incomes from it – the rest, much more than half the population, will require a permanent transfer from this minority. (The alternative interpretation – that there is an ideological consensus that India will grow at far less than 8 per cent a year, is too depressing to contemplate). This is an admission that our growth path will be inherently unequalising, that the Prime Minister's stated vision of one *decent* job in every household will not come to pass; for if it did, then the UBI would not be necessary for a majority of Indians! The Economic Survey touches upon this in a footnote saying that we cannot expect income and employment to move together any longer. But we must face reality in more than a footnote. The cross-ideological support for UBI is an admission that inclusive growth is not a realistic part of the future India story, and the State will therefore need to intervene continuously and massively to correct the income distribution even before the economy is at full potential.

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