



ECONOMIC EFFECTS OF BRITISH COLONIALISM

Britain's relationship with her Indian colony was one of political subordination, but economic exploitation formed the core of this relationship. This process of colonization was geared clearly to benefit the mother country, even at the cost of the colony. In this chapter we will discuss the aspect of economic exploitation within the process of colonization.



OBJECTIVES

After studying the lesson, you will be able to:

- delineate the three phases of British colonization in India
- comprehend the changes brought by colonial revenue settlements in the Indian countryside
- analyse the mixed impact of colonial capitalist innovations within the colony;
- explain the 'drain of wealth' theory propounded by early nationalists and
- understand the distinct nature of colonial 'modernisation' in the colony and that it did not necessarily imply 'progress'

PHASES OF BRITISH COLONIALISM

Colonial exploitation was carried on broadly through three phases. The **first phase (1757-1813)** of 'mercantilism' was one of **direct plunder** in which surplus Indian revenues were used to buy Indian finished goods to be exported to England. In the **second phase (1813-1858)** of **free trade** India was converted into a source of raw material and a market for British manufactured goods. The **third phase (1858 onwards)** was one of **finance imperialism** in which British capital controlled banks, foreign trading firms and managing agencies in India. This phased exploitation was carried out through a range of economic policies, primarily in the industrial and agricultural sectors of the colonial economy.

17.1 THE FIRST PHASE OF BRITISH COLONIALISM

This 'First Phase' is generally dated from 1757, when the British East India Company acquired the rights to collect revenue from its territories in the eastern and southern parts of the subcontinent, to 1813, when the Company's monopoly over trade with India came to an end.



The British had come to India in the seventeenth century, purely as a trading company, backed by an exclusive royal charter to trade with India, from their queen, Elizabeth I. They set up their first 'factory' on the banks of the Hugli River in Bengal. The Company had managed to acquire permits or a 'dastak' from the Mughal emperor that exempted it from having to pay duties on its trade. This led to a great deal of corruption among the employees of the Company, as the 'farman' was widely misused by them for their private trade. It also meant heavy losses in revenue for the Bengal governors (later nawabs) in way of customs duties. This became a contentious issue and one of the chief factors, which led to the Battle of Plassey, fought in 1757.

The primary function of the British East India Company in this period was to buy spices, cotton and silk from India and sell them at huge profits to the large market these goods enjoyed in Britain. This meant that large quantities of bullion would flow out of Britain into India to pay for these commodities. Despite efforts, it seemed difficult to find British goods that could be sold in India in exchange, to stem this outflow of bullion. Besides the expenditure on buying commodities, the Company also spent very large amounts on the wars that it had to fight with other European powers, all in search of the same goods to trade in. These included the Portuguese, the Dutch and the French. Thus the acquisition of 'diwani' (right to collect revenue) in Bengal, after the Battle of Buxar, which followed the Battle of Plassey, opened the way for the Company to raise money for its expenditure in India.

LAND REVENUE POLICIES

After the diwani of Bengal, Bihar and Orissa was granted to the East India Company in 1765, the maximization of revenue from the colony became the primary objective of the British administration. Agricultural taxation was the main source of income for the company, which had to pay dividends to its investors in Britain. Therefore, the British administration tried out various land revenue experiments to this aim. These experiments also partly determined the relationship that the colonial state would share with the people it governed.

In 1772, the Governor of Bengal, Warren Hastings, introduced a system of **revenue farming** in the province of Bengal. In this system European District Collectors would 'farm' out the right to collect revenue to the highest bidder. This system was a total failure and ruined the cultivators because of the arbitrarily high revenue demands.

To undo this disaster, Cornwallis introduced the system of **Permanent Settlement** in 1793. Under this system, 'zamindars', who earlier only had the right to collect revenue, were established as the proprietors or owners of land. The state's demand for land revenue was permanently fixed. But if the zamindars were unable to pay the full tax on time, their lands would be taken away and auctioned by the state. Through this system, the state tried to create an enterprising class of landowners, who would try to improve crop production in their fields to earn profits. Besides, it would be simpler for the state to deal with a limited number of zamindars than with every peasant, and a powerful section of society would become loyal to the British administration.

But this system led to greater impoverishment of the tenant-cultivator because of the burden of high revenue assessment. It also caused great difficulty for zamindars, many of whom were unable to pay the revenue on time and lost their lands. A large number of traditional zamindar houses collapsed. The system also encouraged subinfeudation i.e. many layers of intermediaries between the zamindar and cultivator, adding to the woes of the peasantry.

**Notes**

To keep out intermediaries from revenue collection, so that the state could acquire a larger share of the income from land, the **Ryotwari System** was started by Alexander Read in 1792, for the Madras Presidency. Later it was introduced in the Bombay Presidency as well. Under this system, revenue was initially collected from each village separately, but later each cultivator or 'ryot' was assessed individually. Thus, peasants not zamindars were established as property owners. Although this system increased the revenue collected by the state, the assessments were faulty and the peasants overburdened by the taxes. The landed intermediaries continued to flourish.

In the north and northwest of India the **Mahalwari Settlement** was followed after 1822 where the state made settlements with either the village community or, in some cases, the traditional 'taluqdar'. Each such fiscal unit was called a 'mahal'. Under this system, some recognition was given to collective proprietary rights.

As a result of the revenue policies of the British, agriculture stagnated and peasants almost became tenants at will. They also increased the number of landed intermediaries, and strongly entrenched the figure of the moneylender in the countryside. Landlords and zamindars became an important class and collaborators of British colonial rule.

The acquisition of diwani rights meant that the Company could now tap the wealth of local rulers, zamindars and merchants in the rich province of Bengal and use them to buy the goods that would be shipped to Britain for sale. Large quantities of wealth, including illegal incomes of company officials, made its way to Britain from Bengal. Company officials amassed huge fortunes before they returned home, and they were referred to as 'nabobs' in Britain, on account of their flashy lifestyles. A lot of this money was used to fuel the Industrial Revolution in Britain. The greed for incomes from land revenue also led the Company to pursue an aggressive policy of territorial expansion in India.

**INTEXT QUESTIONS 17.1**

1. What were the three phases of colonization in British India?

2. What was one of the chief factors that led to the Battle of Plassey?

3. With whom did the Company permanently settle the revenue in Bengal?

4. In which presidencies was the Ryotwari settlement first introduced?

17.2 THE SECOND PHASE OF BRITISH COLONIALISM (FREE TRADE)

The 'Second Phase' is generally seen to have begun with the charter Act of 1813, when the Company lost its monopoly trading rights in India, and ended in 1858, when the British crown took over the direct control and administration of all British territory in India.



As the Company's profits grew, the support they enjoyed from the British government became precarious. Earlier many members of the parliament had 'East Indian' interests, who used the Company's resources to maintain their patronage within the government. But as unprecedented levels of industrialization were achieved in Britain, there was a gradual change in the constitution of the parliament. Adam Smith's book, *An Inquiry into the Nature and Causes of the Wealth of Nations*, heralded a new school of economic thought, which critiqued the idea of companies enjoying exclusive monopolies and lobbied for a government policy of 'free trade' or 'laissez faire'. In a bid to acquire greater control over the Company's earnings, the parliament started attacking individual Company officials with charges of 'misconduct'. The 'Free Traders', dominant in the parliament with the turn into the 19th century, demanded free access to India, which led to the passing of the Charter Act of 1813, thus ending the monopoly enjoyed by the Company in India, while subordinating its territorial possessions to the overall sovereignty of the British crown.

'Free Trade' changed the nature of the Indian colony completely, through a dual strategy. Firstly it threw open Indian markets for the entry of cheap, mass-produced, machine-made British goods, which enjoyed little or almost no tariff restrictions. The passage of expensive, hand-crafted Indian textiles to Britain, which had been very popular there, was however obstructed by prohibitive tariff rates. And secondly British-Indian territory was developed as a source of food stuff and raw material for Britain, which fuelled rapid growth in its manufacturing sector, crucial to the emergence of a powerful capitalist economy. These changes reversed the favourable balance of trade that India had enjoyed earlier. This phase laid the foundations of a classic colonial economy within India through the complex processes of commercialization of agriculture and deindustrialization, which are discussed below.

COMMERCIALIZATION OF AGRICULTURE

It is often believed that the colonial administration encouraged the **commercialization of agriculture** that improved the position of peasants in many areas of the Indian colony. From the 1860s onwards, the nature of agricultural production was determined by the demands of the overseas markets for Indian primary products. The items exported in the first half of the nineteenth century included cash crops like indigo, opium, cotton and silk. Gradually raw jute, food grains, oil seeds and tea replaced indigo and opium. Raw cotton remained the most in demand item. This expansion in cash crop production was accompanied by the building of railways, after 1850, to improve trade networks.

But commercialization seems to have been a forced artificial process that led to very limited growth in the agricultural sector. It led to differentiation within the agricultural sector, but did not create the figure of the 'capitalist landowner' as in Britain. The lack of any simultaneous large scale industrial development meant that accumulated agrarian capital had no viable channels of investment, for it to be converted into industrial capital. Initiatives to expand the productive capacity and organization of agriculture was also a risky proposition, as the sector catered to a distant foreign market with wildly fluctuating prices, while the colonial state provided no protection to agriculturists. Commercialization thus, increased the level of sub-infeudation in the countryside and money was channelised into trade and usury.

The larger part of the profits generated by the export trade went to British business houses, which controlled shipping and insurance industries, besides commission agents, traders and bankers. Those who benefited in the colony were big farmers, some



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Indian traders and moneylenders. Commercialization further intensified the feudal structure of landlord-moneylender exploitation in rural areas.

The so called process of commercialization, which was supposed to lead to capitalist agriculture, was often carried out through very exploitative and almost unfree forms of labour. Tea was grown in plantations in Assam, owned by whites, and they used **indentured labour**, which was almost like slavery. White planters had to force farmers to grow indigo because it yielded low profits and upset the harvesting cycle. This involved inhuman levels of coercion, which eventually led to the indigo-rebellion in 1859-60. Commercialization did lead to limited phases of success in the cotton producing areas of western India in 1860s and in jute production in eastern India, but they were because of increases in demand rather than capitalist innovation in production and organization.

Farmers were forced to grow cash crops also because they had to pay the high revenue, rents and debts in cash. The shift away from food crops like jowar, bajra and pulses to cash crops often created disaster in **famine** years. A decline in world demand for Indian cotton led to heavy indebtedness, famine and agrarian riots in the Deccan cotton belt in the 1870s. The jute industry collapsed in the 1930s, which was followed by a devastating famine in 1943 in Bengal. Although, causes of these famines have been widely debated by historians, it is undeniable that the aggregate production of food crops remained far behind population growth, and millions of people died of starvation and epidemics.



Fig. 17.1 Bengal Famine 1943

Among the limited steps that the colonial government took towards improving agricultural productivity included the construction of some **irrigation canals** in northern, north-eastern and south-western parts of India. 'Permanently Settled' eastern India got left out this government initiative, because there was no scope of increasing the revenue any further. Thus revenue maximization and limited famine-relief in extreme situations were the factors that motivated this public investment. It did lead to great prosperity and commercial agriculture in limited enclaves, especially in the canal colonies of Punjab, but



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it was confined to a small number of already well-off farmers who could pay the high water rates. It also encouraged the cultivation of cash crops like sugar, cotton and wheat, while reducing the production of millets and pulses. In some cases, like the United Provinces, it did not suit local conditions and caused swamps and excessive salinity.

In 1853, Lord Dalhousie took the decision to construct railways in India. Very often the railways have been seen as a marker of the modernization that took place under British rule. But the construction of the railways in India only further strengthened the colonial nature of India’s economic development. The railway network made it easier to penetrate the interior markets and sources of raw material in the colony and linked them to port cities, instead of linking internal markets to each other. The railway network was thus primarily geared to serve the interest of foreign trade. Railway lines built in frontier regions would facilitate army movement and some “famine lines” were built in scarcity areas. Moreover, the whole project was built with British capital, and investors in Britain were guaranteed 5% interest, which was paid out of Indian revenue. Most of the high level expertise and railway equipment like machinery, railway lines and even coal to an extent, was imported from Britain. This ensured that the ‘multiplier’ effects of constructing the railways also remained absent in India.

Amongst other factors, the penetration of the interiors of the country, made possible by the railways, had another grave fall out – the ruin of the Indian handicrafts industry, which had enjoyed patronage both from local ruling elites and markets overseas. With the expanding control of the British, traditional native courts disappeared. The British also enforced an unequal tariff system, whereby the entry of Indian commodities in British markets was restricted by high custom duties. In turn, the Industrial Revolution in Europe enabled the mass production of cheap machine-made goods, which flooded Indian markets. Unable to compete with this, Indian commodities lost both their overseas and domestic markets. This destructive process led to **deindustrialisation** that increased pressure on land.



INTEXT QUESTIONS 17.2

1. Which economist propounded the idea of free trade or *laissez faire* in the 18th century?

2. How did the commercialization of agriculture cause famine?

3. Which region benefited most by the irrigation canals built by the British?

4. How did the Industrial Revolution in Britain lead to ‘deindustrialisation’ in British India?

17.3 THE THIRD PHASE OF BRITISH COLONIALISM

The third phase is seen to have begun from the 1860s, when British India became part of the ever-expanding British empire, to be placed directly under the control and sovereignty of the British crown. This period was one of ‘finance-imperialism’, when some

**Notes**

British capital was invested in the colony. This capital was organized through a closed network of British banks, export-import firms and managing agencies.

Although the process of colonization has been divided into stages, one should keep in mind that this periodisation is in some ways arbitrary. The third phase was merely a consolidation of the trends that were already witnessed clearly in the second phase. It may be more useful to study these phases as heavily overlapping, where new and more subtle forms of exploitation existed alongside older, cruder forms. However, the new development that marked out the third phase was an intensification of the rivalry between developed and industrialized countries, for colonies in Asia, Africa and Latin America. In the 19th century, countries like France, Belgium, Germany, the United States, and even Japan witnessed rapid industrialization. In the face of competition in the world market, Britain's lead in this regard dwindled. In search for newer markets and sources of raw material, these countries stepped up their drive for colonies and strengthened their control over existing ones. Industrial development also led to capital accumulation, which was concentrated in a small number of banks and corporations. This capital was invested in the colonies to sustain the rapid inflow of raw materials to fuel further expansion of industrial production.

High tariff restrictions in other developing capitalist countries led to a contraction of markets for British manufactured goods. And the need for heavy imports of agricultural products into Britain, was making her position vulnerable in her trade with other countries. India proved crucial in solving the problem of Britain's deficits. Britain's control over India ensured that there would always be a captive market for Lancashire textiles. Moreover, India's export surplus in raw material with countries other than Britain, counter-balanced her deficits elsewhere.

While on the one hand indigenous handicrafts faced impoverishment, on the other hand, there were few attempts at developing modern industries in the colony. Although the colonial government spoke about 'free trade', indigenous enterprise faced many obstructions perpetuated by the state's discriminatory policies. British capital was initially invested in railways, jute industry, tea plantations and mining. The Indian money market was dominated by European banking houses. While British entrepreneurs had easy access to capital made available by this banking network, Indian traders had to depend on family or caste organizations for their capital needs. British banking houses and British trading interests were well organized through Chambers of Commerce and Managing Agencies and could also influence the colonial state, to carefully deny Indian entrepreneurs access to capital. Before the First World War, British Managing agencies controlled 75% of industrial capital, and most of the profits from this limited industrialization were also sent back to Britain.

But, in spite of heavy odds, Indian entrepreneurs found opportunities to expand and grow, whenever Britain underwent periods of economic hardship. It was during the First World War that some Marwari businessmen from Calcutta, like G.D. Birla and Swarupchand Hukumchand invested in the jute industry. Gradually their control started expanding into other areas like coal mines, sugar mills and paper industry, and they could even buy up some European companies. The greatest success of Indian capital was seen in the cotton industry in western India, which took advantage of high demands during the war years (1914-18) to consolidate its successes, and eventually was in competition with Lancashire. Certain traditional trading communities like Gujarati Baniyas, Parsis, Bohras and Bhatias became important in this sector. The Tata Iron



and Steel Company under government patronage provided leadership to the fledgling iron and steel company of India.

After the first world war, links with the foreign market was re-established, but again in the Depression years (1929–1933), the domestic market became relatively free to be exploited by indigenous industry, as foreign trade declined. The colonial government also provided some protection to the sugar and cotton industries, in the face of falling prices in the agricultural sector. Low prices forced capital from land into the manufacturing sector. Indians also ventured into the field of insurance and banking. Again, during the Second World War (1939–45), as foreign economic influence declined, Indian entrepreneurs managed to make huge profits. Strengthened by its limited success, the Indian capitalist class strengthened their links with the nationalist movement. They soon started demanding the establishment of heavy industries under state ownership and started organizing themselves to resist the entry of foreign capital.

But, to place these markers of success in perspective, on an overall level, these developments remained confined to the domestic market and indigenous capital still had a long battle ahead, against the structural weaknesses of a colonial economy. The potential for growth remained depressed given the massive poverty of the Indian people.

Early Indian nationalists like Dadabhai Naoroji, M.G. Ranade and R.C. Dutt had expected Britain to undertake capitalist industrialization in India, but were deeply disillusioned with the results of colonial industrial policies. Consequently, they formulated a strong economic critique of colonialism in the late nineteenth century. Dadabhai Naoroji put forward the **drain of wealth theory**. Poverty in India, according to them, was the result of a steady drain of Indian wealth into Britain—a result of British colonial policy. This drain occurred through the interest that India paid for foreign debts of the East India Company, military expenditure, guaranteed returns on foreign investment in railways and other infrastructure, importing all stationery from England, ‘home charges’ paid for the Secretary of State in Britain and salaries, pensions and training costs of military and civilian staff employed by the British state to rule India. Even if this drain was a small fraction of the value of India’s total exports, if invested within the country it could have helped generate a surplus to build a capitalist economy.

The ultimate question that has been asked of colonial economic policies in India is whether there had been any development at all. The answer to this question is not simple. We may start with looking at eighteenth-century Mughal India, before the British had entrenched themselves as an invincible territorial power. The view that eighteenth century Mughal India was undergoing a deep economic crisis and decline has been pervasive among historians. It has been seen as the decisive broader context within which we may locate the decline of the Mughal empire. But some later historians have refuted this view, and have instead drawn attention to the rise of new rebellious groups into power, to account for the fall of the empire. They have argued that the Mughal period was in fact a period of over all well-being and economic growth rather than stagnation or crisis. Within the political structure, there was sufficient space and autonomy in the hands of local landed elites and urban guilds to generate and accumulate surplus. Moradabad-Bareilly, Awadh. Banaras and Bengal were some such ‘surplus areas’. Forests were being cleared to expand cultivation. Consequent rises in agricultural yield and the establishment of a cash nexus made surplus accumulation possible in the hands of erstwhile landlords and zamindars, who challenged Mughal paramourty to emerge as the new regional power elite.

**Notes****INTEXT QUESTIONS 17.3**

1. Which world event provided Indian entrepreneurs the first opportunity to expand and grow?

2. Who propounded the 'drain of wealth' theory?

3. Have later historians seen the 18th century as a period of economic backwardness?

Thus, the picture we get of India is one of a buoyant economic climate with a reasonable potential for growth. How do we then explain the backwardness and poverty that we encounter, at the end of the subsequent 200 years of British colonialism? Some writers have argued that the British did try to partially 'modernize' India, but it failed because of the strong hold of traditional structures. But we have noted above that these half-hearted attempts at 'modernisation' were motivated primarily to benefit the 'mother country'. Backwardness in the 'peripheral' colonies needs to be seen as the necessary flip side of the Industrial Revolution in the 'core', centred on the West. The same processes that led to industrialization in Britain, generated and sustained backwardness in her Indian colony, because the British economy was linked parasitically to the Indian economy, in an integrated world economic system of 'free trade'.

India in 1947 was not at a pre-industrial stage, and so her post-independence economic growth patterns may not be compared with processes of industrialization in the West. In 1947, India had already been a part of capitalist development in the west for 200 years, but in capacity of a colony. So, in 1947, independent India embarked into a process of modernization from a 'colonial' mode rather than a 'traditional' mode, which was structurally backward and underdeveloped.

**WHAT HAVE YOU LEARNT**

Phased economic exploitation of the colony was the core motive for the British to establish their rule in the Indian subcontinent. The nature of this exploitation changed over the course of their reign, owing to changes within Britain, and these in turn had specific economic, social and political consequences for the colony. Most economic initiatives undertaken by the colonial state was couched in the language of development and 'modernisation', but they had a differential impact on the colony, often leading to backwardness rather than growth. And finally most of these initiatives helped exploit the resources of the country to enable industrialization in Europe.

**TERMINAL QUESTIONS**

1. What were the revenue policies introduced by the British, and what changes did they bring about in the countryside in the colony?
2. Why was the commercialization of agriculture in the colony a 'forced' process?



3. Explain the phase of 'finance imperialism'.

**ANSWERS TO INTEXT QUESTIONS****17.1**

1. The first phase (1757-1813) of 'mercantilism' was that of direct plunder, the second phase (1813-1858) was that of free trade and the third phase (1858 onwards) was that of finance imperialism.
2. The misuse of the 'dastak' by Company employees for their private trade angered the Nawab of Bengal
3. Zamindars
4. Madras and Bombay Presidencies

17.2

1. Adam Smith
2. The production of cash crops was encouraged at the cost of food crops.
3. Punjab
4. Cheap machine made goods from Britain flooded the markets in India, and Indian handicrafts could not compete with them.

17.3

1. The First World War
2. Dadabhai Naoroji
3. No, later historians have characterised the 18th century as a period of general well-being and economic growth.

HINTS FOR TERMINAL QUESTIONS

1. See section 17.1 'Land Revenue Policies'
2. See section 17.2 'Commercialisation of Agriculture'
3. See section 17.3 'The Third Phase of British Colonialism'

GLOSSARY

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|-----------------|---|--|
| 1. Mercantilism | – | an economic theory followed in Europe between the 16 th and 18 th centuries, in which states used warfare to ensure an inflow of bullion, and control trade and resources through colonies |
| 2. Bullion | – | wealth in the form of precious metals like gold and silver |
| 3. Diwani | – | the right to collect revenue |
| 4. Taluqdar | – | a revenue official in the countryside in pre-British India |

**Notes**

5. Monopoly – the exclusive right to a certain trade
6. Tariff – custom duties payable to country of export
7. Free Trade – international trade free of any government regulation or restriction
8. Commercialisation – modifying something for the purpose of trade
9. Unfree forms of labour – labour undertaken not only for a money wage but under other kinds of force – mental, physical, customary, political etc.
10. Multiplier effect – a concept in economics where an increase in spending is expected to stimulate other economic activities. For instance the building of railways would involve building of wagons and tracks that would push up the yield of iron and steel and coal. It would also lead to the employment of a large number of people.
11. Deficit – when incomes from trade are less than expenditure.