

KAUTILYA – THE TRUE FOUND OF ECONOMICS

ONE

KAUTILYA AND HIS TIMES

PROLOGUE

KAUTILYA'S VISION

Kautilya set out to lay down the foundation, erect the necessary pillars and structures to build and sustain such an ideal economy. He believed that the establishment of rule of law, an impartial judicial system, private property rights, an incentive mechanism to ensure efficiency and honesty of government officials, and establishment of *dharm* through the moral and spiritual rules of human behavior, were the key ingredients for the creation of a prosperous economy.

Kautilya's *Arthashastra* is comprehensive, internally consistent, original and wide in scope. It contains sufficiently large number of significant concepts and hypotheses that clearly establish Kautilya as the founder of economics.

Vishnugupta Chanakya (son of Chanaka), also known as Kautilya, wrote the *Arthashastra*, the science of wealth and welfare, during the latter half of the 4th century BCE. It has 150 chapters that are distributed subject-wise in fifteen books. Kautilya was addressed as an *Acharya* (professor) and a statesman. He has been credited with

the destruction of the oppressive and corrupt Nanda Dynasty and installing Chandragupta Maurya (321-297 BCE) on the Magadha throne. Chandragupta Maurya considered him as mentor and sought his advice on both political and economic matters. Some writers incorrectly claim that he served as a Prime Minister to Chandragupta Maurya. Nehru (1946, p 123) describes their special relationship quite appropriately as: 'He sat with the reins of empire in his hands and looked upon the emperor more as a loved pupil than as a master. Simple and austere in his life, uninterested in the pomp and pageantry of high position.' Kautilya was an independent thinker and it would be incorrect to label him as an administrator only.

It may be reasonable to assume that he was older and undoubtedly wiser than Chandragupta Maurya. Kautilya was probably born around 360 BCE, was very influential during Chandragupta's rule (321-297 BCE), and might have lived beyond the latter date.

This implies that he was a junior contemporary of Aristotle (384-322 BCE). However, there is absolutely no evidence that Kautilya was aware of Aristotle's ideas. Moreover, Aristotle wrote very little (if any) on economics. Kautilya's *Arthashastra* was very widely referred to and was revered by scholars for more than a thousand years after its writing.

There is no reference to the emperor Chandragupta Maurya or to his kingdom Magadha in the *Arthashastra* since it was meant to be a theoretical treatise designed to instruct kings everywhere and in all times. Kautilya is also credited with two other

works, *ChanakyaSutras* (Chanakya's Precepts) and *ChanakyaRajanitisastra*(Chanakya's Statecraft).

1.1 PROVISION OF HUMAN SECURITY

Kautilya had a grand vision of building an empire encompassing the whole of the Indian subcontinent, prosperous (free from wants), secure against foreign threats, crime-free (free from fear), internally stable and based on secular virtues such as non-violence, compassion, benevolence, truth and honesty. There was a big gap between Kautilya's ideal economy and the one actually prevailing at the time. His goal was to write a theoretical treatise for transforming the actual economy into an ideal economy and sustaining it. Kautilya's genius lay in developing a conceptual framework while anticipating various problems that might arise in the intended transformation, and devising appropriate policies to resolve them. The level of abstraction achieved in the *Arthashastra* is remarkable for his times.

Kautilya set out to lay down the foundation, erect the necessary pillars and structures to build and sustain such an ideal economy. He believed that the establishment of rule of law, an impartial judicial system, private property rights, an incentive mechanism to ensure efficiency and honesty of government officials, and establishment of *dharm* through the moral and spiritual rules of human behavior, were the key ingredients for the creation of a prosperous economy. He critically examined, extended and codified the existing rules

and regulations to establish the rule of law. However, he believed that in the absence of moral anchoring, no amount of rules and regulations could prevent systemic risks.

Joan Robinson (1953) has observed that neoclassical thought paid too much attention to little issues like 'why does an egg cost more than a cup of tea' and ignored the big issues like growth and distribution, which were pursued by the classical economists. However, both classical and neoclassical economists ignored the systemic risk arising from moral decline, foreign aggression or calamities like famine. Kautilya's *Arthashastra* was quite concerned about the losses arising from such disruptions whereas now the sole emphasis is on losses resulting from the distortions (called deadweight loss). For example, understanding the distinction between disruptions and distortions is of paramount importance when the effects of a lump sum tax are compared to those of an income tax. Accordingly, Kautilya formulated three kinds of policies:

- economic policies (*Arthaniti*) to promote economic growth and prevent natural and man-made calamities,
- a judicial fairness policy (*Dandaniti*) for administration of justice, and
- a foreign affairs policy (*Videshniti*) to help maintain independence and to expand the kingdom.

He put heavy emphasis on acquiring new territories, developing the land and building settlements. He invariably analyzed all the available alternatives and recommended the best one. He laid

emphasis on having a diversified economy with good infrastructure and irrigation facilities. He formulated detailed outlines for the various government departments, spelling out responsibilities and salaries of the officers. It was in the pursuit of formulating these policies that Kautilya originated more than a score of fundamental concepts of economics.

A brief review of the existing views on Kautilya's *Arthashastra* is provided in Section 1.2. 'Why Another Book on Kautilya?' is explained in Section 1.3. Reasons for using Rangarajan's (1992) translation of the *Arthashastra* for the basis of this work are provided in the Appendix A.

1.2 PREVALENT VIEWS ON KAUTILYA'S CONTRIBUTIONS

Spengler (1971) and Dasgupta (1993) discuss Kautilya's *Arthashastra* in limited detail. Spengler presents a few but quite fundamental economic concepts contained in the *Arthashastra*. He (1971, p 158) observes: 'Kautilya was, of course, familiar with the general nature of man's response to changes in price and income as well as to changes in the structure of rewards and penalties.' Spengler (1971, p 74) explains: 'His analysis, of course, was implicit, not explicit; it rested upon the assumption that individual behavior could be controlled in large measure through economic rewards and penalties, particularly when these were commensurate with the action to be encouraged or discouraged. Accordingly, while Kautilya looked at economic issues through the eyes of an economic administrator, he was aware that rules must fit man's economic

propensities and foster rather than repress useful economic activity.’ Spengler acknowledges that Kautilya not only recognized the agency problems but also suggested many solutions befitting the contemporary situation.

On taxation, Spengler (1971, p 72) remarks, ‘Kautilya’s discussion of taxation and expenditure, apparently in keeping with traditional doctrine, gave expression to three Indian principles: taxation power is limited; taxation should not be felt to be heavy or excessive; tax increases should be graduated. One of his main concerns seems to have been the collection and expenditure of revenue in such ways as to build up the permanent revenue-yielding capacity of the economy. While he manifested little knowledge of tax shifting and incidence, he emphasized the long run, cautioned against too heavy taxation in the short run, and noted that a ruler could not tax at his pleasure, particularly in frontier regions whence disgruntled taxpayers could flee to neighboring countries.’ This phenomenon is now called the Dupuit-Laffer Curve. In fact, as asserted below, a slightly differently shaped curve, which may be called the Kautilya Curve is discernible in his analysis.

On the concept of diminishing returns, Spengler (1971, p 71) observes, ‘He does not explicitly recognize the tendency to Ricardian diminishing returns implicit in his account of the quite unequally colonisable and unevenly cultivable character of India’s lands’. This is a very significant observation since it makes the debate over priority to Smith or Ricardo for diminishing returns irrelevant.

On factors of production, Spengler (p 75) notes that Kautilya understood the 'distinction' between 'interest' and 'profit'. Kautilya discussed wages and rent also. In fact, not only did Kautilya understand the distinction among different factors of production but also discussed how to maximize profits from public enterprises, adjust interest rate for risk premium, pay efficiency wages to reduce shirking and how to determine the circumstances under which to have a wage system or a sharecropping arrangement on Crown land. It is obvious that Spengler acknowledges Kautilya's understanding and his application of the most fundamental concepts in economics. Unfortunately, he explores only a few aspects of Kautilya's contributions to economic thought.

On the other hand, Dasgupta does not think much of the contributions of ancient writers to economic thought (including those of Kautilya). He (p 6-7) makes a sweeping observation, 'In my judgment, "analytic or scientific aspects of economic thought" of the kind Schumpeter was referring to in defining economic analysis, cannot be found in Hindu, Buddhist, or Islamic writings on economic topics; nor for that matter in their Greek, Roman, Jewish or Scholastic counterparts. A history of economic analysis in India would have to start sometime in the nineteenth century.'

The author strongly disagrees with Dasgupta's claims. Reference is made to a few of Kautilya's ideas to refute the prevalent myths about his *Arthashastra*. Chapters 3 to 20 contain Kautilya's treatment of several concepts which, it is hoped, provide sufficient evidence to

correct the prevailing misrepresentations regarding his contributions and maturity of the Hindu civilization.

The most likely reason for the many important omissions by Spengler, Dasgupta and others seems to be that they overlooked the chapters relating to law and order and foreign affairs to which Kautilya applied many important economic concepts. Similar omissions in other works have also been endured for centuries. For example, an important omission regarding Adam Smith's knowledge of diminishing returns persisted for more than two centuries as Samuelson (1980) points out, 'Ricardo and his contemporaries may, however, be in no need of enemies if their defenders must write on their behalf that they missed what was in the *Wealth of Nations* because the relevant material was "scattered" and appears in out of the way chapters where such esoteric subjects as colonies are discussed.'

Evaluation of Kautilya's *Arthashastra* on Political Issues by Non-economists

In the literature on political science, Kautilya has been compared to Machiavelli and even to Plato and Aristotle. The author is not competent to comment on the relevance or nature of such comparisons. However, a summary of their conclusions is presented below. The reader interested in further investigations of this aspect may refer to Basham (1959), Drekeimer (1962), Kangle (2000, part III), Parmar (1987), Ray(1999) and Varma (1995-96).

It is not surprising that different commentators read Kautilya's *Arthashastra* differently. Some find it merely a synthesis, although brilliant, of existing ideas. For example, according to Kamandaka, who wrote *Nitisara* (a set of thoroughly proved policies) during 4th or 5th CE (see Karwal, 1966), Kautilya 'churned the nectar of the science of policy from the ocean of political sciences.'

Others like Ghoshal (see Kangle, part III, p 56) find Kautilya's *Arthashastra* 'a virtual reconstruction of the science'. Kangle (Part III, p 55) concludes, 'It appears reasonable to suppose that except in those cases where divergent opinions are specifically attributed to Kautilya, the bulk of the teaching in this text is materially the same as he found it in the source-books on which he relied'. He (p 56) adds, 'It is, therefore, possible to say that the *shastra* as it emerges from Kautilya's hand is more sober, more rational and inevitably more advanced than was the case in the earlier writings.'

1.3 WHY ANOTHER BOOK ON KAUTILYA?

A serious attempt is made to revise the currently accepted history of economic thought. First, it is claimed that presentation of Kautilya's monumental contributions should succeed in dispelling the deep seated myth that economics originated during the eighteenth century and Adam Smith is the founder of economics.

A claim is only as good as the arguments it stands on. For the first time, strong arguments are provided why Kautilya should be considered as the founder of economics in the 4th century

BCE. Secondly, it is argued that Kautilya's *Arthashastra* may be correctly designated as *Dharmanomics*: economics built on an ethical foundation, projecting economics and economic policy in a more meaningful and socially desirable perspective. Thirdly, it is shown that Hindu civilization is not averse to economic growth as an important goal. A brief overview is provided below.

Kautilya as the Founder of Economics

Kautilya provided consistent and coherent interpretations of more than a score of modern economic concepts. It is claimed that Kautilya pioneered political economy much before appearance of Adam Smith's *Wealth of Nations* (1776). Adam Smith came to be accepted as the founder of economics based on the arguments that (i) he was the first one to write a treatise on economics, and (ii) he synthesized brilliantly the existing ideas. Samuelson has added another argument that Smith was also a theorist, who made original contributions. It is shown in Chapters 3-20 that Kautilya was the first economist who accomplished all these feats two thousand years earlier than Adam Smith. Kautilya carved out economics as a separate discipline.

Additionally, Kautilya's *Arthashastra* is much more sophisticated, both in method and content than Adam Smith's *Wealth of Nations*. In fact, based on the degree of sophistication of his analysis, it could be claimed that Kautilya was a neoclassicist well before the classicists came on the scene.

A strong critique of the prevailing orthodoxies regarding the origins of economics and Adam Smith being its founder is provided here. It is not claimed that Kautilya provided any formal proofs or that the *Arthashastra* as a book is as sophisticated as Samuelson's *Foundations*.

It can thus be claimed that Kautilya's *Arthashastra* is, at least, as important a contribution as Adam Smith's *Wealth of Nations*. It is shown that despite the non-availability of the calculus and statistical methods, Kautilya's economic analysis was reasonably organized, adequately developed, and applied to a variety of problems. The following table provides an insight into Kautilya's contribution and genius.

Table 1.1: A Partial List of Concepts Used by Kautilya

It may be noted that the above illustratively enumerated twenty-one concepts, used in modern economic analysis, were already used and applied in Kautilya's formulations. Adam Smith has the credit for only two. Undoubtedly, the social, the political and the economic institutions and conditions prevailing at the time of Kautilya were markedly different from those of today. Yet, remarkably, almost all of his insights, concepts, and methodology are as relevant today in our industrialized and globalized world as they were in his times.

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