Taking a fresh look at the institutions of economic management in colonial India explains much about the history of the last decades of the raj. The concept of political economy—the interaction of economic forces and political choices—provides a useful approach to the study of government economic policy and practice that can give a new perspective on the history of the late British Empire as a whole.

The economic historiography of the British Empire is at present in a confused and confusing state. This is especially true of that period which saw the decline of colonialism, the first half of the twentieth century. There are two major difficulties. The first is that the old notion of a distinct imperial economy has collapsed in recent years, and researchers have preferred to seek the key to imperial economic history elsewhere—in the local economies of the dependent territories, in the metropolitan economy of Britain, or in the international economy of which both Britain and her colonial possessions were merely particular localized expressions.1 The second is in trying to relate the explanations of the end of the British empire that deal with economic matters to those that deal with political ones.2

One solution that has become increasingly popular focuses attention on the political economy of the Empire—the interaction between economic forces and political choices in territories bound to Britain by some formal tie. It has even been suggested recently that this approach offers "the best evidence for a unified field theory of the British..."
Empire,” since “the institutions of economic management, the terms of trade, the broad conditions of the international economy, and the standardisation of data through statistics, allow for comparisons.” The term political economy, however, cannot be used as a magic talisman: it requires further specification to be a useful tool. In imperial economic history it is government policy and official institutions that offer the most promising subjects for refining the approach and demonstrating its value. The example of India makes an especially good case study, for the British raj was one of the longest-lasting and institutionally most complex of colonial administrations.

In examining the relationship of economic realities to political practicalities in official policy making in India the first priority is to isolate the interests the policy was intended to serve. “What is the purpose of British rule in India?” was not a question of much interest to the majority of colonial bureaucrats, and yet the trend of their actions showed that they did have an answer to it. Government policy, at least the “high policy” made on the telegraph wires between London and New Delhi, was meant to secure a narrow range of objectives of particular interest to government itself, and in the attainment of which government action was all-important. This lowest common denominator of official concern can be termed India’s “imperial commitment,” the irreducible minimum that the subcontinent was expected to perform in the imperial cause. The commitment was three-fold: to provide a market for British goods, to pay interest on the sterling debt and other charges that fell due in London, and to maintain a large number of British troops from Indian revenues and make part of the local army available as an “imperial firebrigade.”

During the last decades of the raj contradictions within the imperial commitment released a malign dialectic of their own. From the Indian perspective, imperial commitments depended on the twin foundations of British rule—political consent and public revenue. Each arm of the imperial commitment cost the government of India dear and diverted Indian resources into the pockets of British businessmen, bond-holders, and taxpayers. At the same time the relative poverty of the Indian economy limited the amount that could be extracted, while the British bureaucracy was convinced that the secret of successful government in India lay in low taxation. From the 1860s onwards India followed a policy of financial and administrative decentralization for fiscal as well as political reasons. By 1919 the central government had surrendered its rights over the staple Land Revenue to provincial administrations in an

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4 As Lord Canning pointed out in the early 1860s, “I would rather govern India with 40,000 British troops without an income tax than govern it with 100,000 British troops with such a tax”; quoted in A. D. D. Gordon, Businessmen and Politics: Rising Nationalism and a Modernising Economy in Bombay, 1918–33 . . . (New Delhi, 1978), p. 11.
attempt to buy the political peace needed to expand the tax base. In the interwar years the government almost entirely depended on tariffs and income tax for any significant increase in revenue. Customs duties were raised repeatedly, indirect taxes being much easier to collect and also politically more popular. Ultimately local revenue needs severely damaged India’s role as a market for British goods.\(^5\) Over the same period the government found it increasingly difficult to keep its military establishment up to strength. In the great crisis of imperial defense from 1939 onwards, as in 1914–1918, the British government was forced to take over financial responsibility for much of India’s war effort.\(^6\)

The financial problems that the government in London faced were caused by competition between imperial and domestic interests for scarce resources. The difficulties created by India’s sterling payments were of a different order and represented one of the most intractable problems for British policy after 1919. It has been suggested that the payments of interest and principal on loan capital, and the Home Charges, represented ‘‘the most important ‘vested interest’ of Britain in India’’ between the wars.\(^7\) The payments, however, were more significant for British taxpayers than for British bondholders. During the economic crisis of the early 1930s the British government became convinced that it could not avoid making good the payments should the government of India default, and that this would severely damage international confidence in sterling as well as the political credibility of the Indian authorities. The result was that the Secretary of State for India, trying to reconcile ‘‘the demands of political expediency with the needs of stable finance’’ in the drawing up of a new constitution, was encouraged to make sure that the creation of an Indian finance minister responsible to a popular assembly would not lead to a real transfer of authority over external financial policy.\(^8\) The compromise made it difficult to seek new political support in India by financial or constitutional concessions.\(^9\) No real progress could come until 1945, by which time the novel arrangements for financing India’s participation in World

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\(^7\) Rajat K. Ray, \textit{Industrialization in India: Growth and Conflict in the Private Corporate Sector 1914–47} (Delhi, 1979), p. 7. This characterization is based on the “financial imperialism” that some authors have seen at work in India in the interwar years; see R. Palme Dutt, \textit{India Today} (Bombay, 1940).


\(^9\) As an India Office official pointed out late in 1930, “‘the financial stake of His Majesty’s Government and the British people in India remains, for all practical purposes, as a permanent obstacle to anything that could reasonably be termed financial self-government’”; private note by C. K\[isch\] Dec. 1930 in India Office Finance Department file L/F/7/2396, Finance Collection 381, India Office Records.
War II had resulted in the repayment of all the old debt and the acquisition of sterling balances four times as large.

Throughout the first half of the twentieth century British rulers in India were constantly under pressure to admit that their economic policy was designed to favor foreign interests at the expense of Indian ones. By the interwar period native critics of the colonial government had refined the old nineteenth-century critiques of the drain theory and the swadeshi movement into an attack upon imperial costs, the rupee ratio, and tariff policy. Thus the eyes of the economic nationalists were firmly fixed on what we have termed India’s imperial commitment. There can be no doubt that the particular interests of the colonial government determined that the main lines of its day-to-day economic policy should encourage the externally-oriented sectors of the local economy at the expense, if necessary, of the internally-oriented ones. This was a plausible policy so long as it seemed likely that the international economy’s influence on India was benign, or could be made so by improvements in native economic institutions. In the interwar years, however, this view became increasingly hard to sustain. Yet the colonial government was still committed to its external obligations and, however reluctantly, saw these as an inescapable first priority. Thus, when in the late 1920s the government of India was faced by a shortage of remittance to meet its obligations in London, it was compelled to withdraw currency notes from circulation in India in order to make exchange from the currency reserves in London available to the Secretary of State. The action unfortunately exacerbated the tight money and capital scarcity that had caused the shortage of remittance.¹⁰ The difficulties of the domestic credit-distribution system at the time, which were certainly not eased by the action government took to meet its own obligations, were in turn a major cause of the dislocations in the domestic economy, leading to widespread discontent and political protest in the 1930s.¹¹

In reality the raj was fast running out of room in which to maneuver.¹² The colonial administration that had developed in India in the late-


The decline of colonialism in India cannot be understood properly without an awareness of both economic and political factors. Studying official institutions is useful, although government policy by itself does not provide all the answers. The best way of putting policy into a larger context is by looking at the areas where economic realities and political practicalities met and interacted. The concept of political economy can be used to give a fresh perspective of the dynamics and constraints that underpinned the economic history of the British empire in the twentieth century.