PRIVATISING PUBLIC ASSETS: INCREASE WEALTH INEQUALITY

(Mains GS3: Indian Economy and issues relating to planning, mobilization, of resources, growth, development and employment & Effects of liberalization on the economy, changes in industrial policy and their effects on industrial growth.)

Context:

- Government is putting the flagging economyback on center stage after announcing the biggest privatization drive in more than a decade and making renewed attempts to ring fence the crisis-ridden shadow banking sector.
- But the government has adduced no reasons for the proposed privatisation of several public sector assets other than to generate resources for its spending.
- Selling public assets, which is analogous to a fiscal deficit leads to poor economics and increases wealth inequality

Selling government assets:

- Selling public sector assets does not "release" any resources from private use for government spending.
- The resources the government obtains by spending the sale proceeds of public assets are none other than the resources lying idle in the economy.
- Output that could have been produced by utilising idle capacity and unemployed labour, but is not produced because of lack of demand, now gets produced as demand gets generated by government spending financed by the sale of public assets.
- For example: The government borrows say Rs 100 from banks, uses it for spending, and then sells public assets worth Rs 100 to raise this money and return it to the banks, so that its net indebtedness does not go up.

Financing government spending and fiscal deficit:

- Financing government spending by selling public sector assets is basically no different from a fiscal deficit.
- In the fiscal deficit case, the government puts its bonds — directly, or indirectly via banks — in private hands
- And in the financing government spending case, the government puts its equity (held in public sector assets) in private hands.
- The only difference between a fiscal deficit and selling public assets lies in the nature of the government paper that is handed to the private sector.
- The macroeconomic consequences of a fiscal deficit on the economy are no different from those of selling public assets.
- Finance capital, and institutions like the IMF, do not recognise this fact, and treat the sale of public assets on a different footing from a fiscal deficit, for ideological — not economic — reasons, because they ideologically favour a dismantling of the public sector.

Fiscal deficit and wealth inequality:

- In a situation of demand-constraints, where unutilised capacity and unemployed workers exist aplenty, if an appropriate monetary policy is pursued, it can have only one adverse effect i.e. It gratuitously increases wealth inequality in society.
- A fiscal deficit generates an excess of private savings over private investment exactly equal to itself.
- The government expenditure financed by the fiscal deficit creates additional aggregate demand that increases output and incomes until the additional savings generated out of such incomes exactly match the fiscal deficit (with private investment given).
- These additional savings accrue to the savers without their having to reduce their consumption, compared to the initial situation (that is, prior to government expenditure increase).
- Since savings represent additions to wealth, this amounts to putting extra wealth gratuitously into the hands of the rich (who are primarily the savers).
- If the same government expenditure was financed by taxation, no matter who was taxed, then there would be no addition to private wealth, and hence no increase in wealth inequality.

Tax- financed government expenditure:

- Avoiding a fiscal deficit is important for wealth equality.
- Thus, Tax-financed government expenditure should always be preferred to fiscal-deficit-financed government expenditure.

Selling public assets create wealth inequality

- Selling public assets, which is analogous to a fiscal deficit, also increases wealth inequality quite gratuitously.
- It does so by putting into private hands not just wealth in the form of claims on the government (as a fiscal deficit does), but in the form of public assets, and that too at prices well below the capitalised value of earnings (for otherwise private buyers would not accept them).
- Instead of taxing away the additional wealth that a fiscal deficit puts into private hands, this strategy actually puts public assets into private hands.
- This increases wealth inequality for two reasons: First, it does so exactly as a fiscal deficit does; and second, the public asset it puts in private hands is under-priced.
- Thus, the privatisation of public assets for financing government expenditure is utterly inexcusable.
- It increases either poor economics or increase wealth inequality.

Conclusion:

- Taxing the private wealth will help in maintaining fiscal deficit and decrease in wealth inequality.
- If the government is unwilling to impose higher wealth or profit taxes, it can raise GST rates on several luxury goods, after consultation with the states.
- Thus selling public assets to finance government spending is both undesirable and unnecessary.