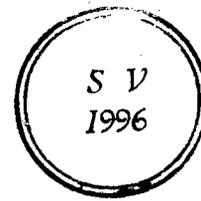


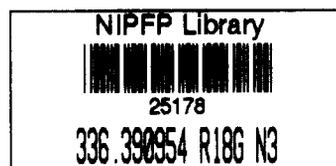
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**GOVERNMENT EXPENDITURE IN INDIA  
LEVEL, GROWTH AND COMPOSITION**

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**August 1993**



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## **PREFACE**

The National Institute of Public Finance and Policy is an autonomous, non-profit organisation, whose major functions are to carry out research, undertake consultancy work and impart training in the area of public finance and policy.

The study on ***Government Expenditure in India: Level, Growth and Composition*** was carried out by the State Finances Unit of the Institute at the instance of the World Bank. The research team responsible for the study consisted of M. Govinda Rao, Tapas K. Sen, Dipchand Maity and Madanmohan Ghosh.

The Governing Body of the Institute does not take any responsibility for the views expressed in this Report. That responsibility belongs to the staff of the Institute and more particularly to the authors of the report.

August 1993

**Amaresh Bagchi**  
Director

## **ACKNOWLEDGEMENTS**

There has not been a study of public expenditures in India in recent years combining analyses of the aggregate and disaggregated trends, both at the Central and the individual State level. With the programme of stabilisation and structural adjustment well under way, such a review has become necessary to assess the strengths and weaknesses of related policies. Perhaps these reasons prompted the World Bank to sponsor a study on Government Expenditure in India by the National Institute of Public Finance and Policy. William Byrd has taken personal initiative in this study which had to be completed in a relatively short period of about 10 months. He has also taken active interest in the actual research, right through the various stages involved.

Suresh D. Tendulkar went through an earlier draft very meticulously and provided detailed comments and suggestions which have improved this Report considerably. Amaresh Bagchi also read the draft and provided valuable suggestions for improvement. The draft Report was presented at an internal workshop in the Institute and we have had the benefit of comments from the participants, particularly V.B. Tulasidhar, Sudipto Mundle and Arindam Das-Gupta.

This study has utilised the data bank on government finances maintained at the National Institute of Public Finance and Policy extensively. Dipchand Maity and Madanmohan Ghosh have put in very hard work in retrieving and managing the mass of data, and consolidating them into tables needed for the analysis. Sathish Kamath, Diwan Chand and Kuldeep Sati also chipped in when needed.

Secretarial assistance was provided by R. Periannan and Anil Sharma. N. Natarajan took care of the production of this Report.

To all of the above, our sincere thanks. We alone are responsible for the remaining errors of omission and commission.

**M. Govinda Rao**  
**Tapas K. Sen**

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## CHAPTER I

### THE STATE, INTEREST GROUPS AND PUBLIC EXPENDITURE POLICY

#### **1.1 Introduction**

During the last decade, the strategy of fiscal compression has gained the centre-stage of economic policy in many of the countries of the developing world that have embarked on a programme of structural adjustment. Although in many of these countries economic crisis provided the immediate motivation, the basic rationale for fiscal compression arose from the reappraisal of the role of the State. The experiences of many countries have shown that indiscriminate State intervention, instead of providing a corrective to market failure, may actually worsen economic performances. Contrary to the assumption of the 'benevolent' public goods provider, it is seen that the State is often used by special interest groups to further their own interests resulting in adverse effects on both efficiency and equity.

In India although the need to provide greater leeway to activate the market mechanism has been felt since the early 1980s, the immediate motivation for the reappraisal of the past policy regime was the unprecedented economic crisis in 1990. This necessitated immediate stabilization and structural reforms (India, 1989). It was perceived that the root cause of economic crisis was the large and growing fiscal imbalance. Therefore, a major component of reform was to reduce fiscal imbalances by phasing out unproductive government expenditures and by providing public services cost-effectively. Reduction in fiscal deficits in a planned manner, however, requires a proper understanding of the factors determining the size and composition of government expenditures and its growth pattern over time. An analysis of Government expenditure trends is necessary to evolve an effective expenditure reform strategy.

#### **1.2 Market Failure and Government Intervention**

In the traditional development economics literature, the justification for governmental intervention is rooted in 'market failure' arguments. The market does not always live upto competitive norms and even when it does, it may not secure Pareto-optimal resource allocation when private and social valuations diverge. In particular, market equilibrium solution will not be efficient in the presence of (i) public goods (ii) externalities (iii) increasing returns to scale and (iv) 'merit' goods. Nor can the market bring about appropriate corrections in income distribution (Musgrave, 1981). In such cases, the necessary corrections have to be brought about through public expenditure policy.

The need for active State intervention in order to provide a corrective for market failures became obvious with the success of Keynesian-type policies in fighting the Great Depression and in the reconstruction of war-damaged economies of the West. The achievements of Soviet industrialisation signified the importance of social engineering and of centralised allocation of investments according to a plan. The poorer countries realised that speedy industrialisation could effectively transfer the surplus labour from unproductive agriculture to the more productive manufacturing sector; but the "vicious cycle of poverty" made it difficult for them to achieve the required rate of capital accumulation (Nurkse, 1953). It was also agreed that the social overhead capital (which creates externalities) in poor countries was scarce and private initiatives would not appreciably enhance capital accumulation in them (Rosenstein-Rodan, 1943). The investment allocation, therefore, had to be undertaken through active State intervention.

In keeping with the above perspective, the traditional explanations of the size, composition and growth of government expenditures have been advanced in terms of providing public goods, correcting for externalities and bringing about the desired state of income distribution in the society. These analyses brought out the effect of several important economic factors causing changes in the level and composition of government expenditures. In particular, the empirical analyses tried to quantify the effects of median voters' incomes, relative cost of providing public services and the various 'taste' variables on the level of public expenditures (Borcherding, 1985, Mueller, 1989). While both income and taste variables were supposed to reflect the demand for public services, the coefficient of the relative cost variable was interpreted to infer the productivity lag.<sup>1</sup>

### **1.3 Interest Groups and Public Expenditure Theory<sup>2</sup>**

Implicit in the above analysis is the assumption that the State is a benevolent entity with the objective function of maximising social welfare. It is not taken to be a strategic actor in the interactive game of interest groups. The recent neo-classical political economy approaches to the growth of government, however, are based on behavioral assumptions. When political parties' objective in a democratic polity is to maximise the probability of being reelected, the electoral competition leads them to seek out special interest groups and dispense patronage to them in return for political gains. (Myhrman, 1985). At another extreme we have a malevolent revenue maximizer exploiting the power to tax to the maximum extent to finance the ever

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1. This is called the "Baumol effect". According to the hypothesis, over time there will be a relative increase in the price of government provided goods and services because, general productivity increases come largely from technological change which is typically embodied in capital and the potential for absorbing these changes in labour intensive government services is less. Further, if the organised labour in the government sector can secure increases in wages more than its overall productivity, the expenditure increases would be even larger.

2. For a detailed review of interest groups and public expenditure policy, see Mueller, (1989).

expanding 'Leviathan' (Brennan and Buchanan, 1980, Niskanen, 1971). In addition, in a planned economy, where *inter-alia*, public expenditure policy plays a crucial role in allocating investments, the working of special interest groups can enhance the cost of providing public services by charging oligopolistic prices on the labour and material input sales to the government. Similarly, the special interest groups may use their power to appropriate greater share of the benefits. The rent seeking by the sellers to the government and attempts to 'free-ride' by the powerful groups,<sup>3</sup> can affect both the size and composition of government expenditure and its productivity. In order to evolve appropriate public expenditure policy it is necessary that the potential role of interest groups in determining the level and composition of expenditure are properly understood.

The difficulty of achieving optimal expenditure outcomes merely through electoral competition when the coalition of interest groups influence public expenditure policies has been highlighted by Tullock (1959).<sup>4</sup> He argues that the government's decision to provide 'quasi-public' or private goods and the log-rolling<sup>5</sup> of interest groups under the majority rule necessarily results in the provision of more than optimal (welfare maximising) levels of government expenditure. But, if there are other coalitions favouring tax reduction with 'Christmas-tree tax bills' decorated with numerous tax loopholes, this might yield the opposite outcome (Breton, 1974). However, there is no direct linkage between taxpayers and beneficiaries of public services, and as argued by Becker (1983, 1985) when each group applies pressures to increase its share of subsidies and reduce its share of taxes, in the equilibrium, marginal costs of applying pressure to increase subsidies and to reduce taxes are equated.<sup>6</sup> Such a competition results in an outcome where the groups that can be subsidised cheaply and those which are expensive to tax tend to do better. For this reason, special interest groups with organisational abilities<sup>7</sup> disproportionate to their numerical strength are more successful in minimising their tax shares and maximising their consumption of public services. These coalitions, however, are 'non-encompassing', for, small and homogeneous interest groups can organise more effectively and at low costs.<sup>8</sup> Thus, a small proportion of population is able to

3. 'Free-riding' is defined as availing the benefits of public services without making commensurate payments.
4. It has been shown that when the political parties attempt to maximise their probabilities of being reelected, median voter equilibrium will result. However, the introduction of cost-sharing arrangements will result in majority cycling and log-rolling, wherein the interest groups play an effective role. See, Brennan (1981).
5. 'Quasi-public' goods are the goods provided by the government with high private good characteristics. 'Log-rolling' is a form of vote trading between political parties/interest groups. See, Mueller (1989).
6. Becker's analysis is in terms of pure redistributive gains for the special interest groups, but can be extended to the provision of quasi public goods also.
7. Olson calls them 'distributional coalitions' as their motivation is mainly to get larger share of the available output rather than increasing the volume of output itself. For a detailed discussion, see Olson (1982), pp. 42-45.

appropriate a large proportion of the benefits of public services. It has also been shown that once a coalition succeeds in introducing a quasi-public good which would benefit its members, it would be rational even for other members of the society to prefer an increase in total government expenditure rather than a reduction in their own share of public services (Mueller and Murrell, 1985). This could result in the over-expanded supply of publicly provided private goods.<sup>9</sup>

The more than optimal allocation of resources to quasi-public goods resulting from log-rolling among interest groups imposes additional costs. The oligopolistic behaviour of these coalitions and their rent-seeking behaviour causes serious loss of efficiency. The rent-seeking behaviour gets further impetus in a regulatory and protective environment inherent in the 'dirigistic' developmental strategy.<sup>10</sup> The distributional coalitions emerging in such an event tend to reduce efficiency and productivity in the economy (Olson, 1982).

The brief survey of literature presented above highlights the possible influences on the size and composition of government expenditure when special interest groups play an important role in State policy. As already mentioned, when the government purchases goods and services, the sellers of these goods and services to the government may organise themselves into special interest groups and charge oligopolistic prices, thereby increasing the level of Government expenditure. The employees organising themselves to claim wage rates higher than their marginal productivity is a case in point. Similarly, the special interest groups may, in the process of gaining a larger share of the benefits of public services, influence the size and composition of Government expenditure. In such cases, the expansion will be seen particularly in the Governments' provision of private and quasi-public goods and transfer payments, the benefits of which can be appropriated by the special interest groups. These would be financed not by effective cost recoveries from the beneficiaries of these services, but passed on to the general public. Spreading the burden of financing such services to the public through broad

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8. Olson (1982, p.31) states "....the incentive for group action diminishes as the group size increases, so that large groups are less able to act in their common interest than small ones". See also, Olson (1965).

9. Similar conclusions have been reached by the 'Leviathan' theorists. The studies by Brennan and Buchanan (1977, 1980), for example, distinguish between 'constitutional' and 'in-period' choices. The citizens are assumed to exercise control over fiscal decision only at the constitutional decision stage, and all 'in-period' decisions are taken by the elected governments given that the governments are constitutionally given power, they are modelled to exercise the monopoly power to tax so as to maximise revenue, resulting in the over-provision of public services. Similarly, Niskanen (1971) attributes over-expansion of public sector to the behaviour of bureaucrats. The 'bureau heads', far from being public servants become the monopolistic suppliers of public services as they maximise their personal incomes or prestige. This monopoly practice aided by agenda setting results in the governments assuming the role of 'Leviathan'. As bureaucrats too can be considered as one of the interest groups, we have not discussed this contribution in detail here. For a critical appraisal of the 'Leviathan' literature, see, Musgrave (1981, 1985) and Cullis and Jones (1987).

10. The strategy of development through State accumulation is termed as 'dirigistic'. See, Toye (1981).

based indirect taxes or through budget deficits is a common strategy followed. Although the interest group activity may result in the governmental over-provision of private and quasi-public goods, it is by no means clear that there will be excess supply of public goods and goods with high degree of externalities. In fact, the public goods having long term benefits like social and economic infrastructure may be underprovided (Krueger, 1990).

An important precondition for the success of special interest groups to act collectively towards enhancing their gains is stability in the society (Olson, 1982). Ensuring protection from external aggression and internal strife and protecting property rights calls for spending on certain public goods like defence, police and general administrative services at adequate levels. A major source of instability in the economy, however, can arise from very high increases in prices and the existence of mass poverty.<sup>11</sup> The taxation structure, therefore, has to have an egalitarian tone (but not necessarily the content) and the majority of persons should perceive that the Government expenditure policies would be beneficial to them. This perception can be brought about by both rhetoric<sup>12</sup> and thinly spread (small amount of) allocations to programmes directly benefiting a large number of persons.<sup>13</sup> Similarly, the requirement of price stability necessitates judgements about a tolerable rate of inflation. This and the judgements about the relationship between deficit financing and inflation sets the limit for budget deficits.

It must be noted that it is difficult to clearly identify various special interest groups in any economy and trace the government expenditure trends to the operation of these groups. This is particularly true in a developing democratic polity where much of the lobbying is done in informal ways. Further, when the economy is buoyant and resource constraints are soft it is difficult to identify the consequences of special interest group actions as all expenditures generally show increases (although some items increase faster than others). However, the effect of distributional coalitions on size and composition of government expenditure become more evident when the Government faces hard resource constraint.

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11. Bardhan (1992) for example states, "..... it is the rate of inflation ..... that strikes at the roots of short-term political legitimacy of the rulers ..... The hypersensitivity of the polity even to moderate inflation is understandable in a democratic polity where average income is already precariously low and the overwhelming majority of the labour force is in the unorganised sector with no 'dearness allowance' to cover it".
  12. Rhetoric about removal of poverty and illiteracy in public speeches of politicians at frequent intervals is a case in point.
  13. Allocation of a small fraction of total expenditure for poverty alleviation and distributing it thinly across the poor in the country can create both goodwill and hope which can be an important instrument of stability.

#### **1.4 Indian Development Policy and Public Expenditures**

The adoption of centralized planning in a mixed economy framework to achieve accelerated economic growth with import substituting heavy industry-based strategy in India envisaged a governmental role of both a catalyst and a direct participant in economic activity. The public expenditure policy has had to play a crucial role in this policy of State accumulation. Therefore, government expenditures were deliberately expanded to stimulate the accumulation of productive capital. However, over time, the decision-making process got increasingly influenced by the special interest groups. The special interest groups became active rent-seekers in a regulatory environment. Forty years of regulated and planned economic regime in a democratic set-up gave ample scope for the emergence of several distributional coalitions which in turn exerted significant influence on the level, growth and composition of government expenditures.

The unprecedented crisis in 1990 which was triggered off by fiscal imbalances once again brought public expenditure policy into focus. Fiscal imbalances in India, which assumed serious proportions since the mid-Eighties, had two important facets. First, the outpacing of the rate of growth of revenues by the expenditure growth considerably reduced the resources available for public investment in the economy. The increasing use of borrowed funds to meet current expenditures rendered the latter self-propelling. Second, the increasing diversion of household savings to meet public consumption requirements not only resulted in the expansion of public debt to unsustainable levels (Chelliah, 1992), but also reduced the resources available for private investment. In addition to the usual allocative distortions arising from the crowding out of private sector investments and poor performances of public sector enterprises, the rent-seeking activities of the coalitions arising from the regulatory regime contributed to further decline in the productivity in the Indian economy.<sup>14</sup> The fiscal developments have also had adverse macro-economic repercussions. A portion of the excess demand generated by the expansionary fiscal policy spilled over into higher imports and consequently, aggravated the balance of payments problem. The deficit in the current account of balance of payment was a mere 1.2 per cent of GDP in 1980-81 but increased to 2.5 per cent in 1989-90. At the same time, inadequate public investment outlay created severe infrastructural bottlenecks. All these combined together to create a stagflationary situation (Mundle and Rao, 1992).

In stabilising the economy and in making structural adjustments, the compression of public expenditures plays a crucial role. As already mentioned, given the role of special interest groups in influencing expenditure policies, unless properly planned and executed, the expenditure compression may fall not on socially unproductive private and quasi-public goods provided by the government, but on more socially productive administrative, social and economic infrastructure outlays. A detailed analysis of government expenditure trends in India

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14. For a more detailed analysis of the fiscal developments in India, See, Bagchi and Nayak (1990).

will help in understanding the mechanics of expenditure growth including the role of interest groups.

Considering its importance in a planned economy, it must be stated that the public finance literature in India has paid relatively little or no attention to analysing the growth, allocation, and efficiency of government expenditures (Mundle and Rao, 1992). The few studies that were carried out concentrated on testing the Wagner's Law and "displacement effect" (Reddy, 1972, Nagarajan, 1979). There were some studies which attempted to quantify the impact of government expenditure on the economy using input-output models (Sarma and Tulasidhar, 1984, Reddy, Sarma and Sinha, 1984). In a sense, the first study to question the 'benevolent state' assumption and look upon expenditure growth as a consequence of the pursuit of self interest by 'dominant classes' was by Toye (1981). It analysed the growth of government expenditures during the period from 1960 to 1970. Recently, some attempts have been made to explain the changes in the level and composition of government expenditures in the studies by Mundle (1988) and Rao and Tulasidhar (1991). However, these attempts are only preliminary, nor do they analyse the expenditure trends of the Centre and of individual States in detail. Bardhan (1984, 1992) attributes the phenomenal increases in non-developmental expenditures and subsidies to the coalitions of organised interest groups in India. He identifies three dominant coalitions namely, industrial capitalists and large traders, rich farmers and white-collar workers<sup>15</sup> and professionals, and a number of not-so-dominant coalitions like unionised manual workers, small traders and other small propertied groups each demanding and securing political patronage and claiming an increasing proportion of State resources by way of implicit and explicit subsidies and transfers. This again does not explain the changes in the level and composition of government expenditures fully. There is considerable ambiguity and lack of conceptual clarity in the classification into 'developmental' and 'non-developmental'. Many 'non-developmental' items are in the nature of providing administrative infrastructure which is an essential precondition for economic growth. At the same time, developmental expenditures even on education and health need not necessarily contribute to growth if they are used merely to pay salaries higher than the marginal productivities to teachers and administrators. To understand the nature of the influence of distributional coalitions on expenditure policies it is necessary to make a detailed and disaggregated analysis of government expenditures.

The foregoing discussion suggests that in a democratic polity, the level and composition of government expenditures are influenced by not only the economic factors determining the demand for and supply of public services, but also the interplay of special interest group politics. However, identification of the effect of special interest groups on public expenditure is by no means easy, for, the methods adopted to influence government expenditures are not necessarily transparent.

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15. Pederson (1992) does not consider bureaucrats and white collar workers as a dominant coalition. However, the evidence of declining wage share of Government employees put forward by him is not supported by facts. See p.18 for more details.

In this study, however, we make an attempt at analysing the broad trends in government expenditure in India over the last 15 years and speculate on the effect of various economic factors and special interest groups. This is only a descriptive analysis and no rigorous attempt is made to quantify the effect of these coalitions on the level, growth and composition of government expenditures or their impact on allocative efficiency and equity. Our limited endeavour in this study is to analyse the trends in government expenditures over time and bring out, wherever possible, the influence of the special interest groups as well as the economic factors on the expenditure pattern. This is only the first step in relating economic factors and special interest groups to public expenditure policy.

The concept of government expenditure taken to analyse in this study is conventional. It includes all budgetary expenditures on government consumption and investment as well as on transfer payments, though the latter is purely a redistributive item. At the same time, it does not include off-budget items like tax-expenditures arising from tax concessions to individuals, business entities and charitable organizations. This also does not include spending by public enterprises except to the extent that budgetary allocation is made for them.

### **1.5 Sources of Data**

The budget documents and the Finance Accounts of Central and State governments published by the Comptroller and Auditor General are the basic data sources for any study on Government expenditure trends. However, a number of adjustments must be made in order to ensure comparability of data over time and across States and to eliminate inter-departmental transfers. Fortunately, the Union Ministry of Finance makes the necessary adjustments in the data to correct for the anomalies in its annual publication, *Indian Economic Statistics - Public Finance*. Comparable data from this source are available for the period, 1974-75 to 1990-91. We have based our analysis of aggregate government expenditure mainly on this source of data.

*The Indian Economic Statistics*, however, contains expenditure data on the Central government and of the State governments taken together. It does not contain the details of expenditures of individual States. Besides, detailed analysis of expenditure trends requires greater level of disaggregation than that is contained in this source. It may be mentioned that the expenditure classification made in this publication is not always helpful in gaining insights into the dynamics of government expenditure growth. Therefore, the detailed analysis of Central government expenditures and the analysis of and States' expenditures has been done on the basis of budgetary data suitably classified by us, after making the necessary adjustments. This classification has been done for the Central government as well as the 14 selected States.<sup>16</sup>

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16. The exclusions are the 10 special category States, and the small State of Goa, which attained Statehood in 1987.

In regard to the data on government expenditures of the Central government and of the selected States, we have eliminated inter-departmental transfers and have made the data comparable across States besides carrying out a number of other adjustments. In particular, we have excluded the expenditures on the item, "Appropriation for Reduction and Avoidance of Debt" which is essentially a contribution to the sinking fund. As many of the States have been making this contribution even when they have deficits in the revenue account, it is meaningless to consider this expenditure in the analysis. Similarly, under irrigation, a sizeable amount is shown as expenditure on account of interest payments to the government. This is merely a notional entry and actually no payment is made by the departments to the State governments. We have also excluded expenditure on State lotteries as this does not represent expenditure on any governmental function. Actually, the revenue from lotteries should net out this expenditure. We have also had to make a number of other adjustments to ensure comparability of data over time, particularly to correct for the changes in budgetary classification introduced after 1985-86. Although these changes were not as far-reaching as those introduced in 1974-75, we have had to make a number of changes to conform to the prevailing budgetary classification in all the States.

Insights into government expenditure behaviour, however, can not be gained merely by analysing the expenditure data contained in budget documents. This must be supplemented with the analysis of expenditures classified into economic cum functional categories. While the budgetary data and those contained in the *Indian Economic Statistics* give a fairly disaggregated picture on functional categories, they do not help us to analyse expenditures in terms of economic classification. In particular, the revenue and capital expenditure categories in the budgets are based on monetary ceiling of expenditure and not on the basis of whether the expenditure is incurred for the maintenance of capital assets or for their creation. Similarly, budgetary items do not help us to segregate the expenditures on 'wages and salaries', 'goods and services' and transfer payments. In order to assess the macro-economic impact of government expenditures as also to identify the sources of government expenditure growth, it is necessary to supplement the analysis of budgetary item of expenditures with that of economic cum functional categories. We have, therefore, supplemented the government expenditure analysis based on budgetary data with the analysis of economic and functional items of expenditure wherever feasible and appropriate.

However, data on expenditures classified into economic cum functional categories are not available in the public domain. Although the Union Ministry of Finance does undertake a detailed exercise of classifying Central government expenditures and publishes them every year, this is not done at the State level. Some of the States' statistical departments do classify expenditures into economic and functional categories. But, a reasonable time series of such data are not available, nor are the classifications done by adopting identical concepts and methodology. Fortunately, the Central Statistical Organisation (C.S.O.) undertakes this task in a systematic manner and these data have been obtained from the files of the C.S.O. for the Centre and the individual States for the period, 1974-75 to 1989-90.<sup>17</sup> The analysis of government expenditure trends undertaken in the following is based on these data.

There are, however, some differences between the C.S.O. data and the budgetary data which must be noted. The important differences are (i) C.S.O. data do not include interest payments and (ii) the subsidy figures according to economic classification (C.S.O.) include losses from departmentally run commercial activities like irrigation projects, which are shown after deducting revenue receipts from the sale of water, whereas in the budgetary data, gross expenditures under the items are shown. Also, the general, social and economic service categories in the functional classification do not strictly correspond to the budgetary classification.<sup>18</sup>

The two important adjustments required to be made in the analysis of government expenditures are to make adjustments for differences in scale and changes in prices. To take care of the differences in sizes of the States, we have, by and large, analysed the data in per capita terms. For this purpose, we have adjusted the mid-year population estimates of the Registrar General to correspond to financial years by making pro-rata adjustments. To account for the price changes, we have deflated government expenditure in current prices with the wholesale price index.<sup>19</sup>

### **1.6 Plan of the Study**

The analysis of aggregate government expenditures of Centre, State and Union Territories is undertaken in Chapter 2. The trends in Central government expenditures are analysed in Chapter 3. This chapter also brings out some recent developments, particularly the trends in expenditures after the reform programme was initiated in 1991-92. The analysis of State government expenditures and inter-State differences in the size, composition and their changes over time is carried out in Chapter 4. Chapter 5 brings out the major findings.

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17. Although data from this source are available from 1971-72, major changes in budgetary data effected in 1974-75 renders the data prior to 1974-75 not strictly comparable.

18. For example, water supply in the budgetary classification is put under social and community services whereas according to the CSO's classification this is put under economic services.

19. There are certain advantages of estimating a separate price index to deflate government expenditures based on its cost composition. In particular, if the objective is to analyse the real increases in Government services, such an index should be preferred. However, if the objective is to analyse the volume of real resources used in the provision of public services, a general index like the wholesale price index may be used for deflating government expenditures. To the extent the changes in relative input costs of public services are different from the changes in wholesale price index, the two deflators would differ. For these conceptual details, see, Musgrave (1981).

## CHAPTER II

### GOVERNMENT EXPENDITURE IN INDIA: COMBINED CENTRE AND STATES

In this chapter trends in aggregate expenditures of Central and State governments taken together are analysed. As mentioned in the previous chapter, the analysis carried out here is based mainly on the data collected from the *Indian Economic Statistics - Public Finance*, brought out by the Union Finance Ministry (Government of India) every year. Comparable data from this source are available for the period, 1974-75 to 1990-91. This analysis is supplemented with the analysis of the expenditure data on economic cum functional categories collected from the CSO.

#### **2.1 Level and Growth of Aggregate<sup>1</sup> Expenditure**

Aggregate government expenditure in India increased substantially over the period of one and a half decade. The per capita expenditure at constant (1981-82) prices increased by over 2.7 times from Rs 366 in 1974-75 to Rs 997 in 1990-91 (Table 2.1). At a rate of about 6 per cent per year, the growth of per capita government expenditure in India at constant prices exceeded the growth of per capita Gross Domestic Product (GDP) as well as the growth of revenue receipts. The per capita GDP during this period increased at only about 2.5 per cent per year which was lower than that of per capita expenditure by about 3.5 percentage points. Similarly, both tax revenues (4.9 per cent) and non-tax revenues (2.9 per cent) in per capita terms increased at rates much lower than that of government expenditure.

The analysis of government expenditure growth brings out two important consequences. As revenue expenditures grew faster than revenue receipts, governmental dissavings increased considerably over time and consequently, significant volume of household saving had to be diverted to meet public consumption needs (Bagchi and Nayak, 1990, India, 1989). By 1990-91, deficits formed almost 3.5 per cent of GDP. Second, the rate of expenditure growth was substantially higher than the growth of non-tax revenues signifying the increasing volume of implicit subsidies in the provision of public services. A recent study (Mundle and Rao, 1991) has shown that the difference between cost of providing social and economic services and cost recoveries increased from 8.8 per cent of GDP in 1977-78 to 15 per cent of GDP in 1987-88; and the cost recovery rates during this period declined from 55 per cent to 41 per cent in the case of economic services and 6.2 per cent to 3.6 per cent in the case of social services.

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1. 'Aggregate' expenditure denotes expenditures of the Centre, State and Union Territory governments but excludes the expenditure of local bodies.

Table 2.1

## Levels of Government Expenditure in India: 1974-75 to 1990-91

Year	Government Expenditure as a Percentage of GDP			Per Capita Expenditure in Constant (1981-82) Prices			Share of capital expenditure in total
	Revenue	Capital	Total	Revenue	Capital	Total	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1974-75	13.2	5.7	18.9	256.0	109.9	315.9	30.2
1981-82	17.1	7.4	24.5	385.3	166.3	557.6	30.1
1985-86	21.0	7.4	28.4	570.2	201.2	771.4	26.1
1986-87	22.3	8.2	30.5	625.9	231.0	856.9	26.9
1987-88	22.7	7.0	29.7	658.2	201.6	859.8	23.6
1988-89	22.3	6.2	28.5	698.9	195.1	894.0	21.8
1989-90	23.4	6.4	29.8	765.2	210.5	975.7	21.5
1990-91(RE)	23.4	5.9	29.3	794.7	201.9	996.6	20.1

Note: RE = Revised Estimates.

Source: 1. Indian Economic Statistics, Ministry of Finance, Government of India.  
 2. Central Statistical Organisation, Ministry of Planning, Government of India.  
 3. Registrar General, Government of India.

During the period 1974-75 to 1990-91, aggregate government expenditure at current prices in India increased at the rate of 16.4 per cent per year and the growth at constant prices was 8.2 per cent and in per capita terms at constant prices about 6 per cent which was higher than the rate of growth of per capita GDP by almost 3.5 percentage points.

The plot of per capita expenditure at current and constant prices (Figure 2.2) brings out an interesting feature. Clearly, the plot of nominal expenditures shows a smooth upward slope and this *price facie*, confirms the hypothesis that the governments by and large, follow the 'incremental' budgeting, with the outlay in the succeeding years higher by some percentage over the previous year in nominal terms. This does not, however, ensure that adequate provision in real terms is made. The plot of per capita expenditure in constant prices shows noticeable discontinuities, particularly in 1981-82 and 1986-87.

Government expenditure trends, both in per capita terms (at 1981-82 prices) and as a proportion of GDP plotted in figures 2.2 and 2.3 bring out three distinct phases. During the first phase, from 1974-75 to 1981-82, per capita expenditure had some degree of year-to-year

Figure 2.1

# Per Capita Govt. Expenditure in current Prices

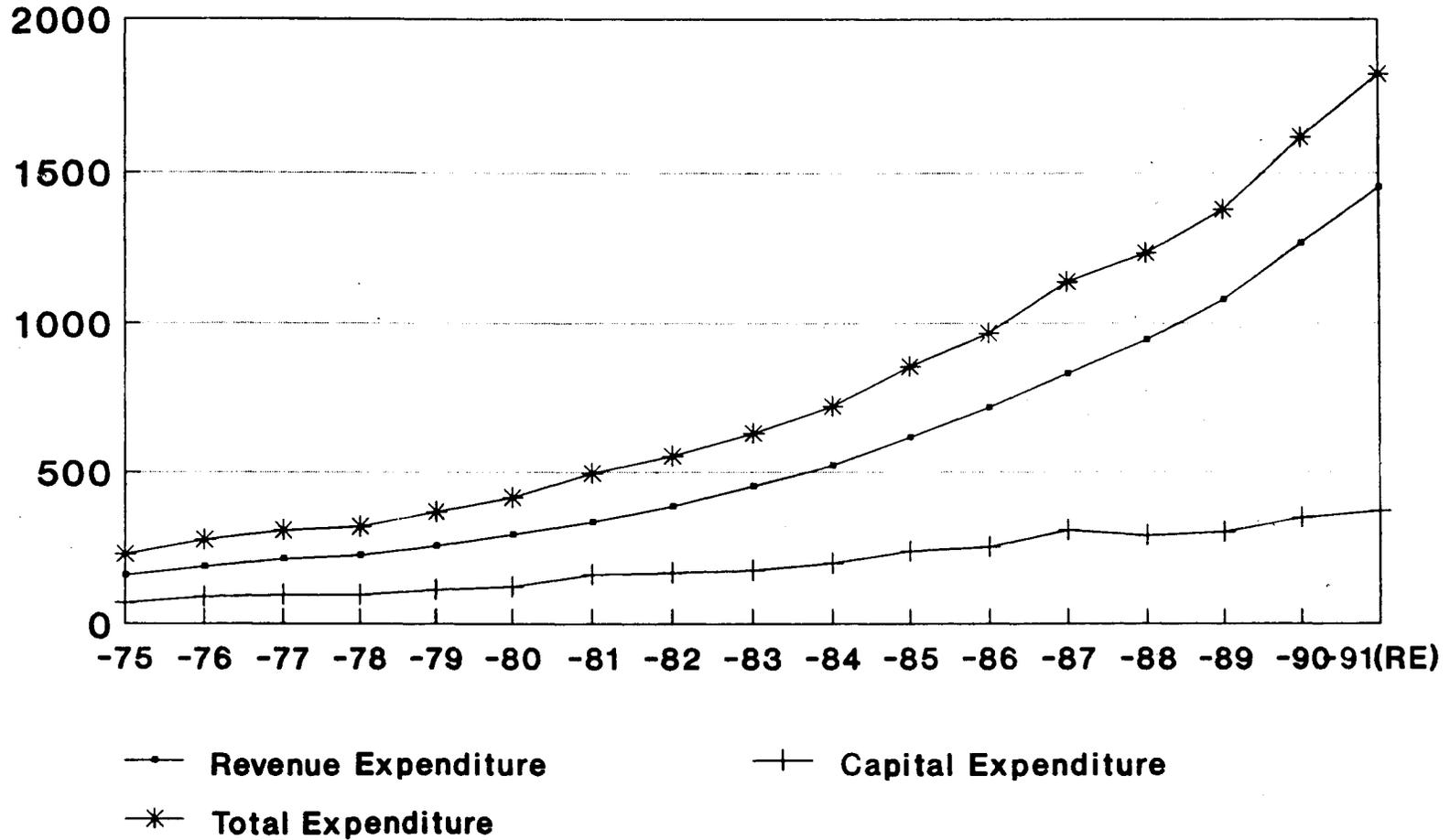
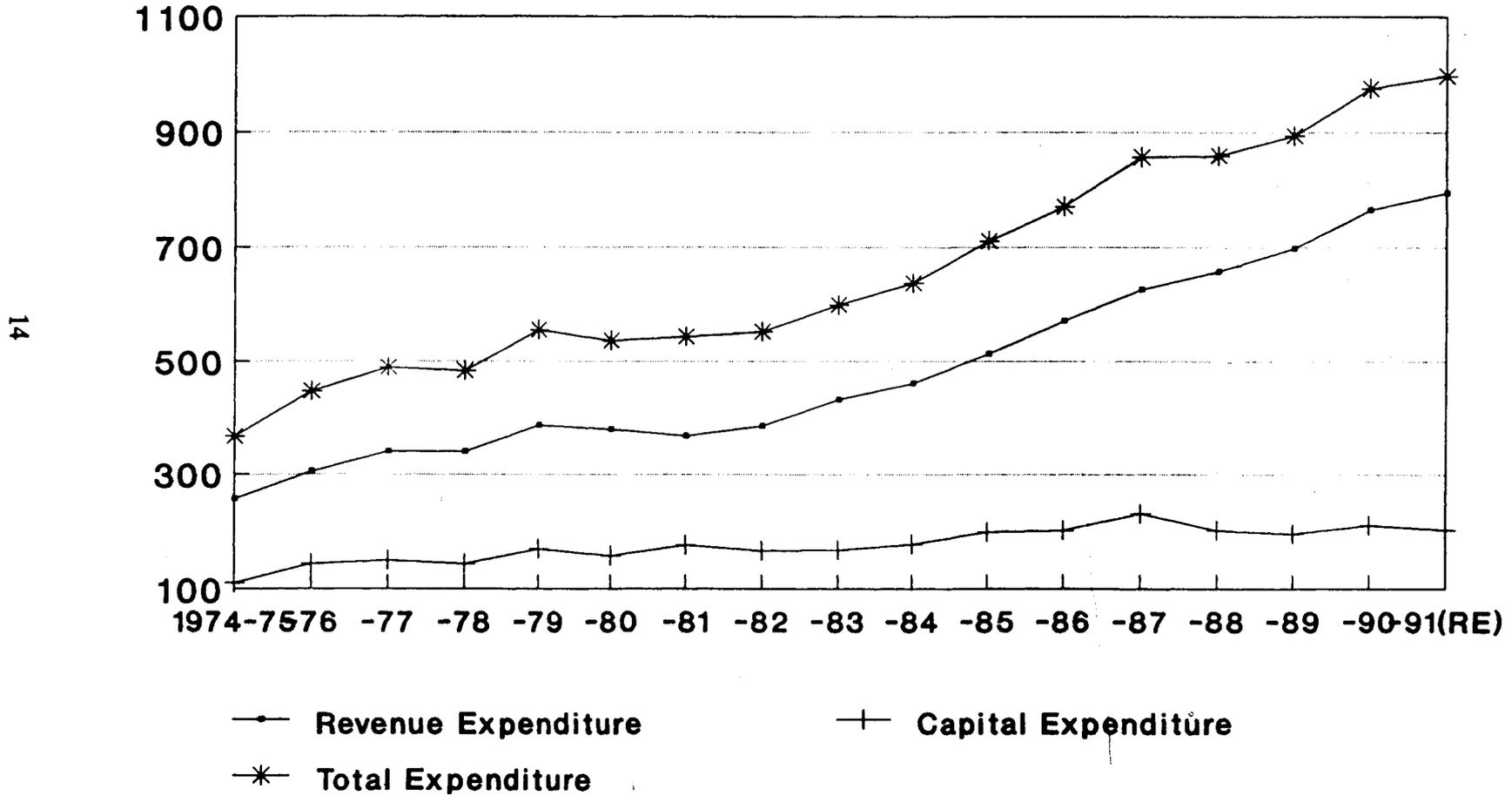


Figure 2.2

# Per Capita Govt. Expenditure at Constant 1981-82 Rupees



fluctuations though, on the average, grew at 4.7 per cent per year.<sup>2</sup> The expenditure-GDP ratio increased from 18.9 per cent in 1974-75 to 24.5 per cent in 1981-82. In the second phase, from 1981-82 to 1986-87, the growth rate was steady and showed a significant acceleration to average 7.6 per cent per year with the result that the expenditure-GDP ratio during these five years increased by six percentage points (from 24.5 per cent to 30.5 per cent). However, this tempo could not be maintained and in the third phase (1986-87 to 1990-91), the growth rate declined to broadly equal the growth rates seen in the first phase, at a little below 5 per cent per year. As a ratio of GDP, government expenditure actually showed a decline during the last phase to reach 29.3 per cent in 1990-91.

The three phases of expenditure growth noted can be explained by the state of the economy and particularly by the stringency of resource constraint. The political uncertainties in the latter half of the 1970s and the oil shock in 1979-80 resulted in the per capita net national product (NNP) in real terms increasing at just 1.5 per cent per year on the average during 1974-75 to 1981-82 and the annual growth of per capita (constant prices) revenues during this period was only 3 per cent (Table 2.2). The slow and fluctuating growth of revenues could not sustain very high growth of expenditures. Yet, as the fiscal deficit during the period averaged just about 5.6 per cent of GDP, the overall constraint was not very stringent and expenditures grew faster than the revenues. At the same time, the political uncertainties<sup>3</sup> and the oil shock contributed to fluctuations in the expenditure trend. The second phase (1981-82 to 1986-87) is marked by a significant acceleration in the rate of growth of expenditures. This must be attributed mainly to the economy shifting to a higher growth path. The per capita real NNP on an average during this period increased at 2.2 per cent per year, the government revenues increased at even higher rates (5.7 per cent per year). Besides, the reform of the tax system<sup>4</sup>

2. The growth rates for the sub-periods have been estimated by employing the kinked exponential regression model suggested by Boyce (1986), by introducing dummy variables ( $D_1$ ,  $D_2$  and  $D_3$  separated by two kinks ( $K_1 = 1981-82$  and  $K_2 = 1986-87$ )). The estimating equation is;

$${}_n Y_t = a_1 D_1 + a_2 D_2 + a_3 D_3 + (b_1 D_1 + b_2 D_2 + b_3 D_3)t \dots\dots\dots(1)$$

$D_1$  taking the value 1 for the period 1974-75 to 1981-82,  $D_2$  taking the value 1 for the period 1981-82 to 1986-87 and  $D_3$  taking value 1 for the period 1986-87 to 1990-91, and zero otherwise. Discontinuity is eliminated by putting linear restrictions at breaks  $K_1$  and  $K_2$  such that,

$$a_1 + b_1 k_1 = a_2 + b_2 k_1 \text{ and}$$

$$a_2 + b_2 k_2 = a_3 + b_3 k_2 \dots\dots\dots(2)$$

From these, the estimating equation can be derived as

$${}_n Y_t = a_1 + (b_1 - b_2)k_1 D_2 + [(b_1 - b_2)k_1 + (b_2 - b_3)k_2]D_3 + b_1 t + (b_2 - b_1)D_2 t + (b_3 - b_1)D_3 t \dots\dots\dots(3)$$

3. The period was marked by political instability. This period witnessed the imposition of emergency (1975-76), emergence of non-Congress party rule (1977-79) and return of Congress party into power (1980).

and the replacement of physical restrictions on imports with tariffs also contributed to revenue buoyancy. Given the relatively stable political environment and buoyant revenues in the second phase, the growth of Government expenditures showed a significant acceleration. This was further fuelled by the emergence of significant revenue deficits since 1982-83 and their feed-back in terms of increased interest payments. This phase can be easily characterised as the period of fiscal expansion.

However, this tempo of expenditure growth could not be sustained with the hardening of the budget constraint from 1986-87 due to two important factors. First, buoyant revenue expenditures had to be increasingly financed out of borrowed resources and in order to maintain relative price stability governmental borrowing beyond a certain level could not be sustained. It may be noted that increase in the net liabilities of the government reached the highest level of 12 per cent of GDP in 1986-87, and in this year Reserve Bank of India's net credit to government was also the highest, at close to 5 per cent of GDP (Dandekar, 1992). Second, increases in the emoluments of government employees consequent to the implementation of the recommendations of the Fourth Pay Commission at the Centre in 1987-88 and in many of the States in subsequent years significantly enhanced relative cost of providing public services.<sup>5</sup> In addition, the unprecedented drought of 1987-88 not only necessitated diversion of resources to relief expenditures, but also decelerated the growth of revenues to average 5 per cent per year after 1986-87. With increasing proportion of revenue expenditures being financed from borrowed funds and with the limits on aggregate government borrowing set by judgements about acceptable rate of inflation, the overall expenditure level had to be contained. Thus, in the third phase the share of expenditure in GDP actually showed a marginal decline. This period can be characterised as the period of fiscal restraint.

Interestingly, a major part of the increase in government expenditure share in GDP (almost three percentage points) in the early 1980s was due to the phenomenal expansion in revenue expenditures (Table 2.2). While the per capita capital expenditure (at 1981-82 prices) grew at broadly uniform rates during the latter half of the 1970s and the first half of the 1980s at a little over 4 per cent, the growth rate of per capita revenue expenditures accelerated by almost four percentage points to record a growth rate of 8.9 per cent per year during the period 1981-82 to 1986-87 (Table 2.2). At the same time, the compression that followed in the next phase came about more by compressing capital expenditure and not by reducing revenue expenditure. While the per capita revenue expenditure continued to increase at a relatively high rate of 6.9 per cent per year during the latter half of the 1980s, growth of per capita capital expenditure was actually

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4. This occurred in 1984-85 and 1985-86, with the emphasis on reasonable tax rates and better enforcement as enunciated in the Long Term Fiscal Policy (India, 1985) and the introduction of Modified Value Added Tax.

5. The effect of pay revision in the States in 1988-89 was estimated to increase total wages and salaries by 18 per cent.

**Table 2.2**  
**Growth of Revenues, Expenditures and GDP**

(per cent per year)

Period	Total Expenditure (Current prices)			Per Capita Expenditure (1981-82 prices)			Per Capita Revenue (1981-82 prices)		
	Revenue Expenditure	Capital Expenditure	Total Expenditure	Revenue Expenditure	Capital Expenditure	Total Expenditure	Tax Revenue	Non-tax Revenue	Total Revenue
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
1974-75 to 1981-82	15.6	15.0	15.4	4.9	4.4	4.7	3.3	1.7	3.0
1981-82 to 1986-87	19.4*	14.2	17.9*	8.9*	4.2	7.6*	6.2*	5.1*	6.0*
1987-88 to 1990-91	17.2*	8.1*	15.0*	6.9*	-1.5*	4.9*	5.7	0.5*	5.0
1974-75 to 1990-91	17.4	13.4	16.4	6.9	3.3	5.9	4.9	2.9	4.6

*Note:* Growth rates are estimated by employing the kinked exponential regression model [Boyce, 1986].  
\* Significantly different from the previous period growth rates.

**Table 2.3**  
**Government Expenditure by Functional Categories: Level and Composition**

	Interest Payments		Administrative Services		Social and community Services		Economic Services		Net Loans and Advances		Total Expenditure	
	Per cent of GDP	Per cent of total expenditure	Per cent of GDP	Per cent of total expenditure	Per cent of GDP	Per cent of total expenditure	Per cent of GDP	Per cent of total expenditure	Per cent of GDP	Per cent of total expenditure	Per cent of GDP	Per cent of total expenditure
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
<b>1. Revenue Expenditure</b>												
1974-75	1.6	8.5	5.1	27.0	3.9	20.6	2.6	13.8	-	-	13.2	69.8
1981-82	2.3	9.4	5.4	22.0	5.0	20.4	4.4	18.0	-	-	17.1	69.8
1986-87	3.6	11.8	6.9	22.6	6.2	20.3	5.6	18.4	-	-	22.3	73.1
1990-91 (RE)	4.7	16.0	6.4	21.8	6.3	21.5	6.0	20.5	-	-	23.4	79.8
<b>2. Capital Expenditure</b>												
1974-75	-	-	0.3	1.6	0.2	1.1	3.2	16.9	1.9	10.1	5.7	30.2
1981-82	-	-	0.3	1.2	0.4	1.6	4.3	17.5	2.4	9.8	7.4	30.2
1986-87	-	-	0.9	2.9	0.6	2.0	4.2	13.8	2.5	8.2	8.2	26.9
1990-91 (RE)	-	-	1.0	3.4	0.4	1.4	2.9	9.9	1.6	5.5	5.9	20.1
<b>3. Total Expenditure</b>												
1974-75	1.6	8.5	5.4	28.8	4.1	22.0	5.8	30.7	1.9	10.0	18.9	100.0
1981-82	2.3	9.4	5.7	23.2	5.4	22.0	8.4	35.5	2.4	9.8	24.5	100.0
1986-87	3.6	11.8	7.8	25.5	6.8	22.3	9.8	32.2	2.5	8.2	30.5	100.0
1990-91 (RE)	4.7	16.0	7.4	25.2	6.7	22.9	8.9	30.4	1.6	5.5	29.3	100.0

negative (-1.5 per cent). Thus, in absolute terms, per capita capital expenditure declined from Rs 231 in 1986-87 to Rs 202 in 1990-91 (Table 2.1) while per capita revenue expenditure increased from Rs 626 to Rs 795. As a proportion of GDP too, capital expenditures declined

from 8.2 per cent to 5.9 per cent during the above period (Figure 2.1). Consequently, capital expenditures which constituted about one-third of total expenditure in 1980-81 declined to just about 20 per cent by 1990-91. The increased resource availability during the expansionary phase accelerated the growth of mainly the revenue expenditure, but during the period of fiscal restraint, the cutback was mainly in capital expenditure virtually relegating it to a residual category.<sup>6</sup>

These findings are reinforced when we consider the CSO data on economic-cum-functional classification of government expenditure (Table 2.4). The shares of all the three items of capital expenditure namely, gross fixed capital formation, financial outlay and capital transfers and loans showed substantial decline whereas, the current expenditure (excluding interest payments) increased from 60 per cent in 1974-75 to 74 per cent in 1989-90. The decline was particularly marked with the hardening of resource constraint since 1986-87.

The largest increase in the share of revenue expenditures over the period came about on account of increase in interest payments. The expenditure on interest payments as a proportion of GDP increased from 1.6 per cent in 1974-75 to 4.7 per cent in 1990-91 and as a proportion of total expenditure, it increased from 8.5 per cent to 16 per cent (Table 2.3 and Figure 2.4). The increase in interest payment was particularly marked in the Eighties as in per capita terms at constant prices it registered a growth rate of over 13 per cent per year throughout the decade. This is due to increase in both the volume of indebtedness of the government and increases in effective rates of interest on government borrowings. Quite a good proportion of the indebtedness was on account of small savings schemes (14 per cent of total borrowings in 1990), which, besides involving high tax-expenditures offered very high interest rates. The high effective rates of return from tax-savings and interest rate offered surely has benefited mainly those having large savings. The high after tax rate of return on saving instruments is given to encourage savings, but, it is doubtful whether this was, in fact, achieved (Rakshit, 1982), although the high and varied after-tax rates of returns did contribute to the distortions in financial markets (Das-Gupta, 1989).

An important source of government expenditure growth is the significant increase in the emoluments of government employees. In per capita terms, at constant prices, this item increased from Rs 92 in 1974-75 to Rs 207 in 1989-90 registering an average annual growth rate of 5.3 per cent. This item of expenditure maintained its share of about 26 per cent in total expenditures.

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6. In his analysis of Government expenditure in India during 1960-70, Toye [1981] also observes that capital expenditure was residually determined.

Figure 2.3

# Percentage of Govt. Expenditure in GDP (Revenue, Capital and Total)

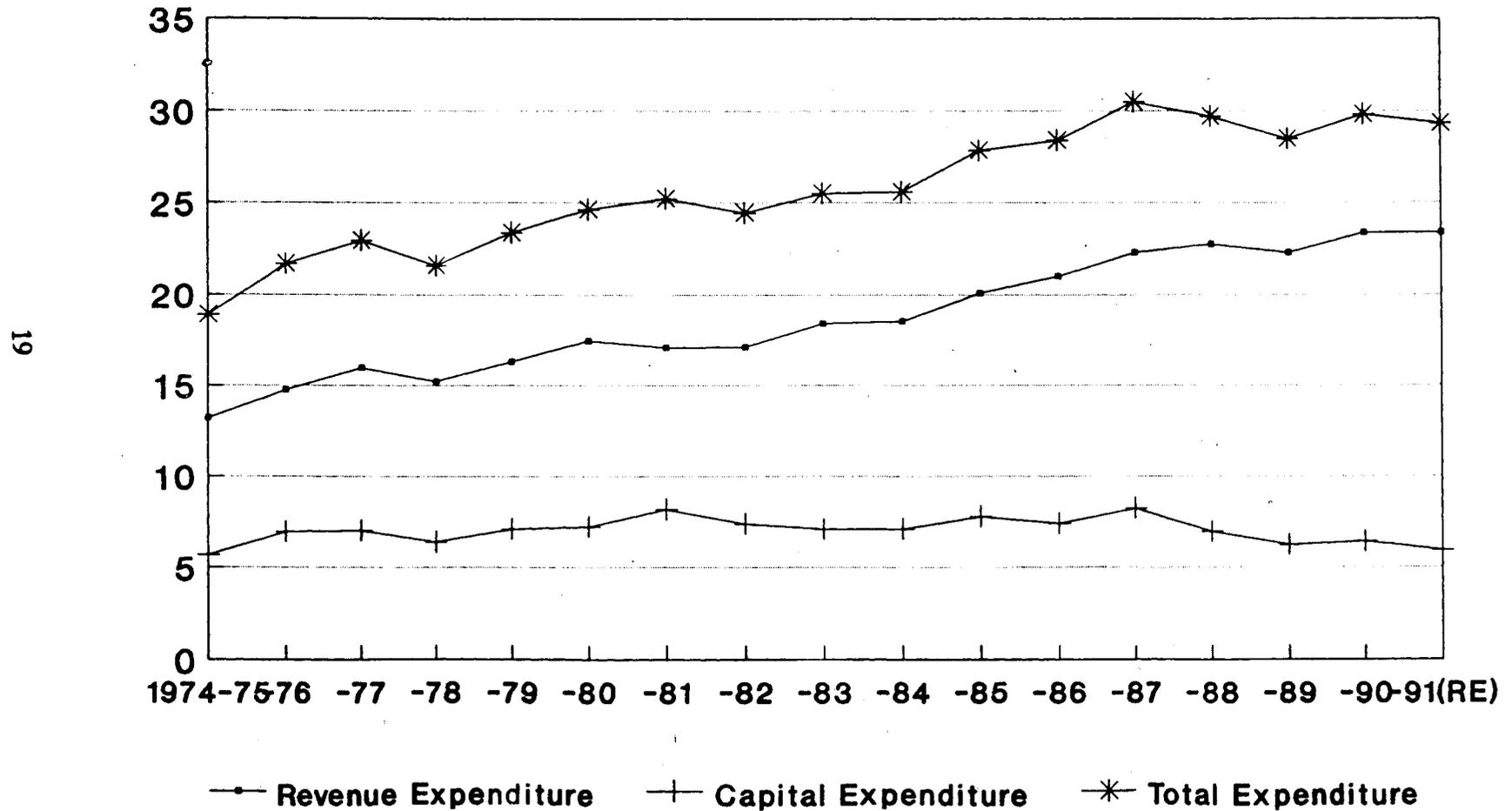
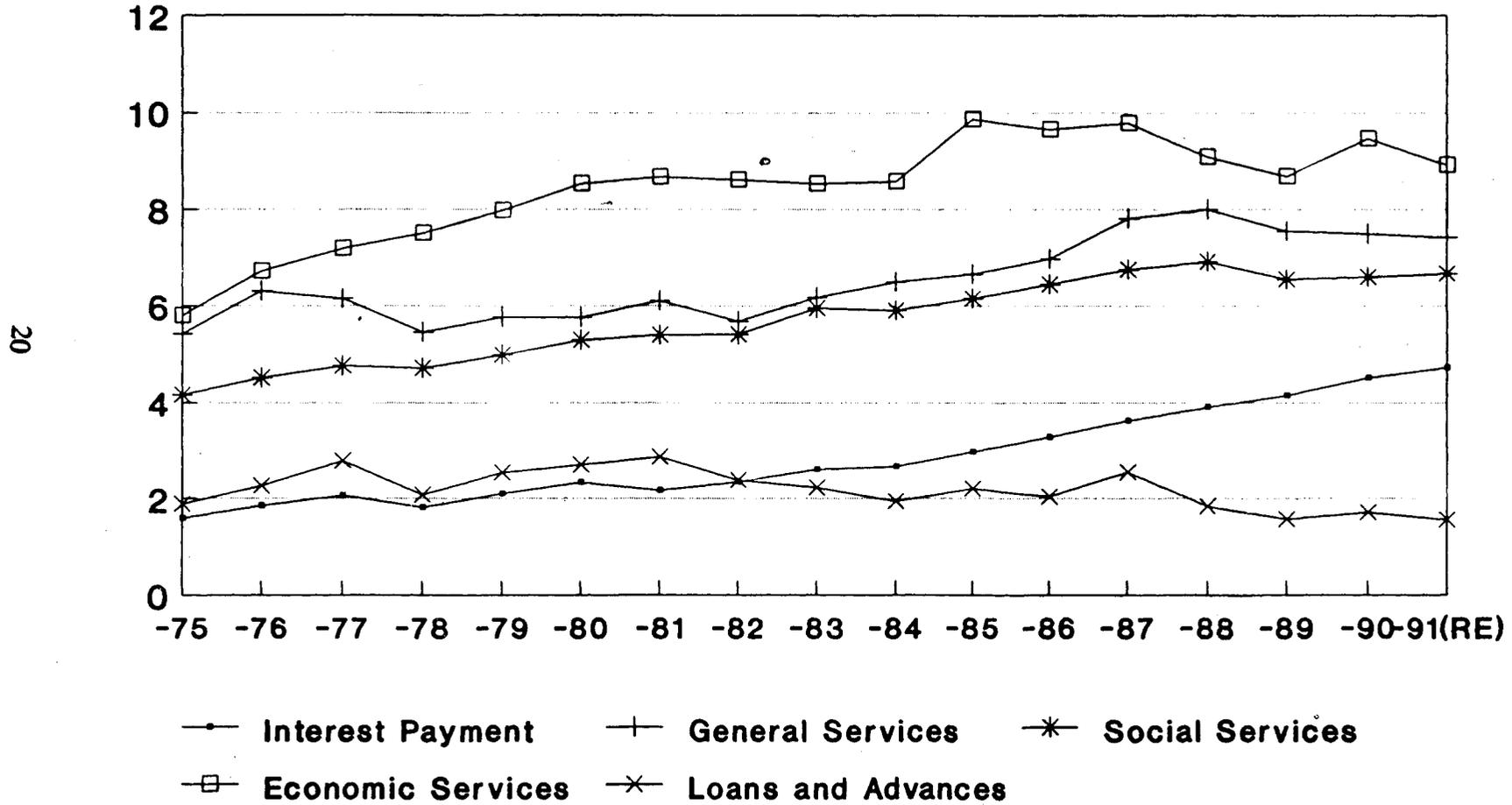


Figure 2.4

# Percentage of Govt. Expenditure in GDP (By Functional Categories)



**Table 2.4**  
**Government Expenditure in India by Economic Categories**

	Per Capita Expenditure (in 1981-82 rupees)				Percentage of Expenditure to GDP				Percentage of Total Expenditure			
	74-75	81-82	86-87	89-90	74-75	81-82	86-87	89-90	74-75	81-82	86-87	89-90
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
<b>1. Consumption expenditure °</b>												
a. Compensation to employees	91.7	112.6	168.5	207.4	4.7	5.0	6.0	6.3	26.7	24.2	24.2	26.2
b. Net government expenditure	49.6	75.2	110.2	117.7	2.6	3.3	3.9	3.6	14.4	16.1	15.8	14.9
Total - 1	141.2	187.8	278.7	325.1	7.3	8.3	9.9	9.9	41.1	40.4	40.0	41.2
<b>2. Transfer Payments</b>												
a. Subsidies	19.6	44.6	36.1	125.4	1.0	2.0	3.1	3.8	5.7	9.6	12.3	15.9
b. Transfer to local bodies	16.3	19.8	23.8	35.9	0.8	0.9	0.8	1.1	4.7	4.3	3.4	4.5
c. Other transfer payments	29.8	46.4	82.1	99.6	1.5	2.1	2.9	3.0	8.8	10.0	11.8	12.6
Total - 2	65.8	110.8	192.0	260.9	3.4	4.9	6.8	8.0	19.2	23.8	27.5	33.1
<b>3. Total Current Expenditure (1+2)</b>	207.0	298.6	470.7	586.0	10.7	13.2	16.8	17.9	60.3	64.2	67.5	74.3
<b>4. Gross Fixed Capital Formation</b>	38.5	39.2	63.3	49.9	2.0	1.7	2.3	1.5	11.2	8.4	9.1	6.3
<b>5. Financial Outlay</b>	25.8	36.9	49.8	42.2	1.3	1.6	1.8	1.3	7.5	7.9	7.1	5.3
<b>6. Total Capital Transfers and Net Advances</b>												
a. Local bodies	10.8	13.0	15.7	15.3	0.6	0.6	0.6	0.5	3.1	2.8	2.3	1.9
b. Others	61.1	77.2	97.9	95.6	3.1	3.4	3.5	2.9	17.8	16.6	14.0	12.1
Total 6	71.9	90.2	113.5	110.9	3.7	4.0	4.0	3.4	20.9	19.4	16.3	14.1
<b>7. Total capital Expenditure (4+5+6)</b>	136.2	166.3	226.7	203.1	7.0	7.4	8.1	6.2	39.7	35.8	32.5	25.7
<b>8. Total Expenditure (3+7)</b>	343.2	464.9	697.4	789.1	17.7	20.6	24.0	24.1	100.0	100.0	100.0	100.0

*Note:* Excludes interest payments.

*Source:* Central Statistical Organisation, Ministry of Planning, Government of India.

The analysis of compensation to employees clearly brings out the influence of a dominant coalition in Indian polity namely, government employees, in influencing the level and growth of government expenditures. The Central and State government employees formed just about 1.2 per cent of population in 1989-90<sup>7</sup>, but the share of wages and salaries received by them constituted 6.3 per cent of GDP. The wages and salaries per government employee in 1989-90 amounted to Rs 20,140 in current prices which is over 6.5 times the per capita income in the country (or 2.2 times the income of the standard family of three).

Not only that the income of government employees is high in relation to the per capita income in the country, but also the difference between emoluments of government employees and per capita income has been increasing over the years. In 1974-75, emolument per government employee was 4.3 times the per capita income and in 1989-90, it was 6.3 times. While the per capita income at constant prices on the average increased only at 2.5 per cent per year over the period 1974-75 to 1989-90, emolument per employee during the same period recorded a growth rate of 5.7 per cent per year. It must be noted that the emoluments do not include the in-kind incomes given by way of perquisites like subsidised housing and transport, subsidised loans for house building and for the purchase of other durable assets, free telephones (to the eligible categories) and subsidised educational and medical facilities.<sup>8</sup> Thus, the government employees by their ability to organise have not only been able to exercise oligopolistic power to claim a disproportionate share of community output but also enhance their share over the years.<sup>9</sup> Another indication of the strength of the government employees is seen in the sustained fast growth of wages and salaries even during the period of fiscal restraint. The compensation to employees in per capita terms (at constant prices) increased at the average annual rate of 8.3 per cent during the period of fiscal expansion when aggregate per capita expenditures increased at 7.8 per cent (Table 2.5) and even during the period of fiscal restraint, compensation to employees increased at 6.3 per cent when the aggregate expenditures increased at 3.4 per cent.

The sustained fast increases in wages and salaries was not the only source of high growth of current expenditure even during the period of fiscal restraint. The per capita expenditure on subsidies increased at the average annual rate of 12.4 per cent and per capita transfer payments

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7. Total number of employees in 1989-90 was 102.84 lakhs.

8. The evidence presented here does not agree with Pederson's (1992) conclusion that real wages for public employees have declined since the early 1970's. As declining real wages was cited as a principal argument against considering government employees as a dominant class, the argument does not hold in the light of the evidence presented here.

9. For the same reason, the share of higher echelons of bureaucracy would be even more. As in a democratic polity, very high salaries may not be acceptable to the politician, a good proportion of the incomes of this group are paid through perquisites like virtually free housing and use of government vehicles for personal reasons.

increased at 9 per cent per year. The increase in subsidies was mainly under food, fertilizer and irrigation heads which accrue largely to the rich farmers (Bardhan, 1984). The fast growth of outlay on these items indicates the ability of the recipient interest groups in influencing expenditure policy.

The analysis of government expenditures classified into broad functional categories clearly brings out the three phases of expenditure growth discussed earlier. In fact, per capita expenditure on all the items (except interest payments) shown in Table 2.6, show a significant acceleration in the growth rate during the period of fiscal expansion and significant deceleration during the period of fiscal restraint.<sup>10</sup> For reasons already explained, the decline in the growth rate of revenue expenditure during the period of fiscal restraint was lower than that of capital expenditures. In fact, under economic services, the growth rate of revenue expenditure during this period was marginally higher (but not significantly so) than the previous period. It must also be noted that the decline in per capita capital expenditures even in absolute terms was mainly due to the negative growth rates recorded in economic services and net loans and advances.

**Table 2.5**  
**Growth of Per Capita Government Expenditure in India (1981-82 prices)** (per cent)

(1)	1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
(1)	(2)	(3)	(4)	(5)
1. Consumption Expenditure				
a. Compensation to employees	2.27	8.25*	6.39	5.28
b. Net government maintenance	4.30	8.09	2.60*	5.69
Total	3.03	8.20*	4.91*	5.43
2. Transfers				
a. Subsidies	11.78	10.90	10.38	11.23
b. Transfer to local bodies	2.24	4.96	12.39*	4.58
c. Other transfers	5.39	10.37*	9.03	7.93
Total	6.96	9.96	10.00	8.60
3. Total current (1+2)	4.39	8.93	7.01	6.62
4. Gross Fixed Capital Formation	1.99	12.47*	-7.05*	5.15
5. Financial Outlay	3.42	7.97*	-9.78*	3.62
6. Total Capital Transfers & Advances				
a. Local bodies	5.26	5.93	-1.19*	4.74
b. Others	2.51	1.12	-2.65	1.28
Total	2.81	1.77	-2.35	1.73
7. Total Capital Expenditure (4+5+6)	2.64	5.56	-5.05*	2.91
8. Total Expenditure (3+7)	3.72	7.84*	3.37*	5.41

*Note:* Growth rates have been estimated by using the kinked exponential regression model. See Boyce (1986).

\* Significantly different from the previous period.

10. The growth rate of net loan and advances, however, has shown a continuous decline.

**Table 2.6**

**Growth of Per Capita Expenditures in Constant Prices**

Particulars	(Per cent per year)			
	1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
(1)	(2)	(3)	(4)	(5)
1. Interest payments	6.4	13.1*	13.2*	10.3
2. Administrative services				
- Revenue	1.6	8.9*	3.3*	4.9
- Capital	0.5	24.8*	12.3*	12.1
- Total	1.5	10.2*	4.5*	5.6
3. Social and community services				
- Revenue	5.3	7.9*	5.4*	6.4
- Capital	7.5	10.9*	-3.5*	6.9
- Total	5.5	8.2*	4.7*	6.5
4. Economic services				
- Revenue	8.7	7.4*	8.3	8.1
- Capital	5.2	2.9*	-4.1*	2.6
- Total	6.8	5.5*	3.3*	5.7
5. Net loans and advances	3.5	0.5*	-2.8*	1.0
6. Total expenditure				
- Revenue	4.9	8.9*	6.9*	6.9
- Capital	4.3	4.2*	-1.5*	3.3
- Total	4.7	7.6*	4.9*	5.9
7. Per capita GDP (per 1980-81 prices)	1.6	2.7*	4.3*	2.5

*Note:* \* denotes that the growth rate is significantly different from the previous period. All growth rates have been estimated by using the kinked exponential regression model. (Boyce, 1986).

To sum up, the major findings of the aggregate analysis are:

- (i) Government expenditure in India over the last decade and a half grew at a phenomenal rate, faster than both GDP and government revenues. With low and declining level of cost recoveries, the subsidies grew at a rate faster than government expenditures. The benefit of the large and growing subsidies have accrued to relatively more affluent people and to more developed regions (Mundle and Rao, 1991, Rao and Mundle, 1992). There is thus *prima facie* evidence that the beneficiary groups have been successful in seeking increases in

outlays on 'quasi-public' goods and transfers beneficial to them. At the same time, as the financing of these expenditures has been done not through better cost recoveries but by increasing resort to budget (fiscal) deficits, it is also clear that these groups have been able to pass on the burden of financing to the common man and unenfranchised sections (future generations) through fiscal illusion.

- (ii) The pattern of expenditure growth over time reveals that when the resources position was relatively more comfortable, the revenue expenditure registered faster increases. However, when the budget constraint hardened, capital expenditures, particularly those on economic services, received a cut-back. Thus, during the periods of political and economic stability, the special interest groups were able to secure disproportionate increases in outlays on quasi-public and private goods provided by the Government in which current components predominate. What is more, even when the resource constraint hardened, these groups were able to maintain the allocation to such services as a ratio of GDP. In particular, mention must be made of compensation to employees, subsidies and transfer payments which continued to grow even during the period when the resource constraint hardened. In the event, the resource constraint necessarily caused compression of capital expenditures, particularly on economic services. Thus, socially productive expenditures with high degree of externalities and those benefiting large sections of the society were found to be easily dispensable during the period of fiscal restraint.

It may, however, be argued that all capital expenditures are not necessarily productive and all revenue expenditures not necessarily unproductive. Expenditure on social services with a large revenue component contributes to human capital formation. Similarly, expenditure on maintenance of capital equipments can enhance overall productivity. To draw implications on the social productivity of changes in expenditures, it is necessary to analyse the growth of expenditure in further disaggregation and examine whether the increases in outlays are due to increased provision of the services in response the voters' demand or merely due to the operation of various special interest groups like government employees, rich farmers and industrialists and businessmen.

## **2.2 Analysis of Functional Categories**

**2.2.1. Administrative services:** As already mentioned, per capita expenditure on administrative services (at constant prices) after being virtually stagnant during the period 1974-75 to 1981-82, increased at a phenomenal rate of 10.5 per cent during the period of fiscal expansion (1981-82 to 1982-87). However, the growth rate decelerated thereafter to 4.5 per cent.

The disaggregated analysis of the growth of per capita expenditure on general administrative services in constant prices shows that the trend of acceleration in the expansionary phase and contraction during the period of fiscal restraint in aggregate expenditures is also seen the case of individual items (Table 2.7). It is seen that the growth rate of per capita defence expenditure accelerated from 0.6 per cent in the first period to over 10 per cent in the expansionary phase and then declined to 3.2 per cent during the period of fiscal restraint. Other administrative expenditures and expenditures on police also showed a similar trend. As a ratio of GDP, the defence expenditure after reaching the peak of 3.9 per cent declined to 3.3 per cent by 1990-91 (Table 2.8). Other administrative expenditures including those on police stabilised at around 4 per cent of GDP after 1986-87.

A notable feature of the trends in general administrative expenditure is the increasing importance of capital expenditure. The growth rate of per capita capital expenditure (1981-82 prices) increased from a mere 0.4 per cent in the first period to 20.3 per cent in the second and further to 26.3 per cent during the third even as the resource constraints necessitated general compression of expenditures. In per capita terms (at constant prices), capital expenditures increased from Rs 5.6 in 1974-75 to Rs 30.8 in 1990-91. A part of this increase came about by compressing revenue expenditures on defence, which, in per capita terms, declined from Rs 94.6 in 1986-87 to Rs 80.8 in 1990-91. As a proportion of GDP, there was a one percentage point reduction (from 3.4 per cent in 1986-87 to 2.4 per cent in 1990-91). However, a large part of the increase in capital expenditure on defence was achieved by crowding out capital expenditures on economic services.

**Table 2.7**  
**Growth of Per Capita Expenditure on Administrative Services (1982-82 Prices)**

			(per cent per year)			
			1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
			(1)	(2)	(3)	(4)
1.	Defence	- Revenue	0.7	8.8*	-1.6*	3.6
		- Capital	0.4	20.3*	26.3*	12.6
		- Total	0.6	10.3*	3.2*	5.0
2.	Other Administrative Services of which					
		- Revenue	2.7	8.3*	6.6	5.7
		- Capital	18.6	36.4*	-17.1*	18.2
		- Total	2.7	9.6*	4.9*	5.9
	(i) Police	- Revenue	3.1	7.6*	6.8	5.6
3.	Total Administrative Services					
		- Revenue	1.6	8.9*	3.3*	4.9
		- Capital	0.5	24.8*	12.3*	12.2
		- Total	1.5	10.2*	4.5*	5.6

*Note:* Growth rates have been estimated using the kinked exponential regression model.  
\* indicates that the growth rate is significantly different from the previous period.

**2.2.2 Social and community services:** Expenditure on social services at 6.7 per cent of GDP formed about 23 per cent of total expenditures in 1990-91. As these services are employment-intensive, wage cost predominated and almost 94 per cent of the expenditure was of current nature. The important items under this functional category were i) education, art and culture and scientific services (54 per cent), ii) medical and public health and family welfare (26 per cent) and (iii) social security and welfare (12 per cent). The share of other items like housing and urban development (4 per cent), relief for natural calamities (2 per cent) and labour and employment (3 per cent) were financially not very significant.

As was seen in the case of aggregate expenditures, the growth of expenditure on social and community services showed a spectacular increase during the expansionary phase (1981-82 to 1986-87) and thereafter, declined significantly (Table 2.9). As a percentage of GDP, after a steady increase from 4.2 per cent in 1974-75 to 6.9 per cent in 1987-88, expenditure on these services stabilised at around 6.6 per cent during the next three years (Table 2.10).

**Table 2.8**  
**General Administrative Expenditure - Level and Composition**  
**(1974-75 to 1990-91)**

Description	1974-75			1981-82			1986-87			1990-91		
	Reve- nue	Capital	Total									
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
<b>I. Percentage of GDP</b>												
a. Defence	2.6	0.3	2.9	2.6	0.3	2.9	3.4	0.5	3.9	2.4	0.9	3.3
b. Police	0.8	n	0.8	0.9	n	0.9	1.0	n	1.0	1.1	n	1.1
c. Other administrative services	1.7	n	1.7	1.9	n	1.9	2.5	0.4	2.9	2.9	0.1	3.0
d. Total- administrative services	5.1	0.3	5.4	5.4	0.3	5.7	6.9	0.9	7.8	6.4	1.0	7.4
<b>II. Per Capita (1981-82 rupees)</b>												
a. Defence	50.8	5.6	56.4	58.8	7.3	66.1	94.6	13.0	107.6	80.8	30.8	111.6
b. Police	14.8	n	14.8	19.4	-	19.4	26.3	-	28.3	36.5	-	36.5
c. Other administra- tive services	33.6	0.5	34.1	42.8	-	42.8	71.8	11.8	83.6	99.5	5.1	104.6
d. Total	99.2	6.1	105.3	121.0	7.3	128.3	194.7	24.8	219.5	216.8	35.9	252.7

n - negligible.

**Table 2.9**

**Growth of Per Capita Expenditure (1981-82 prices) on Social Services**

	(per cent per year)			
	1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
	(1)	(2)	(3)	(4)
<b>1. Revenue Expenditure</b>				
a. Education	3.6	7.3*	8.1*	5.9
b. Medical and public health	6.4	7.1	3.4*	6.2
c. Family welfare	3.0	14.9*	-0.6*	7.2
d. Housing and urban development	8.6	5.9*	6.4	7.1
e. Social security and welfare	10.3	9.9	3.7*	9.0
f. Total social services	5.3	7.9*	5.4	6.4
<b>2. Capital Expenditure</b>				
a. Education	4.2	15.0*	-0.6*	7.7
b. Medical and public health	11.9	3.6*	-4.8*	5.4
c. Family welfare	13.7	36.2*	-6.1*	18.6
d. Housing and urban development	5.3	8.2*	-7.9*	4.1
e. Social security and welfare	-	-	-	-
Total social services	7.5	10.9*	-3.5*	6.9
<b>3. Total Expenditures</b>				
a. Education	3.6	7.3*	8.1	5.9
b. Medical and public health	7.1	6.7	2.5*	6.1
c. Family welfare	3.4	15.8*	-0.7*	7.6
d. Housing and urban development	7.4	6.9	1.5*	6.2
e. Social security and welfare	16.3	9.9*	3.7*	9.0
f. Total social services	5.5	8.2*	4.7*	6.5

*Note:* Growth rates have been estimated by using the kinked exponential model.

\* denotes that growth rates are significantly different from the previous period.

The significant expansion of government expenditure on social and community services during the expansionary period occurred in both revenue and capital expenditures. Also, as a proportion to GDP, both revenue and capital expenditure under each of the major items showed some increases. However, notably, even as the proportion of capital expenditure was small, the government compressed capital expenditure further during the period of fiscal restraint. This

clearly indicates that the government found it easy to cut outlays on school and hospital buildings, but not the salaries of teachers and medical personnel. In fact, revenue expenditure on social services continued to increase at a relatively high rate (5.4 per cent) even during the contractionary phase. The growth rate of expenditure on wages and salaries in per capita terms was even higher at 6.4 per cent during this period. Thus, much of the increase in expenditures must be attributed to increase in relative cost of providing these services rather than the increase in the standards of services of these employment intensive activities. It is also seen that growth rate of per capita capital expenditures during the contractionary period was negative in the case of each of the individual items of social services (Table 2.9).

The significant acceleration in the growth of per capita expenditure during the expansionary phase, however, was mainly due to high growth rate recorded in the case of two items -- education and family welfare (Table 2.9). The growth rates in respect of all other major items under social and community services did not increase during this period, and in the case of social security and welfare, the growth rates actually showed a decline. The growth rate of medical and public health, for example, declined from 7.1 per cent in the first period to 6.7 per cent in the second; growth rate of housing and urban development decelerated from 7.4 per cent to 6.9 per cent and that of social security and welfare, from 10.3 per cent to 9.9 per cent. The decline in the growth rate during the third period, however, occurred in respect of all the items under social services except education. Thus, in the case of medical and public health, housing and urban development and social security and welfare, there was a continuous decline in the growth rates during the successive periods and in respect of the first two categories, the decline in the growth rate during the third period was particularly severe in capital expenditures. In contrast, the growth of education expenditures continued to accelerate even during the contractionary period. Of course, in spite of this fast growth, government expenditure on education (excluding art, culture and scientific services) as a proportion of GDP was just about 3.3 per cent which does not compare favourably with the level of public spending in developing countries taken together (4.1 per cent).<sup>11</sup>

Spending on medical and public health, family welfare, housing and urban development reflects socially productive forms of expenditure. Yet, the level of expenditure on health and family welfare was only 1.7 per cent of GDP. In fact, the reasonably high growth seen in the first two periods did help to spread the benefits of health and family welfare facilities to a number of persons in rural areas through the expanded network of rural public health centres, but, with the resource constraint hardening during the third phase, there was a significant decline in the growth rates of expenditures on these items. Per capita expenditure on medical and public health during this period increased at 2.5 per cent per year and per capita expenditure on the other two items remained virtually stagnant. At the same time, during this period, outlay on wages and salaries under these heads continued to increase fast (Table 2.11). With the cost of

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11. This estimate for developing countries refers to 1987 and is taken from Statistical Year Book, 1989, UNESCO.

providing these services increasing at high rates, the standards of services provided had to be reduced. Surely, the beneficiaries of these services did not wield enough power or were not organised well enough to lobby and secure a stable expenditure share on these items.

Expenditure on 'social security and welfare' mainly consists of various pensions and reliefs to vulnerable sections like the old, the widows and the destitutes. The high growth rates of expenditure on this item seen in the first two periods has to be viewed against the low levels of expenditures on these items in 1974-75, which as a share of GDP was just about 0.4 per cent. It appears that very little attention was paid to providing social security to the poor and vulnerable sections who form almost 38 per cent of population and the amount of money spent on providing social security to them was negligible. Even so, the governments found it easy to decelerate growth of expenditures on these items during the period 1986-87 to 1990-91, when the resource constraint hardened.

Expenditure on other social services includes spending on scheduled castes, scheduled tribes and other backward classes and on natural calamity relief. Again, it is seen that scheduled castes and tribes formed 24 per cent of total population but, direct expenditures incurred on them was just about 1.5 per cent of the total. While a lot of rhetoric is indulged in to explain how the government has been improving the conditions of these socially deprived sections, it appears, very little is actually done in terms of direct spending on their social and economic development, particularly by way of enhancing their human capital.

Growth of expenditure on education, however, continued to accelerate even during the period of fiscal restraint. The growth rate of per capita expenditure (constant prices) during the sub-period was as high as 8.1 per cent per year as compared to 7.3 per cent (1981-87) and 3.6 per cent (1974-81) during the two previous periods. This, however, should be viewed in the light of the significant increase in the relative cost of providing education due to the revision in the pay scales of the teachers, and the consequent shift in the cost of providing the services. The growth of per capita expenditure on wages and salaries under education during the period of fiscal restraint was 6.6 per cent per year and as this component formed about 35 per cent of expenditures on education almost 2.3 per cent growth in education expenditure must be attributed to cost increases arising from increase in wages and salaries.

To sum up:

- (i) the growth rate of expenditure in social services accelerated significantly during the expansionary phase, but declined thereafter. This is attributable mainly to the trends in capital expenditure. After increasing at about 11 per cent per year during the expansionary period, per capita capital expenditure in constant prices recorded a negative growth rate during the period, 1986-87 to 1990-91. Revenue expenditure, on the contrary, accelerated in the expansionary phase and continued

Table 2.10

**Share of Expenditure on Social Services of the Centre, State and  
Union Territories in Gross Domestic Product (GDP)**

(per cent)

	1974-75	1986-87	1987-88	1990-91 (RE)
(1)	(2)	(3)	(4)	(5)
<b>1. Revenue Expenditure</b>				
a. Education, art, culture and scientific services	2.31	3.24	3.46	3.53
b. Medical and public health and family welfare	0.85	1.40	1.43	1.29
c. Housing and urban development	0.10	0.22	0.20	0.23
d. Social security and welfare	0.37	0.80	0.78	0.81
e. Others	0.30	0.49	0.55	0.42
Total social and community services	3.92	6.16	6.41	6.28
<b>2. Capital Expenditure</b>				
a. Education, art, culture and scientific services	0.05	0.12	0.09	0.09
b. Medical, public health and family welfare	0.09	0.10	0.19	0.14
c. Housing and urban development	0.06	0.17	0.13	0.07
d. Others	0.03	0.12	0.10	0.09
Total social and community services	0.24	0.59	0.51	0.39
<b>3. Total (Revenue plus Capital Expenditure)</b>				
a. Education, art, culture and scientific services	2.36	3.37	3.59	3.63
b. Medical and public health and family welfare	0.94	1.58	1.62	1.43
c. Housing and urban development	0.17	0.38	0.33	0.30
d. Social security and welfare	0.37	0.80	0.78	0.81
e. Others	0.33	0.61	0.65	0.51
Total social and community services	4.16	6.75	6.92	6.67

Table 2.11

**Growth of Per Capita Expenditures (at 1981-82 prices) on  
Wages and Salaries in Services**

(per cent per year)

	1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
	(1)	(2)	(3)	(4)
1. Education	6.5	7.8	6.6	7.1
2. Health	6.3	8.3	5.8	7.1
3. Social security and welfare	3.1	8.1	9.2	6.2
4. Housing and community services	0.9	11.6	1.1	5.3
5. Cultural services	1.3	-1.8	11.0	1.1
6. Total social services	5.6	8.0	6.4	6.7

*Note:* Growth rates have been estimated using the kinked exponential regression model.

*Source:* Central Statistical Organisation, Ministry of Planning, Government of India.

to grow at a high rate even during the contractionary period. Thus, even during the period of resource constraint, the wages and salaries continued to increase at a fast rate.

- (ii) Expenditure on education and family welfare were the two items the growth of which accelerated significantly during the period of fiscal expansion. During the contractionary period, however, growth of expenditure on all the items under social services except education decelerated significantly mainly due to the reduction in capital expenditure, although it formed only a small proportion of the total expenditure. This is not surprising as there was no special interest group to protect outlay on school and hospital buildings. It must also be noted that increase in the emoluments of the teachers was one of the factors responsible for the high growth rate of education expenditure recorded throughout the 1980s.
- (iii) The significant deceleration in the growth of expenditure on medical and public health, family welfare, housing and urban development during the period of fiscal restraint, even when wage rates escalated, indicates the serious decline in the level of these socially productive services, again because there was no powerful special interest group to protect outlay on these services.
- (iv) The analysis also reveals that disproportionately low allocation of just 1.5 per cent was made to the direct spending on the welfare of scheduled castes and tribes though they formed about 24 per cent of population. Similarly, less than 3 per cent of total expenditures was allocated for providing social security, aimed at the poor and vulnerable sections even though the poor formed about 30 per cent of the population. This shows that howsoever socially deserving the expenditures may be, and howsoever encompassing the beneficiary groups are, when the groups are not cohesively organised, the allocation will be disproportionately small, just enough to maintain the political stability.

**2.2.3. Economic Services:** Expenditure on economic services formed about one third of total expenditures and this share remained more or less stable over the last one and a half decades. As a proportion of GDP, the expenditure on economic services increased appreciably until 1986-87, but declined thereafter. The expenditure-GDP ratio increased from 5.8 per cent in 1974-75 to 9.8 per cent in 1986-87 and subsequently, declined to 8.9 per cent in 1990-91 (Table 2.12). We have also noted earlier that the decline in the share in 1986-87 was mainly due to cutbacks in capital expenditure which, in per capita terms (at 1981-82 prices), declined from Rs 118 in 1986-87 to Rs 100 in 1990-91 (Table 2.13).

The trend in expenditure on economic services differed markedly from the trends in other categories in one important respect; the growth rate of expenditure on economic services

showed a continuous decline throughout the period. Thus, even during the expansionary phase, growth rate of expenditure on economic services showed a marginal decline (from 6.8 per cent to 5.5 per cent) from the previous period (Table 2.14).

The decline in the rate of growth of expenditures on economic services has to be attributed to the deceleration in the growth of capital expenditure which formed a third of total expenditures. Consequently, the share of capital expenditure in economic services declined from 60 per cent in 1974-75 to just about 33 per cent in 1990-91. Even during the expansionary phase (1981-82 to 1986-87), per capita capital expenditure on economic services at 1981-82 prices in the aggregate increased at only 2.9 per cent per year, and the growth rate was as low as (-)3.2 per cent in agriculture and allied activities and 1.2 per cent in power and irrigation (Table 2.14). During the period of fiscal restraint, the growth rate of per capita capital expenditure declined further to -4.2 per cent. Among the individual items, except power, irrigation and flood control, per capita capital expenditure on all other items showed negative growth rate. In fact, the growth of capital expenditure on economic services was well below that of GDP throughout the 1980's and consequently, the capital expenditure-GDP ratios in respect of every major item of economic services were significantly lower in 1990-91 than in 1981-82 (Table 2.12).

**Table 2.12**  
**Share of Expenditure on Economic Services in GDP**

	1974-75	1981-82	1986-87	1990-91
(per cent)				
<b>1. Revenue Expenditure</b>				
a. Direct subsidies	0.54	1.01	1.64	1.83
b. Agriculture and allied services	0.89	1.52	1.87	2.25
c. Industry and minerals	0.25	0.50	0.62	0.52
d. Power irrigation and flood control	0.24	0.38	0.53	0.45
e. Transport and communication	0.43	0.62	0.56	0.50
f. Others	0.22	0.31	0.37	0.45
Total economic services	2.56	4.34	5.58	5.99
<b>2. Capital Expenditure</b>				
a. Agriculture and allied	0.62	0.15	0.08	0.10
b. Industry and minerals	0.74	1.06	1.23	0.29
c. Power, irrigation and flood control	0.98	1.55	1.46	1.42
d. Transport and communication	0.72	1.13	1.14	0.74
e. Others	0.18	0.39	0.29	0.37
Total economic services	3.24	4.28	4.20	2.94
<b>3. Total (Revenue plus Capital Expenditure)</b>				
a. Direct subsidies	0.54	1.01	1.64	1.83
b. Agriculture and allied services	1.51	1.67	1.94	2.35
c. Industry and minerals	0.99	1.57	1.84	0.81
d. Power, irrigation and flood control	1.22	1.92	1.99	1.88
e. Transport and communication	1.15	1.74	1.70	1.24
d. Others	0.40	0.70	0.66	0.82
Total economic services	5.80	9.62	9.78	8.93

Source: 1. Indian Economic Statistics - Ministry of Finance, Government of India.  
2. Central Statistical Organisation.

**Table 2.13**

**Per Capita Expenditure on Economic Services**

(in 1981-82 rupees)

	1974-75	1981-82	1986-87	1990-91 (RE)
(1)	(2)	(3)	(4)	(5)
<b>1. Revenue Expenditure</b>				
a. Subsidies	10.47	22.85	46.84	62.22
b. Agriculture and allied services	17.34	34.35	52.39	76.37
c. Industry and minerals	4.89	11.36	17.32	17.56
d. Power irrigation and flood control	4.58	8.51	14.81	15.46
e. Transport and communication	8.24	13.90	15.60	16.87
f. Others	4.22	7.02	10.43	15.14
Total economic services	49.73	97.97	156.61	203.62
<b>2. Capital Expenditure</b>				
a. Agriculture and allied	11.93	3.31	2.22	3.45
b. Industry and minerals	14.32	24.01	34.44	10.01
c. Power, irrigation and flood control	19.03	34.92	41.13	48.36
d. Transport and communication	13.97	25.45	32.05	25.26
e. Others	3.48	8.83	8.21	12.74
Total economic services	62.73	96.51	118.06	99.82
<b>3. Total (Revenue plus Capital Expenditure)</b>				
a. Subsidies	10.47	22.85	46.04	62.22
b. Agriculture and allied services	29.26	37.66	54.61	79.82
c. Industry and minerals	19.21	35.36	51.77	27.57
d. Power, irrigation and flood control	23.61	43.42	55.95	63.82
e. Transport and communication	22.22	39.35	47.65	42.13
f. Others	7.71	15.85	18.65	27.88
Total economic services	112.47	194.48	262.62	303.45

Source: 1. Indian Economic Statistics, Ministry of Finance, Government of India.  
2. Office of the Registrar General, Government of India.

Even as per capita total expenditures on economic services showed decelerating trend in the successive periods, curiously, revenue expenditure continued to grow at a very high rate. In fact, during the contractionary period, the growth rate of revenue expenditure on economic services actually showed a marginal increase (8.3 per cent) over the previous period (7.4 per cent). The disaggregated analysis shows that this is attributable mainly to the growth of expenditures on rural poverty alleviation scheme. It may be noted that a part of the revenue expenditure on agriculture and allied activities was on rural poverty alleviation under self employment and wage employment schemes.<sup>12</sup> Both these items were in the nature of transfer payments to identifiable beneficiaries.

12. The self-employment programme on poverty alleviation scheme was Integrated Rural Development Programme (IRDP) and the wage employment programmes were Rural Landless Employment Guarantee Programme (RLEGP) and National Rural Employment Programme (NREP). These were consolidated into Jawahar Rozgar Yojana (JRY) in 1989-90.

Table 2.14

## Growth of Expenditures on Economic Services

(per cent per year)

	1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
	(1)	(2)	(3)	(4)
<b>1. Revenue Expenditure</b>				
a. Subsidies	9.8	10.3	11.9	10.4
b. Agriculture and allied activities	10.5	6.7*	9.2	8.7
c. Industry and minerals	8.4	9.63	2.50*	7.8
d. Power, irrigation and flood control	8.8	10.6	2.1*	8.3
e. Transport and communications	7.2	1.1*	5.0*	4.2
f. Total economic services	9.8	10.3	11.9	10.4
<b>2. Capital Expenditure</b>				
a. Subsidies	-	-	-	-
b. Agriculture and allied activities	-9.1	-3.2*	-6.7*	-6.3
c. Industry and minerals	3.0	6.5	-28.2*	-1.8
d. Power, irrigation and flood control	8.2	1.2*	5.2*	4.7
e. Transport and communication	8.6	2.9	-2.1	4.3
Total economic services	5.2	2.9	-4.2*	2.6
<b>3. Total Expenditures</b>				
a. Subsidies	9.8	10.3	11.9	10.4
b. Agriculture and allied activities	5.8	7.5	6.7	6.7
c. Industry and minerals	4.5	7.7	-15.0*	2.1
d. Power, irrigation and flood control	8.3	3.4*	4.4	5.5
e. Transport and communication	8.0	2.2*	0.6	4.3
f. Total economic services	6.8	5.5	3.3*	5.7

*Note:* Growth rates have been estimated by employing a kinked exponential regression model.

\* Significantly different from the previous period.

*Source:* Indian Economic Statistics, Ministry of Finance, Government of India.

The above analysis of the trends in expenditures on economic services brings out the following:

- a. The growth rate of per capita expenditure on economic services has shown a continuous decline over the successive periods. The growth rate, even during the expansionary phase was lower than in the previous periods. But as the growth rate was higher than that of per capita GDP until 1986-87, expenditure-GDP ratio showed a gradual increase until that year, but declined thereafter.
- b. The analysis of government expenditures in terms of economic and functional categories reveals that major sources of high growth of current expenditures on economic services were subsidies and other transfers. The share of these items to total expenditure on economic services was just about 15 per cent in 1974-75 but increased to almost 42 per cent by 1989-90 (Table 2.15). In per capita terms, transfer payments increased from Rs 34 to Rs 145 during this period and as a proportion of GDP it increased by 3.3 percentage points from 1.2 per cent to 4.5 per cent. The annual growth rate of per capita expenditure on subsidies at constant prices averaged about 11 per cent for the period as a whole and in every sub-period growth rate was more than 10 per cent (Table 2.16). Similarly, growth in expenditure on other transfers in per capita terms, after increasing at 10.4 per cent and 8.5 per cent in the first two periods, accelerated significantly to 17 per cent during the third sub-period. It must be noted that the largest shares of the subsidies were in irrigation and food and fertilizer subsidies which directly benefited a dominant interest group, namely, the rich farmers. The continued expansion of these subsidies even during the period of fiscal restraint underlines the power of this coalition in securing higher share of expenditures in their favour.
- c. As already mentioned, the expenditure on subsidies and on rural poverty alleviation programmes under agricultural and allied activities also witnessed high growth rates even during the period of fiscal restraint. This is partly explained by the fast expansion of poverty alleviation programmes. The Integrated Rural Development Programme (IRDP), started in 1978-79 was confined to 300 blocks until 1980, but was expanded to cover the entire country thereafter. Similarly, substantial increases in the allocation were made for National Rural Employment Programme (NREP) and Rural Landless Employment Guarantee Programme (RLEGP) during the Sixth (1980-85) and the Seventh plan periods (1985-90). What is however important to note is that, even with the high growth of allocation to this sector, spending on direct rural poverty alleviation programmes in 1990-91 formed only about 3 per cent of total expenditures although the proportion of people below poverty line formed about

33 per cent of rural population. The spending per rural poor in 1987-88 amounted to less than Rs 150. This again shows that in spite of the rhetoric and publicity given to eradication of poverty, only a token provision is made for eradicating poverty. This, besides ensuring stability to the society, also helps in directing the rest of the spending to the non-poor on the plea that the poor are taken care of through the poverty alleviation schemes.<sup>13</sup>

- d. It is also seen that in spite of the hardening resource constraint during the third phase, the growth rate of per capita expenditure on wages and salaries accelerated to 6.7 per cent from 5.8 per cent in the previous period (Table 2.16). In contrast, growth rate of expenditure on net government maintenance decelerated in every successive period and after 1986-87, the per capita expenditure on the item increased at the rate of just about 2 per cent per year. This again indicates the effectiveness of a dominant coalition, namely, the unions of government employees in securing a larger share.

**Table 2.15**  
**Expenditure on Economic Services**

(1)	Per Capita Expenditure (in 1981-82 rupees)				Percentage of Expenditure to GDP				Percentage of Total Economic Services			
	74-75	81-82	86-87	89-90	74-75	81-82	86-87	89-90	74-75	81-82	86-87	89-90
(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	
Compensation to employees	11.6	16.1	21.9	27.2	0.6	0.7	0.8	0.8	7.4	7.5	7.1	7.8
Net Government maintenance	6.9	13.4	16.8	18.0	0.4	0.6	0.6	0.6	4.4	6.2	5.5	5.2
Subsidy	19.5	44.2	83.4	120.2	1.0	2.0	3.0	3.7	12.5	20.6	27.1	34.4
Other transfers	4.7	9.7	18.0	25.2	0.2	0.4	0.6	0.8	3.0	4.5	5.9	7.2
Current expenditure total	42.6	83.4	139.9	190.6	2.2	3.7	5.0	5.8	27.3	38.8	45.5	54.6
Gross capital formation	27.1	23.1	28.4	27.7	1.4	1.0	1.0	0.8	17.4	10.7	9.2	7.9
Financial outlay	25.5	35.0	44.8	35.8	1.3	1.6	1.6	1.1	16.4	16.3	14.6	10.2
Capital transfers and net advance	60.6	73.4	94.2	95.3	3.1	3.3	3.4	2.9	38.9	34.2	30.6	27.3
Capital expenditure total	113.2	131.5	167.4	158.8	5.8	5.8	6.0	4.9	72.7	61.2	54.5	45.4
Total economic services	155.8	214.9	307.4	349.4	8.0	9.5	11.0	10.7	100.0	100.0	100.0	100.0

*Note:* The figures in this table do not strictly correspond to those in Table 2.12 and 2.13 as the data sources are different.

*Source:* Central Statistical Organisation, Ministry of Planning, Government of India.

13. On this, see, Kurian (1989) and also Rao and Das-Gupta (1992).

**Table 2.16**  
**Growth of Per Capita Expenditure on Economic Services**

Expenditure Category	(per cent per year)			
	1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
(1)	(2)	(3)	(4)	(5)
<b>1. Current Expenditures</b>				
1.1 Compensation to employees	4.3	5.8	6.7	5.3
1.2 Goods and services	8.5	3.6	2.0	5.6
1.3 Subsidy	11.8	10.2	10.5	11.0
1.4 Other transfers	10.4	8.5	17.2	10.4
Total current expenditure	9.4	8.4	9.8	9.0
<b>2. Capital Expenditures</b>				
2.1 Gross capital formation	-0.7	7.0*	-3.3*	2.4
2.2 Financial outlay	3.0	6.9	-11.2*	2.8
2.3 Capital transfers	1.7	1.9	-0.5*	1.6
Total capital expenditure	1.6	3.9	-3.6*	2.0
Total Economic Services**	4.2	6.1	2.8*	4.8

*Note:* Growth rates have been estimated by employing a kinked exponential regression model.

\* denotes that the growth rate is significantly different from the previous period.

\*\* The growth rates do not correspond to the figures given in Table 2.14 as the data sources are different.

*Source:* Central Statistical Organisation, Ministry of Planning, Government of India.

- e. The compression of expenditure in the contractionary phase occurred mainly in capital expenditure. What is worrisome, per capita capital expenditure on agriculture showed a continuous decline throughout the period. It may be noted that the private sector capital formation in agriculture too has not been showing significant increases during this period. The declining capital formation in the agricultural sector is further accentuated by the stagnancy in the capital expenditure GDP ratio in irrigation and power sector (1.6 per cent in 1981-82 and 1.4 per cent in 1986-87). Declining investment in agriculture, power and irrigation sectors would have adverse effects on both economic growth and rural employment and reduction in poverty.<sup>14</sup>
- f. Another disconcerting feature is the compression in the allocation to infrastructural sectors. Apart from power and irrigation sectors, expenditure-GDP share declined in transport and communications since 1986-87. The reduction in the allocation to these sectors was particularly severe in capital expenditures.

The above analysis clearly demonstrates the government's preference for spending on items with immediate and transparent benefits to the dominant coalitions as against providing social and economic infrastructures the benefits of which will accrue only in the longer term, the

14. Capital formation on agriculture and irrigation enhances long-term agricultural growth and it is argued that the "trickle down" effect of agricultural growth is very high. For details on declining rate of capital formation in agricultural sector and its adverse effects on growth, see Rao, C.H.H. (1992).

externalities accrue widely and benefits would be more encompassing. The consequences of these unfortunately are to adversely affect the growth potential and equity in the economy.

**2.2.4 Expenditure Trends at the Central and State Levels:** In a federal polity, with more than one half of the expenditure being incurred at the State level, it is helpful to analyse the trend at the Central and State levels separately to gain a better understanding of the expenditure policies. The detailed analysis of expenditure patterns and trends at the two levels will be undertaken in the subsequent chapters. In this section, however, the broad features on expenditure growth at Central and State levels are brought out.

It may be noted that the expenditure incurred at the State level in 1990-91 formed about 54 per cent of total expenditure (Table 2.17) and the States' share in revenue expenditure was close to 55 per cent and in capital expenditure about 45 per cent. The States' role in providing social and community services was particularly important as about 85 per cent of the total expenditure on these services was incurred by them. The States' shares in expenditures on social and economic services broadly remained constant throughout the period of one and a half decades. The decline in the States' share in interest payment was mainly due to the rescheduling and reduction in interest rates on Central loans to States done by the Seventh and Eighth Finance Commissions. Similarly, the States' share of net loans and advances disbursed increased tremendously over the years mainly due to the increasing accommodation given to State Electricity Boards.

**Table 2.17**  
**Share of State Level Expenditures in Total Expenditures**

Description	(per cent)											
	1974-75			1981-82			1986-87			1990-91		
	Reve- nue	Capital	Total									
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
1. Interest payments	46.4	-	46.4	38.9	-	38.9	38.7	-	38.7	35.3	-	35.3
2. General Administrative services	32.2	4.2	30.6	35.7	1.2	33.8	33.4	0.4	29.7	33.4	0.5	36.4
3. Social and community services	85.7	70.0	84.9	87.1	72.3	86.0	84.4	57.4	82.0	84.4	73.5	84.5
4. Economic services	67.0	42.6	53.4	64.7	46.9	55.9	58.4	42.5	51.6	58.4	50.4	54.5
5. Net loans and advances	-	38.3	38.3	-	50.6	50.6	-	42.2	42.2	-	57.6	57.6
6. Total expenditure	56.5	40.2	51.6	58.6	47.3	55.3	54.6	39.0	50.4	54.6	45.0	53.8

*Note:* States include Union Territories also.

A comparison of per capita expenditures (1981-82 prices) and expenditure-GDP shares at the State level with per capita aggregate expenditures of the Centre and States shows some important differences in the trends. First, the increase in expenditures in the expansionary phase was slower in the case of States as compared to the aggregate. In fact, the expenditure-GDP ratio at the State level increased only by about two percentage points during the period 1981-82 to 1986-87 as compared to six percentage point increase seen in the case of aggregate expenditures (Table 2.18). It is also seen that in the case of capital expenditure-GDP share, there was in fact a decline, *albeit* marginal, at the State level during the expansionary phase in contrast to the increase of one percentage point seen in aggregate capital expenditure-GDP ratio.

Secondly, unlike in the case of aggregate expenditures which, as a proportion of GDP declined in the contractionary phase (1986-87 to 1990-91), the State level expenditures actually showed a marginal increase. This was mainly due to the continued increase in revenue expenditures. Further, during this period, the decline in the capital expenditure-GDP share at the State level was also substantially smaller (0.6 per cent) than that of aggregate expenditures (2.3 points).

**Table 2.18**

**Government Expenditure as Percentage of Gross Domestic Product**

	Total (Centre + States and Union Territories)			State and Union Territories		
	Revenue expenditure	Capital expenditure	Total expenditure	Revenue expenditure	Capital expenditure	Total expenditure
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1974-75	13.20	5.67	18.87	7.47	2.28	9.74
1981-82	17.00	7.37	24.45	10.01	3.50	13.52
1986-87	22.29	8.23	30.52	12.17	3.21	15.38
1990-91 (RE)	23.38	5.94	29.32	13.10	2.67	15.76

*Source:*

1. Indian Economic Statistics, Ministry of Finance, Government of India.
2. Central Statistical Organisation, Ministry of Planning, Government of India.

The difference in the trends between aggregate and State level expenditures becomes clearer when we examine the growth rates in the four sub-periods, summarised in Table 2.19. The State level expenditures did not differ markedly from one period to another and therefore, did not follow the periodicity seen in the case of aggregate expenditures. The revenue expenditure growth which accelerated during the expansionary phase continued to grow at a high rate even when the resource constraint hardened during the third phase at both Central and

State levels. Thus, the difference in the trends between the Centre and States was mainly in capital expenditures. At the State level, compression in capital expenditures set in right from the beginning of the 1980's and the growth rate which was -1.2 per cent even during the period of fiscal expansion continued to be low (1.1 per cent) during the latter half of the decade. In contrast, in the case of total expenditure, deceleration in the growth rate started only from 1986-87.

**Table 2.19**  
**Growth of Per Capita Expenditure (1981 Prices) at**  
**Aggregate and at State Levels**

(per cent per year)

Expenditure Category	Growth Rates								
	74-75 to 81-82		81-82 to 86-87		86-87 to 90-91		74-75 to 90-91		
	Total	State	Total	State	Total	State	Total	State	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	
A. Interest payment	6.4	2.8*	13.1*	12.3	13.2*	12.1	10.3	8.3	
B. General administrative services									
- Revenue	1.6	3.8*	8.9*	8.0	3.3*	8.6	4.9	6.3	
- Capital	0.5	-14.3*	24.8*	12.8	12.7*	24.0	12.1	3.5	
- Total	1.5	3.7	10.2*	8.1	4.5*	8.6	5.6	6.3	
C. Social and community services									
- Revenue	5.3	5.9	7.9*	7.0	5.4*	5.7	6.4	6.3	
- Capital	7.5	9.9*	10.9*	6.7	-3.5*	0.9*	6.9	7.0	
- Total	5.5	6.1	8.2*	7.0	4.7*	5.5	6.5	6.4	
D. Economic services									
- Revenue	8.7	9.4	7.4*	6.2	8.3*	4.1	8.1	7.1	
- Capital	5.2	6.4*	2.9*	-0.3	-4.1*	0.8	2.6	2.6	
- Total	6.8	8.1*	5.5*	3.7	3.3*	3.1	5.7	6.4	
E. Loans & advances	Total	3.5	9.3*	0.5*	-4.8	2.8*	1.5	1.0	1.9
F. Total expenditure									
- Revenue	4.9	6.0	8.9*	7.5	6.9*	6.6	6.9	6.8	
- Capital	4.4	7.6*	4.2*	-1.2	-1.5*	1.1	3.3	2.7	
- Total	4.7	6.4	7.6*	5.4	4.9*	5.7	5.9	5.9	

Note: Growth rates have been estimated by employing a kinked exponential regression model.

\* denotes that the growth rate is significantly different from the previous period.

The share of State level expenditures in aggregate expenditures, however, does not indicate any clear trend (Table 2.17). State level expenditures as a percentage of total increased from 51.6 per cent in 1974-75 to 55.3 per cent in 1981-82, but thereafter fell to 53.8 per cent in 1990-91. The absence of a clear trend cannot, however, be taken to infer that expenditure

centralisation did not take place over the period. It must be noted that, over the years, with the proliferation and increase in the volume of assistance under Central sector and Centrally Sponsored Schemes, increasing proportion of States' expenditures were decided by the Central Ministries. Therefore, even the constancy in the States' share would indicate increased centralisation in expenditure decisions.

Similar pattern is seen in the expenditure shares computed from CSO's economic and functional classification. The trend in the shares of State governments is unclear if 1974-75 is taken as a base year. However, with 1981-82 as the base year, the States' shares in total spending were lower in 1989-90 in respect of both current and capital expenditures, mainly due to the sharp decline in the case of economic services from 49 per cent to 42 per cent (Table 2.20). In particular, significant decline was seen in the case of two sectors, namely, (i) energy, water supply and gas, and (ii) transport and communication. In the case of the energy sector, the decline was continuous right from 1974-75, and particularly sharp in capital expenditures.<sup>15</sup> The States' share of capital expenditure in the sector declined from 83 per cent in 1974-75 to 75 per cent in 1981-82 and further to 57.4 per cent in 1989-90.

**Table 2.20**  
**Share of State Expenditures in Total Expenditure**

Expenditure Category	1974-75	1981-82	1986-87	1989-90
(1)	(2)	(3)	(4)	(5)
1.1 General Administrator	55.7	66.6	63.4	68.5
1.2 Defence	-	-	-	-
1. Total-General Services	27.6	31.1	28.8	31.7
2.1 Education	90.2	92.9	92.6	92.0
2.2 Health	92.6	86.7	88.0	85.0
2.3 Social Welfare	87.6	90.4	90.0	89.4
2.4 Housing	88.9	89.6	88.7	87.0
2. Social Services	88.0	89.4	90.1	89.2
3.1 Agriculture and Irrigation	36.3	53.9	54.1	60.2
3.2 Mining, Manufacturing and Construction	10.2	16.6	15.8	17.3
3.3 Energy, Water Supply and Gas	77.5	71.7	65.9	60.3
3.4 Transport and Communication	48.2	70.1	62.0	55.6
3. Total Expenditure				
Current	50.1	57.3	53.6	53.9
Capital	35.2	50.3	49.2	48.3
Total	44.2	54.8	52.2	52.4

*Source:* Central Statistical Organisation, Ministry of Planning, Government of India.

15. This was noted also in Bagchi and Sen (1992).

## CHAPTER III

### LEVEL AND COMPOSITION OF CENTRAL GOVERNMENT EXPENDITURES

#### 3.1 Introduction

Central Government expenditures including grants and loans to the States in 1990-91 constituted about 65 per cent of aggregate expenditures and the proportion of direct Central expenditures (excluding the transfers) in total was about 46 per cent. The share of direct expenditure of the Centre in the revenue account was 44 per cent and in the capital account, it was about 55.8 per cent.<sup>1</sup>

Significant share in total expenditures is not the only reason meriting a detailed analysis of Central government expenditures. It is the Central Government that determines the broad macroeconomic policy parameters and hence, exerts overall control on aggregate government expenditure policy. The State governments do not have independent borrowing powers nor can they resort to unlimited overdrafts from the Reserve Bank of India (RBI)<sup>2</sup>. In the event, Central government also exercises indirect control on their spending levels.

The Central Government can affect the level and pattern of States' expenditures by influencing the amount and method of resources devolved to them. The resource availability to the States can be influenced by the amount of shared taxes, grants and net loans received from the Centre and by the volume of market borrowing allocated to them.<sup>3</sup> The Centre can also affect the composition of States' expenditures through specific purpose matching grants or shared cost programmes.

This power to transfer resources to the States gives an additional handle to the Centre to bring about fiscal adjustment and stabilisation. Although the Constitution provides for the appointment of a semi-judicial body, the Finance Commission, every five years to recommend the distribution of shared taxes and grants, such formula based transfers constitute only 43.3 per cent of total Central transfers to States. The transfers given by the Planning Commission and

1. In gross terms (including transfer to States), Central share in revenue expenditure was 60 per cent and in capital expenditure 66 per cent.
2. The overdraft regulation scheme introduced in January, 1985 stipulates that the Reserve Bank of India can dishonour the States' cheques if the latter resort to overdrafts for a period of seven continuous working days.
3. It may be noted that the States do not have independent power to borrow from the market so long as they are indebted to the Centre. As all the States are indebted to the Centre, the market borrowing is allocated by the Reserve Bank of India to the States in consultation with the Union Finance Ministry. For details, see, Rao and Chelliah (1992).

from various Central ministries for Centrally sponsored schemes form over 41 per cent of the total transfers. Although the Central government does not have absolute discretion to determine the relative shares of the States in the strict sense,<sup>4</sup> it can exercise considerable leeway in determining the total volume of transfers, and to some extent, also the broad shares of the States by choosing the pattern of allocation to different Centrally sponsored schemes.

Thus, the Central government can achieve the stipulated fiscal targets either by reducing its own expenditures or by reducing transfers to States. As the latter option is easy to achieve, the burden of adjustment can be passed on to the States. In the States too, given that the distributional coalitions wield enough power to maintain or even increase expenditures on items beneficial to them, the reduced resource availability may simply crowd out allocations to social and economic infrastructures. The analysis of Central government expenditure, particularly the manner of achieving fiscal compression attempted in the recent years will help us to gain better understanding of the process of determining expenditure policy.

### **3.2 Central Government Expenditures: General Trends**

The expenditure of the Central government (including grants and loans to States) as a proportion of GDP increased from 12 per cent in 1974-75 to 19 per cent in 1990-91 (Table 3.1). Of the 7 percentage points increase, 6.3 percentage points were simply due to increase in revenue expenditures; the share of revenue expenditure in GDP increased from 7.9 per cent to 14.3 per cent during the period. On the other hand, the share of capital expenditure in GDP during this period increased by just 0.7 percentage point. Thus, naturally, the share of capital expenditure in total expenditure declined sharply from 34.4 per cent in 1974-75 to 25.5 per cent in 1990-91. In per capita terms (at 1981-82 prices), during the sixteen years, while the revenue expenditures recorded more than three-fold increase (from Rs 154 to Rs 485), the capital expenditures only doubled (from Rs 81 to Rs 166).

The trend in Central government expenditure shows an identical pattern to the increase in the aggregate expenditures analysed in the previous Chapter. The per capita expenditure of the Central government including grants and loans to States at constant (1981-82) prices increased from Rs 235 in 1974-75 to Rs 650 in 1990-91 (Table 3.1) although, after 1986-87, the increase was slower. Throughout the period, per capita revenue expenditures showed a steady increase but, per capita capital expenditures which reached a peak of about Rs 191 in 1985-86 declined thereafter to settle at Rs 166 in 1990-91.

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4. The shares of individual States in plan transfers are determined on the basis of the 'Gadgil formula', determined by the National Development Council and modified by it from time to time. Further, the relative share of States in different Centrally sponsored schemes are also predetermined on the basis of the objectives of individual schemes.

**Table 3.1**

**Central Government Expenditures in India: 1974-75 to 1991-92**

Period	As Percentage of GDP			Per Capita (1981-82) Rupees			Ratio of capital expenditure to total (per cent)
	Revenue	Capital	Total	Revenue	Capital	Total	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1974-75	7.9	4.2	12.1	153.8	80.8	234.6	34.4
1981-82	10.1	5.1	15.2	228.3	114.4	342.7	33.4
1985-86	13.3	7.0	20.3	361.9	190.8	552.7	34.5
1986-87	14.2	6.8	21.0	400.9	189.9	590.8	32.1
1987-88	14.3	5.4	19.7	413.1	156.8	569.9	27.5
1988-89	14.0	5.2	19.2	438.3	162.6	600.9	27.1
1989-90	14.6	5.2	19.8	477.4	170.3	647.7	26.3
1990-91	14.3	4.9	19.1	484.6	165.6	650.2	25.5

*Source:*

1. Central Government Budget Documents.
2. Central Statistical Organisation, Ministry of Planning.
3. Registrar General, Government of India.

The expenditure-GDP ratio presented in Table 3.1 bring out the different phases of expenditure increases clearly. The ratio recorded only about 3 point increase during the first seven years from 12.1 per cent in 1974-75 to 15.2 per cent in 1981-82. During the expansionary phase of the next 5 years, however, it increased by almost six percentage points to reach 21 per cent. During the next four years, the ratio declined to touch 19.1 per cent in 1990-91.

It is also seen that until 1986-87, the shares of both revenue and capital expenditures increased steadily, the former more than the latter. Thereafter, the share of revenue expenditure remained stable at a little over 14 per cent whereas, the share of capital expenditure declined sharply from 7 per cent to 4.9 per cent (Table 3.1). The growth rate of per capita expenditure at constant prices increased from 3.8 per cent during the first period to 9.5 per cent during the period of fiscal expansion (1981-82 to 1986-87); and thereafter, declined to 4.2 per cent during the period of fiscal restraint. Interestingly, although revenue expenditure trend broadly followed a similar pattern, it continued to grow at a high rate of 6.2 per cent even during the period of fiscal restraint. Capital expenditure, on the other hand, recorded a negative growth of -3.5 per cent during the period, 1986-87 to 1990-91 after increasing at 8.6 per cent per year during the expansionary period (Table 3.4).

An important reason for the high growth rate in revenue expenditures even during the period of fiscal restraint was the continuous acceleration in the growth of interest payments. In fact, the share of interest payments in total expenditures increased at a relatively slow rate from

about 11 per cent in 1974-75 to 14 per cent in 1981-82, but thereafter increased very sharply to 21 per cent in 1990-91. This must be attributed to both the increased volume of indebtedness to meet government consumption and investment requirements and increase in the effective rate of interest over the years. At the same time, even the past investments financed from borrowed funds did not yield adequate financial returns as the non-tax revenues including interest receipts were virtually stagnant during the 1980's (Mundle and Rao, 1992).

**Table 3.2**  
**Composition of Central Government Expenditure**

(per cent)							
(1)	Interest payments	General services	Social services	Economic services	Grants or loans to States	Other loans	Total expenditure
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<b>Revenue Expenditure</b>							
1974-75	17.2	44.4	5.0	15.1	18.3	-	100.0
1981-82	19.8	35.3	4.3	22.9	17.7	-	100.0
1986-87	22.1	33.4	4.5	21.5	18.5	-	100.0
1990-91	28.4	26.0	4.5	23.5	17.6	-	100.0
<b>Capital Expenditure</b>							
1974-75	-	6.9	0.9	45.0	18.7	28.5	100.0
1981-82	-	6.3	1.5	42.0	26.1	24.1	100.0
1986-87	-	13.2	2.7	37.2	24.3	22.6	100.0
1990-91	-	19.2	1.3	25.5	38.1	15.9	100.0
<b>Total Expenditure</b>							
1974-75	11.2	31.5	3.6	25.5	18.4	9.8	100.0
1981-82	13.2	25.6	3.4	29.3	20.5	8.0	100.0
1986-87	15.0	26.9	3.9	26.5	20.4	7.3	100.0
1990-91	21.2	24.3	3.7	24.0	22.8	4.0	100.0

The analysis of the composition of Central Government expenditure in terms of major functional categories (Table 3.2) reveals that in 1990-91, both general services (including defence) and economic services each claimed about a quarter of total expenditures. The share of interest payments was 21 per cent and statutory and plan grants (excluding grants under Centrally Sponsored Schemes) and loans to the States constituted 23 per cent. The share of expenditure on social services was the lowest at 3.7 per cent.

The analysis of the composition of Central government expenditures by economic categories (Table 3.3), brings out some interesting features. First, as already mentioned, the share of current expenditure increased steadily from 54 per cent in 1974-75 to 72 per cent in 1989-90 and correspondingly, during this period, the share of capital expenditure declined from 46 per cent to 28 per cent. Second, within current expenditures, the subsidies and transfers increased at a very high rate to significantly enhance their relative shares. The share of subsidies increased from less than 10 per cent in 1974-75 to over 24 per cent in 1989-90 and that of transfers to individuals increased from 3.8 per cent to 7 per cent during this period. Third, wages and salaries broadly maintained its share of almost one-fifth of total expenditures during the period. Although the share of this item showed a marginal decline until 1986-87, it substantially regained it in subsequent years. Fourth, within capital expenditure, significant decline in the share was seen in both gross fixed capital formation expenditure and capital transfers, whereas the share of financial outlay showed a marginal increase.

**Table 3.3**

**Composition of Central Government Expenditures by Economic Categories**

	(per cent)			
	1974-75	1981-82	1986-87	1989-90
	(1)	(2)	(3)	(4)
1. Consumption expenditure				
a. Compensation to employees	21.6	18.9	17.9	19.0
b. Net government maintenance	18.3	22.9	23.2	21.6
Total - 1	39.9	41.8	41.1	40.6
2. Transfers				
a. Subsidies	9.6	14.0	18.2	24.1
b. Transfer to local bodies	0.7	0.5	0.2	0.3
c. Other transfers	3.8	4.3	6.0	7.0
Total - 2	14.1	18.8	24.4	31.3
3. Total current expenditure (1+2)	54.0	60.6	65.5	72.0
4. Gross fixed capital formation	10.1	3.7	4.3	3.1
5. Financial outlay	11.4	14.2	12.1	15.4
6. Total capital transfers	24.5	21.5	18.0	16.3
7. Total capital expenditure	46.0	39.4	34.5	28.0
8. Total expenditure (3+4)	100.0	100.0	100.0	100.0

*Note:* Interest payments are not included in total expenditure.

*Source:* Central Statistical Organisation, Ministry of Planning, Government of India.

The shares of expenditures in GDP of various functional categories bring out the expenditure trends during different phases (Table 3.4). As already pointed out, aggregate expenditure-GDP share increased by just about 3 percentage points during the first seven years

(from 12.1 per cent to 15.2 per cent), but during the expansionary phase of the next 5 years, it increased a little less than 6 percentage points and showed a decline after 1986-87. Of this 6 percentage point increase in expenditure-GDP ratio, more than 4 points were on account of increase in revenue expenditures. Increase in direct capital expenditure by the Centre during this period contributed just about 0.7 point increase and transfers to States and loans and advances contributed only 0.6 point. During the period of fiscal restraint, the percentage of revenue expenditure in GDP continued to increase in respect of all the functional categories except general services where the cut-backs in defence expenditure reduced the share from 4.8 per cent in 1986-87 to 3.7 per cent in 1990-91. In contrast, during this period, the capital expenditure-GDP share declined in respect of all items except grants and loans to States and the sharpest decline was in economic services (from 2.5 per cent in 1986-87 to 1.2 per cent in 1990-91).

**Table 3.4**  
**Central Government Expenditure as a Percentage of GDP**

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	Interest payments	General services	Social services	Economic services	Grants or loans to States	Other loans	Total expenditure
<b>Revenue Expenditure</b>							
1974-75	1.37	3.52	0.40	1.20	1.45	-	7.94
1981-82	2.00	3.57	0.44	2.32	1.79	-	10.12
1986-87	3.16	4.77	0.64	3.06	2.64	-	14.28
1989-90	4.00	3.70	0.65	3.35	2.50	-	14.25
<b>Capital Expenditure</b>							
1974-75	-	0.29	0.03	1.88	0.78	1.18	4.17
1981-82	-	0.32	0.08	2.13	1.33	1.22	5.07
1986-87	-	0.63	0.11	2.50	1.65	1.53	7.02
1989-90	-	0.94	0.06	1.24	1.85	0.78	4.87
<b>Total Expenditure</b>							
1974-75	1.37	3.81	0.43	3.08	2.23	1.18	12.10
1981-82	2.00	3.89	0.51	4.45	3.12	1.22	15.19
1986-87	3.16	5.66	0.82	5.58	4.29	1.53	21.04
1989-90	4.00	4.64	0.71	4.59	4.35	0.78	19.12

The expenditure trends in the different phases noted above come out clearly when we consider the growth of per capita expenditures (at constant prices) during the different sub-periods (Table 3.5). The significant acceleration in the expenditure growth rate during the period of fiscal expansion and the sharp decline in the subsequent period have already been pointed out. It was also noted that during the expansionary phase the growth rate of both

revenue and capital expenditures increased significantly, but the contraction during the period of fiscal restraint was mainly in capital expenditure. In per capita terms, capital expenditure at constant prices actually recorded a decline at the average annual rate of 3.5 per cent. The analysis by functional categories shows that during this period of fiscal restraint, besides interest payments which continued to record a high growth rate (12.7 per cent), the per capita revenue expenditure on economic services (1981-82 prices) which were mainly in the nature of subsidies and transfer payments recorded the fastest growth (10.7 per cent). On the other hand, per capita capital expenditure on economic services declined at the rate of 12.3 per cent per year.

**Table 3.5**  
**Growth of Per Capita Expenditure at 1981-82 Prices**

(per cent per year)

(1)	Interest payments	General services	Social services	Economic services	Grants and loans to States	Total loans and advances	Total expenditure
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<b>Revenue Expenditure</b>							
1974-75 to 1981-82	6.7	1.5	-1.2	11.3	4.4	-	4.8
1981-82 to 1986-87	13.7*	8.1*	11.4*	6.1	9.3	-	9.2
1986-87 to 1989-90	12.7	0.2*	7.9	10.7	0.9	-	6.2
1974-75 to 1989-90	10.6	4.0	6.5	9.0	5.8	-	6.8
<b>Capital Expenditure</b>							
1974-75 to 1981-82	-	2.5	6.9	2.7	13.7	6.4	4.5
1981-82 to 1986-87	-	21.6*	22.7*	8.9*	6.7*	5.6	8.6
1986-87 to 1989-90	-	9.7*	-15.6*	-12.3*	2.4*	-0.8*	-3.5
1974-75 to 1989-90	-	11.4	8.7	2.4	8.7	4.8	4.8
<b>Total Expenditure</b>							
1974-75 to 1981-82	6.7	1.6	1.8	6.7	8.1	6.4	4.7
1981-82 to 1986-87	13.7*	9.6*	13.4*	7.5	8.1	5.6	9.0
1986-87 to 1989-90	12.7	1.9*	4.1*	1.7*	1.5*	-0.8	3.3
1974-75 to 1989-90	10.6	4.9	6.9	6.1	6.9	4.8	6.2

*Note:* Growth rates have been estimated by employing the kinked exponential regression model.  
\* represents that growth rate is significantly different from the previous period.

It is interesting to see that the grants and loans to States too followed broadly a similar pattern. These items of Central transfers to States, in per capita terms at constant prices recorded an average annual growth of over 8 per cent in the latter half of the 1970's and in the first half of 1980's. During the expansionary period the deceleration in the growth rate of loans was offset by the acceleration in the growth of grants. However, during the period of fiscal

restraint, the growth rates of both grants and loans declined sharply, although as ratios of both GDP and total Central expenditures, spending on this item continued to show marginal increases. Let us now examine the expenditure trends in general, social and economic services in greater detail.

### 3.3 General Services

As already mentioned, expenditure on general services as a proportion of GDP increased from 3.8 per cent in 1974-75 to 5.7 per cent in 1986-87 and declined thereafter to 4.6 per cent in 1990-91. The expenditure on this category formed almost one-third of total expenditures in 1974-75 but in 1990-91, it was less than one-fourth. After growing at a phenomenal rate of 9.6 per cent per year during the expansionary phase, the growth of per capita expenditure on general services declined to 1.9 per cent during the period of fiscal restraint.

**Table 3.6**  
**Expenditure on General Services**

Particulars	Per Capita Expenditure (in 1981-82 rupees)				Percentage of GDP			
	74-75	81-82	86-87	90-91	74-75	81-82	86-87	90-91
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
<b>1. General Administrative Expenditure (including police)</b>								
- Revenue	14.4	19.1	43.2	53.6	0.74	0.84	1.54	1.57
- Capital	0.5	0.4	12.5	2.7	0.03	0.02	0.44	0.08
- Total	14.9	19.5	55.6	56.3	0.77	0.86	1.98	1.65
<b>2. Police</b>	4.5	5.1	8.9	11.5	0.23	0.22	0.32	0.34
<b>3. Defence Expenditure</b>								
- Revenue	53.9	61.5	90.9	72.3	2.78	2.73	3.24	2.13
- Capital	5.0	6.8	12.4	29.2	0.26	0.30	0.45	0.86
- Total	59.0	68.4	103.3	101.5	3.04	3.03	3.68	2.98
<b>4. Total-General Services Expenditure</b>								
- Revenue	68.3	80.6	134.0	125.9	3.52	3.57	4.77	3.70
- Capital	5.6	7.3	24.9	31.9	0.29	0.32	0.89	0.94
- Total	73.9	87.9	158.9	157.8	3.81	3.89	5.66	4.64

The disaggregated analysis of general services (Table 3.6) shows that expenditures on general administration as well as on defence increased sharply during the period of fiscal expansion, but declined thereafter. As a ratio of GDP, expenditure on defence increased from 3 per cent in 1974-75 to 3.7 per cent in 1981-82 and thereafter declined to settle at 3 per cent in 1990-91 (Table 3.6). The ratio of administrative expenditure to GDP increased from 0.8 per cent in 1974-75 to 2 per cent in 1986-87 and thereafter, declined to 1.7 per cent in 1990-91. It is also seen that the growth rate of both revenue and capital expenditures of these items accelerated significantly in the first half of the 1980's (Table 3.7). Interestingly, even during the period of fiscal restraint the capital expenditure on defence continued to increase.

**Table 3.7**  
**Growth of Per Capita Expenditure in General Services at Constant Prices**

Expenditure Category		(per cent per year)			
		1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
(1)		(2)	(3)	(4)	(5)
<b>1. Police</b>					
	- Revenue	-0.4	10.8*	8.2	5.4
	- Capital	n	n	n	n
	- Total	-0.4	10.8*	8.2	5.4
<b>2. General Administrative Expenditure**</b>					
	- Revenue	0.4	10.5*	2.5*	4.9
	- Capital	18.6	36.4*	-17.1*	18.2
	- Total	0.8	13.9*	-1.3*	5.7
<b>3. Defence</b>					
	- Revenue	0.7	8.8*	-1.6*	3.6
	- Capital	0.4	20.3*	26.4	12.6
	- Total	0.6	10.3*	3.2*	5.0
<b>4. Total: General Services</b>					
	- Revenue	0.4	9.3*	0.2*	4.0
	- Capital	1.5	24.6*	12.8*	12.6
	- Total	0.5	11.1*	2.5*	5.2

*Note:* Growth rates have been estimated by employing the kinked exponential model.

n = expenditure is negligible.

\* = denotes growth rate is significantly different from the previous period.

\*\* = includes police.

### **3.4 Social Services**

The provision of social and community services is mainly the responsibility of State governments and role of the Central government in this task is only subsidiary. Less than 4 per cent of total expenditure of the Central government in 1990-91 was on social services and as a proportion of total spending on social services, Central government's share was just about 10 per cent. Thus, it is not surprising that in terms of both per capita expenditures and

expenditure-GDP shares, Centre's spending on social services was very low (Table 3.8) and therefore, did not significantly affect the overall trends.

Given that the responsibility of providing important social services is primarily assigned to State governments, Centre's interference in providing them is called for only in the case of services involving significant inter-State spill-overs or 'merit' goods, where the independent actions of the States may result in their less than optimal provision. However, the level of spending on social services like education, health and urban infrastructure by the Centre can at best be considered as symbolic. The Central government spends just about 0.12 per cent of GDP on school education and 0.14 per cent of GDP on higher and technical education (Table 3.8). If it is argued that Central government's involvement is necessary for the reasons cited above, then it is doubtful whether with this token involvement, it is possible to raise spending to optimal levels. At the level of school education, it is seen that much of the involvement of the Central government is in providing highly subsidised education to the wards of its own employees through the Central Schools. Similarly, a good proportion of expenditure on health care by the Central government is on Central Government Health Scheme (CGHS) meant to benefit only its employees. Thus, much of the Central intervention seems to be not in the interest of providing optimal levels of these services but, merely to enable the Central government employees to gain access to the highly subsidised services. In the case of higher and technical education, the rationale seems to be to provide better opportunities at highly subsidised rates only to the children of the elite, for, the illiterates who form 48 per cent of the population above the age of seven, cannot anyway get access to the institutions of higher learning.

**Table 3.8**  
**Expenditure on Social Services**

Expenditure Category	Per Capita Expenditure (in 1981-82 rupees)				Percentage of GDP			
	1974-75	1981-82	1986-87	1990-91	1974-75	1981-82	1986-87	1990-91
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
1. General Education	3.0	3.4	5.9	7.6	0.15	0.15	0.21	0.22
a. Elementary education	0.2	0.3	0.4	0.7	0.01	0.01	0.02	0.02
b. Secondary education	1.0	1.1	2.3	3.3	0.05	0.05	0.08	0.10
c. Higher education	1.4	1.6	2.5	2.7	0.07	0.07	0.09	0.08
2. Technical Education	0.7	0.8	1.6	2.1	0.04	0.04	0.06	0.06
3. Health Care Expenditure	1.3	2.0	3.9	4.4	0.07	0.09	0.14	0.13
4. Housing & Urban Develop.	0.6	1.4	2.9	2.1	0.03	0.06	0.10	0.06
5. Other Social Services	2.8	4.0	9.0	7.9	0.14	0.18	0.32	0.23
6. Total Social Services								
- Revenue	7.7	9.9	18.0	22.0	0.40	0.43	0.64	0.65
- Capital	0.7	1.7	5.1	2.2	0.03	0.08	0.18	0.06
- Total	8.4	11.6	23.1	24.2	0.43	0.51	0.82	0.71

Source: Budget Documents of the Central Government, Ministry of Finance, Government of India.

Another reason for the continued high priority of expenditures on social and community services even during the period of fiscal restraint is the revision of pay scales of school and college teachers, medical personnel and the persons involved in administering social services. In fact, the growth of per capita expenditure on wages and salaries (at 1981-82 prices) under social services actually showed a significant acceleration to 7.2 per cent per year during the period 1986-87 to 1989-90, over the previous period when it grew at -0.9 per cent per year (Table 3.10).

**Table 3.9**  
**Growth of Per Capita Expenditure on Social Services (1981-82 Prices)**

Expenditure Category	(Per cent per year)			
	1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
(1)	(2)	(3)	(4)	(5)
1. General Education	-0.3	10.6*	8.0	5.6
a. Elementary education	2.1	8.2	11.5	6.2
b. Secondary education	-0.7	14.1*	12.7	7.8
c. Higher education	-0.9	9.0*	2.4*	3.7
2. Technical Education	0.3	16.8*	5.1*	7.6
3. Health Care	2.5	11.5*	8.3	7.1
4. Housing and Urban Development	10.3	7.5	-1.9*	6.9
5. Other Social Services	1.6	17.5*	0.6*	7.8
- Revenue	1.2	11.5*	7.2*	6.5
- Capital	6.9	22.7*	-15.6*	8.7
Total Social Services	1.8	13.4*	4.1*	6.9

Note: Growth rates have been estimated by employing the kinked exponential regression model.

\* indicates that the growth rates are significantly different from the previous period.

Source: Budget Documents of Central Government.

**Table 3.10**  
**Growth of Per capita Expenditure on Wages and Salaries of the Central Government**

(1)	(Per cent per year)			
	1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
(1)	(2)	(3)	(4)	(5)
1. General services				
a. General administration	-3.2	11.1*	0.3*	3.1
b. Defence	-2.3	10.0*	6.1*	3.8
Total - 1 General services	-2.4	10.2*	4.9*	3.7
2. Social services				
a. Education	2.1	6.1*	6.8*	4.4
b. Health	12.9	-4.2*	5.6*	4.4
c. Social welfare	1.4	5.7*	15.9*	4.9
d. Housing and community services	2.7	6.8*	-5.1*	3.4
Total - 2 - Social services	4.5	-0.9*	7.2*	2.5
3. Economic services				
a. Agriculture	-0.5	18.0*	2.1*	7.3
b. Mining, manufacturing and construction	11.2	16.9	-2.4*	11.8
c. Energy, water supply and gas	3.2	13.1*	7.1*	7.8
d. Transport and communication	-1.6	10.1*	-5.1*	2.8
Total - 3 - Economic services	2.7	14.0*	1.1*	7.1

Note: Growth rate has been estimated using the kinked exponential regression model.

\* indicates that the growth rates are significantly different from the previous period.

Source: Central Statistical Organisation, Ministry of Planning, Government of India.

### **3.5 Economic Services**

The share of expenditure on economic services in total spending of the Central Government in 1990-91 constituted about 25 per cent (Table 3.2). Centre's share in total spending in economic services was a little over 50 per cent. The expenditure incurred by the Central government on economic services in 1990-91 formed 4.6 per cent of GDP.

The important activities under economic services include agriculture and rural development, industry and minerals, energy and transport and communication. The most important item, however, was subsidies on food, fertilizers and exports, which together constituted 1.8 per cent of GDP or 35 per cent of Centre's spending on economic services in 1990-91.

The spending on economic services by the Central government broadly follows the general trend noted in the previous chapter (Table 3.11). The expenditure-GDP share showed a steady increase from 3.1 per cent in 1974-75 to 5.6 per cent in 1986-87 and thereafter, declined to 4.6 per cent in 1990-91. This happened mainly due to the steep decline in the share of capital expenditure in GDP from 2.5 per cent in 1986-87 to 1.2 per cent in 1990-91. In per capita terms at constant prices, capital expenditure declined from Rs 71 in 1986-87 to Rs 42 in 1990-91. Capital expenditures as a ratio of total expenditure on economic services declined from 61 per cent in 1974-75 to a mere 27 per cent in 1990-91. The share of revenue expenditure in GDP on economic services, in contrast, continued to increase even during the period of fiscal restraint.

The expenditure trends noted above come out clearly when we consider the growth rates (Table 3.12). Per capita expenditure on economic services at constant prices increased at 7.5 per cent per year during 1981-82 to 1986-87, but the growth rate declined thereafter to 1.7 per cent during the period, 1986-87 to 1990-91. The average annual growth rate of per capita revenue expenditure on economic services during the period of fiscal restraint was actually higher at 10.7 per cent per year as compared to 6.1 per cent during the previous period. In contrast, the per capita capital expenditure during this period recorded a decline at the rate of 12.3 per cent per year, which actually caused the growth of total expenditure on economic services to decelerate.

A major source of sustained revenue expenditure growth was increase in the volume of subsidies. Of about 1 percentage point increase in revenue expenditure-GDP share during the period from 1981-82 to 1990-91 (from 2.3 per cent to 3.3 per cent), as much as 0.8 percentage point was simply due to increase in the share of food, fertilizer and export subsidies and about 0.4 point was due to increase in transfers to poverty alleviation programmes under 'Agriculture and rural development' (Table 3.11). In terms of the growth rates, per capita expenditure on fertilizer subsidy at constant prices increased at 17.5 per cent during the expansionary period and continued to grow at over 10 per cent per year even during the period of fiscal restraint (Table 3.12). Export subsidy, in per capita terms actually recorded a growth rate of 29 per cent per year during the expansionary phase due to the relatively buoyant exports during the first half

of the Eighties and although the growth rate in the next period declined, it was still high by any standard (7 per cent). Only the growth rate of food subsidy during the period of fiscal restraint was negative (-2.7 per cent). The per capita revenue expenditure (at constant prices) on agricultural and rural development too increased at a spectacular rate (40 per cent per year) due to the increased allocation to poverty alleviation programmes, particularly during the year of unprecedented drought (1987-88). This was perhaps necessary to maintain stability, even if only a part of the total allocation actually reached the beneficiaries due to leakages.<sup>5</sup>

**Table 3.11**  
**Expenditure on Economic Services**

Particulars	Per Capita Expenditure (in 1981-82 rupees)				Percentage of GDP			
	74-75	81-82	86-87	90-91	74-75	81-82	86-87	90-91
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
<b>1. Agriculture, Rural Development and Allied Activities</b>								
- Revenue	2.8	5.3	7.4	21.3	0.15	0.24	0.27	0.62
- Capital	9.8	0.5	2.6	0.9	0.50	0.02	0.09	0.03
- Total	12.6	5.8	10.0	22.1	0.65	0.26	0.36	0.65
<b>2. Industry and Minerals (Including Fertilizer Subsidy)</b>								
- Revenue	3.6	18.0	30.5	38.2	0.18	0.80	1.09	1.12
- Capital	12.6	22.0	32.3	8.4	0.65	0.97	1.15	0.25
- Total	16.2	40.0	62.8	46.6	0.83	1.77	2.24	1.37
<b>3. Fertilizer Subsidy- Revenue</b>	-	5.3	18.2	28.1	-	0.23	0.65	0.83
<b>4. Energy</b>								
- Revenue	1.1	2.6	5.1	4.9	0.06	0.17	0.18	0.14
- Capital	2.6	6.7	10.2	14.0	0.13	0.30	0.37	0.42
- Total	3.7	9.3	15.3	18.9	0.19	0.41	0.55	0.56
<b>5. Transport and Communication</b>								
- Revenue	2.0	4.5	7.2	6.3	0.10	0.20	0.25	0.18
- Capital	10.6	16.7	23.2	17.5	0.55	0.74	0.83	0.52
- Total	12.6	21.2	30.4	23.8	0.65	0.94	1.08	0.70
<b>6. Food Subsidy</b>	7.8	9.9	20.2	15.8	0.40	0.44	0.72	0.46
<b>7. Export Subsidy</b>	2.3	6.0	8.9	10.3	0.12	0.32	0.29	0.53
<b>8. Other Economic Services</b>								
- Revenue	3.6	5.0	7.6	9.5	0.18	0.23	0.27	0.28
- Capital	0.9	2.1	2.2	1.5	0.05	0.08	0.08	0.04
- Total	4.5	7.1	9.8	11.0	0.23	0.31	0.35	0.32
<b>9. Total Economic Services</b>								
- Revenue	23.3	52.4	86.0	113.9	1.20	2.32	2.06	2.35
- Capital	36.4	48.0	70.7	42.3	1.88	2.13	2.52	1.24
- Total	59.8	100.0	156.6	156.2	3.08	4.45	5.58	4.59

Source: Budget Documents of Central Governments, Ministry of Finance, Government of India.

5. For a careful evaluation of rural poverty alleviation programmes, see, Kurian (1991), Palley (1989) and also, Dreze (1990).

Table 3.12

## Growth of Per Capita Expenditure on Economic Services (1981-82 Prices)

(Per cent per year)				
Expenditure Category	1974-75 to 1981-82	1981-82 to 1986-87	1986-87 to 1990-91	1974-75 to 1990-91
(1)	(2)	(3)	(4)	(5)
1. Agriculture and Rural Development				
- Revenue	7.4	1.6	41.0*	10.0
- Capital	-27.3	36.3*	-26.4*	-5.6
- Total	17.4	12.9*	26.9*	6.2
2. Industry and Minerals (Including Fertilizer Subsidy)				
- Revenue	26.3	4.0*	7.5*	13.3
- Capital	3.2	9.3*	-29.1*	-0.9
- Total	11.3	6.6*	-6.8	6.1
3. Fertilizer Subsidy	21.9	17.5*	10.1*	17.2
4. Energy				
- Revenue	10.8	13.2	-3.0*	9.3
- Capital	18.6	8.0*	6.9	12.0
- Total	15.8	9.5*	3.9*	11.1
5. Transport and Communication				
- Revenue	11.2	8.2	3.9*	8.6
- Capital	6.6	5.8	-3.1*	4.5
- Total	7.5	6.5	-1.0*	5.6
6. Food Subsidy	1.8	12.8*	-2.7*	5.4
7. Export Subsidy	-10.6	-4.1	29.1*	7.0
8. Other Economic Services	1.1	8.2*	4.2*	4.5
9. Total - Economic Services				
- Revenue	11.3	6.1*	10.7*	9.0
- Capital	2.7	8.9*	-12.3*	2.4
- Total	6.7	7.5*	1.7*	6.1

Note: Growth rates have been estimated by employing the kinked exponential regression model.

\* denotes the growth rates are significantly different from the previous growth rates.

Source: Budget Documents of the Central Government.

The analysis of the C.S.O.'s data on economic and functional expenditure categories confirm the above findings. The high growth rate of current expenditures on economic services during the period of fiscal restraint was mainly due to the sharp increases in subsidies and transfers. The per capita expenditure on subsidies (1981-82 prices) increased at 9.4 per cent per year during the period of fiscal restraint, and this was not significantly different from the growth rate on the item recorded in the previous period. Similarly, spending on transfers increased at over 17 per cent per year throughout the 1980's. Much of this occurred by crowding out not only the capital outlay, but also the maintenance expenditures and even wages and salary

expenditures. Per capita expenditure on wages and salary declined by one per cent during the period of fiscal restraint and as the wage rates were increased significantly during this period, this represents cut back in employment. Disaggregated analysis shows that this occurred mainly in agricultural, manufacturing and transport and communication sectors.<sup>6</sup>

**Table 3.13**

**Growth of Per Capita Expenditure on Economic Services at Constant Prices**

(Per cent per year)

Expenditure Category	1974-75	1981-82	1986-87	1974-75
	to 1981-82	to 1986-87	to 1990-91	to 1990-91
(1)	(2)	(3)	(4)	(5)
1. Current expenditure				
a. Compensation to employees	0.4	11.6*	-1.0	4.9
b. Net government maintenance	3.0	11.4*	-1.9*	5.9
c. Subsidy	7.2	12.8*	9.4	9.8
d. Other transfer payments	1.3	17.7*	17.4	9.9
Total - 1 - Current expenditure	5.7	13.18	8.5*	9.1
2. Capital expenditure				
a. Gross capital formation	-14.3	20.2*	-6.8*	0.1
b. Financial outlay	3.2	7.4*	-15.6	2.5
c. Capital transfers and advances	-3.0	4.9*	1.6*	0.9
Total - 2 - Capital expenditure	0.4	9.6*	1.4*	4.3

*Note:* Growth rates have been estimated by the kinked exponential regression model.  
\* denotes that the growth rate is significantly different from the previous period.

*Source:* C.S.O. - Ministry of Planning, Government of India.

As already mentioned, growth rate of capital expenditure increased at a rate faster than the growth of GDP during the expansionary phase in almost all the activities under economic services. However, during the next period, the capital expenditure-GDP ratio in economic services declined from 2.5 per cent in 1986-87 to 1.2 per cent in 1990-91 (Table 3.11). The decline was particularly sharp in the socially productive infrastructural sectors like transport and communication (0.3 point) and promotional activities like industry and minerals (0.9 point). In terms of growth rates, per capita (Table 3.12) capital expenditures at constant prices declined sharply during the period of fiscal restraint in the case of agriculture and rural development (-26 per cent), industry and minerals (-29 per cent) and transport and communication (-3 per cent), thus reducing aggregate per capita capital expenditure on economic services even in absolute terms (-12 per cent). Interestingly, even during this period, the growth of per capita capital

6. The growth rate during 1986-87 to 1989-90 in agricultural sector was 0.3 per cent, in manufacturing -4.5 per cent and in transport and communication -7 per cent.

expenditure on energy continued to register a reasonably high rate (6.9 per cent). This partly offset the declining investments in the energy sector at the State level. Given that electricity is not only a major input to both industry and agriculture but also an essential item of household consumption by the urban consumers, the attempt to maintain the overall investment rate in this sector is not very surprising.

### **3.6 The Structural Adjustment Programme and Fiscal Compression**

As a consequence of the outpacing of the rate of growth of revenues by the revenue expenditure growth throughout the 1980s, the revenue deficit which first emerged in 1982-83 increased rapidly to reach over 3 per cent of GDP by 1990-91.<sup>7</sup> The increasing resort to borrowed funds to meet not only the capital expenditure needs but also a growing component of current expenditures eventually resulted in a vicious spiral of growing deficits, increasing debt, rising interest costs and further expansion of the deficit. Consequently, the fiscal deficit of the Centre and the States reached about 10.3 per cent of GDP in 1990-91.

The large and growing fiscal imbalance has been a major source of severe macroeconomic and balance of payment imbalances. To meet consumption and capital expenditure needs of the government and to finance inefficient and unviable public enterprises the government resorted to heavy borrowing to unsustainable levels.<sup>8</sup> The preemption of sizeable volume of household savings for government consumption and investment has tended to push up interest rates including the administered rates. As the growth of productive capacity did not keep pace with the growth of aggregate demand, a portion of the increase in demand spilled over into increase in imports, thus expanding the trade deficit, and aggravating balance of payments problem. At the same time inadequate investments in infrastructural sectors created severe supply bottlenecks. All these factors combined to create a stagflationary situation towards the end of 1980s. The problem was further compounded by indiscriminate external commercial borrowing. A crisis of unprecedented proportions was reached when the oil prices doubled in August, 1990, following Iraq's invasion of Kuwait. The fear of defaulting loan repayments loomed large as the foreign exchange reserves fell to an abysmally low level, barely enough to meet two weeks' imports. With foreign exchange inflows inadequate to service and repay the external commercial loans, and the institutional lenders refusing to roll over the credit, India was forced to seek the stand-by arrangement with the IMF and to undergo the stabilisation and structural adjustment programme in August, 1991.

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7. The revenue deficit first emerged at the Centre in 1979-80 and for the Centre and States taken together, in 1982-83.

8. Some recent studies have shown that the present path of public debt is unsustainable. See, Chelliah (1992), Buitter and Patel (1990) and also, Rangarajan, Basu and Jadhav (1989).

A major component of the adjustment programme was fiscal compression. The Memorandum of Economic Policies accompanying the request for stand-by arrangement to the International Monetary Fund specified that adjustments will be undertaken in key parameters including substantial reduction in the proportion of fiscal deficit to GDP. Thus, the economy passed on from a period of fiscal restraint (1986-87 to 1990-91) to that of fiscal contraction (1990-91 to 1993-94).

As per the programme of adjustment, the fiscal deficits were to be reduced from 8.4 per cent in 1990-91 to 6 per cent in 1991-92 and further to 5.3 per cent in 1992-93. The budgeted deficits for 1993-94 is estimated at 4.7 per cent of GDP (Table 3.14). In this section, we analyse the nature of Government expenditure compression undertaken at the Central government level since 1990-91.

**Table 3.14**

**Central Government Revenues, Expenditures and Deficits  
as Percentages of GDP: 1990-91 to 1993-94**

(per cent of GDP)

	1990-91 (Actual)	1991-92 (BE)	1991-92 (Actual)	1992-93 (BE)	1992-93 (RE)	1993-94 (BE)
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1. Revenue expenditure	13.9	13.3	13.5	12.9	13.7	12.9
2. Capital expenditure	6.0	5.3	4.8	4.2	4.3	3.7
3. Total expenditure	19.9	18.6	18.3	17.1	18.0	16.6
4. Revenue receipt	10.4	11.1	10.8	10.9	11.3	10.6
5. Capital receipt	1.1	1.3	1.5	1.3	1.4	1.3
5.1 Of which disinvestment	-	0.4	0.5	0.4	0.5	0.4
6. Total receipt	11.5	12.4	12.3	12.2	12.7	11.9
7. Revenue deficit	3.5	2.3	2.7	2.0	2.4	2.2
8. Fiscal deficit	8.4	6.2	6.0	5.0	5.3	4.7

*Note:* BE = Budget estimates  
RE = Revised estimates

*Source:*

1. Budget Documents of Central Government, 1982-93 and 1993-94.
2. Central Statistical Organisation, Ministry of Planning, Government of India.

The manner of phasing out of fiscal imbalances while operating under the IMF conditionality provides ample testimony to the influence of special interest groups in determining fiscal decisions. At the outset, from the point of view of reducing inflationary potential in the economy, phasing out of governmental dissaving by cutting back unproductive spending, and reducing revenue deficit should have received greater attention.<sup>9</sup> Yet, emphasis

9. Rakshit (1991) for example suggests, ".....neither empirical evidence nor economic logic suggests that reduction of fiscal deficit should be the prime concern of the government in the process of macroeconomic management.

was given to reducing fiscal deficit because it gave greater degree of freedom to the government to fulfill the conditionality. Thus, the government could fulfill the commitment to the IMF, not by reducing outlay on wages and salaries, subsidies and other transfer payments, but by cutting down capital expenditures on infrastructures, reducing transfers to State governments, selling public sector equity and transferring the surpluses of government enterprises, which could otherwise have been reinvested. Emphasising fiscal deficit reduction gave the Finance Ministry sufficient flexibility in fulfilling the stipulated targets without reducing the benefits going to dominant coalitions.

How was the reduction in fiscal deficit in fact achieved in the Indian context? Table 3.14 summarises the contribution of various elements to fiscal deficit reduction in the years after 1990-91. Of the 2.4 percentage point reduction in fiscal deficit-GDP share in 1991-92 over 1990-91, 1.6 points (or two-thirds) were due to compression in expenditure and 0.8 point was due to higher revenues. Of the increase in revenues as much as 0.7 points or about 87 per cent accrued from one time measures like disinvestment in public sector equity (0.5 points) and recovery of arrears of royalty on off-shore crude (0.2 points) which imposed virtually no visible burden on any special interest groups. There was hardly any attempt to raise the tax ratio or effect higher cost recoveries from various social and economic services provided, although the scope for raising such non-tax revenue is acknowledged to be very large (Mundle and Rao, 1991). Similarly, in the second year (1992-93), disinvestment in public sector equity, appropriation of RBI profits (Rs 350 crore) and additional dividends from railways (Rs 420 crore) provided additional revenues. The tax revenue increases were expected to be higher by 0.2 percentage point of GDP, but more recent estimates show that these optimistic estimates have not been realised.<sup>10</sup> Of course, even during this period of fiscal crisis, virtually no attempt was made to enhance user charges and cost recoveries from public services.

The compression in expenditures was the main means to achieve fiscal adjustment. Indeed, in the first year (1991-92), the government could achieve the budgeted target of compressing expenditure by 1.6 percentage points. In the second year (1991-92), however, though the government intended to reduce the share of government expenditure in GDP by over one percentage point as shown in the difference between actual of 1991-92 and budget estimates of 1992-93, it could hardly achieve any economy and the revised estimate of 1992-93 was almost at the same level as the actuals of the previous year.

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10. Das-Gupta and Mookherjee (1993) argue that the revised estimates of tax revenue are optimistic. The implicit buoyancies of tax revenue particularly excise duties and corporate income taxes are overestimates. The newspaper reports did confirm the fact that the estimated revenues were not realised. The latest estimates of collections of income and corporation taxes in 1992-93 were Rs.16,600 crore, which shows a shortfall of Rs.900 crore from the revised estimates for the year.

Our analysis of expenditure compression demonstrates the influence of interest groups in expenditure even more clearly. Of the 1.6 percentage points reduction in the total expenditure-GDP share (Table 3.14) in the first year, reduction in revenue expenditure was a mere 0.4 points and compression in capital expenditure amounted to 1.2 points or 75 per cent. Similarly, in the next year (1991-92) reduction in total expenditure-GDP share was just 0.3 per cent, but capital expenditure had to be compressed by 0.5 points to achieve this because, revenue expenditure share rather than showing a decline, actually increased by 0.2 per cent. Thus, it was found to be easy to compress capital expenditures in spite of the adverse effects on infrastructural facilities and the expenditures on quasi-public goods, and those like emoluments of Government employees, subsidies and transfers were not reduced.

It may be clearly seen from Table 3.15 that over 75 per cent of fiscal compression in the first year was achieved by reducing capital expenditures. Quite a good proportion of this (0.5 points) was by reducing non-plan loans and advances to States. The Plan capital expenditure-GDP ratio was reduced by 0.3 percentage points in the first year and by another 0.2 point in the second year. The compression in plan expenditure in the first year was severe in the case of economic services (0.5 points) including assistance to poverty alleviation programmes under rural development (0.13 per cent) and budgetary support to public sector enterprises (0.29 points) mainly in sectors such as power (0.14 points) coal (0.06 points) and railways (0.02 points). Thus, the Central Government found it easy to reduce expenditures on these infrastructural sectors and on those intended to provide safety net to the vulnerable sections like poverty alleviation schemes even at the time of structural adjustment, but not expenditures on those activities directly benefiting the dominant interest groups like spending on wages and salaries in administrative departments and subsidies and transfers.

Equally notable was the inability of the Government to carry out even the small degree of compression in revenue expenditures intended in the budget estimates (Table 3.16). In the first year, the non-plan revenue expenditure as a ratio of GDP was budgeted to be reduced by one percentage point, but in actual practice, the Government could reduce it by only 0.5 point. Similarly, total revenue expenditure was to be reduced by 0.5 percentage point in 1991-92 over the previous year, but the actual reduction was just by 0.3 point. Again, in 1992-93, the budgeted reduction in non-plan revenue expenditure was 0.7 point (as compared to 1991-92 actual), but the revised estimates for the year show a reduction of only 0.3 point in the case of non-plan revenue expenditures and in the case of total revenue expenditure, the revised estimate of 1992-93 was actually higher than the actuals of 1991-92. Thus, in the second year, rather than achieving reduction in the ratio of revenue expenditure to GDP, there was actually an increase!

The details of non-plan expenditures presented in Table 3.16 show that the share of interest payments in GDP continued to increase, the shares of defence and other direct expenditures on general, social and economic services remained broadly constant and the shares of grants to States and subsidies showed some decline. But interestingly, among the subsidies,

**Table 3.15****Compression in Expenditure as a Percentage of GDP: 1990-91 to 1993-94**

(Per cent per year)

Expenditure Item	1990-91 Actual	1991-92 B.E.	1991-92. Actual	1992-93 B.E.	1992-93 R.E.	1993-94 B.E.
(1)	(2)	(3)	(4)	(5)	(6)	(7)
Revenue expenditure	13.8	13.3	13.5	12.9	13.7	12.9
<b>I. Non-plan revenue expenditure</b>						
a. Interest payments	4.0	4.6	4.4	4.6	4.7	4.8
b. Defence	2.0	1.8	1.9	1.7	1.8	1.7
c. Subsidies including debt relief to farmer	2.3	1.7	2.0	1.5	1.7	1.1
d. Grants to States/Union Territories	0.8	0.4	0.6	0.4	0.4	0.3
e. Others -						
(i) General services	1.3	1.1	1.1	1.1	1.2	1.1
(ii) Social services	0.3	0.3	0.3	0.3	0.3	0.3
(iii) Economic services	0.5	0.4	0.4	0.4	0.4	0.3
(iv) Postal services	0.0	0.0	0.0	0.0	0.0	0.0
(v) Grants to foreign governments	0.0	0.0	0.0	0.0	0.0	0.0
(vi) Expenditure on Union Territories without legislature	0.2	0.2	0.2	0.2	0.2	0.2
Total Non-plan revenue expenditure	11.5	10.5	11.0	10.3	10.7	9.8
<b>II. Plan revenue expenditure</b>						
a. Central plan (Budget support)	1.6	1.7	1.5	1.5	1.7	1.9
(i) Economic services						
(ii) Social services						
(iii) General services						
b. Central Assistance for State/Union Territories Plan	0.8	1.1	1.0	1.2	1.3	1.2
<b>III. Capital expenditure (including loans)</b>	6.0	5.3	4.8	4.2	4.3	3.7
a. Non-plan, of which	3.0	2.5	2.2	1.9	1.9	1.6
*loans and advances to States/	1.4	1.1	0.9	0.8	0.7	0.6
b. Plan, of which	3.0	2.7	2.6	2.3	2.4	2.2
Central capital assistance to States/Union Territories	1.2	1.4	1.3	1.2	1.2	1.1
<b>IV. Total expenditure</b>	19.8	18.6	18.3	17.1	18.0	16.6
a. Total plan expenditure	5.3	5.5	5.1	5.0	5.3	5.2
b. Total non-plan expenditure	14.5	13.1	13.2	12.2	12.6	11.4

Note: BE = Budget estimates  
RE = Revised estimates

Source: \* Central Budget Documents: 1992-93 and 1993-94 Expenditure Vol. 1

significant decline was seen only in export subsidies, and food and fertilizer subsidies continued to be as important as they were before the adjustment programme. The reduction in export subsidies was attributable to the reform in the exchange rate regime and not related to expenditure policy *per se*; it must also be noted that the attempts to reduce food (excluding the consumer subsidy involved) and fertilizer subsidies have not met with much success. Even as attempts were made to reduce fertilizer subsidies in the budgets, the subsequent pressure from the farm lobby did not allow the subsidy to be reduced.

**Table 3.16**  
**Non-Plan Expenditures Compression 1990-91 to 1993-94**

		Percentage of Non-Plan Expenditure to GDP				1990-91	1991-92	1992-93
		1990-91	1991-92	1992-93	1993-94	minus 1991-92	minus 1992-93	1992-93 (RE) minus 1993-94 (BE)
				(RE)	(BE)		(RE)	
1.	Defence	2.05	1.88	1.78	1.73	0.17	0.10	0.05
2.	Subsidies							
	(i) Food Subsidy	0.46	0.47	0.40	0.38	-0.01	0.06	0.02
	(ii) Fertilizer (Indigenous)	0.70	0.57	0.69	0.38	0.13	-0.12	0.31
	Fertilizer (Imported)	0.12	0.21	0.14	0.06	-0.09	0.07	0.08
	Fertilizer (Small/Marginal Farmers)	0.00	0.07	0.00	0.00	-0.07	0.07	0.00
	Total Fertilizer Subsidy	0.83	0.85	0.83	0.44	-0.03	0.02	0.39
	(iii) Export Promotion etc.	0.52	0.29	0.13	0.06	0.23	0.16	0.06
	(iv) Debt Relief to Farmers	0.28	0.23	0.22	0.06	0.05	0.02	0.15
	(v) Other Subsidies	0.20	0.17	0.16	0.11	0.03	0.01	0.05
	Total Subsidies	2.29	2.01	1.74	1.06	0.28	0.27	0.69
3.	Grants to States and UT's	0.75	0.64	0.39	0.28	0.11	0.25	0.10
4.	Non-Plan Loans and Advances to States and UT's, of which	1.43	0.91	0.70	0.56	0.53	0.21	0.14
	States Share of Small Savings	1.33	0.90	0.63	0.57	0.43	0.27	0.07
5.	Non-Plan Loans to PSU's	0.20	0.12	0.09	0.09	0.08	0.04	-0.00
6.	Assistance to Foreign Governments							
	(a) Grants	0.03	0.02	0.02	0.02	0.00	0.00	0.00
	(b) Loans	0.32	0.19	0.08	0.01	0.14	0.10	0.07

Source: 1. Budget Documents of the Central Government 1992-93 and 1993-94.  
2. Central Statistical Organisation, Ministry of Planning, Government of India.

## CHAPTER IV

### ANALYSIS OF GOVERNMENT EXPENDITURE: STATES

#### 4.1 Introduction

In the Indian federal polity, the Constitution assigns the responsibility of providing important social and economic services to the State governments. In 1990-91, the States spent about 54 per cent of total expenditures incurred; their share in government expenditure on social services was close to 85 per cent and in the case of economic infrastructure, about 55 per cent. Besides ensuring law and order and providing social and economic infrastructure, the States have an important role in ameliorating the condition of the poor as well.

For a number of reasons, the study of State government expenditures from a public choice perspective is important. It has been suggested that fiscal decentralisation exerts a significant effect on the level of public expenditures, though the direction of the bias is not clear. According to Brennan and Buchanan (1980), decentralisation can act as an effective mechanism to control the 'Leviathan's' expansionary tendencies, as inter-jurisdictional competition and mobility of people across jurisdictions 'shopping' for their optimal tax-expenditure combination prevents a bloated government sector by requiring efficiency, i. e., least cost provision of all services, in the government sector. However, empirical studies did not support this hypothesis (Oates, 1985). On the contrary, Olson (1982) suggests that the special interest groups wield greater influence at sub-central levels causing overexpansion of the Government budget. Also, significant proportions of States' expenditures are financed from inter-governmental transfers and the consequent delinking of revenue raising and expenditure decisions can create misperceptions about the true marginal cost of funds, resulting in more than optimal supply of public services.<sup>1</sup>

There are also other reasons why the study of State government expenditure is important. The lack of independent powers to borrow from the market and limitations on overdrafts from the Reserve Bank of India restrict the States' manoeuvrability in raising resources. As the option of more borrowing is ruled out, the only alternative left to the States is to raise its own revenue receipts or to reduce spending. The special interest groups, particularly rich farmers, make it difficult to raise revenues through direct taxes on the agricultural sector, although the Constitution empowers the States to levy agricultural income tax and land revenue. Similarly, it has not been possible to collect user charges at rates that would cover the costs of publicly

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1. This phenomenon is widely known as the "flypaper effect" in the fiscal federalism literature. It is generally observed that the expenditure-inducing effect of lump-sum grants is greater than the effect of lump-sum transfers to individuals or increases in per capita incomes, though both are supposed to have an equivalent effect. For a detailed analysis of the flypaper effect, see Mieszkowsky and Oakland (1980).

provided goods and services even as we know that the benefits of the resultant subsidies have accrued mainly to better-off regions and individuals (Rao and Mundle, 1993). At the same time, as the government employees have been able to secure wage revisions disproportionate to increases in prices and general productivity in the economy, there has been a significant cost escalation in the important services provided by the States which are labour-intensive. Further, an overwhelming proportion of the services provided at the State level are 'quasi-public' and 'merit' goods, or simply transfer payments. As the benefits of these services can be appropriated by individuals, the special interest groups can organise themselves to influence public spending policies in favour of services beneficial to them and work out strategies to gain better access to these services. Unlike in the case of the Central government, resources cannot be raised by incurring deficits at the State level. Given the above constraints on receipts, increases in spending on the quasi-public and merit goods, *ceteris paribus*, can be achieved only by displacing socially productive expenditures on capital formation and maintenance of the capital stock.

In this chapter, we attempt to analyse the trends in State expenditures in 14 selected States, leaving out the 10 'Special category' States<sup>2</sup> and the small State of Goa formed only in 1987. This has been done to ensure comparability of data over time and for the sake of generality in the broad conclusions drawn. It may be noted that the 14 selected States cover 94.6 per cent of the total population in the country according to the 1991 census, and account for 90.8 per cent of revenue expenditures and almost 90 per cent of total expenditures in 1990-91.

## **4.2 Broad Trends**

Over the period 1974-75 to 1990-91, total expenditures of the 14 selected States at current prices grew at an average annual rate of 16 per cent. With capital disbursements growing at a little above 12 per cent and revenue expenditures growing at 17 per cent, a plot of nominal expenditures shows fairly smooth curves (Figure 4.1). However, when we consider per capita expenditures in constant prices (Figure 4.2), certain kinks are noticeable. Given that the nominal expenditures show a steady increase, the fluctuations seen in the expenditure trends are essentially due to fluctuations in the wholesale price index that has been used for deflating government expenditures. *Prima facie*, this lends credence to the concept of "incremental budgeting" defined in *nominal terms*, since the smooth curves seen in Figure 4.1 imply a fairly constant rate of growth.

Our analysis of State government expenditure shows that it does not follow the time pattern observed in the case of aggregate as well as Central government expenditures. In fact, the public expenditure in the States increased at a fast clip in the latter half of the Seventies, but there was a deceleration in the last decade whereas, in the case of the Central and aggregate

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2. This term is used by the Planning Commission to denote the States of Arunachal Pradesh, Assam, Himachal Pradesh, Jammu & Kashmir, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim and Tripura.

Figure 4.1

## Growth of Govt. Expenditure 14 Selected States (combined)

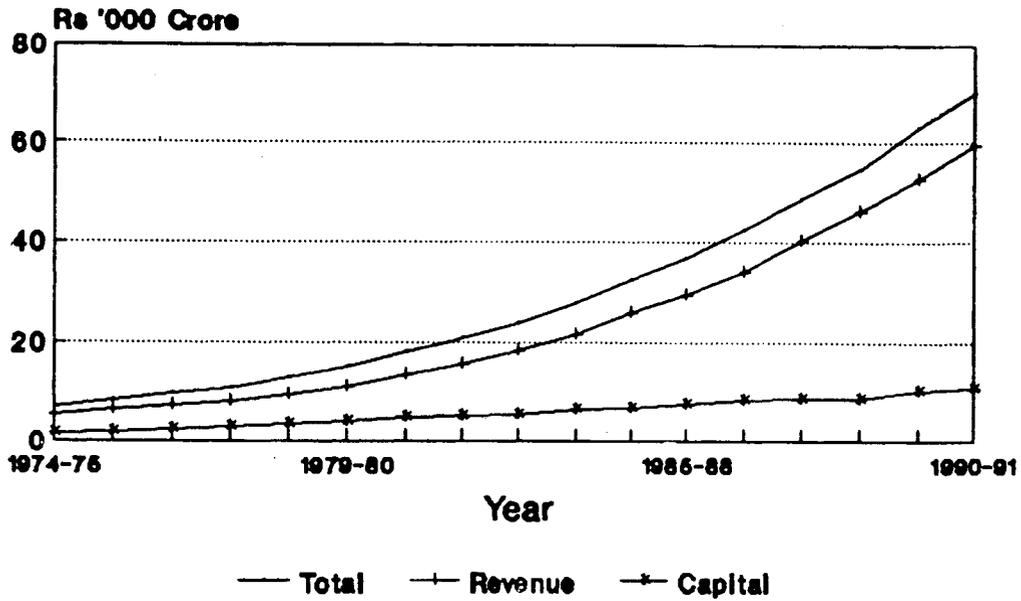
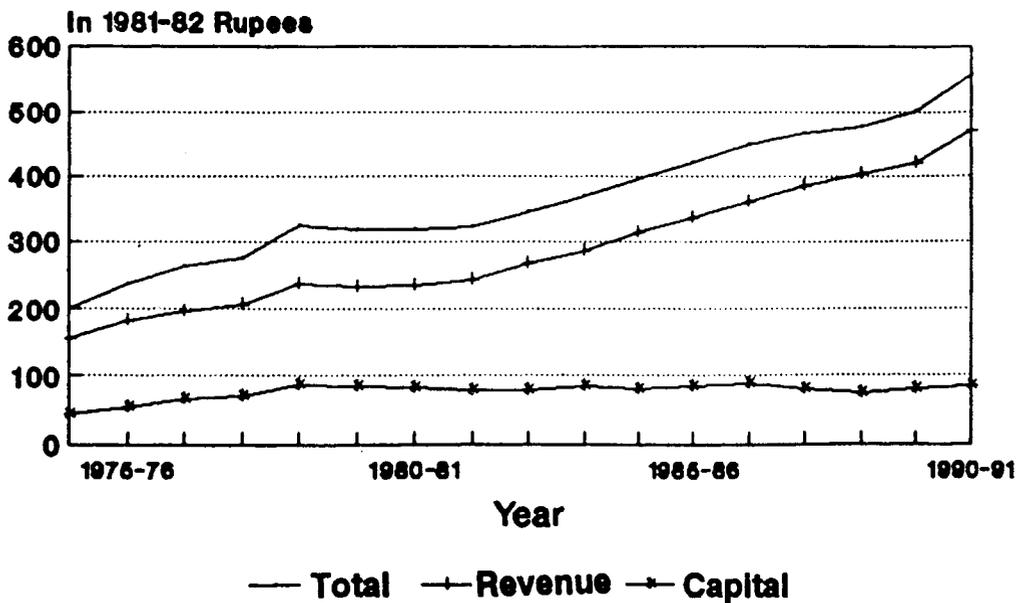


Figure 4.2

## Per Capita Govt. Expenditure 14 Selected States (combined)



government expenditures, there was a significant fiscal expansion during 1981-82 to 1986-87. In the case of the States, the ratio of government expenditures to State Domestic Product (SDP) showed a phenomenal increase of over 6 percentage points from 12.8 per cent in 1974-75 to 19 per cent in 1980-81, but registered only a marginal increase thereafter to reach 21.5 per cent in 1990-91 (Table 4.1). Thus, as far as the States are concerned, it appears that the entire decade of the Eighties was a period of fiscal restraint.

**Table 4.1**  
**Government Expenditures as a Ratio of SDP**  
**14 Selected States (combined)**

Year	Percentage of Expenditure to SDP			Share of capital exp. in total (per cent)
	Revenue	Capital	Total	
1974-75	10.0	2.8	12.8	21.8
1980-81	14.1	4.9	19.0	26.0
1985-86	16.9	4.2	21.2	20.1
1986-87	17.9	4.4	22.3	19.5
1987-88	18.5	3.9	22.4	17.5
1988-89	17.6	3.2	20.8	15.4
1989-90	17.6	3.4	20.9	16.0
1990-91*	18.2	3.3	21.5	15.2

\* Excludes Bihar as detailed information is not available.

The above finding comes out clearly when we consider the growth of per capita State expenditures at constant prices (Table 4.2). The computed growth rates show that the per capita total expenditure of the States continued to grow steadily throughout the 17 year period. However, capital expenditures stagnated during the Eighties. Figure 4.2 shows that the growth in per capita capital disbursements was actually halted after 1978-79. The revenue expenditure, on the other hand, continued to increase steadily at a high rate and given its predominance in total expenditures, the steady growth in the latter too should only be expected.

**Table 4.2**

**Growth of Government Expenditures (in 1981-82 prices): All Selected States  
(By Functional Categories)**

(per cent per year)

	Revenue Expenditure			Capital Expenditure			Total Expenditure		
	1974-75 to 1981-82	1981-82 to 1990-91	1974-75 to 1981-82	1974-75 to 1981-82	1981-82 to 1990-91	1974-75 to 1990-91	1974-75 to 1981-82	1981-82 to 1990-91	1974-75 to 1990-91
Administrative Services	3.5	8.0	6.1	11.3	2.8	6.2	3.7	7.9	6.2
Interest Payments	3.6	11.7	8.3	-	-	-	3.6	11.7	8.3
Social Services	6.0	6.4	6.3	9.0	-2.7	5.6	6.2	6.3	6.2
Economic Services	8.0	5.3	6.4	6.2	-0.3	2.3	7.3	3.6	5.1
Net Loans and Advances	-	-	-	8.9	-3.1	1.7	8.9	-3.1	1.7
Total Expenditures	6.0	6.8	6.5	7.6	-1.2	2.3	6.3	5.2	5.6

The different pattern of States' expenditure growth from that of the Centre analysed in the previous chapter calls for some explanation. To begin with, a significant increase in tax devolution consequent to the implementation of the Seventh Finance Commission's recommendations<sup>3</sup> improved their resource position in the early Eighties, enabling the expenditures to grow at a faster rate than that was seen in previous years. The pressure to increase expenditures on quasi-public goods, subsidies and transfers continued to persist following the high expenditure growth at the Central level. This was also aided by the proliferation of Centrally Sponsored Schemes in the early Eighties. But the growth in the

3. The recommendation raising the States' share of Union excise duties from 20 to 40 per cent, implemented since 1979-80 is probably the most important in this context.

revenue receipts of the States was not really adequate to support the spurt in expenditures, and by 1984-85 a deficit appeared in the revenue account of all the 14 States taken together (Figure 4.3). An examination of the Statewise figures also confirms the change (Table 4.3) in the overall situation under the revenue account (which contains practically all the non-debt receipts of the States). The States tried to soften the constraint to some extent by borrowing from institutional

**Table 4.3**  
**Revenue Surplus(+)/Deficit(-) in the Selected States**

(Rs. crore)

States\Year	Average 1974-80	Average 1980-85	Average 1985-91
<b>High Income States</b>	<b>303</b>	<b>153</b>	<b>-762</b>
Gujarat	55	90	-326
Haryana	44	19	-10
Maharashtra	150	6	-215
Punjab	55	38	-211
<b>Middle Income States</b>	<b>170</b>	<b>-118</b>	<b>-1155</b>
Andhra Pradesh	68	-70	-318
Karnataka	58	51	-73
Kerala	23	3	-219
Tamil Nadu	27	94	-213
West Bengal	-6	-196	-332
<b>Low Income States #</b>	<b>401</b>	<b>183</b>	<b>-684</b>
Bihar *	114	-10	54
Madhya Pradesh	121	128	10
Orissa	16	11	-20
Rajasthan	8	-19	-216
Uttar Pradesh	142	73	-503
<b>All Major States #</b>	<b>874</b>	<b>218</b>	<b>-2601</b>

\* Due to lack of reliable figures for 1990-91, the last column actually refers to average for the period 1985-90.

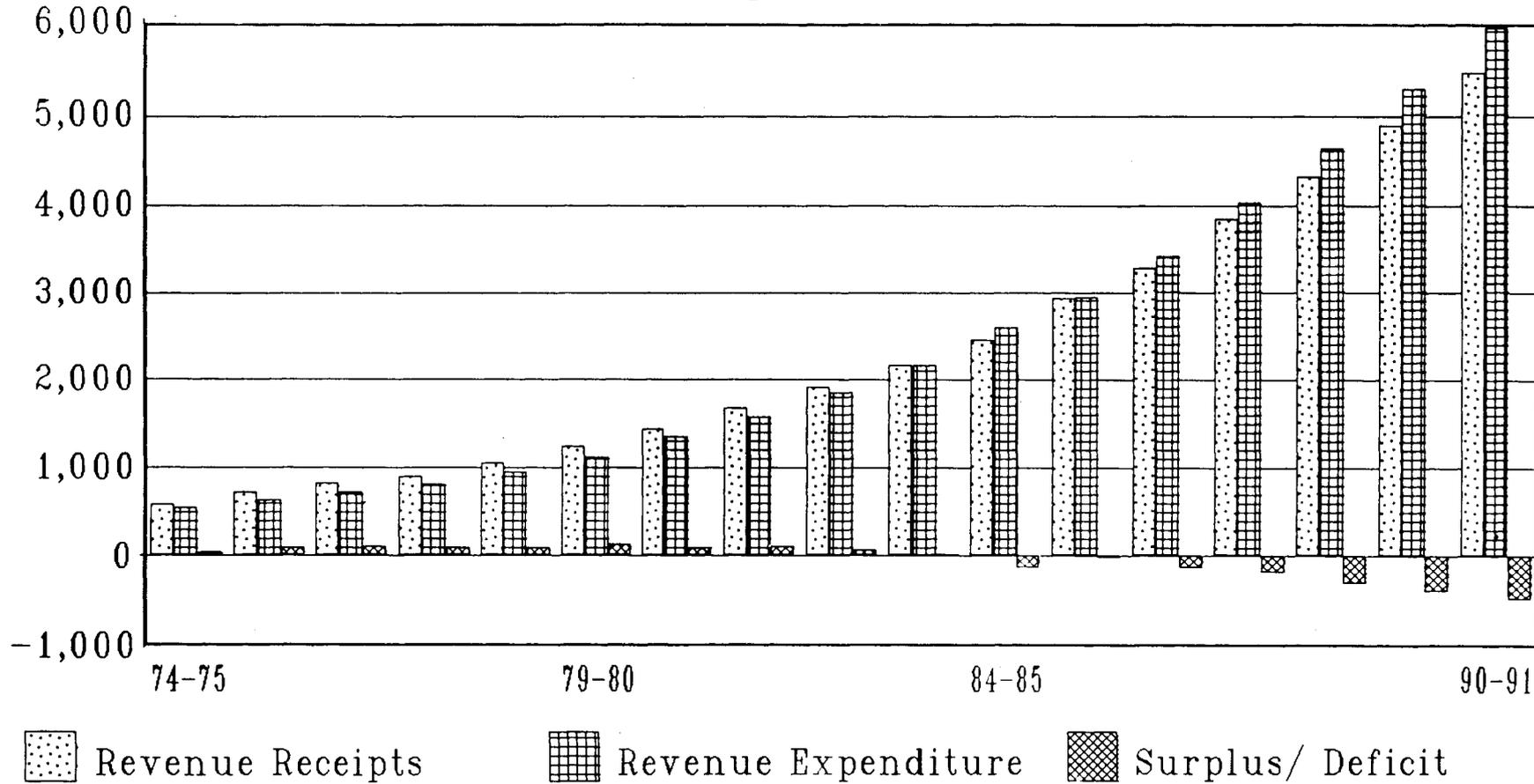
# Figures in the last column exclude the figure for Bihar for the year 1990-91.

financial agencies for specific programmes, but the amount that could be obtained thus was limited. However, with expenditures on wages and salaries, interest payments, subsidies and transfers and on Centrally Sponsored Schemes being considered as of 'committed' nature, and with the resources not keeping pace with burgeoning expenditures, increase in revenue expenditure had to be achieved by compressing capital spendings. Thus, deceleration in capital

Figure 4.3

# Revenue Account of 14 Selected States

(In current prices: Rs. billion)



expenditure started from 1981-82 itself and after the overdraft regulation scheme was introduced, the hardening of the budget constraint caused a decline in per capita capital expenditures even in absolute terms, particularly after 1986-87.<sup>4</sup> Thus, during the decade of the Eighties, while the revenue and aggregate expenditure of the States continued to grow at high rates of over 6 and 5 per cent respectively, capital expenditures actually declined (See Table 4.2). As a result, the share of capital expenditures in total expenditures declined from 26 per cent in 1980-81 to 15 per cent in 1990-91. Surely, capital expenditures got a residuary treatment.<sup>5</sup>

An examination of the expenditures of the 14 selected States classified by economic categories brings out a few notable features.

i. A major source of acceleration in the growth of revenue/current expenditure was the increase in wages and salaries. Although the overall growth rate of wages and salaries in per capita terms was almost the same as for total expenditures, it was about 5 per cent per year during the Seventies, which accelerated to 7.2 per cent during the decade of the Eighties (Table 4.4). In other words, the total expenditure on wages and salaries in constant prices increased at about 10 per cent per year and given that the net employment increased at about 3 per cent per year during the decade, the salary per employee increased at about 7 per cent per year and this was about twice the rate of growth recorded in per capita income. It must also be mentioned that the wages and salary expenditure does not include various perquisites to the employees which also seems to have grown over the years. This clearly reflects the oligopolistic strength of the employees' organizations in securing a share of the community output in their favour disproportionate to their contribution to the community output.

Since both wages and salaries and total expenditures grew at almost the same rate over the entire period, the share of the former in the latter does not show much change. But disaggregated data do show variations between States (Table 4.5). The shares seem to be inversely related to per capita SDP as the figures for high, middle and low income States show. Further, the share seems to be growing only in low income States. The highest share during the period 1985-90 was observed in Madhya Pradesh (46 per cent), and the lowest (18 per cent) in Gujarat. During the same period, the share of wages and salaries was relatively high in Kerala (41 per cent) and Bihar (40 per cent) as well, while in Maharashtra the share was almost as low as in Gujarat.

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4. When the overdraft regulation scheme was introduced in January, 1985 the Government of India gave a loan to clear the overdrafts and this improved their financial position temporarily. Thus, the scheme can be said to have hardened the budget constraint of the States from 1986-87 i.e. after two years.

5. A similar trend was seen in the case of expenditure classified by economic categories. The growth of per capita current expenditure accelerated from 5.8 per cent in the Seventies to 6.2 per cent in the Eighties. At the same time, the growth rate of capital expenditure decelerated from 8.4 per cent in the Seventies to 1.5 per cent in the Eighties.

**Table 4.4**  
**Growth of Per Capita State Government Expenditures**  
**by Economic Categories**  
**(Constant Prices)**

(Per cent per year)

	1974-75 to 1981-82	1981-82 to 1989-90	1974-75 to 1989-90
1. Consumption Expenditures			
a. Compensation to Employees	5.86	7.37	6.32
b. Net Government Maintenance	8.39	2.72	5.25
Total	5.88	6.22	6.86
2. Transfers			
a. Subsidies	34.70	6.02	18.16
b. Transfer to Local Bodies	1.71	7.43	4.80
c. Other Transfers	6.70	8.48	7.67
Total	7.69	8.35	8.85
3. Total Current (1+2)	6.38	7.15	6.89
4. Gross Fixed Capital Formation	9.25	4.55	6.65
5. Financial Outlay	3.01	4.84	4.01
6. Total Capital Transfers and Advances			
a. Local Bodies	9.68	1.95	5.38
b. Others	8.78	-2.06	2.71
Total	8.76	-1.20	3.19
7. Total Capital Expenditure (4+5+6)	8.35	1.49	4.54
8. Total Expenditure (3+7)	7.09	5.46	6.20

ii. Subsidies and transfers too increased at a phenomenal rate of about 8 per cent per year in per capita terms throughout the sixteen year period (Table 4.4) and during the Eighties the growth was 8.4 per cent. The share of subsidies in total expenditure in the case of all selected States together rose from 4 per cent during 1974-80 to 8 per cent during 1985-90. The same trend was seen in varying degrees in all the States, though it was most evident in Tamil Nadu, where the share rose by over 300 per cent from 3 per cent to 13 per cent. The sharp increases in expenditures must be attributed to the fast increases in implicit subsidies arising from pure losses in irrigation and other

**Table 4.5**  
**Share of Economic Categories in Total Expenditure**  
**(Annual Average for the Period)**

(Per cent)

State	Wages and Salaries			Net Govt. Maintenance			Subsidy			Tot Transfer (Rev+Cap)			Capital Expenditure			Loans and Advances		
	74-80	80-85	85-90	74-80	80-85	85-90	74-80	80-85	85-90	74-80	80-85	85-90	74-80	80-85	85-90	74-80	80-85	85-90
<b>High Income States</b>	<b>24.5</b>	<b>23.0</b>	<b>23.7</b>	<b>6.4</b>	<b>7.8</b>	<b>7.3</b>	<b>4.0</b>	<b>7.8</b>	<b>9.0</b>	<b>32.5</b>	<b>31.9</b>	<b>34.1</b>	<b>12.2</b>	<b>12.6</b>	<b>12.1</b>	<b>20.4</b>	<b>16.9</b>	<b>13.8</b>
Punjab	39.1	38.8	34.5	5.0	6.6	7.7	3.7	6.0	5.3	12.9	11.7	16.0	16.2	10.9	8.1	23.2	26.1	28.5
Haryana	37.6	35.0	37.4	8.8	7.8	9.0	6.4	9.8	9.9	11.5	16.0	20.0	13.4	13.7	7.5	22.3	17.7	16.3
Maharashtra	20.2	18.7	19.8	6.6	7.9	5.9	3.9	9.5	9.5	38.7	36.4	40.2	10.3	14.1	14.8	20.3	13.4	9.8
Gujarat	18.3	16.7	18.3	6.0	8.4	8.8	3.5	5.0	10.2	41.7	42.0	40.6	12.5	10.3	11.7	18.0	17.5	10.4
<b>Middle Income States</b>	<b>30.1</b>	<b>28.3</b>	<b>30.1</b>	<b>10.9</b>	<b>10.4</b>	<b>8.4</b>	<b>4.2</b>	<b>6.8</b>	<b>8.9</b>	<b>28.8</b>	<b>31.4</b>	<b>34.5</b>	<b>11.4</b>	<b>10.5</b>	<b>8.5</b>	<b>14.7</b>	<b>12.7</b>	<b>9.6</b>
Karnataka	38.3	35.0	28.0	9.0	7.6	4.8	5.5	8.7	9.1	16.5	19.4	37.1	14.8	14.5	8.5	15.9	14.7	12.6
West Bengal	25.7	25.1	26.8	14.9	11.5	9.9	2.6	4.4	3.9	31.3	37.8	39.9	10.1	9.5	11.0	15.4	11.8	8.4
Andhra Pradesh	26.3	26.9	25.5	10.4	10.8	8.9	6.7	11.0	12.1	33.4	37.1	39.2	11.4	7.9	8.1	11.8	6.3	6.1
Tamil Nadu	27.7	22.6	33.3	9.5	10.9	8.4	3.0	5.6	12.7	30.4	30.1	25.7	10.2	9.5	5.6	19.2	21.3	14.2
Kerala	38.6	39.4	41.3	9.4	10.3	10.1	2.7	3.1	3.2	29.3	29.6	29.7	11.7	13.2	10.6	8.3	4.5	5.2
<b>Low Income States</b>	<b>33.4</b>	<b>32.4</b>	<b>35.0</b>	<b>10.2</b>	<b>10.7</b>	<b>9.1</b>	<b>3.4</b>	<b>5.3</b>	<b>6.6</b>	<b>22.6</b>	<b>21.6</b>	<b>23.9</b>	<b>13.5</b>	<b>16.5</b>	<b>17.6</b>	<b>17.0</b>	<b>13.5</b>	<b>7.8</b>
Rajasthan	40.1	37.6	37.4	9.9	9.3	8.8	5.0	7.8	7.2	19.0	18.9	25.8	13.4	14.7	13.1	12.5	11.7	7.7
Madhya Pradesh	43.2	37.5	45.8	10.0	10.2	9.0	3.2	5.7	5.3	10.3	12.1	12.6	13.7	17.5	21.9	19.5	17.0	5.4
Uttar Pradesh	26.1	22.6	25.2	8.1	9.1	9.0	3.6	6.2	9.4	29.5	29.1	31.4	11.7	16.4	15.9	20.9	16.6	9.1
Orissa	33.3	31.6	36.6	11.9	12.6	6.7	4.1	4.2	5.1	26.7	28.8	29.4	16.4	17.1	17.7	7.7	5.7	4.5
Bihar	33.4	43.0	40.5	14.2	14.4	10.9	1.1	1.8	2.8	21.4	15.6	16.8	15.1	16.1	19.8	14.8	9.2	9.3
<b>14 Selected States</b>	<b>29.8</b>	<b>28.3</b>	<b>30.2</b>	<b>9.4</b>	<b>9.8</b>	<b>8.4</b>	<b>3.8</b>	<b>6.5</b>	<b>8.1</b>	<b>27.5</b>	<b>28.0</b>	<b>30.5</b>	<b>12.4</b>	<b>13.2</b>	<b>12.8</b>	<b>17.0</b>	<b>14.1</b>	<b>10.1</b>

departmental commercial ventures. In contrast, the rise in transfers was neither universal nor so apparent. But there has been a substantial expansion of poverty alleviation schemes and social security and welfare measures during the Sixth (1980-81 to 1984-85) and the Seventh (1985-86 to 1989-90) Plan periods though expenditure on these items constituted less than 1.5 per cent of SDP even in 1989-90.

iii. Given the constraint on resources, an important consequence of burgeoning expenditures on wages and salaries, interest payments and transfers and subsidies was to crowd out expenditures on maintenance of capital assets and capital outlay on infrastructural and promotional sectors with adverse implication on economic growth. The share of expenditure on maintenance in total current expenditures which ranged between 14 to 16 per cent during 1974-75 to 1980-81 declined steadily to 11.6 per cent in 1989-90. The per capita expenditures or net government maintenance at constant prices increased at just about 2.7 per cent per year in the Eighties as compared to the growth rate of 6.2 per cent in the case of per capita current expenditures and 5.5 per cent in the case of aggregate expenditures. It must also be noted that per capita maintenance expenditures increased at 8.4 per cent during the earlier period, i.e., 1974-75 to 1981-82 (Table 4.4). Also, our cross-section regressions for the selected States reveal that the expenditure on maintenance associated with per rupee of salary expenditures steadily declined from Re.0.44 in 1971-72 to Re.0.26 in 1980-81 and further to 0.22 in 1989-90 (Table 4.6).<sup>6</sup> The weakening of the relationship was seen in all the service categories and was particularly notable in economic services (Table 4.6).

Disaggregated data show that the share of net government maintenance in total expenditure fell in the aggregate for the selected States, but not for any of the high income States except Maharashtra. The middle and low income States that do not conform to the falling trend are Kerala and Uttar Pradesh.

Other inferences that can be drawn from the economic classification of the budgetary data are discussed within the context of the functional categories they refer to in subsequent sections.

### **4.3 Statewise Trends**

As can be expected, the Statewise picture exhibits substantial variations. The periodisation carried out earlier could not be resorted to in this case because of lack of uniformity among States in terms of discontinuities in the trend. However, annual growth rates of per capita expenditures in 1981-82 prices for the entire period (1974-75 to 1990-91) were computed and are depicted in Figure 4.4. The States exhibiting higher growth of total expenditures than that for all 14 States together are Bihar, Gujarat, Madhya Pradesh,

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6. The relationship has been estimated by regressing expenditures for goods and services on wages and salary expenditure in a linear equation using cross-section data.

**Table 4.6****Regression Coefficients of Expenditure on Wages and Salaries in Estimated Equations with Expenditure on Net Government Maintenance as the Dependent Variable: All Selected States**

Types of services/ year	Administ- rative service	Social service	Economic service	All services
1971-72	0.242	0.217	0.664	0.439
1976-77	0.307	0.051*	0.375	0.315
1980-81	0.250	0.045*	0.393	0.260
1985-86	0.238	0.041*	0.359	0.238
1989-90	0.238	0.102	0.313	0.218

Note: Coefficients marked \* are not significant at 5 per cent level.

Maharashtra, Punjab, and Tamil Nadu. Overall growth of per capita real public expenditure in Andhra Pradesh exactly equalled the average growth rate of 5.6 per cent. The other seven States showed growth rates below the group average. However, relatively large deviations from the rate for all 14 States together were noticed in Bihar (which experienced the highest growth in total expenditure of 6.8 per cent), Tamil Nadu (6.3 per cent), West Bengal (lowest growth rate of 4.6 per cent), Haryana (4.9 per cent), Rajasthan (5.0 per cent), and Orissa (5.1 per cent).

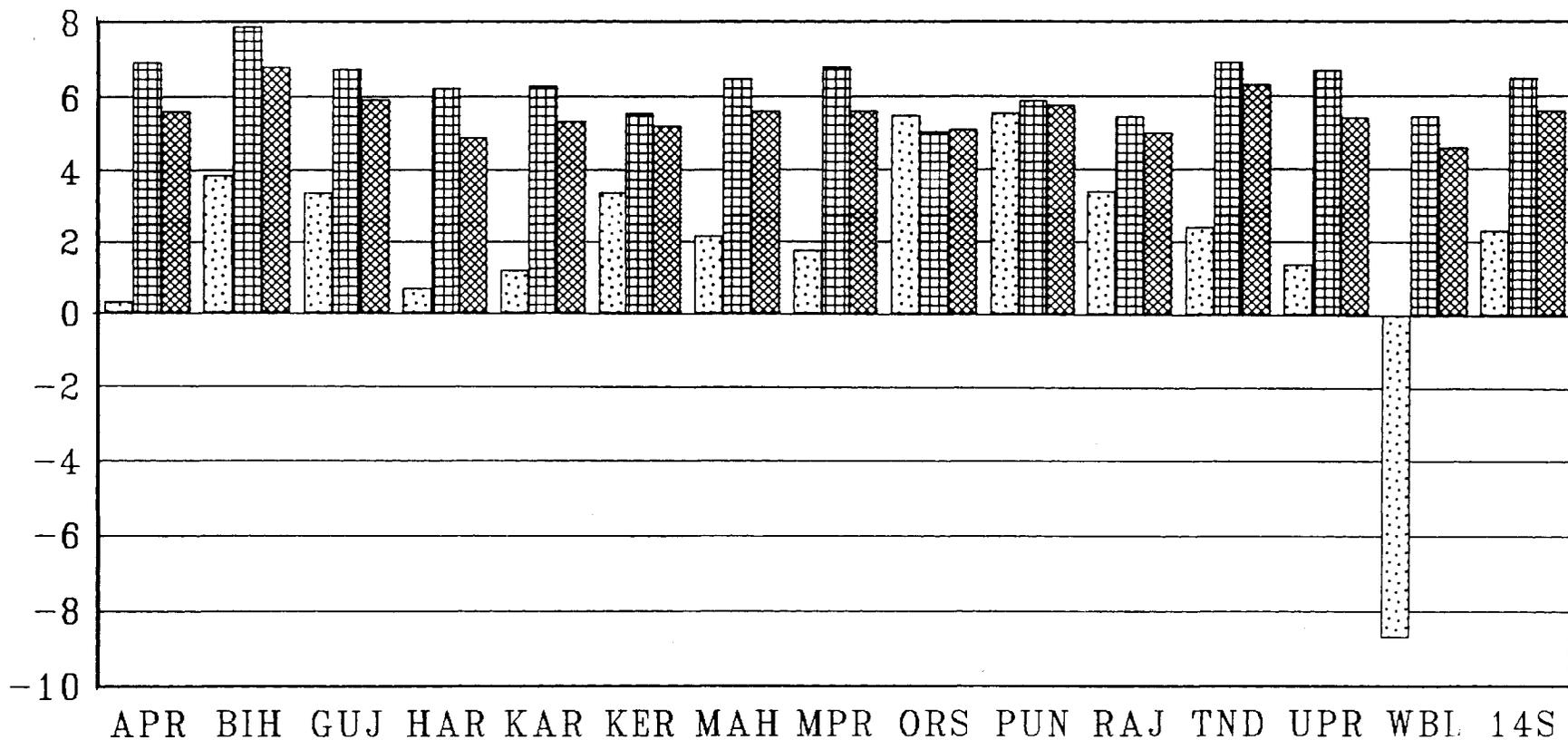
Bihar also recorded the highest growth in per capita real revenue expenditures at 7.8 per cent as compared to 6.5 per cent for the group as a whole, followed by Andhra Pradesh, Tamil Nadu, Madhya Pradesh, Uttar Pradesh and Gujarat in the same order. The lowest growth of revenue expenditures was noticed in Orissa (5.1 per cent); the growth of real per capita revenue expenditures was relatively low in Kerala, Rajasthan and West Bengal also (5.5 per cent in all the three States).

The fastest growth in real per capita capital disbursements was observed in Punjab and Orissa (5.5 per cent); in fact, capital disbursements and revenue expenditures grew almost at the same rate in Punjab, while capital expenditures grew faster than revenue expenditures in Orissa. The lowest positive growth of per capita capital disbursements was noticed in Andhra Pradesh (0.3 per cent); other States exhibiting significantly lower growth as compared to the whole group were Haryana, Karnataka and Uttar Pradesh. The case of West Bengal was, however, unique in that it was the only State to exhibit a negative growth rate for per capita net capital

Figure 4.4

# Growth Rates of Per Capita Government Expenditure

(in 1981-82 prices: per cent)



 Capital Disbursements       Revenue Expenditure       Total Expenditure

disbursements in constant prices, partly due to the fact that net capital disbursements were actually negative in 1984-85.<sup>7</sup>

If public expenditures are primarily developmental, and if the institutional set up with respect to State finances is inherently equitable between States, then one would expect an inverse relationship between the level of development (represented by per capita GDP) and the level of per capita government expenditure. On the other hand, if income elasticity of demand for public goods is positive and if government expenditures are subject to supply constraints through availability of resources, then one would expect a positive relationship between per capita government expenditures and per capita GDP. The relative strength of these opposite effects would determine the actual relationship.

Table 4.7 below gives per capita government expenditures of the selected States, categorised into three groups on the basis of their average level of per capita incomes, for three selected years. The numbers clearly and consistently show that public expenditures were positively related to the level of per capita GDP or to the level of development. The high income States had an average expenditure level of Rs.297, Rs.662, and Rs.761 in 1974-75, 1985-86 and 1990-91 respectively, as compared to the 14-State averages of Rs.221, Rs.482 and Rs.597. Both middle income and low income States, in contrast, had expenditure levels below the all-State average in all the three selected years. Assuming that the unit cost of providing public services in middle and low income States is the same as in the high income States, this clearly indicates the tremendous inequalities in the levels of public services provided. As tax efforts put in by the States do not show any systematic variation with the level of incomes (India, 1990), this is indicative of the failure of the Indian federal polity to ensure inter-State equity with respect to the provision of administrative, social and economic infrastructure through properly designed intergovernmental transfer schemes. The gap between the high income, middle income, and low income States seems to be narrowing only a little over time. Between 1974-75 and 1990-91, the per capita real expenditure in high income States went up by 156 per cent while that of middle income and low income States went up by 166 and 182 per cent. The trends would bear further investigation, which is attempted below.

Figure 4.4 does not indicate any clear relationship between *growth* in government expenditure and *level* of per capita GDP. However, a regression using pooled time series and cross-section data to explain variations in the share of government expenditures in GDP with only per capita GDP in constant prices (along with State dummies) as the explanatory variable confirms that *ceteris paribus*, an increase in GDP would raise public expenditures more than

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7. This was primarily due to a large negative figure for net loans and advances, which in turn was caused by a spurt in repayments in that year. While calculating the growth rate, we have taken this to be a very small positive value to enable us to include the observation in the computation; the alternative was to exclude the observation as negative numbers do not have log values.

proportionately.<sup>8</sup> Hence, growth of public expenditures does appear to be positively related to the level of SDP. This is despite the fact that the unit costs of supplying public goods and services seem to have increased faster in poorer States compared to high income States.<sup>9</sup>

**Table 4.7**  
**Per Capita Government Expenditure: Selected Years**  
**(in 1981-82 prices)**

(Rs.)

	1974-75			1985-86			1990-91		
	Revenue	Capital	Total	Revenue	Capital	Total	Revenue	Capital	Total
<b>High Income States</b>	<b>219</b>	<b>78</b>	<b>297</b>	<b>494</b>	<b>167</b>	<b>662</b>	<b>617</b>	<b>144</b>	<b>761</b>
Punjab	238	91	329	521	263	784	691	192	883
Haryana	235	87	323	482	196	678	619	125	744
Maharashtra	206	56	262	535	110	645	594	110	704
Gujarat	196	80	275	439	100	539	565	148	713
<b>Middle Income States</b>	<b>174</b>	<b>35</b>	<b>210</b>	<b>389</b>	<b>74</b>	<b>463</b>	<b>494</b>	<b>66</b>	<b>559</b>
Karnataka	177	42	219	395	97	491	489	81	570
West Bengal	150	31	181	313	47	361	419	50	470
Andhra Pradesh	149	38	187	398	61	458	465	68	533
Tamil Nadu	193	29	222	389	89	478	564	57	621
Kerala	203	36	239	449	77	526	530	72	602
<b>Low Income States</b>	<b>134</b>	<b>37</b>	<b>170</b>	<b>279</b>	<b>78</b>	<b>358</b>	<b>396</b>	<b>85</b>	<b>481</b>
Rajasthan	174	34	208	327	75	402	434	91	524
Madhya Pradesh	137	39	176	298	85	382	399	69	468
Uttar Pradesh	114	46	160	244	84	328	369	74	443
Orissa	151	33	184	289	78	367	383	105	488
Bihar*	91	32	123	237	71	308	260	70	330
<b>14 Selected States</b>	<b>173</b>	<b>48</b>	<b>221</b>	<b>380</b>	<b>102</b>	<b>482</b>	<b>502</b>	<b>95</b>	<b>597</b>

\* The last three columns give the figures for 1989-90. The averages for low income States and for the 14 selected States for 1990-91 therefore exclude Bihar.

8. Ignoring the coefficients of State dummies, the estimated equation is:

$$(\text{PUBEXP}/\text{SDP}) = 7.55 + 0.0039 \text{ PCYCP} \quad R^2 = 0.47,$$

(6.99)

where PUBEXP is total public expenditure in current prices, SDP is also in current prices and PCYCP denotes per capita SDP in constant prices.

9. Average salary levels were lower in the low-income States, by and large, as compared to the high-income States to begin with; their pay scales, however, tended to catch up in the latter years. Consequently, wage costs have risen faster in poorer States.

Combining the above two conclusions with respect to the relationship between per capita GDP and both level and growth of government expenditure, the prognosis that emerges is one of widening gap in government expenditure levels between States as the average per capita GDP grows (more so with respect to actual service levels); to check or reverse this, one or both of the following two conditions have to be met:

- (a) the rate of growth of GDP should be inversely related to the present levels;
- (b) the rate of growth of per capita government expenditures should be inversely related to their levels; the poorer States should make a special effort to push up their per capita government expenditure. Increased infrastructural investment would also reinforce (a) above.

**Table 4.8**

**Coefficients of Variation**

Year	<u>Per Capita Govt. Expenditure</u>			Per Capita SDP
	Capital	Revenue	Total	
1974-75	0.450	0.249	0.271	0.268
1975-76	0.401	0.270	0.276	0.310
1976-77	0.517	0.271	0.304	0.350
1977-78	0.285	0.246	0.236	0.338
1978-79	0.359	0.250	0.251	0.355
1979-80	0.403	0.250	0.274	0.377
<b>Avg: 74-80</b>	<b>0.403</b>	<b>0.256</b>	<b>0.269</b>	<b>0.333</b>
1980-81	0.291	0.244	0.239	0.329
1981-82	0.306	0.243	0.240	0.341
1982-83	0.440	0.224	0.260	0.340
1983-84	0.435	0.239	0.271	0.311
1984-85	0.578	0.242	0.279	0.323
<b>Avg: 80-85</b>	<b>0.410</b>	<b>0.238</b>	<b>0.258</b>	<b>0.329</b>
1985-86	0.563	0.258	0.294	0.329
1986-87	0.374	0.225	0.236	0.324
1987-88	0.597	0.256	0.290	0.333
1988-89	0.466	0.248	0.265	0.331
1989-90	0.467	0.254	0.266	0.358
<b>Avg: 85-90</b>	<b>0.494</b>	<b>0.248</b>	<b>0.270</b>	<b>0.335</b>

Of course, the desirability of increased government expenditure itself would be somewhat subjective and would depend on ideological leanings; even in an objective sense, it would depend on the effectiveness of government expenditure in achieving social objectives like promotion of economic development and more equitable distribution of income and wealth. We shall have some comments on the quality of government expenditure when examining disaggregated trends.

#### **4.4 Variation in Government Expenditure -- A Statistical Analysis**

As per capita expenditures vary directly with per capita GDP, if the cost differences among the States are assumed away, variations in per capita expenditures essentially reflect inequalities in the levels of public services. The trends in coefficients of variation (C.V.) of States' per capita expenditures and per capita GDP over the 16 years from 1974-75 to 1989-90 presented in Table 4.8 help us to draw some important inferences. First, we cannot discern any systematic trend in inter-State variations in per capita expenditures and clearly, the inequalities in the levels of public services have not decreased over the years. There was a marginal decline in the coefficient of variation during the first half of the Eighties, but in later years the trend was reversed. Second, by and large, the coefficients of variations in per capita GDP were higher than that of per capita expenditures, and this probably indicates that inter-State inequalities in per capita expenditure were lower than inequalities in per capita GDP. This partly reflects the attempt to reduce per capita expenditure variations among the States through Central transfers. Third, the analysis shows that the Central transfers were mainly used to equalise revenue expenditures among the States. Consequently, the C.V. in per capita revenue expenditure was lower than that of per capita GDP, and the C.V. also remained relatively stable over the years. In contrast, the C.V. in capital expenditure was much higher than that of per capita GDP throughout the period indicating thereby that the inter-State inequalities in capital expenditures have been large and persistent. As capital expenditures are presumed to contribute directly to the income generation process in the economy, the observed trend points towards the possibility of accentuation in inter-State inequalities in per capita incomes. Finally, the C.V. in capital expenditures shows a very high degree of fluctuations from year to year. This supports the hypothesis that capital expenditure are residually determined, only after meeting the requirement of revenue expenditure. This is not very surprising, as political returns to current expenditures would generally be perceived to be immediate and also higher than to capital expenditures.

A clear trend over time is not visible if we look at the yearwise figures of coefficients of variation. Hence, we have given in the table averages for the first 6 years and two subsequent 5-year periods. These averages show clearly that inequality in all the variables declined in the period 1980-81 to 1984-85 as compared to the preceding 6 years, but increased again during the next 5-year period which is also the Seventh Plan period. Dampening of the variation in GDP by total government expenditure, defined as the difference in coefficients of variation for the two variables divided by the coefficient of variation for GDP, followed the same trend. In other

words, not only that the dispersion in per capita SDP was the least during the Sixth Plan period, but also the equalising tendency in overall government expenditures was the greatest in the same period. The reversal of trends during the Seventh Plan period should be a matter of concern and the causes and consequences merit close scrutiny of researchers.

We have seen above that the coefficients of variation of total government expenditures and revenue expenditures show a fall in the Sixth Plan period as compared to the earlier period and then a rise again in the Seventh Plan period. It would be interesting to decompose the variations in total expenditures by the various items of expenditure and examine the sources of these variations more specifically. There are, however, two minor problems. First, disaggregation of total (that is, revenue plus capital) expenditure has the limitation that net loans and advances by State governments are not available with us by various functional categories and hence the sum of total expenditures under various functional heads will not add up to the grand total; net loans and advances would be the difference. Further, we have already seen that revenue expenditures predominate in total expenditures and hence, most conclusions regarding dispersions reached on the basis of revenue expenditures data are likely to hold good for total expenditures as well; any interesting deviation in capital disbursements is likely to be overwhelmed by the larger share of revenue expenditures. Hence, we first look at revenue expenditures alone. This, of course, is supplemented by a similar analysis of capital disbursements where we consider net loans and advances as a functional head. Second, the summary statistic of coefficient of variation (standard deviation/ mean) is not amenable to easy decomposition without making restrictive assumptions. There are other summary statistics reflecting dispersion/ inequality, and several studies have attempted decomposition of one or more of these in various ways (a summary is provided by Fields, 1980, pp. 101-11). Gini coefficients, Lorenz ratios, the Theil index and variance are some of these statistics. Our problem, however, is simpler than what most of these studies had to address in that it is not inequality but dispersion which we seek to decompose. We, therefore, use a fairly simple (and inexact) measure of relative contribution of individual components to the total dispersion. If  $X$  represents total revenue expenditure and is the sum of  $m$  components:

$$X = X_1 + \dots + X_i + \dots + X_m,$$

the relative contribution of each component to the total variation in any year is taken to be the weighted coefficient of variation of  $X_i$  for the year as a ratio of the sum of the weighted coefficients of variation of all the components, with weights equal to  $[\text{Mean}(X_i)/\text{Mean}(X)]$ .<sup>10</sup>

For the initial exercise, we consider the disaggregation of per capita revenue expenditures into the following categories:

10. This is not a proper decomposition but an approximation only as the dispersion in total revenue expenditure is not equal to the weighted sum described above. The total variation computed as above ignores the covariances between  $X_i$ s.

- (i) General Administration;
- (ii) Interest Payments;
- (iii) Social Services;
- (iv) Economic Services;
- (v) Compensation and Assignments to Local Bodies.

**Table 4.9**  
**Relative Contribution of Broad Categories**  
**to Inter-State Variation in Revenue Expenditures**

(per cent)

Year	General Administm	Interest Payments	Transfers to Local Bodies	Social Services	Economic Services
1974-75	15.5	9.2	4.5	36.4	34.3
1975-76	13.1	8.5	3.5	40.1	34.9
1976-77	12.3	9.7	4.0	39.0	35.0
1977-78	9.9	9.6	4.3	36.6	39.6
1978-79	11.5	10.6	3.5	35.9	38.5
1979-80	11.3	7.3	4.6	35.9	40.8
<b>Avg: 74-80</b>	<b>12.3</b>	<b>9.2</b>	<b>4.1</b>	<b>37.3</b>	<b>37.2</b>
1980-81	11.7	8.8	4.4	33.2	41.8
1981-82	13.1	10.3	4.5	30.1	42.1
1982-83	12.7	9.9	4.3	31.5	41.5
1983-84	11.8	8.9	4.3	35.5	39.6
1984-85	12.5	12.2	3.9	30.3	41.1
<b>Avg: 80-85</b>	<b>12.4</b>	<b>10.0</b>	<b>4.3</b>	<b>32.1</b>	<b>41.2</b>
1985-86	12.8	10.7	3.3	36.4	36.8
1986-87	16.0	11.4	3.8	32.9	35.9
1987-88	12.8	9.3	3.0	34.6	40.3
1988-89	13.9	10.4	3.5	39.9	32.3
1989-90	16.0	9.4	4.7	33.1	36.8
<b>Avg: 85-90</b>	<b>14.3</b>	<b>10.2</b>	<b>3.7</b>	<b>35.4</b>	<b>36.4</b>

*Note:* The figures in the above table are mean-weighted coefficients of variation for each category, as a percentage of the sum of them for all five categories.

Table 4.10

## Share of Broad Categories in Total Revenue Expenditure

(per cent)

State	General Administration			Interest Payments			Compensation & Assignments to Local Bodies			Social Services			Economic Services		
	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91
<b>High Income States</b>	<b>16.4</b>	<b>15.4</b>	<b>16.2</b>	<b>8.6</b>	<b>9.2</b>	<b>11.3</b>	<b>0.5</b>	<b>0.4</b>	<b>0.5</b>	<b>39.3</b>	<b>37.9</b>	<b>38.7</b>	<b>35.1</b>	<b>37.1</b>	<b>33.3</b>
Punjab	15.8	16.6	18.7	10.4	12.7	12.4	0.2	0.4	1.1	41.6	39.5	41.7	32.0	30.8	26.1
Haryana	14.4	13.9	14.2	9.7	9.7	12.6	0.2	0.1	0.2	32.6	34.8	36.7	43.0	41.5	36.3
Maharashtra	18.0	16.0	16.7	6.7	6.4	9.4	0.5	0.4	0.3	38.4	36.4	36.4	36.3	40.8	37.2
Gujarat	17.5	15.0	15.1	7.5	8.2	10.8	0.9	0.6	0.5	44.7	41.0	40.0	29.3	35.2	33.5
<b>Middle Income</b>	<b>17.4</b>	<b>16.6</b>	<b>17.4</b>	<b>8.6</b>	<b>7.9</b>	<b>10.1</b>	<b>2.7</b>	<b>2.8</b>	<b>2.4</b>	<b>44.6</b>	<b>45.3</b>	<b>43.7</b>	<b>26.7</b>	<b>27.5</b>	<b>26.5</b>
Karnataka	16.9	17.5	16.9	7.9	7.3	9.7	2.7	4.1	2.9	40.5	40.2	41.4	32.0	31.0	29.1
West Bengal	17.7	15.7	16.8	10.0	10.3	12.7	2.7	3.1	3.0	45.5	48.0	44.0	24.0	22.9	23.6
Andhra Pradesh	17.3	16.5	16.0	8.6	6.7	9.0	3.2	2.7	1.9	41.3	43.7	40.9	29.5	30.4	32.2
Tamil Nadu	17.8	15.0	16.3	7.7	7.0	7.5	3.5	2.7	3.1	43.0	44.1	44.3	28.1	31.2	28.8
Kerala	17.3	18.4	20.9	8.6	8.4	11.4	1.2	1.2	1.1	52.9	50.3	47.9	20.0	21.8	18.7
<b>Low Income States</b>	<b>17.6</b>	<b>16.6</b>	<b>16.8</b>	<b>11.3</b>	<b>10.7</b>	<b>13.1</b>	<b>0.7</b>	<b>1.1</b>	<b>0.9</b>	<b>39.8</b>	<b>41.3</b>	<b>39.9</b>	<b>30.6</b>	<b>30.3</b>	<b>29.4</b>
Rajasthan	16.6	17.4	15.5	13.5	12.5	14.1	0.6	0.6	0.4	40.2	40.3	39.5	29.1	29.1	30.5
Madhya Pradesh	17.1	15.4	16.4	8.6	8.5	10.0	0.5	2.6	2.1	41.6	38.5	40.8	32.2	35.0	30.6
Uttar Pradesh	16.6	16.4	16.9	9.9	9.7	13.0	1.1	1.1	0.9	37.1	39.4	37.5	35.2	33.4	31.8
Orissa	16.3	15.7	16.3	12.2	10.8	15.6	0.8	0.6	0.5	38.6	45.6	40.4	32.1	27.3	27.2
Bihar*	21.2	18.2	18.8	12.1	11.9	12.9	0.7	0.5	0.4	41.7	42.9	41.2	24.4	26.6	26.7
<b>Simple Average of All 14 States</b>	<b>17.2</b>	<b>16.3</b>	<b>16.8</b>	<b>9.5</b>	<b>9.3</b>	<b>11.5</b>	<b>1.3</b>	<b>1.5</b>	<b>1.3</b>	<b>41.4</b>	<b>41.8</b>	<b>40.9</b>	<b>30.5</b>	<b>31.2</b>	<b>29.4</b>

\* The averages for 1985-91 are actually for 1985-90.

Table 4.9 lays out the results of this exercise. It can be seen that the inter-State variations in per capita revenue expenditures can be largely attributed to social services and economic services. About 70 per cent of the inter-State variation is explained by just these two broad groups. This is not surprising, as their weights in total revenue expenditure are quite large (as can be seen from Table 4.10). By the same token, the increasing share of interest payments in total revenue expenditure is responsible for its rising contribution in the total variation (above 10 per cent during the last five years of our reference period). The tendency of relative weights to dominate the dispersion effect is quite strong; but the dispersion effect of general administration, though rising, is smaller than its share in revenue expenditures. The same is true of social services. In the case of economic services (and transfers to local bodies), it is the opposite. The tentative conclusion then is that the dispersion in revenue expenditure on economic services is a major source of disparity in per capita revenue expenditure. Given that the share of economic services is considerably lower than that of social services, the absolute amount of redistribution necessary to bring about a substantial difference in dispersion in this category would be smaller than in the case of social services. An inference can also be drawn that the States probably attach greater priority to expenditures on social services as compared to economic services (on the revenue account); given constraints on total expenditure, economic services are sacrificed to maintain social services. Inadequate maintenance of capital assets, an important part of revenue expenditure on economic services, has actually been pointed out before (Rao, 1992).

The results of a similar exercise for capital disbursements with capital expenditure on general administration, on social services and on economic services, and net loans and advances as its components is presented in Table 4.11. Table 4.12 gives the shares of the components in the total capital disbursements. The shares of general administration and social services are not large and this is reflected in the relative importance of these groups in total variation. Given their limited impact, the dispersion effect of capital expenditure on general administration fell, while that of social services rose during the Sixth Plan period and fell again. The dispersion effect of economic services, the group with the largest share in capital disbursements, fell fairly steadily. If this trend continues, the overall dispersion in capital disbursements, which is much higher than that in revenue expenditures, can be expected to fall gradually. However, net loans and advances, another important component of capital disbursements, showed increasing contribution to dispersion. Its share also increased in total capital disbursements, probably reflecting a tendency to shift responsibilities from departmental to non-departmental agencies while underwriting the expenses through loans. Although in principle, this should result in a certain amount of decentralisation in decision-making and thus increase efficiency, in practice it often results in inefficiency through multiplicity of government agencies with overlapping jurisdictions working at cross-purposes and with a woeful lack of coordination. Further, audit and critical examination of non-departmental undertakings is not as much as in departmental undertakings, and hence accountability sometimes suffers. The increasing contribution of net loans and advances to overall dispersion in capital disbursements should be seen in this light; it is also necessary to bear in mind the distinct possibility of these being a function of overall

resource availability, given that the repayment of these loans and advances cannot be taken for granted. The possibility that emerges then is that of relatively resource-rich States frittering away a part of their resources through loans and advances of dubious merit, probably as a result of pressure group tactics.

#### 4.5 *The Disaggregated Picture -- Budgetary Categories*

In our inter-State analysis of disaggregated data, we have so far concentrated on broad expenditure categories. Let us now look at the trends in government expenditure further disaggregated by budgetary categories, and identify the issues that arise therefrom.

**Table 4.11**  
**Relative Contribution of Broad Categories**  
**to Inter-State Variation in Capital Disbursements**

(per cent)

Year	General Administration	Social Services	Economic Services	Net Loans and Advances
1974-75	1.3	7.5	35.3	56.0
1975-76	1.4	8.3	39.9	50.4
1976-77	1.7	6.2	44.5	47.6
1977-78	1.7	8.2	45.0	45.1
1978-79	1.2	6.5	45.6	46.7
1979-80	1.0	6.3	52.3	40.4
<b>Avg 1974-80</b>	<b>1.4</b>	<b>7.2</b>	<b>43.8</b>	<b>47.7</b>
1980-81	1.7	11.3	39.6	47.5
1981-82	1.1	12.8	33.5	52.7
1982-83	1.4	14.0	29.7	54.8
1983-84	0.9	8.8	39.9	50.4
1984-85	1.7	7.4	41.2	49.7
<b>Avg 1980-85</b>	<b>1.3</b>	<b>10.9</b>	<b>36.8</b>	<b>51.0</b>
1985-86	0.6	5.9	24.1	69.4
1986-87	1.4	10.5	33.4	54.7
1987-88	1.6	8.5	29.4	60.4
1988-89	1.0	6.9	37.6	54.5
1989-90	1.1	5.8	51.9	41.2
<b>Avg 1985-90</b>	<b>1.2</b>	<b>7.5</b>	<b>35.3</b>	<b>56.1</b>

*Note:* The figures in the above table are mean-weighted coefficients of variation for each category, as a percentage of the sum of them for all five categories.

**Table 4.12**  
**Share of Broad Categories in Total Capital Disbursements**

(per cent)

States	General Administration			Social Services			Economic Services			Net Loans & Advances		
	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91
<b>High Income</b>	<b>1.0</b>	<b>1.4</b>	<b>1.2</b>	<b>6.3</b>	<b>6.4</b>	<b>6.1</b>	<b>48.8</b>	<b>48.2</b>	<b>42.6</b>	<b>43.7</b>	<b>44.1</b>	<b>50.1</b>
Punjab	0.8	1.1	1.2	7.0	5.5	4.4	36.2	34.6	20.3	56.0	58.8	74.2
Haryana	1.5	1.4	1.5	4.6	7.1	5.6	52.1	54.3	39.9	41.0	37.2	53.0
Maharashtra	1.1	1.8	1.5	5.1	3.7	5.0	54.8	53.7	59.6	39.0	40.8	33.9
Gujarat	0.7	1.1	0.6	8.4	9.4	9.5	52.0	50.0	50.6	38.8	39.5	39.3
<b>Middle Income</b>	<b>1.2</b>	<b>1.8</b>	<b>2.3</b>	<b>7.5</b>	<b>9.5</b>	<b>8.2</b>	<b>51.8</b>	<b>49.4</b>	<b>50.7</b>	<b>39.5</b>	<b>39.2</b>	<b>39.7</b>
Karnataka	0.8	1.7	1.7	3.4	2.9	3.9	60.2	56.3	61.6	35.7	38.8	37.0
West Bengal*	1.5	1.9	2.3	7.8	6.1	10.2	35.4	36.7	43.7	55.3	55.4	43.9
Andhra Pradesh	0.6	1.3	2.2	4.7	7.8	6.2	69.7	70.1	62.2	25.0	20.8	29.5
Tamil Nadu	1.4	2.0	2.5	7.1	7.4	7.1	33.8	26.8	30.8	57.7	63.9	59.5
Kerala	1.9	2.3	2.6	14.4	23.4	13.5	60.1	56.9	55.3	23.7	17.4	28.6
<b>Low Income</b>	<b>1.2</b>	<b>1.2</b>	<b>1.8</b>	<b>6.1</b>	<b>9.0</b>	<b>12.5</b>	<b>63.6</b>	<b>62.7</b>	<b>64.6</b>	<b>29.1</b>	<b>27.2</b>	<b>21.1</b>
Rajasthan	1.1	0.8	1.2	10.7	21.3	26.2	68.7	53.2	48.4	19.5	24.8	24.1
Madhya Pradesh	0.4	0.8	2.7	4.7	4.0	9.6	57.1	56.7	72.9	37.9	38.4	14.9
Uttar Pradesh	1.2	1.9	1.6	2.3	4.9	6.8	49.7	52.8	64.1	46.8	40.4	27.5
Orissa	2.3	1.7	2.3	7.0	6.1	8.4	77.7	87.3	82.0	13.0	4.9	7.3
Bihar#	0.9	0.6	1.1	5.8	8.6	11.5	64.9	63.4	55.4	28.4	27.4	32.0
<b>Simple Average of all 14 States</b>	<b>1.2</b>	<b>1.5</b>	<b>1.8</b>	<b>6.6</b>	<b>8.5</b>	<b>9.1</b>	<b>55.2</b>	<b>53.8</b>	<b>53.3</b>	<b>37.0</b>	<b>36.3</b>	<b>36.0</b>

\* The averages for the period 1980-85 exclude the year 1984-85.

# The averages for the period 1985-91 exclude the year 1990-91.

#### 4.5.1 General Administration

Under general administration, one normally includes expenditures on those parts of the government machinery which do not directly provide a service, good, or benefit to the residents of the State. These include expenditures on the legislative set up, Governors, tax collection, the law and order setup, and so on. These are closest to the concept of pure public goods and constitute the basic minimum of a government. These also represent the role of the government as a facilitator or a regulator as opposed to those of a producer or an intervener. We have, however, not included interest payments in this category in view of their contractual nature and their size, which makes it a category by itself.

**Table 4.13**  
**Expenditure on General Administration**  
**(Revenue plus Capital -- in constant prices)**

State	Per capita Expenditure (Rs.)			Share in Total Expenditure (%)			Annual Growth Rate (%) 1974-91
	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	
<b>High Income</b>	<b>47.0</b>	<b>59.3</b>	<b>91.4</b>	<b>12.3</b>	<b>11.6</b>	<b>13.1</b>	<b>5.9</b>
Punjab	50.5	66.1	112.6	11.6	12.1	14.0	7.4
Haryana	43.1	56.1	81.8	10.4	10.5	11.7	5.8
Maharashtra	50.9	64.4	94.3	13.9	12.8	14.2	5.8
Gujarat	43.6	50.7	77.0	13.1	11.2	12.4	5.1
<b>Middle Income</b>	<b>39.4</b>	<b>50.2</b>	<b>76.5</b>	<b>14.1</b>	<b>14.0</b>	<b>15.4</b>	<b>6.1</b>
Karnataka	39.2	53.5	76.1	13.0	14.0	14.6	6.5
West Bengal	36.3	41.7	60.1	14.7	14.0	15.0	4.8
Andhra Pradesh	36.5	48.8	69.4	12.9	13.8	14.1	6.2
Tamil Nadu	39.5	47.5	76.8	14.9	12.4	14.6	6.2
Kerala	45.7	59.3	100.3	14.8	15.6	18.5	7.2
<b>Low Income</b>	<b>29.8</b>	<b>37.6</b>	<b>55.1</b>	<b>13.2</b>	<b>12.6</b>	<b>13.8</b>	<b>6.3</b>
Rajasthan	37.2	45.1	61.1	13.3	13.2	13.0	4.9
Madhya Pradesh	28.9	37.5	58.7	12.4	11.4	13.9	6.5
Uttar Pradesh	25.1	32.6	50.8	12.0	12.2	13.9	6.8
Orissa	33.7	39.9	57.1	13.4	12.5	13.3	4.9
Bihar*	24.0	32.5	48.0	15.1	13.8	15.0	6.7
<b>Average of 14 Selected States</b>	<b>38.1</b>	<b>48.3</b>	<b>73.7</b>	<b>13.2</b>	<b>12.8</b>	<b>14.1</b>	<b>6.2</b>

\* The averages for 1985-91 exclude the year 1990-91.

Note: The growth rates refer to per capita expenditure in 1981-82 prices.

On an average, the expenditure on general administration grew almost in line with the overall expenditure, as a result of which its share in total expenditure did not show much change. The levels of per capita expenditure on General administration as a whole -- depicted in Table 4.13 -- varied considerably across the States. The variation was much less when these were taken as ratios of total expenditure. This is not very surprising because, as we have seen, the public expenditure ratio (representing the relative size of the public sector) does vary with the per capita GDP and consequently those parts of expenditure on general administration that are related to the size of the public sector (e. g., expenditure on tax collection, and pensions and retirement benefits) also vary. However, even when we examine the growth of expenditures on general administration, there appears to be substantial differences between States. To find the causes for such divergent trends, it is necessary to look into further disaggregation of general administrative expenditures.

**Table 4.14**

**Share of Major Components in Total Expenditure on General Administration  
and their Growth Per Capita in 1981-82 Prices**

(per cent)

State	Tax Collection				Police				Justice and Jails			
	Average 1974-80	Average 1980-85	Average 1985-91	Growth 1974-91	Average 1974-80	Average 1980-85	Average 1985-91	Growth 1974-91	Average 1974-80	Average 1980-85	Average 1985-91	Growth 1974-91
<b>High Income</b>	<b>15.1</b>	<b>9.8</b>	<b>7.9</b>	<b>-2.2</b>	<b>34.7</b>	<b>36.0</b>	<b>35.1</b>	<b>5.6</b>	<b>6.7</b>	<b>6.0</b>	<b>5.5</b>	<b>4.1</b>
Punjab	10.4	9.3	6.8	3.4	36.1	35.8	37.2	7.7	8.4	7.5	6.2	4.7
Haryana	10.3	9.1	8.4	3.9	33.0	36.3	35.7	6.7	6.7	5.9	5.8	4.5
Maharashtra	20.8	11.8	8.8	-4.2	33.0	32.6	30.0	4.7	6.1	5.1	4.9	3.7
Gujarat	18.7	9.0	7.5	-2.4	36.5	39.2	37.6	5.4	5.6	5.6	5.2	4.6
<b>Middle Income</b>	<b>15.7</b>	<b>14.1</b>	<b>12.4</b>	<b>4.1</b>	<b>29.8</b>	<b>27.9</b>	<b>25.3</b>	<b>4.4</b>	<b>7.8</b>	<b>6.3</b>	<b>5.7</b>	<b>3.2</b>
Karnataka	17.6	14.1	13.2	3.5	25.0	23.3	23.1	5.5	7.5	6.1	6.0	4.2
West Bengal	16.2	14.6	12.1	2.3	43.2	39.2	37.0	3.3	8.6	6.8	5.9	1.3
Andhra Pradesh	13.1	11.4	12.8	5.9	29.0	28.1	24.8	4.8	6.7	5.8	5.5	4.4
Tamil Nadu	11.9	13.6	10.7	5.2	25.9	26.4	23.3	5.0	8.4	7.1	6.2	3.2
Kerala	19.9	16.8	13.2	3.5	25.9	22.4	18.0	4.0	7.7	5.8	5.0	3.3
<b>Low Income</b>	<b>19.3</b>	<b>16.7</b>	<b>15.3</b>	<b>4.0</b>	<b>35.0</b>	<b>36.0</b>	<b>33.2</b>	<b>6.0</b>	<b>8.3</b>	<b>7.3</b>	<b>6.5</b>	<b>3.9</b>
Rajasthan	19.4	17.4	17.0	3.4	32.5	31.9	30.1	4.0	6.5	6.1	6.1	4.2
Madhya Pradesh	20.3	16.8	16.3	4.3	38.1	39.8	34.1	5.5	8.7	7.1	5.4	2.2
Uttar Pradesh	22.2	18.0	15.1	3.4	38.8	41.3	39.7	6.8	8.6	8.1	7.3	5.1
Orissa	20.6	18.6	17.0	3.2	30.1	29.4	29.3	4.5	7.0	6.3	5.9	3.3
Bihar*	13.8	12.7	10.9	4.4	35.4	37.8	32.7	6.1	10.7	9.0	7.6	3.3
<b>Average of 14 Selected States</b>	<b>16.8</b>	<b>13.8</b>	<b>12.1</b>	<b>3.7</b>	<b>33.0</b>	<b>33.1</b>	<b>30.9</b>	<b>5.4</b>	<b>7.7</b>	<b>6.6</b>	<b>5.9</b>	<b>3.7</b>

\* Averages for the period 1985-91 and growth rates exclude the year 1990-91.

Table 4.14 (contd.)

**Share of Major Components in Total Expenditure on General Administration  
and their Growth Per Capita in 1981-82 prices**

(per cent)

State	Pensions and Retirement Benefits				Public Works				Capital Expenditure			
	Average	Average	Average	Growth	Average	Average	Average	Growth	Average	Average	Average	Growth
	1974-80	1980-85	1985-91	1974-91	1974-80	1980-85	1985-91	1974-91	1974-80	1980-85	1985-91	1974-91
<b>High Income</b>	<b>10.2</b>	<b>14.8</b>	<b>21.9</b>	<b>14.2</b>	<b>8.5</b>	<b>9.1</b>	<b>7.7</b>	<b>7.2</b>	<b>2.4</b>	<b>3.0</b>	<b>1.9</b>	<b>4.6</b>
Punjab	10.5	15.3	20.8	14.1	9.8	10.3	9.0	6.1	1.9	2.5	2.2	34.9 <sup>#</sup>
Haryana	11.2	14.9	22.3	13.0	12.9	10.0	7.2	-0.2	4.4	3.6	2.6	1.5
Maharashtra	6.6	11.4	17.9	15.3	5.1	9.1	8.0	10.6	1.9	3.2	1.7	4.7
Gujarat	12.4	17.7	26.7	13.3	6.3	7.1	6.5	6.6	1.5	2.7	0.9	0.4
<b>Middle Income</b>	<b>17.6</b>	<b>23.5</b>	<b>30.7</b>	<b>11.9</b>	<b>3.5</b>	<b>3.8</b>	<b>4.5</b>	<b>8.5</b>	<b>1.6</b>	<b>2.4</b>	<b>2.0</b>	<b>7.1</b>
Karnataka	25.3	33.1	33.1	9.5	3.7	4.4	6.3	12.1	1.5	2.8	1.9	8.8
West Bengal	8.8	12.8	19.8	12.9	2.3	5.1	5.6	15.5	2.0	2.0	1.8	4.1
Andhra Pradesh	16.1	21.5	27.8	11.9	2.5	3.7	3.1	7.9	1.1	1.7	2.3	10.9
Tamil Nadu	15.7	17.4	28.5	12.3	5.4	5.0	4.6	4.8	1.5	3.1	2.0	8.3
Kerala	22.0	32.4	44.2	14.0	3.6	0.7	2.8	-2.8	2.1	2.6	1.9	5.6
<b>Low Income</b>	<b>8.8</b>	<b>12.0</b>	<b>17.7</b>	<b>13.4</b>	<b>3.6</b>	<b>4.3</b>	<b>3.9</b>	<b>8.6</b>	<b>2.3</b>	<b>2.4</b>	<b>2.5</b>	<b>1.0</b>
Rajasthan	13.6	19.7	22.4	10.2	4.3	3.1	3.0	3.5	2.0	1.7	1.7	5.0
Madhya Pradesh	9.8	11.3	17.8	12.7	0.1	3.1	0.3	16.4	0.9	1.8	3.6	18.1
Uttar Pradesh	6.5	9.3	13.7	14.3	1.2	1.7	5.5	20.7	3.1	4.3	1.6	14.5
Orissa	6.6	9.6	17.4	14.5	6.1	7.1	4.7	0.0	3.6	3.0	3.8	5.4
Bihar*	7.5	10.1	17.0	15.4	6.5	6.5	6.1	5.5	1.8	1.0	1.8	4.2
<b>Average of 14 Selected States</b>	<b>12.3</b>	<b>16.9</b>	<b>23.5</b>	<b>12.9</b>	<b>5.0</b>	<b>5.5</b>	<b>5.2</b>	<b>8.0</b>	<b>2.1</b>	<b>2.6</b>	<b>2.1</b>	<b>6.2</b>

# The growth rate is high due to a negative figure in 1974-75, treated as a small positive number. Excluding 1974-75, the growth rate is 7.9 per cent.

\* Averages for the period 1985-91 and growth rates exclude the year 1990-91.

Table 4.14 provides the necessary information. Clearly, police claims the largest share in this broad group, but the fastest growing part of expenditure on general administration were those on pensions. This is a function of pension rates and the number of beneficiaries. In recent years, the rates in most States have converged around the rates applicable at the Central level (though there are exceptions, e.g., Punjab), but they have done so from different starting points, and at different pace. The number is a function of demographic factors and life expectancy (and of course the retirement age), both of which vary considerably across States. A judgement by the Supreme Court enhancing pensions and raising retirement benefits in 1984 was an important factor in the conspicuous rise in expenditure on this item. Tax collection costs do not appear to

have grown much (their share shows a gradual fall), and as a ratio of own tax revenue, show noticeable decline over the years (Table 4.15).<sup>11</sup> Neither have Police expenditures gone up very much, except in a few States (viz., Punjab, Haryana, Uttar Pradesh and Bihar), although Bardhan (1992) implies that they have, by citing the growth in police expenditures in isolation. But those

**Table 4.15**  
**Collection Costs as Percentages**  
**of Own Tax Revenue**

(per cent)

State	Average 1974-80	Average 1980-85	Average 1985-91
<b>High Income</b>	<b>4.1</b>	<b>2.5</b>	<b>2.0</b>
Punjab	2.5	2.4	2.2
Haryana	2.4	2.2	1.3
Maharashtra	5.8	3.3	2.4
Gujarat	5.9	2.2	2.0
<b>Middle Income</b>	<b>5.2</b>	<b>4.6</b>	<b>4.3</b>
Karnataka	5.3	4.4	4.0
West Bengal	5.9	5.4	4.8
Andhra Pradesh	4.2	3.8	4.1
Tamil Nadu	3.7	3.4	3.1
Kerala	7.0	6.0	5.5
<b>Low Income</b>	<b>9.2</b>	<b>8.6</b>	<b>8.2</b>
Rajasthan	9.1	8.0	7.5
Madhya Pradesh	7.4	6.8	7.2
Uttar Pradesh	8.5	7.9	7.3
Orissa	13.9	11.9	10.8
Bihar*	7.0	8.3	8.2
<b>Simple Average of All 14 States</b>	<b>6.3</b>	<b>5.4</b>	<b>5.0</b>

\* The last column is based on data upto 1989-90.

on justice and jails have not gone up commensurately (their share actually fell over the years), which may actually explain the strain on the judicial and the prison system in the country. As far as public works are concerned, the figures show no definite pattern, mainly because (i) public

11. In fact, both time series and cross section evidence point towards substantial economies of scale in tax collection.

Table 4.16

**Share of Selected Economic Categories in Expenditure on General Administration  
and their Growth Per Capita in 1981-82 Prices during 1974-75 to 1989-90  
(Average for the period)**

(per cent)

State	Salaries and Wages				Net Government Maintenance				Construction			
				Growth				Growth				Growth
	1974-80	1980-85	1985-90	1974-90	1974-80	1980-85	1985-90	1974-90	1974-80	1980-85	1985-90	1974-90
<b>High Income</b>												
<b>States</b>	<b>66.5</b>	<b>66.0</b>	<b>63.3</b>	<b>6.2</b>	<b>15.3</b>	<b>14.8</b>	<b>13.0</b>	<b>4.0</b>	<b>5.1</b>	<b>4.8</b>	<b>4.6</b>	<b>4.2</b>
Punjab	75.1	72.7	61.2	5.3	12.7	12.8	15.0	9.1	4.3	4.3	4.3	7.2
Haryana	69.2	69.8	53.1	5.8	17.4	14.3	9.7	3.6	8.6	4.7	8.6	3.8
Maharashtra	56.2	55.6	62.5	6.2	16.5	14.1	12.6	2.7	3.2	4.9	2.4	3.0
Gujarat	65.4	66.0	76.4	7.1	14.7	17.8	14.6	26.2	4.4	5.1	3.3	3.1
<b>Middle Income</b>												
<b>States</b>	<b>65.1</b>	<b>63.8</b>	<b>64.6</b>	<b>5.5</b>	<b>20.0</b>	<b>15.3</b>	<b>13.1</b>	<b>1.5</b>	<b>2.7</b>	<b>3.6</b>	<b>3.1</b>	<b>7.4</b>
Karnataka	64.6	60.1	66.4	7.0	17.6	9.5	4.7	-17.9	3.0	4.3	3.3	8.4
West Bengal	61.0	59.1	55.8	3.9	25.4	15.6	15.3	0.2	2.3	2.8	2.5	6.4
Andhra Pradesh	64.4	65.9	66.8	5.2	18.9	16.8	17.4	3.8	1.3	2.1	3.8	16.5
Tamil Nadu	60.2	60.9	63.7	6.1	21.8	19.6	15.5	1.7	2.7	4.0	2.5	4.4
Kerala	75.2	73.1	70.3	6.5	16.2	15.3	12.5	4.9	4.1	4.7	3.3	4.4
<b>Low Income</b>												
<b>States</b>	<b>67.6</b>	<b>66.8</b>	<b>69.2</b>	<b>5.7</b>	<b>20.8</b>	<b>18.5</b>	<b>14.9</b>	<b>3.3</b>	<b>3.4</b>	<b>3.6</b>	<b>4.9</b>	<b>8.5</b>
Rajasthan	72.5	71.3	73.8	4.7	17.6	16.1	14.4	2.9	2.4	2.3	2.7	5.0
Madhya Pradesh	64.6	62.4	65.6	6.0	19.8	17.3	11.9	1.0	1.7	4.1	5.0	6.9
Uttar Pradesh	69.4	65.0	66.9	5.8	17.7	17.5	17.1	5.6	5.3	6.3	4.1	3.5
Orissa	70.8	71.6	77.1	5.3	17.6	15.1	9.2	-1.1	5.2	3.7	3.7	-1.8
Bihar	60.6	63.6	62.9	6.3	31.4	26.2	21.8	2.8	2.4	1.5	8.8	15.5
<b>14 Selected States</b>	<b>64.5</b>	<b>63.4</b>	<b>65.2</b>	<b>5.7</b>	<b>19.5</b>	<b>16.6</b>	<b>14.4</b>	<b>2.8</b>	<b>3.3</b>	<b>4.0</b>	<b>3.9</b>	<b>7.0</b>

construction activity usually takes place in occasional spurts, and (ii) the figures are net of recoveries from other governmental agencies on whose behalf the Public Works Department may carry out constructions, and annual figures would thus depend on the promptness in settling accounts on the part of its clients.

The data on economic classification (Table 4.16) reveal that as far as general administration is concerned, the share of salaries did not go up in general as one would expect (due to the pay revisions in the third period). They remained fairly stable at around two-thirds of the expenditure on general administration, though in the low income States the share went up in an attempt to catch up with other States. Consumption of goods and services (net government maintenance) clearly fell (from 19.5 per cent in the period 1974-80 to 14.4 per cent during 1985-91), while constructions of buildings, roads etc. claimed a greater share (about 4 per cent) in the last two periods as compared to the first period. The case of Karnataka is a peculiar one where the share of expenditure on goods and services fell and the growth rate was negative, probably due to the transfer of several functions to local bodies; the share of wages and salaries, however, did not show any commensurate fall.

#### **4.5.2. Interest Payments**

Interest payments show clearly a rising trend over the years, and this is quite evident in States which did not have a high interest burden in 1974-75 (Table 4.17). In general, the three States with low per capita SDP -- Rajasthan, Orissa and Bihar -- had to pay out the largest percentages of their total expenditure among the selected States as interest payment until the Eighties. This was obviously because of their expenditure needs far exceeding their own resources and the federal transfers they received. In fact, since a large part of the plan transfers came as loans, they could be at least partly responsible for the heavy interest burden on these States. By 1984-85, two other States with resource problems though not low SDP -- West Bengal and Punjab -- had joined these States with high interest burden. After 1986, several other States had similar problems. By 1990-91, only Tamil Nadu could be said to have had no immediate concern on this account; Guhan (1992) points out that this was mainly due to slowdown of capital expenditure and the consequent lower requirement of debt financing. The spread of interest burden problem could be partly attributed to the Overdraft Regulation Scheme enforced by the Reserve Bank of India in the mid-'Eighties which turned the 'soft' budget constraint of States into 'hard' ones and forced the States to substitute relatively cheap debt with costlier debt. The basic reason, of course, was the appearance of revenue account deficits in most of the State budgets in this period. Rising interest rates, changing composition of debt in favour of more costly debt (supply of cheaper debt -- basically from the Centre -- has been

restricted but for a few States like Punjab), and bureaucratic and political irresponsibility<sup>12</sup> also contributed to the rising interest burden. This was despite the reliefs mandated by the Seventh and the Eighth Finance Commissions.

**Table 4.17**  
**Share of Interest Payments in**  
**Total expenditures: 14 Selected States**

(per cent)

States	Average 1974-80	Average 1980-85	Average 1985-91	Growth Rate(%) 1974-91
<b>High Income</b>	<b>6.2</b>	<b>6.8</b>	<b>8.9</b>	<b>9.1</b>
Punjab	7.5	9.0	9.0	7.5
Haryana	6.7	7.1	10.1	8.6
Maharashtra	5.1	5.0	7.8	9.5
Gujarat	5.6	6.0	8.8	10.1
<b>Middle Income</b>	<b>6.8</b>	<b>6.5</b>	<b>8.7</b>	<b>7.6</b>
Karnataka	6.0	5.7	8.2	8.1
West Bengal	8.1	9.1	11.1	7.6
Andhra Pradesh	6.4	5.5	7.8	7.3
Tamil Nadu	6.4	5.5	6.6	6.8
Kerala	7.2	6.9	10.0	8.5
<b>Low Income</b>	<b>8.4</b>	<b>7.9</b>	<b>10.5</b>	<b>8.3</b>
Rajasthan	10.6	9.3	11.6	5.7
Madhya Pradesh	6.2	6.2	8.2	8.5
Uttar Pradesh	6.9	6.9	10.5	9.3
Orissa	9.6	8.3	12.3	7.4
Bihar*	8.5	9.0	10.0	8.3
<b>Simple Average of All 14 States</b>	<b>6.9</b>	<b>6.8</b>	<b>9.2</b>	<b>8.3</b>

\* The last two columns are based on data excluding 1990-91.

Note: The growth rates refer to per capita interest payments in 1981-82 prices.

12. Soft loan options with deferred repayment liabilities enable them to pass on the problem of finding resources for debt servicing to future incumbents.

### 4.5.3 Compensation and Assignments to Local Bodies

This is an item where one would expect a lot of inter-State variations, because local bodies are created and continue on the basis of the authority conferred on them by the State Legislature, and the extent of delegation of authority is decided by each State, and within each State, each government that comes to power after elections. No clear pattern can therefore be expected. Further, inter-governmental transfers can take place in different ways, which would show up in the expenditure pattern of the higher level government differently. For example, if local bodies have delegated authority to design and levy certain taxes on their own and use the proceeds, it does not show up in the expenditures of the higher level government (except perhaps as a reduction in overall budget size). But if the tax is designed and levied by the higher level government, and then transferred entirely to the local bodies, it does. In such cases, it is difficult to draw any conclusions regarding decentralisation from the expenditure of the higher level government alone<sup>13</sup>. We, therefore, refrain from making any analysis of these figures. In any case, these constitute a very small proportion of total expenditure.

### 4.5.4 Social Services

Among the five broad categories of State government expenditure, this is the largest in terms of the amounts involved, and along with economic services, constitutes the bulk of government expenditure in the States. In fact, under the Constitutional arrangements, the State governments are vested with the primary responsibility of providing social services. Given the low level of per capita income in the country and the relatively high incidence of poverty, these are services that directly affect the quality of life and the capacity to earn a living of a large number of residents. By convention, all expenditures on human capital formation is a part of this broad group. Given their high visibility, immediate impact and the potency in ameliorating the conditions of the poor, it is naturally an area to focus on in a democracy if politicians determine expenditure priorities -- the returns on these expenditures are fairly high in terms of votes. These can also be claimed to be equitable insofar as the benefits are expected to be more for the poor.<sup>14</sup>

Production and provision of most of the social services require much more labour than capital, and hence, it is not surprising that only a small fraction of the total expenditure on social services was in the capital account. However, the growth of capital expenditure in the social services has been nowhere near the growth of revenue expenditures -- just as in the case of total expenditures. This is perhaps a less serious problem in the area of education while direct welfare

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13. The budgetary figures under this head do not represent all the transfers from the States to the local bodies. Several specific purpose grants are actually included under the relevant functional heads in the State budgets; it is not easy to cull out the amounts of all such transfers.

14. This is not always the case in fact. Several programmes meant for the lower income groups have been hijacked by the less needy. See Vithal(1992) for an exposition of this phenomenon.

activities do not usually have a capital component, but for water supply, sewerage and sanitation, and health -- in that order -- the lack of sufficient capital investment could cause service bottlenecks.

Almost 85 per cent of the total spending on social services was undertaken at the State level and expenditure on social services constituted about 35 per cent of total expenditures of the States in 1990-91. The per capita expenditures and their proportion to per capita SDP in respect of all the selected States taken together on different items under social services are presented in Table 4.18, and their growth rates summarised in Table 4.19 help us to draw the following inferences:

i. The volume of spending on basic community infrastructure like water supply and sanitation, urban development and housing was simply, abysmal. Moreover, the growth rates of expenditure on these items decelerated significantly in the Eighties. With per capita expenditure of Rs. 2.7 (1981-82 prices) on urban water supply<sup>15</sup> and Rs.6 on rural water supply, it would be too much to expect that potable drinking water at satisfactory levels can be provided to urban and rural residents. In the event, the process of natural selection results in the less organized poorer sections being denied access to this basic need. At 5 per cent growth in per capita expenditures seen in the Eighties (Table 4.19), it will take several years to provide even safe drinking water to the poor in the country. Similarly, the amount that was spent on housing at 1981-82 prices was only Rs.2.5 in per capita terms and almost 40 per cent of this was spent on housing of government employees and not on the poorer sections of society. Similarly, expenditure on urban development formed less than 0.2 per cent of the SDP in 1990-91. Surely, social infrastructure was not a priority item for the State governments, the expenditures priorities being decided by the special interest groups.

ii. Nor has the government considered it important to spend adequate amounts on the development and welfare of vulnerable sections of society. The allocation to 'welfare of scheduled castes and tribes' was only about Rs.13.60 (1981-82 prices) and it formed just about 0.5 per cent of SDP. This volume of expenditure was meant to be for the benefit of scheduled castes and tribes who formed 25 per cent of population. Again, given the natural process of selection and the information cost, only the better off among them can get access to these funds and the only objective it serves is to publicise the 'egalitarian' policy of the State governments. Similarly, social security

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15. In several States, this is the responsibility of the local bodies. However, their finances generally do not allow them to even maintain the existing facilities adequately, let alone make further investments, even when capital expenditures are badly needed to solve the urban water supply problems that are fast assuming crisis dimensions. The State governments are not making the necessary capital investments either. In rural areas, the technology involved is different and less capital intensive.

Table 4.18

**Government Expenditures on Social Services in  
All Selected States**

	Per Capita Expenditures (1981-82 rupees)				Percentage of Expenditure to SDP			
	1974-75	1986-87	1985-86	1990-91	1974-75	1980-81	1985-86	1990-91
1. General Education	35.9	48.0	68.4	99.2	2.3	2.9	3.4	3.8
1.1 Elementary Education	18.8	24.3	35.4	50.1	1.2	1.5	1.8	1.9
1.2 Secondary Education	12.0	15.6	22.2	32.9	0.8	0.9	1.1	1.3
1.3 Higher Education	4.1	6.8	8.9	12.4	0.3	0.4	0.4	0.5
2. Technical Education	1.1	1.5	2.2	3.4	0.1	0.1	0.1	0.1
3. Medical and Public Health	11.5	15.9	20.4	26.3	0.7	0.9	1.0	1.0
4. Family Welfare	1.7	2.2	5.3	5.5	0.1	0.1	0.3	0.2
5. Nutrition	0.5	0.9	3.1	3.9	-	0.1	0.2	0.2
6. Water Supply and Sanitation	3.7	7.2	12.4	11.9	0.2	0.4	0.6	0.5
6.1 Urban Water Supply	1.1	1.6	2.4	2.7	0.1	0.1	0.1	0.1
6.2 Rural Water Supply	1.5	4.3	6.9	6.0	0.1	0.3	0.3	0.2
6.3 Sanitation	0.2	0.1	1.5	0.7	n	n	0.1	n
7. Housing	1.5	2.1	2.4	3.5	0.1	0.1	0.1	0.1
7.1 Government Housing	0.9	1.6	1.7	2.0	0.1	0.1	0.1	0.1
7.2 Urban Housing	0.2	0.2	n	0.3	n	n	n	n
7.3 Other Housing	0.4	0.3	0.7	1.2	n	n	n	n
8. Urban Development	1.0	2.2	2.9	4.5	0.1	0.1	0.1	0.2
9. Social Security and Welfare	2.4	4.1	6.9	8.6	0.2	0.2	0.3	0.3
10. Natural Calamity Relief	3.0	3.8	7.8	6.5	0.2	0.2	0.4	0.2
11. Welfare of Scheduled Casts and Tribes	3.3	7.3	10.8	13.6	0.2	0.4	0.5	0.5
12. Labour and Employment	1.2	3.6	2.3	3.3	0.1	0.2	0.1	0.1
Total Social and Community Services - Revenue	65.6	95.9	140.3	186.9	-	-	-	-
- Total	68.5	100.7	146.7	193.4	4.4	6.0	7.4	7.5

n: Negligible.

**Table 4.19****Growth of Per Capita Government Expenditure on Social Services  
All Selected States: in 1981-82 prices**

(Per cent per year)

	1974-75 to 1981-82	1981-82 to 1990-91	1974-75 to 1990-91
1. General Education	3.9	9.4	5.9
1.1 Elementary Education	3.1	7.7	5.8
1.2 Secondary Education	4.1	7.4	6.0
1.3 University and Higher Education	7.1	5.0	5.9
2. Technical Education	3.4	8.0	6.1
3. Medical and Public Health	4.4	4.4	4.4
4. Family Welfare	6.0	8.9	7.7
5. Nutrition	15.9	15.6	15.8
6. Water Supply and Sanitation	15.0	5.0	9.0
7. Housing	5.1	2.9	3.8
8. Urban Development	10.0	5.2	7.2
9. Social security and welfare	13.8	6.5	8.6
10. Welfare of Scheduled-Castes and Tribes	13.1	5.5	8.6
11. Natural Calamity Relief	8.2	3.1	5.2
12. Labour and Employment	11.2	0.9	5.0
13. Total Social Services			
Revenue	6.0	6.4	6.3
Capital	9.9	2.7	5.6
Total	6.2	6.3	6.2

social security and welfare expenditures which was less than Rs.9 per capita (or 0.3 per cent of GDP) was expected to provide social insurance to the 30 per cent of the population that is considered to be poor. As even these were not properly targeted, a general impression that is created is that these are wasteful and this provides an additional argument for the special interest groups to reduce allocations for outlay on these items.

iii. Another important finding is the low allocation made to spending on education and health services. On education, the States spent less than 4 per cent of GDP in 1990-91, and on medical and public health services (including family welfare) it was a little over 1.2 per cent of GDP. In the education sector, given the poor quality of public education and the ability of the better off sections to gain greater access to better quality

private elementary education (including private tuitions and coaching classes), students from the latter group had an edge over others in gaining access to higher education in scientific and technical disciplines. Given that subsidy per student in higher education and particularly in scientific and technical subjects was several times that of elementary education,<sup>16</sup> private spending on elementary education ensures much higher benefits from the subsidy on higher education. Further, due to the high private rate of return on higher and technical education and due to low levels of outlay on education by both public and private sectors, an excess demand situation has arisen. Better manipulative skills of the better-off sections ensures that they gain greater access to institutions of higher learning in scientific and technical fields.

The growth rates of per capita expenditures (constant prices) summarised in Table 4.19 show that expenditure on education accelerated significantly from 3.9 per cent in the Seventies to 7.4 per cent in the Eighties. It must however be noted that the increase was mainly due to increase in wages and salaries (7.5 per cent) which account for the lion's share of government expenditure on education, thanks to the bargaining ability of the teacher's unions. It is doubtful whether the availability of educational services registered any improvement over time. The per capita expenditure on medical and public health received a low priority throughout as the average growth rate was constant at 4.4 per cent during both the Seventies and the Eighties. As the relative cost of providing medical and health services too increased over time due to faster increase in rates of staff emoluments than in general income levels, the increase in the availability of medical and health services was perhaps even lower.

Statewise data also show that the largest component of social services was education, followed by health, direct welfare expenditures and water supply (Table 4.20).<sup>17</sup> While the share of the last two have increased over the years, the shares of the first two have fallen. All the same, education and health together still constitute about 70 per cent of the expenditure on social services. We do not attempt to analyse expenditures to meet natural calamities, as no trends can really be expected *a priori*. Housing and urban development are not priority areas as is evident from their shares and we do not discuss them here. The others are discussed at some length below.

**a. Education:** In general, about a half of the government expenditure on social services was accounted for by education alone (Table 4.20). The inter-State variation in the share of

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16. Guhan (1993) has estimated that in Tamil Nadu, the subsidy per student in higher education was eight times that of elementary education.

17. The category education consists of expenditures on elementary, secondary, university and higher, technical, and adult education. Expenditures on health includes those on medical and public health, family welfare, nutrition and sewerage and sanitation. Direct welfare expenditures include those on social security and welfare, welfare of scheduled castes, other backward castes and tribals, and labour and employment.

Table 4.20

## Share of Major Components in Expenditure on Social Services

(per cent)

State	Education			Health			Direct Welfare Activities			Water Supply			Natural Calamity Relief		
	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91
<b>High Income States</b>	<b>51.7</b>	<b>49.8</b>	<b>49.4</b>	<b>20.2</b>	<b>19.8</b>	<b>18.3</b>	<b>9.0</b>	<b>10.4</b>	<b>11.9</b>	<b>5.2</b>	<b>7.1</b>	<b>7.4</b>	<b>4.6</b>	<b>4.2</b>	<b>5.6</b>
Punjab	52.3	56.8	49.6	17.5	19.2	17.7	12.3	11.5	9.7	5.6	4.9	4.8	3.2	2.4	12.1
Haryana	53.7	46.3	48.2	23.4	20.7	16.2	6.8	8.5	18.2	4.8	9.8	9.0	4.1	5.9	3.0
Maharashtra	50.1	48.9	50.1	19.8	19.6	17.5	8.6	10.5	10.5	6.7	8.5	8.8	1.0	1.8	2.3
Gujarat	50.6	47.2	49.8	20.0	19.8	21.9	8.4	11.3	9.3	3.7	5.0	6.7	10.0	6.9	5.0
<b>Middle Income States</b>	<b>52.1</b>	<b>47.7</b>	<b>49.9</b>	<b>21.7</b>	<b>20.7</b>	<b>20.6</b>	<b>11.6</b>	<b>15.4</b>	<b>15.7</b>	<b>4.1</b>	<b>6.3</b>	<b>4.9</b>	<b>3.6</b>	<b>2.9</b>	<b>3.0</b>
Karnataka	52.0	46.8	47.9	22.3	20.7	22.1	10.9	15.7	18.5	5.1	7.2	5.0	1.1	1.2	1.1
West Bengal	46.4	47.0	53.5	25.1	20.8	20.0	11.7	12.6	9.3	2.3	4.0	3.4	4.0	3.6	3.0
Andhra Pradesh	47.5	44.0	44.9	19.3	16.5	17.1	14.8	22.2	23.1	5.6	5.8	5.4	8.0	6.9	4.7
Tamil Nadu	51.0	43.2	46.4	23.7	27.7	25.7	12.0	13.5	14.9	3.4	7.9	6.3	3.6	1.6	1.4
Kerala	63.8	57.5	56.8	18.2	17.9	18.0	8.6	13.1	12.7	4.3	6.5	4.4	1.1	1.2	4.8
<b>Low Income States</b>	<b>53.4</b>	<b>47.6</b>	<b>50.9</b>	<b>20.3</b>	<b>18.5</b>	<b>18.7</b>	<b>10.7</b>	<b>14.5</b>	<b>12.6</b>	<b>7.1</b>	<b>10.3</b>	<b>9.8</b>	<b>3.3</b>	<b>4.4</b>	<b>3.3</b>
Rajasthan	48.8	46.3	48.1	20.2	18.9	19.4	7.0	6.5	5.3	12.8	20.6	18.9	6.7	3.7	4.8
Madhya Pradesh	50.3	44.1	43.3	20.7	19.5	16.4	13.3	18.2	20.9	6.7	11.3	12.1	2.9	1.2	1.4
Uttar Pradesh	59.4	50.2	55.6	20.9	21.0	23.2	10.3	15.4	10.2	4.1	5.6	4.5	1.9	4.4	3.9
Orissa	51.5	41.9	49.6	21.4	18.7	18.3	12.8	14.4	14.4	5.4	7.3	7.4	0.2	10.1	2.4
Bihar*	56.7	55.3	58.0	18.2	14.6	16.3	10.1	17.9	12.1	6.3	6.8	6.4	4.8	2.8	3.8
<b>14 Selected States</b>	<b>52.6</b>	<b>48.1</b>	<b>50.5</b>	<b>20.8</b>	<b>19.8</b>	<b>19.6</b>	<b>10.7</b>	<b>14.2</b>	<b>13.3</b>	<b>5.3</b>	<b>7.6</b>	<b>7.1</b>	<b>3.8</b>	<b>3.7</b>	<b>3.6</b>

\* Averages for the period 1985-91 actually refer to the period 1985-90.

**Table 4.21**  
**Per Capita Expenditure on Education**  
**(in 1981-82 prices)**

State	Average for the Period (Rs.)			Growth Rate (per cent)
	1974-80	1980-85	1985-91	
<b>High Income States</b>	<b>60.7</b>	<b>75.0</b>	<b>109.4</b>	<b>5.7</b>
Punjab	72.8	91.5	125.3	5.1
Haryana	53.6	67.6	102.5	6.0
Maharashtra	56.5	70.6	103.8	5.8
Gujarat	60.0	70.1	106.1	5.8
<b>Middle Income States</b>	<b>55.5</b>	<b>67.0</b>	<b>96.7</b>	<b>5.3</b>
Karnataka	49.1	57.0	88.8	5.6
West Bengal	44.6	60.1	85.5	6.3
Andhra Pradesh	42.4	57.9	79.6	6.1
Tamil Nadu	49.8	59.9	96.5	6.3
Kerala	91.9	99.9	133.0	3.5
<b>Low Income States</b>	<b>37.1</b>	<b>46.2</b>	<b>70.7</b>	<b>6.1</b>
Rajasthan	46.3	55.8	84.7	5.8
Madhya Pradesh	36.4	42.2	64.2	5.4
Uttar Pradesh	32.9	39.6	64.3	6.3
Orissa	41.8	48.5	71.7	5.2
Bihar*	28.2	44.7	64.8	8.4
<b>14 Selected States</b>	<b>45.7</b>	<b>56.6</b>	<b>84.9</b>	<b>5.9</b>

\* The last two columns are based on data excluding 1990-91.

education was very small, although per capita expenditure on education varied significantly between States (Table 4.21), largely due to resource constraints rather than any lack of demand as can be easily verified from the figures for high, middle and low income States. Nevertheless, three exceptions ought to be pointed out. Punjab had a relatively high per capita SDP and a relatively large share of education in SDP; the result was a fairly high level of per capita government expenditure on education (Rs 125 in the period 1985-91, as against the average of Rs. 85 for all the selected States for the same period). Bihar was in the other extreme on both counts, which resulted in very low per capita expenditure (Rs. 65 during 1985-90). The third case is of Kerala, where per capita government expenditure on education was the highest throughout the reference period (Rs. 133 during 1985-91) despite below average per capita SDP for most of the period, mainly due to a very large share of education.

Per capita expenditures on education do not have much to do with the need for the same; its correlation with literacy rate (not reported) turns out to be non-negative (either positive or insignificant). This is not surprising, because the States with low literacy are the ones with low per capita SDP and therefore face severe resource constraints. On the other hand, the more literate States are the ones where the demand for more costly higher education (besides higher demand for all levels of education) is greater; besides, the higher literacy rate is often a result of a large publicly provided education sector, the maintenance of which pushes up the government expenditure on education. It may also be mentioned that it is not only expenditure, as such that shows this pattern; a similar pattern has been noticed in unrecovered costs also (Rao and Mundle, 1992).

The distribution of public expenditure on education among the major subsectors (elementary, secondary, higher and technical) is important for several reasons, the major consideration being equity. Due to widespread poverty, the literacy rate in India, despite improvement over the years, still stands just above 50 per cent. All expenditures on secondary, higher and technical education therefore benefit only half the population at most. Given the high demand for private schools that operate (mostly in urban areas) and the much higher costs of education for the consumers in such schools, it may not be incorrect to surmise that a certain amount of self-selection makes the government expenditure on elementary schooling quite progressive. Further, the social rate of return on primary education is estimated to be the highest (Psacharopoulos, 1988) and hence it is also more efficient to concentrate on primary education.

Table 4.22 gives the share of the subsectors in total expenditure on education. The striking feature of the table is the surprisingly stable shares of the subsectors in total expenditure on education. To focus on elementary education, its share in low income States was larger than the same in the other two groups. The highest share was observed in Bihar and the lowest in Punjab. This does not, however, necessarily imply that the priority accorded to elementary education in Bihar is the highest and in Punjab the lowest. There are several other factors which are relevant: the pay scales of primary school teachers vary across the States, private provision of primary education also varies, and in some States (e.g., Punjab) local bodies play the major role in the provision of elementary education. All the same, it is worth noting that the high income States seem to be shifting attention to the secondary level, probably after the problem of providing elementary education became less acute with the setting up of a large network of primary schools and after gross enrollment ratios at the primary level rose to around or above 100 per cent. The low income States have a long way to go yet. Table 4.23 lists some indicators of the quality of the primary education in the selected States along with the expenditure on primary education per child in the relevant age group. Columns 3-5 clearly show the inadequacy of governmental initiative in providing primary education in the less developed States, particularly in view of the fact that almost all States formally are aiming at universal primary education. Columns 8-13 show the relatively poor quality of education and educational infrastructure in the low income States, and hence the high probability of dropouts; the gross enrollment ratio reported can be thus misleading as an indicator of spread of education.

Table 4.22

## Distribution of Total expenditure on Education Among Sub-Sectors

(per cent)

	Elementary Education			Secondary Education			University & Higher			Technical Education		
	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91
<b>High Income States</b>	<b>45.5</b>	<b>43.6</b>	<b>43.3</b>	<b>39.1</b>	<b>39.5</b>	<b>39.3</b>	<b>10.6</b>	<b>12.3</b>	<b>12.3</b>	<b>2.7</b>	<b>2.8</b>	<b>3.1</b>
Punjab	36.2	35.0	32.7	48.1	49.1	49.1	11.7	12.4	14.1	1.5	1.5	1.9
Haryana	39.1	39.0	41.4	42.6	42.7	38.0	12.7	13.4	14.8	2.4	2.6	3.2
Maharashtra	49.8	46.3	44.3	35.6	35.2	38.3	10.1	14.1	10.6	3.6	3.8	4.1
Gujarat	56.8	54.2	54.7	30.2	30.8	31.6	7.8	9.3	9.6	3.3	3.3	3.2
<b>Middle Income States</b>	<b>49.4</b>	<b>48.3</b>	<b>47.0</b>	<b>30.2</b>	<b>30.0</b>	<b>32.6</b>	<b>15.0</b>	<b>16.4</b>	<b>14.9</b>	<b>3.6</b>	<b>3.4</b>	<b>3.3</b>
Karnataka	54.5	54.7	52.8	22.3	22.3	28.5	16.6	18.4	14.0	3.6	3.2	2.8
West Bengal	41.2	40.5	38.0	37.5	40.8	42.6	15.7	13.7	12.7	3.1	2.4	2.2
Andhra Pradesh	44.4	46.8	45.8	30.9	28.7	28.5	19.7	19.9	20.8	3.2	2.8	3.1
Tamil Nadu	49.7	46.2	46.7	33.7	29.2	34.1	11.6	18.1	13.8	4.2	4.6	3.9
Kerala	57.1	53.4	51.7	26.4	29.3	29.2	11.4	12.1	13.1	3.9	4.0	4.6
<b>Low Income States</b>	<b>51.9</b>	<b>50.6</b>	<b>57.0</b>	<b>30.5</b>	<b>32.1</b>	<b>26.0</b>	<b>12.6</b>	<b>11.8</b>	<b>10.8</b>	<b>2.3</b>	<b>2.3</b>	<b>2.6</b>
Rajasthan	57.0	54.0	53.0	27.9	32.3	32.7	11.7	10.6	9.7	1.1	1.0	1.5
Madhya Pradesh	49.3	47.4	62.1	34.6	35.4	18.0	10.7	11.2	9.8	3.7	3.6	4.3
Uttar Pradesh	51.9	49.1	52.0	33.9	35.1	33.8	10.0	10.1	8.4	2.8	2.8	3.4
Orissa	41.1	41.5	56.2	37.9	37.4	25.0	13.6	14.0	14.4	1.9	2.8	2.6
Bihar*	60.3	61.1	61.6	18.2	20.1	20.5	16.8	13.0	11.8	2.2	1.5	1.3
<b>14 Selected States</b>	<b>50.3</b>	<b>48.7</b>	<b>49.6</b>	<b>32.2</b>	<b>32.7</b>	<b>32.3</b>	<b>12.6</b>	<b>13.6</b>	<b>12.2</b>	<b>3.1</b>	<b>3.0</b>	<b>3.1</b>

\* Averages for the period 1985-91 actually refer to the period 1985-90.

Table 4.23

## Education Statistics -- Statewise

State	Literacy		Expend on Primary			Pupil-Teacher Ratio (Primary) 1978 1986	Per Cent Female Teachers (Primary)		Per Cent Trained Teachers (Primary)		Elementary Schools with		
	Rate (%)	#	Edn per Child of aged 5-9 years (Rs.)				1978	1986	1978	1986	Building (%)	Drinking Water (%)	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
<b>High Income States</b>													
Punjab	48.1	57.1	202	261	355	41	40	54	53	98	99	93.4	90.7
Haryana	43.9	55.3	140	186	313	39	53	35	44	99	99	94.0	73.6
Maharashtra	55.8	63.0	209	253	376	44	42	34	38	88	90	91.2	51.5
Gujarat	52.2	60.9	238	288	464	53	61	39	45	97	99	98.8	64.2
<b>Middle Income States</b>													
Karnataka	46.2	56.0	187	224	340	55	48	27	33	87	91	98.4	53.3
West Bengal	48.6	57.7	129	182	258	36	41	21	20	51	64	88.5	59.9
Andhra Pradesh	35.7	45.1	132	194	265	50	44	29	37	97	97	85.5	36.1
Tamil Nadu	54.4	63.7	199	233	397	42	56	42	40	100	100	94.3	84.9
Kerala	81.6	90.6	426	470	648	41	40	56	61	91	94	96.0	74.6
<b>Low Income States</b>													
Rajasthan	30.1	38.8	174	204	305	59	55	18	23	92	84	92.9	58.0
Madhya Pradesh	34.2	43.5	119	139	290	36	39	18	22	85	69	89.9	36.7
Uttar Pradesh	33.3	41.7	113	128	219	39	41	18	21	95	95	83.0	56.9
Orissa	41.0	48.5	116	140	290	34	39	9	16	76	88	91.0	28.3
Bihar	32.0	38.5	110	178	263	41	60	15	18	92	93	78.9	52.9
INDIA*	43.6	52.1	159	197	302	41	44	27	31	86	87	88.4	50.8

The last two columns refer to the year 1986.

# For Estimated population aged 7 years or more.

\* Figures in columns 7, 8, and 9 are for the selected States only.

Source:

i. Census data.

ii. Budget documents/ Finance Accounts.

iii. Fourth/Fifth All India Educational Survey, NCERT, New Delhi, 1980 and 1989.

Leakages from the system have been, and continue to be one of the major problems in this area, so that expenditures on education do not translate into provision of the service fully. For example, in some States like Kerala and Gujarat, there have been teachers receiving salaries from the State government without doing any teaching at all. Ravishankar (1989) points out leakages from grants to secondary schools in West Bengal, and Sen (1993) discusses the case of primary teachers engaged in other full-time occupations while receiving salaries from the government in remote tribal villages in Orissa. These leakages generally arise due to inadequacies in the schemes involving government spending, and can be tackled simply by proper designing. Since resources are scarce, leakages need to be minimised.

**b. Health:** Life expectancy and infant mortality - two standard indicators of health status - show India to be much worse than several developing countries (especially Sri Lanka), let alone the developed ones (UNDP, 1993). For any welfare state, it is considered almost obligatory to look after the health of its citizens; even the OECD countries, barring the United States, have substantial governmental intervention in the production, provision, and regulation of health services. In India, though private expenditure on health is substantial and probably far higher than the public expenditure, there is a strong case for government expenditure on health services on equity as well as efficiency grounds, due to the high incidence of poverty and the repeated appearance of epidemics with high externalities. The present analysis takes an integrated view of health in that several health-related expenditures are considered together here, as already stated. Operationally, however, there is very little integration of different health related services and that, in fact, is a major weakness of the health policy in India.

The levels of health expenditure in the selected States are given in Table 4.24 along with the growth in health expenditure by the States. As in the case of expenditure on education, it is immediately apparent that the health expenditures are resource constrained. If one looks at an indicator of health status and health expenditure by the government together (Figure 4.5), it is immediately apparent that the two are strongly related. The inequity of the situation is clear; poor States cannot spend much on health and hence their health status is low. Since the role of the Central government in this area is limited, the situation is likely to continue in future as well. The growth of expenditure on health in constant prices was the highest in high income States, though its growth in low income States was marginally faster than in middle income States, so that over time some equalisation between middle and low income States may take place; however, even such a difference in the trend is not significant for Rajasthan and Orissa although their health status is around the bottom of the heap. All this points towards the urgency of optimising the allocation of health expenditure; the lower the amount spent, the better it must be spent. This, however, requires substantial inputs from economic analyses of health services which is still not forthcoming. There are several models of provision of health services working in India in the private sector and among the voluntary agencies. Perhaps the public provision of health could learn from their *modus operandi*.

**Table 4.24**

**Per Capita Expenditure on Health Services  
(in Constant 1981-82 prices)**

(Rs.)

State	Average 1974-80	Average 1980-85	Average 1985-90	Growth Rate(%)
<b>High Income States</b>	<b>13.6</b>	<b>18.8</b>	<b>27.1</b>	<b>7.5</b>
Punjab	17.9	24.4	36.9	7.2
Haryana	14.9	20.7	23.1	4.7
Maharashtra	11.7	17.3	26.1	9.4
Gujarat	14.5	18.0	25.9	6.0
<b>Middle Income States</b>	<b>15.4</b>	<b>19.2</b>	<b>26.0</b>	<b>5.2</b>
Karnataka	12.8	16.5	21.4	4.9
West Bengal	19.4	22.1	26.8	3.3
Andhra Pradesh	13.3	16.7	23.3	5.9
Tamil Nadu	15.3	20.8	27.4	5.9
Kerala	15.3	19.6	34.1	7.3
<b>Low Income States</b>	<b>8.4</b>	<b>11.4</b>	<b>16.2</b>	<b>6.6</b>
Rajasthan	14.5	17.2	23.9	5.0
Madhya Pradesh	8.8	11.6	17.0	6.3
Uttar Pradesh	7.7	11.2	15.1	7.1
Orissa	10.9	15.4	19.0	5.9
Bihar*	5.5	7.3	12.5	8.1
<b>14 Selected States</b>	<b>11.9</b>	<b>15.6</b>	<b>21.7</b>	<b>6.2</b>

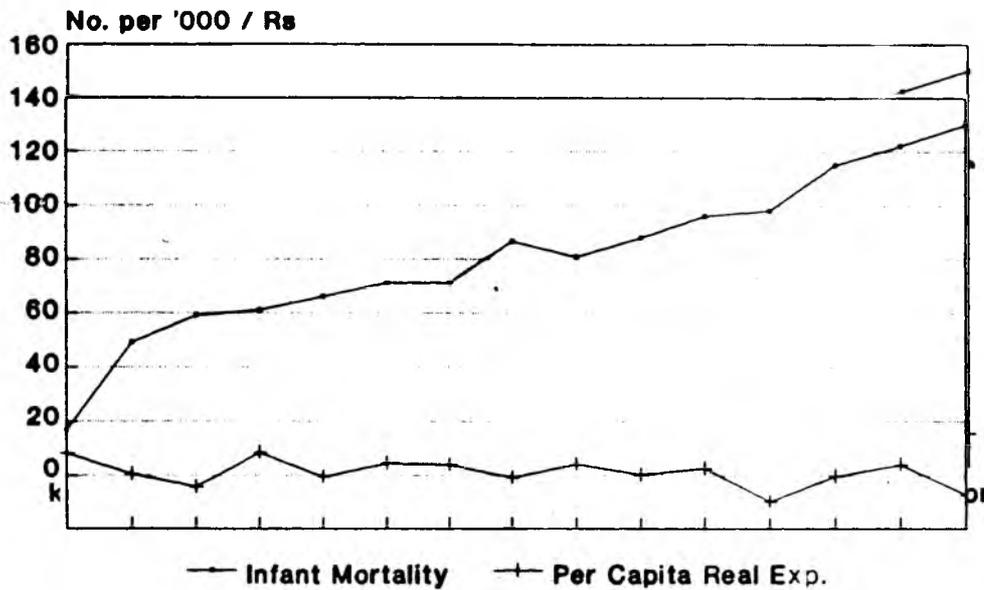
\* The last two columns are based on data excluding 1990-91.

Family welfare is a major component of health expenditures as we have defined it, and expenditure on this head is extremely important for the country due to the urgency of the need to bring down the growth of population. The fact that the decadal growth rate for the period 1980-90 does not show any appreciable fall from the same for the previous decade underlines the need to reconsider the strategy for population control programme. Even the preliminary studies in this area<sup>18</sup> suggest a strong relationship between basic education -- particularly of women -- and family planning, which reinforces the arguments for emphasis on primary education and reduction of illiteracy. Further, preventive health services assume significance due to the observed relationship between infant mortality rates and use of family planning methods. To reduce infant mortality, it is necessary to install a wide network of minimum

18. Berman and Khan (1992) provides a fair sample of these.

**Figure 4.5**

## Health Expenditure and Need (1980-81)



## Health Expenditure and Need (1987-88)

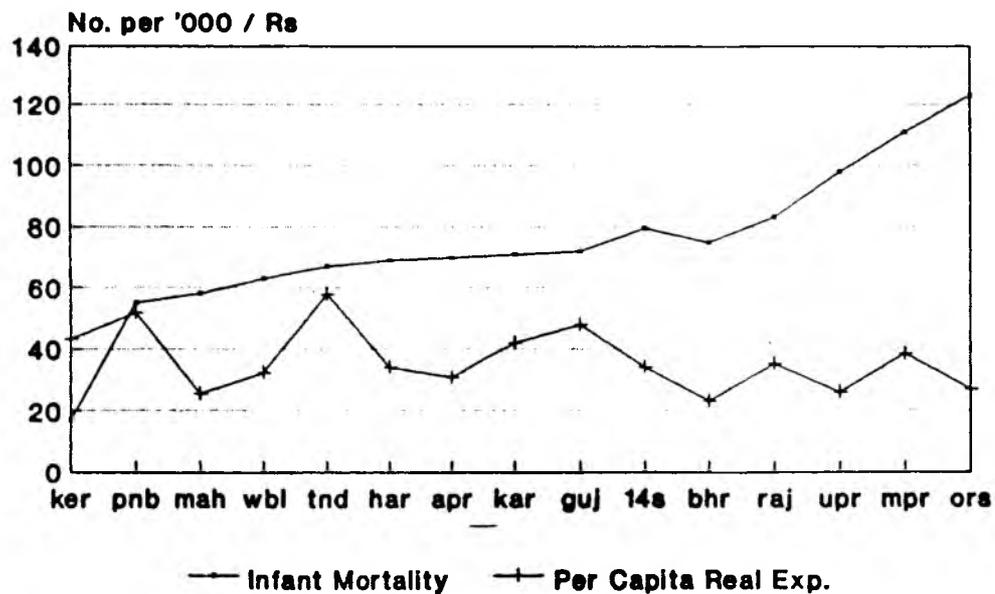


Table 4.25

## Share of Selected Economic Categories in Total Health Expenditure

(per cent)

State	Salaries and Wages				Net Government Maintenance				Capital Expenditure (Building & Mach.)			
				Growth				Growth				Growth
	1974-80	1980-85	1985-90	1974-90	1974-80	1980-85	1985-90	1974-90	1974-80	1980-85	1985-90	1974-90
<b>High Income</b>												
<b>States</b>	<b>50.9</b>	<b>50.0</b>	<b>51.9</b>	<b>9.9</b>	<b>20.8</b>	<b>18.8</b>	<b>17.2</b>	<b>9.6</b>	<b>7.3</b>	<b>8.0</b>	<b>6.6</b>	<b>8.7</b>
Punjab	62.3	65.1	60.0	9.1	19.9	21.4	27.0	12.5	14.2	11.6	10.5	6.3
Haryana	52.5	65.1	74.4	10.9	25.5	17.2	18.4	4.5	15.6	12.5	5.0	-3.7
Maharashtra	53.2	47.8	45.0	10.1	15.2	18.3	14.8	5.9	4.8	6.7	6.9	17.5
Gujarat	42.7	38.7	51.5	10.0	23.9	16.4	14.1	3.5	3.1	6.3	3.6	6.9
<b>Middle Income</b>												
<b>States</b>	<b>54.3</b>	<b>58.4</b>	<b>62.8</b>	<b>8.9</b>	<b>30.5</b>	<b>26.5</b>	<b>22.1</b>	<b>3.6</b>	<b>10.8</b>	<b>8.9</b>	<b>5.7</b>	<b>0.7</b>
Karnataka	60.8	62.2	48.1	4.5	25.5	25.7	18.5	1.9	10.3	7.6	4.5	-0.6
West Bengal	49.1	57.9	62.7	8.3	30.9	25.2	26.9	3.9	18.4	10.5	7.8	-3.1
Andhra Pradesh	53.1	59.7	65.7	10.3	31.3	25.7	16.3	1.0	4.9	3.9	2.5	0.7
Tamil Nadu	53.0	49.2	64.3	9.6	33.9	32.7	24.9	4.3	9.8	14.0	7.9	4.8
Kerala	66.4	74.6	70.6	10.2	27.2	18.7	21.7	4.9	3.3	4.7	4.7	11.7
<b>Low Income</b>												
<b>States</b>	<b>60.4</b>	<b>59.4</b>	<b>66.8</b>	<b>10.0</b>	<b>28.9</b>	<b>28.5</b>	<b>20.6</b>	<b>6.0</b>	<b>6.7</b>	<b>8.3</b>	<b>8.7</b>	<b>11.7</b>
Rajasthan	62.9	68.1	70.9	8.9	31.2	22.9	16.8	2.3	4.8	4.7	8.4	12.7
Madhya Pradesh	61.7	61.2	70.7	10.3	28.0	31.8	21.2	5.7	7.2	4.6	5.4	4.7
Uttar Pradesh	56.4	50.2	59.6	10.0	32.9	34.7	26.4	7.8	5.7	11.5	11.4	17.4
Orissa	63.3	62.4	80.3	10.0	27.2	24.4	12.8	0.7	3.6	9.5	4.1	13.3
Bihar	62.8	68.2	65.6	11.0	19.2	18.4	16.6	9.4	12.7	8.3	10.1	8.5
<b>14 Selected</b>												
<b>States</b>	<b>55.4</b>	<b>56.7</b>	<b>61.5</b>	<b>9.5</b>	<b>28.0</b>	<b>25.4</b>	<b>20.4</b>	<b>5.2</b>	<b>8.7</b>	<b>8.5</b>	<b>7.0</b>	<b>5.9</b>

medical and paramedical services in the villages. The primary health centres, meant to be the first level medical facility for the rural population, have become primarily family planning centres, losing credibility in the process. An overriding concern for population control is thus proving self-defeating to some extent. Another related factor is nutrition. While this is assuming increasing importance in some States, the programmes are non-selective and because of that, often inadequate. The existing nutrition programmes rightly concentrate on children, but wrongly ignore the vital role that nutrition of pregnant women plays in infant mortality. Even this brief discussion here points to the complex interrelationships between various components of health expenditure, education, and family planning, and to the mistake in trying to sell family planning directly like a consumer durable.

A look at the economic classification of the expenditure on health shows that (Table 4.25) the largest share of the expenditure has been for wages and salaries (50-60 per cent); further, this is the fastest growing component as well. Two exceptions must be noted -- Karnataka actually showed a smaller share of wages and salaries in successive periods with a growth rate of only 4.5 per cent, while in Punjab the share went up in the second period and then fell in the third period; the growth rate in Punjab (9.1 per cent per annum) was not much lower than the average (9.5 per cent), but net government maintenance grew faster in Punjab. The case of Karnataka probably shows a gradual reduction of State-level provision of health services and transfer of the same to others including local bodies; this conjecture is supported by a very low growth of net government maintenance and a fall in capital expenditure also. Net government maintenance, which would include the expenditure on consumables including drugs, claimed only about 20-25 per cent of the total expenditure; this share showed a fall over the years in every State except Punjab. As far as capital expenditure on major assets (building and machinery) are concerned, the patterns varied widely between States, with Uttar Pradesh and Maharashtra exhibiting a similar growth rate of above 17 per cent while Haryana and West Bengal showed a growth rate of less than -3 per cent. It is unlikely that these trends are the outcome of a well thought out policy regarding the optimal combination of various inputs to provide the most cost effective medical care; the observed increase in the share of wages and salaries, apparently at the cost of both net government maintenance (including expenditure on drugs and medical consumables) as well as capital formation in this sector may thus represent a movement away from the optimum.

**c. Direct Welfare Activities:** The expenditure on this head is essentially in the nature of social security and social welfare. These have been targeted to specific groups like scheduled castes, scheduled tribes, widows, destitutes, unemployed persons etc. In terms of the terminology adopted by Dreze and Sen (1989), these include both protective (pensions to destitute widows) and promotional [welfare of scheduled castes (SC), scheduled tribes (ST) and other backward classes (OBC)] expenditures. A large part of the expenditures included under rural development would also be social welfare expenditure by their definition, while the entire expenditure on relief from natural calamities would probably be included under protective social welfare

Table 4.26

## Expenditure on Direct Welfare Activities

	Percentage SC/ST		Share in Total Expenditure (per cent)			Per Capita Expenditure in 1981-82 prices (Rs.)			
	1981	1991	Average	Average	Average	Average	Average	Average	Growth Rate(%)
			1974-80	1980-85	1985-91 <sup>e</sup>	1974-80	1980-85	1985-91	
<b>High Income States</b>	<b>19.4</b>	<b>20.0</b>	<b>2.8</b>	<b>3.2</b>	<b>3.5</b>	<b>10.9</b>	<b>15.8</b>	<b>26.6</b>	<b>8.5</b>
Punjab	26.9	28.3	3.9	3.4	3.0	17.3	18.5	24.2	3.6
Haryana	19.1	19.7	1.6	2.3	5.7	6.8	12.6	40.5	16.6
Maharashtra	16.3	18.4	2.6	3.0	3.3	9.7	15.4	21.7	7.7
Gujarat	21.4	19.1	2.9	3.6	3.2	10.0	16.5	19.9	6.8
<b>Middle Income States</b>	<b>20.9</b>	<b>21.3</b>	<b>4.3</b>	<b>6.0</b>	<b>6.1</b>	<b>11.9</b>	<b>21.3</b>	<b>29.9</b>	<b>8.7</b>
Karnataka	20.0	20.4	3.4	5.0	6.6	10.6	19.1	34.1	11.7
West Bengal	27.6	28.1	4.5	5.3	3.7	11.3	15.9	14.7	2.9
Andhra Pradesh	20.8	20.7	4.7	8.3	8.3	13.6	29.7	40.7	10.6
Tamil Nadu	19.4	20.1	4.4	4.9	5.9	11.6	18.8	30.5	8.5
Kerala	11.0	10.8	3.9	6.0	5.5	12.5	22.7	29.6	8.2
<b>Low Income States</b>	<b>26.6</b>	<b>25.0</b>	<b>3.9</b>	<b>6.0</b>	<b>5.1</b>	<b>7.6</b>	<b>13.7</b>	<b>17.4</b>	<b>7.8</b>
Rajasthan	29.2	26.8	2.4	2.3	2.0	6.7	7.7	9.3	3.5
Madhya Pradesh	36.3	32.3	4.1	5.3	7.3	9.8	17.6	30.9	10.9
Uttar Pradesh	21.2	21.1	2.8	4.6	3.2	6.0	12.0	11.6	7.3
Orissa	37.1	34.9	4.1	5.2	4.8	10.4	16.5	20.7	6.0
Bihar*	22.8	21.3	3.1	6.2	4.2	5.3	14.6	13.4	10.9
<b>14 Selected States</b>	<b>23.2</b>	<b>22.8</b>	<b>3.5</b>	<b>4.7</b>	<b>4.7</b>	<b>9.4</b>	<b>16.6</b>	<b>22.3</b>	<b>8.3</b>

\* The expenditure figures do not include those for 1990-91.

spending. Most of the present expenditure category are transfer payments, although certain plan schemes (Tribal Sub-Plan combines schemes meant for the ST falling in various functional categories; Special Component Plan similarly is for the SC) in these areas involve real transactions. In the absence of any effective social security net, and given the clear handicaps faced by the target groups, these are considered necessary. It follows that the States which have a greater percentage of the target groups in their population ought to spend a larger portion of their total spending on these programmes. However, despite encouragement from the Planning Commission, we find that neither the expenditure shares nor the per capita expenditures are positively related to the percentage of scheduled castes and scheduled tribes (the only target groups on which reliable Statewise data are available) in the total population of the State (Table 4.26). Tamil Nadu and Kerala appear to devote a greater part of their expenditures to direct social welfare activities than is warranted going by the average trend; that is probably because

**Table 4.27****Expenditure on Welfare of SC/ST/OBC  
Per Head of SC/ST Population in 1981-82 Prices**

(Rs.)

	1980-81	1990-91
<b>High Income States</b>	<b>33.9</b>	<b>29.2</b>
Punjab	33.3	14.3
Haryana	20.5	16.5
Maharashtra	32.6	30.2
Gujarat	40.7	43.5
<b>Middle Income States</b>	<b>49.8</b>	<b>41.7</b>
Karnataka	34.4	45.7
West Bengal	21.0	12.0
Andhra Pradesh	87.6	81.2
Tamil Nadu	56.0	37.4
Kerala	74.3	53.1
<b>Low Income States</b>	<b>24.9</b>	<b>20.2</b>
Rajasthan	15.2	10.7
Madhya Pradesh	33.7	48.1
Uttar Pradesh	30.5	16.1
Orissa	23.9	21.2
Bihar	12.8	10.4
<b>14 Selected States</b>	<b>34.1</b>	<b>28.5</b>

*Note:* The expenditure data are for the fiscal year 1980-81 and 1990-91 while the SC/ST population are taken from the Census data and relate to the years 1981 and 1991.

of their additional emphasis on various social security schemes not confined to particular groups but for individuals meeting given criteria (e.g., pensions for widows). The growth of direct welfare expenditures (above 8 per cent per annum for all selected States together over the whole reference period) in general has been higher than in areas like education and health, although there should be some overlap in the effects of all three. This is not necessarily a welcome trend, because given the inadequacies of the administrative machinery and the lack of consciousness regarding their dues among the beneficiaries, chances of leakage are higher in the case of expenditures of this kind. Further, because of the huge size of the target groups and the paucity of resources, the welfare spendings get spread over very thinly, especially in the States where the SC/ST population is large; typically, these States are low income States with poor resource base. As a result, the social welfare expenditure per head of the intended beneficiaries is so small (Table 4.27) that it would take a diehard optimist to believe that they can have any significant impact on the problem sought to be addressed. Tamil Nadu and Kerala, for example,

significant impact on the problem sought to be addressed. Tamil Nadu and Kerala, for example, have a large number of social welfare schemes, but Table 4.26 shows per capita expenditure in these States to be less than in Andhra Pradesh and Madhya Pradesh during the period 1985-86 to 1990-91. It is then easy to deduce how effective the various schemes would be in providing social welfare. Expenditure on the welfare of SC/ST per head also fell in all the selected States barring Gujarat, Karnataka and Madhya Pradesh, although the figure for Andhra Pradesh was much higher than for any other State even after a fall. However, given their popular appeal, one might consider these as a part of the expenditures incurred to maintain stability needed by the various pressure groups to be able to enjoy the fruits of their efforts, without really making a serious attempt to achieve a reasonable degree of social security.

**Table 4.28**

**Expenditure on Water Supply**

State	Share in Social Services (%)			Per Capita in 1981-82 prices (Rs.)			
	Average 1974-80	Average 1980-85	Average 1985-91	Average 1974-80	Average 1980-85	Average 1985-91	Growth Rate(%)
<b>High Income States</b>	<b>5.6</b>	<b>7.2</b>	<b>7.7</b>	<b>6.6</b>	<b>10.8</b>	<b>16.2</b>	<b>8.4</b>
Punjab	5.6	4.9	4.8	8.0	7.9	12.0	4.6
Haryana	4.8	9.8	9.0	5.1	14.5	18.5	14.9
Maharashtra	6.7	8.5	8.8	7.6	12.6	17.9	7.6
Gujarat	3.7	5.0	6.7	4.5	7.5	14.2	11.5
<b>Middle Income States</b>	<b>4.0</b>	<b>6.2</b>	<b>5.0</b>	<b>4.1</b>	<b>8.5</b>	<b>9.2</b>	<b>7.6</b>
Karnataka	5.1	7.2	5.0	4.9	8.9	9.1	5.6
West Bengal	2.3	4.0	3.4	2.3	5.1	5.4	8.9
Andhra Pradesh	5.6	5.8	5.4	5.0	7.6	9.6	6.0
Tamil Nadu	3.4	7.9	6.3	3.3	11.5	13.1	13.9
Kerala	4.3	6.5	4.4	6.0	11.4	10.2	19.6
<b>Low Income States</b>	<b>6.6</b>	<b>9.4</b>	<b>9.1</b>	<b>4.3</b>	<b>8.6</b>	<b>11.8</b>	<b>10.0</b>
Rajasthan	12.8	20.6	18.9	12.2	25.1	32.7	9.2
Madhya Pradesh	6.7	11.3	12.1	4.9	10.7	17.7	12.3
Uttar Pradesh	4.1	5.6	4.5	2.4	4.5	5.3	6.9
Orissa	5.4	7.3	7.4	4.4	8.5	10.6	8.2
Bihar	6.3	6.8	6.4	3.2	5.4	7.0	8.3
<b>14 Selected States</b>	<b>5.3</b>	<b>7.6</b>	<b>7.1</b>	<b>4.7</b>	<b>9.0</b>	<b>11.8</b>	<b>8.8</b>

**d. Water Supply:** This is an area which has been assuming greater significance in recent years due to the emphasis put by the Planning Commission on assured drinking water supply and the strains on the urban water supply systems throughout the country (especially in the larger cities) with which the local bodies are unable to cope, with the limited finances at their disposal. The expenditure of all selected States together in constant prices rose by about 11 per cent per annum during the reference period, which is the highest growth rate among the components of social services. Per capita expenditure in constant prices also rose from Rs. 3.60 in 1974-75 to Rs. 10.60 in 1984-85 and to Rs. 11.30 in 1990-91 for all the selected States together. The variations in this amount between the States (Table 4.28) can be hypothesised to depend primarily on cost factors besides resource availability, as is indicated by the consistently high figures for Rajasthan, as a part of the State is covered by desert. Uttar Pradesh, Bihar and West Bengal, with several natural and low-cost man-made sources of water (being in the Gangetic basin), show the lowest per capita expenditures on this head.

Several States have formed autonomous bodies to look after water supply in the State, partly or fully. The reason is not entirely clear, as economies of scale could be reaped by a departmental organisation also. The reason could lie in (a) the relative ease of raising debt capital and (b) less opposition from local bodies when the function of water supply is withdrawn from them and given to an autonomous body specially formed for that purpose, as compared to when it is taken over by the State government. From available accounts, the autonomy of these bodies are, however, much circumscribed.

#### **4.5.5 Economic Services**

In the budgetary classification, economic services contain most of the infrastructural services while social services contain those relevant to human capital formation. Further, economic services also contain all the expenditures on direct poverty alleviation programmes. Hence, expenditure on this broad category is vitally important for the long run economic development as well as removal of poverty. For infrastructural services, revenue expenditures roughly denote maintenance and running expenses while capital expenditures indicate investments, so that for specific services these figures give an approximate idea of availability and upkeep.

The States' share of expenditure on economic services in 1990-91 was about 55 per cent. The spending on economic services constituted about a third of total expenditures of the States. The share of expenditures on economic services in total expenditures of the States increased in the Seventies, but showed a steady decline from 38 per cent in 1980-81 to 33 per cent in 1990-91. The shares of both revenue and capital expenditures under economic services declined from 1980-81 but the decline in capital expenditures was much sharper than in revenue expenditures.

**Table 4.29**

**Per Capita Expenditure on Economic Services: in 1981-82 prices**

(Rs.)

	Revenue Expenditure				Capital Expenditure				Total Expenditure			
	Average 1974-80	Average 1980-85	Average 1985-91	Average Growth Rate(%)	Average 1974-80	Average 1980-85	Average 1985-91	Average Growth Rate(%)	Average 1974-80	Average 1980-85	Average 1985-91	Average Growth Rate(%)
<b>High Income States</b>	<b>101</b>	<b>139</b>	<b>182</b>	<b>5.8</b>	<b>54</b>	<b>64</b>	<b>56</b>	<b>1.0</b>	<b>155</b>	<b>203</b>	<b>239</b>	<b>4.5</b>
Punjab	102	119	154	4.2	48	57	44	N.C.	150	176	198	3.2
Haryana	125	162	202	4.7	71	78	58	-1.6	196	240	259	3.1
Maharashtra	104	159	204	6.8	50	61	64	2.7	154	220	268	5.5
Gujarat	74	116	169	8.0	46	61	61	3.1	119	178	229	6.4
<b>Middle Income States</b>	<b>60</b>	<b>81</b>	<b>113</b>	<b>6.2</b>	<b>32</b>	<b>33</b>	<b>34</b>	<b>1.3</b>	<b>92</b>	<b>113</b>	<b>148</b>	<b>4.8</b>
Karnataka	73	92	127	5.4	44	47	49	1.6	117	139	177	4.2
West Bengal	50	60	82	5.5	17	15	21	2.3	67	75	104	4.7
Andhra Pradesh	62	89	137	7.8	52	43	43	-1.1	114	132	180	4.7
Tamil Nadu	62	94	133	7.1	15	20	18	1.9	77	115	151	6.3
Kerala	52	68	88	5.0	32	37	39	2.9	84	106	126	4.2
<b>Low Income States</b>	<b>53</b>	<b>67</b>	<b>93</b>	<b>5.5</b>	<b>37</b>	<b>47</b>	<b>50</b>	<b>2.9</b>	<b>90</b>	<b>114</b>	<b>143</b>	<b>4.5</b>
Rajasthan	65	74	119	5.7	41	46	40	0.2	106	120	159	3.9
Madhya Pradesh	55	84	106	6.5	39	50	56	3.7	94	134	161	5.5
Uttar Pradesh	52	64	92	5.7	32	40	45	3.2	84	104	137	4.9
Orissa	65	67	92	3.7	43	63	77	6.0	108	131	168	4.7
Bihar*	27	47	67	8.4	31	36	39	2.2	59	83	106	5.6
<b>14 Selected states</b>	<b>63</b>	<b>86</b>	<b>120</b>	<b>6.4</b>	<b>37</b>	<b>43</b>	<b>45</b>	<b>2.3</b>	<b>99</b>	<b>129</b>	<b>165</b>	<b>5.1</b>

N.C. Not computed due to wide fluctuations in the basic data.

\* Averages for the period 1985-91 and the growth rates do not include figures for 1990-91.

Table 4.29 shows per capita expenditures in constant prices on total economic services averaged over three periods as in the preceding section, along with the growth rate for the whole reference period; the figures are given for revenue, capital and total expenditures. It is immediately apparent that while revenue expenditures have generally grown fast, capital expenditures have stagnated, and in some cases, fallen. We shall examine, in the following, particular services where the fall has been particularly sharp; for the moment, it would suffice to note that more than half the capital expenditures of the States are accounted for by economic services, and the stagnation in the former can therefore be traced to the latter.

Table 4.30 gives the share of major components of economic services by budgetary classification. The largest share in government expenditure was usually that of agriculture-related services as a group -- agriculture and allied services, irrigation and rural development;

Table 4.30

## Share of Major Components in Total Expenditure on Economic Services

(per cent)

States	Agriculture and Allied			Irrigation			Industries and Minerals			Energy		
	Average	Average	Average	Average	Average	Average	Average	Average	Average	Average	Average	
	1974-80	1980-85	1985-91	1974-80	1980-85	1985-91	1974-80	1980-85	1985-91	1974-80	1980-85	1985-91
<b>High Income</b>	<b>20.6</b>	<b>19.3</b>	<b>21.3</b>	<b>29.7</b>	<b>27.8</b>	<b>24.1</b>	<b>4.7</b>	<b>4.0</b>	<b>3.9</b>	<b>3.0</b>	<b>4.7</b>	<b>5.2</b>
Punjab	17.3	13.2	17.8	27.1	28.9	31.9	7.7	5.2	7.7	1.6	3.7	5.1
Haryana	11.6	12.2	14.9	32.3	27.8	24.0	3.3	3.7	3.0	5.4	3.1	6.3
Maharashtra	26.8	25.2	26.2	24.5	23.5	20.6	4.3	3.2	2.3	4.0	7.3	5.5
Gujarat	13.2	12.5	15.0	43.2	36.9	29.2	5.1	5.3	6.4	0.2	0.3	4.0
<b>Middle Income</b>	<b>19.6</b>	<b>17.6</b>	<b>17.7</b>	<b>29.4</b>	<b>24.8</b>	<b>19.5</b>	<b>9.6</b>	<b>9.2</b>	<b>8.6</b>	<b>4.5</b>	<b>4.9</b>	<b>6.0</b>
Karnataka	17.3	17.3	17.2	34.3	31.2	26.1	16.1	12.2	11.6	1.2	0.5	3.4
West Bengal	27.6	24.0	20.7	26.9	22.9	17.5	6.3	7.4	7.5	0.0	2.1	7.3
Andhra Pradesh	14.1	10.9	11.5	37.7	32.6	24.2	7.1	6.5	6.1	9.7	8.6	2.9
Tamil Nadu	21.5	19.9	22.6	15.6	10.5	8.2	8.9	11.0	9.9	4.8	8.6	13.5
Kerala	23.3	21.9	23.2	25.1	25.1	19.8	10.3	9.4	10.0	3.0	0.0	0.1
<b>Low Income</b>	<b>16.9</b>	<b>15.4</b>	<b>16.5</b>	<b>40.6</b>	<b>37.0</b>	<b>29.8</b>	<b>5.5</b>	<b>6.7</b>	<b>6.2</b>	<b>1.2</b>	<b>1.9</b>	<b>3.8</b>
Rajasthan	12.5	11.7	14.3	41.1	35.3	30.0	7.9	7.7	6.3	0.4	2.9	1.9
Madhya Pradesh	33.1	27.2	26.9	34.5	34.8	31.4	2.7	3.7	3.8	3.8	5.4	5.8
Uttar Pradesh	11.1	10.0	12.1	40.1	34.6	26.7	6.8	8.5	7.5	0.1	0.2	2.0
Orissa	17.6	16.6	17.4	42.8	44.1	28.7	4.1	7.4	9.0	3.2	0.2	10.6
Bihar	14.6	13.9	14.4	47.1	41.2	37.8	4.5	5.6	4.9	0.0	1.1	2.1
<b>14 Selected States</b>	<b>18.9</b>	<b>17.3</b>	<b>18.3</b>	<b>33.8</b>	<b>30.5</b>	<b>24.9</b>	<b>6.6</b>	<b>6.6</b>	<b>6.3</b>	<b>2.8</b>	<b>3.7</b>	<b>4.9</b>

Contd.

Table 4.30 (Contd.)

## Share of Major Components in Total Expenditure on Economic Services

(per cent)

States	Transport			Food and Civil Supplies			Rural Development			Cooperation		
	Average	Average	Average	Average	Average	Average	Average	Average	Average	Average	Average	Average
	1974-80	1980-85	1985-91	1974-80	1980-85	1985-91	1974-80	1980-85	1985-91	1974-80	1980-85	1985-91
<b>High Income</b>	<b>18.2</b>	<b>16.4</b>	<b>13.1</b>	<b>1.8</b>	<b>1.5</b>	<b>0.2</b>	<b>11.6</b>	<b>15.4</b>	<b>15.2</b>	<b>2.1</b>	<b>2.0</b>	<b>2.8</b>
Punjab	34.7	31.2	27.2	1.7	3.4	-10.5	3.3	6.6	6.6	2.8	4.0	2.9
Haryana	31.7	31.4	30.4	-0.9	2.2	-1.3	5.0	7.0	8.9	2.2	1.4	2.0
Maharashtra	10.0	8.7	7.2	2.4	1.5	1.0	15.9	18.8	18.3	1.7	2.1	3.6
Gujarat	19.8	19.1	12.9	0.2	0.1	1.4	10.9	16.3	14.8	2.1	1.1	1.8
<b>Middle Income</b>	<b>15.0</b>	<b>13.9</b>	<b>10.4</b>	<b>1.6</b>	<b>2.9</b>	<b>6.4</b>	<b>10.7</b>	<b>17.0</b>	<b>19.7</b>	<b>2.8</b>	<b>3.0</b>	<b>3.4</b>
Karnataka	10.5	11.2	9.9	0.9	-0.0	0.4	5.7	12.6	15.8	2.5	2.6	4.3
West Bengal	16.9	19.9	12.6	4.2	2.5	2.0	12.2	15.9	26.5	2.2	2.1	2.9
Andhra Pradesh	12.9	9.8	6.3	1.0	5.7	13.2	8.1	16.7	20.3	2.7	1.8	2.3
Tamil Nadu	19.1	15.4	10.9	2.4	3.4	8.6	17.1	21.3	17.6	4.0	5.3	4.1
Kerala	19.1	17.7	19.4	-1.1	-0.3	-0.1	13.3	18.8	18.3	2.7	3.5	4.4
<b>Low Income</b>	<b>12.8</b>	<b>13.4</b>	<b>11.8</b>	<b>0.3</b>	<b>1.2</b>	<b>0.9</b>	<b>16.3</b>	<b>19.0</b>	<b>23.4</b>	<b>2.3</b>	<b>1.9</b>	<b>2.6</b>
Rajasthan	13.3	17.0	14.1	0.8	0.8	0.4	11.5	13.5	21.9	2.8	1.8	2.2
Madhya Pradesh	14.3	13.5	11.9	0.6	0.8	0.8	7.8	11.9	15.0	2.3	2.0	3.5
Uttar Pradesh	12.3	14.5	12.7	-0.9	1.6	0.9	25.3	24.5	28.6	1.4	0.9	1.4
Orissa	12.3	11.9	11.0	1.5	1.9	1.3	8.3	12.4	16.3	3.8	3.7	3.1
Bihar	12.1	9.5	7.5	1.4	0.7	0.8	15.6	24.4	27.4	3.0	2.5	3.5
<b>14 Selected States</b>	<b>15.0</b>	<b>14.5</b>	<b>11.7</b>	<b>1.2</b>	<b>1.8</b>	<b>2.4</b>	<b>13.2</b>	<b>17.3</b>	<b>19.7</b>	<b>2.4</b>	<b>2.3</b>	<b>2.9</b>

within the group, one of the first two claimed the largest share in almost all the States. The next in terms of expenditure share was transport; in Punjab and Haryana, transport actually claimed the largest share, perhaps because both the States are agriculturally developed, with good irrigation network, and a relatively small number of rural poor. None of the other functional categories were very important in terms of expenditure share, including a vital infrastructural service like power. Of course, one of the reasons for State level government expenditure on power being relatively small is that the true expenditure on power does not show up in the departmental expenditures, due to the existence of State electricity boards which can borrow (usually with State government guarantee) independently, and the fact that budgetary supports may flow through loans and advances for which we do not have functional break up. A similar underestimation can be expected wherever the State road transport service was provided through a non-departmental organisation.

Economic classification of expenditure on economic services<sup>19</sup> reveals some interesting facts. Table 4.31 gives the share of major economic categories in the total expenditure on economic services. These are summarised below:

(i) The largest share of expenditure on major economic services was incurred in the form of loans and advances, usually to the State electricity boards and road transport undertakings. Their share, however, has been falling steadily, and though their share is still the largest in high income and middle income States on an average, in low income States the share was not the highest for the period 1985-86 to 1989-90. Among individual States, the highest share of loans and advances was seen in Punjab in all the three periods, and what is more, was rising steadily in contrast to the general trend. Among high income and middle income States, Maharashtra, Gujarat and Tamil Nadu did not spend the largest part of their expenditure by giving loans and advances.

(ii) The share of subsidies exhibited continuous increase in all States except West Bengal, Andhra Pradesh and Rajasthan; even in these three States, subsidies claimed a larger share in the last period than in the first period. The States where loans and advances did not claim the largest share of the expenditure, it was subsidies that did so. It underlines the need to contain subsidies if expenditure growth is to be contained, necessitating an examination of the issues of efficiency and equity of subsidies. The political economy of subsidies becomes important by association, as the institutional structure that generates these subsidies must be understood for a reform programme at the State level to succeed. This is thus an area that needs to be studied in depth.

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19. The definition of economic services used in the figures supplied by C.S.O. are based on UN-SNA, and are different from the budgetary classification. For example, in the budgetary classification, water supply is taken as a part of the social services while in the economic classification, it is included in economic services and forms a part of utilities like gas and electricity. Economic services here include agriculture and allied services, mining, manufacturing and construction, electricity, gas, steam and water supply, and transport and communication.

**Table 4.31**  
**Share of Economic Categories in Expenditure on Major Economic Services**  
**(Annual Average for the Period)**

(Per cent)

State	Wages and Salaries			Net Govt. Maintenance			Subsidy			Tot Transfer (Rev+Cap)			Capital Expenditure			Loans and Advances		
	74-80	80-85	85-90	74-80	80-85	85-90	74-80	80-85	85-90	74-80	80-85	85-90	74-80	80-85	85-90	74-80	80-85	85-90
<b>High Income States</b>	<b>8.2</b>	<b>7.1</b>	<b>7.3</b>	<b>4.9</b>	<b>6.5</b>	<b>6.7</b>	<b>9.9</b>	<b>18.1</b>	<b>23.5</b>	<b>13.5</b>	<b>15.9</b>	<b>16.1</b>	<b>15.5</b>	<b>14.3</b>	<b>11.8</b>	<b>41.8</b>	<b>33.7</b>	<b>28.9</b>
Punjab	7.6	7.1	7.2	3.6	6.2	4.3	8.6	13.3	10.3	5.6	1.8	5.5	21.5	10.5	9.3	46.4	55.1	58.8
Haryana	7.9	7.6	12.2	8.7	4.8	9.4	12.8	20.6	24.7	7.0	15.8	9.3	17.6	15.8	7.5	41.5	31.7	33.8
Maharashtra	9.1	7.4	8.6	4.9	5.8	5.1	10.4	22.6	29.7	14.6	16.3	19.9	11.2	16.8	12.6	42.6	27.7	20.3
Gujarat	7.5	6.5	4.4	4.1	8.9	9.4	8.9	11.7	22.7	19.7	24.0	20.1	18.1	11.1	14.0	36.6	33.0	19.5
<b>Middle Income States</b>	<b>11.3</b>	<b>11.4</b>	<b>11.5</b>	<b>10.7</b>	<b>10.0</b>	<b>8.5</b>	<b>12.1</b>	<b>17.2</b>	<b>22.2</b>	<b>9.0</b>	<b>14.3</b>	<b>18.2</b>	<b>15.8</b>	<b>14.1</b>	<b>9.0</b>	<b>31.7</b>	<b>28.1</b>	<b>24.8</b>
Karnataka	11.4	11.9	8.7	8.5	8.5	4.3	14.0	19.4	20.8	2.5	5.8	22.0	18.2	15.6	5.9	36.3	31.9	33.7
West Bengal	13.2	12.2	15.3	15.4	11.0	11.9	8.4	14.8	13.1	3.7	10.7	14.8	19.4	19.2	14.5	38.4	33.6	21.0
Andhra Pradesh	8.9	11.1	11.2	8.5	10.5	10.4	16.5	27.7	20.7	16.5	25.6	27.9	7.9	6.2	5.6	26.3	11.2	17.8
Tamil Nadu	11.2	8.6	9.4	9.2	8.3	7.3	9.1	10.8	33.7	12.8	15.5	11.8	17.6	11.1	7.6	32.1	40.7	27.7
Kerala	14.6	19.0	16.7	15.3	16.6	10.7	10.2	10.6	12.4	3.6	9.0	16.4	21.4	29.0	15.7	22.5	9.1	20.4
<b>Low Income States</b>	<b>12.9</b>	<b>12.0</b>	<b>13.7</b>	<b>8.4</b>	<b>8.9</b>	<b>7.8</b>	<b>7.7</b>	<b>13.6</b>	<b>18.8</b>	<b>8.0</b>	<b>10.9</b>	<b>13.8</b>	<b>20.1</b>	<b>22.0</b>	<b>22.5</b>	<b>36.9</b>	<b>28.9</b>	<b>16.3</b>
Rajasthan	12.5	11.1	10.7	10.7	7.7	8.4	12.6	19.3	18.1	9.1	10.1	21.1	23.9	31.8	24.3	26.9	21.5	14.0
Madhya Pradesh	11.0	10.1	15.9	7.9	7.8	7.7	8.0	12.9	17.0	4.0	5.8	5.8	22.5	26.2	38.9	42.7	34.0	10.0
Uttar Pradesh	10.8	8.6	10.7	5.9	6.6	5.7	7.5	15.3	24.9	9.5	13.0	17.1	15.1	16.3	14.8	43.2	35.5	16.4
Orissa	19.7	19.7	23.7	11.9	11.7	7.3	9.8	11.7	16.2	10.8	14.6	8.7	24.9	23.8	19.4	15.9	9.6	9.5
Bihar	17.7	20.5	17.4	12.2	16.1	12.1	2.4	5.7	8.4	6.6	10.4	9.4	25.0	21.2	23.7	32.1	22.5	26.4
<b>14 Selected States</b>	<b>11.1</b>	<b>10.4</b>	<b>11.1</b>	<b>8.1</b>	<b>8.6</b>	<b>7.7</b>	<b>9.7</b>	<b>16.0</b>	<b>21.3</b>	<b>9.9</b>	<b>13.4</b>	<b>15.9</b>	<b>17.4</b>	<b>17.3</b>	<b>15.1</b>	<b>36.6</b>	<b>30.1</b>	<b>22.8</b>

(iii) Transfers (revenue and capital) to local bodies, public enterprises and others also increased their share between the first and the third period in general, the exceptions being Punjab and Orissa. The largest rise was in Kerala -- the share went up from 3.6 per cent to 16.4 per cent. However, several States show a fall in the third period as compared to the second (Haryana, Gujarat, Tamil Nadu, Orissa and Bihar).

(iv) The share of salaries does not show much change in the aggregate over the years. In the high income States, the share fell between the first and the third period, while the trend was the opposite in the low income States. The middle income States just maintained the share of wages and salaries. Among the individual States, the fall in the share was predominant in Gujarat and Karnataka while there was a prominent rise in Haryana, Madhya Pradesh and Orissa. The trends also confirm our earlier observation regarding relatively fast growth of salaries and wages in poorer States. The timing of the implementation of the revised pay scales caused the share in the third period to be higher than in the second in most cases; the exceptions can probably be attributed to late implementation of revised pay scales (Kerala and Rajasthan), reduction in the size of government employees, often by only changing the organisational form while keeping the size of the public sector the same (Bihar), or both (Karnataka).

(v) The share of maintenance expenditure went up in all the high income States between the first and the third period, but fell in the other States. The sharp fall in the share of wages and salaries in Karnataka was observed in the case of net government maintenance also. Apart from the high income States, the only other State where the share of net government maintenance rose between the first and the third period was Andhra Pradesh. This provides some support to the hypothesis of deteriorating maintenance of capital assets and (through falling supply of consumables including spares) suboptimal use of the assets. The high income States could afford to maintain their assets better than other States, as the need for capital expenditure was less urgent. The case of Karnataka probably reflects increased decentralisation and/or delegation of responsibilities to non-departmental organisations.

(vi) The share of capital expenditures, as noted earlier, generally showed a falling trend except in low income States. In the low income States, it was the rising trend in Madhya Pradesh that pushed up the share for low income States as a group. Among the other States, only Maharashtra exhibited a rise in the share of capital expenditure between the first and the third period.

**a. Agriculture and Allied Services:** The role of the State governments in the area of agriculture and allied services is primarily of providing agricultural extension services, supplementing private investments with their own investments in assets with some public good characteristics (like research, construction of marketing yards, building proper warehouses and

establishment of facilities to treat seeds), soil conservation, and ensuring adequate supply of quality inputs. The *raison d'être* of government intervention in this area lies in the fact that agricultural productivity, particularly that of foodgrains, is vital for the country and for the well-being of the economy.

**Table 4.32**  
**Per Capita Expenditure on Agriculture and Allied Activities**  
**(in 1981-82 prices)**

(Rs.)

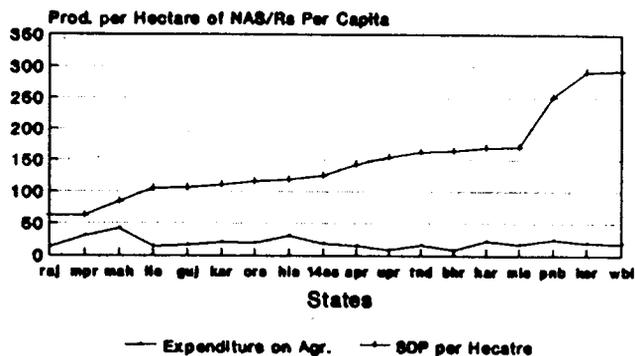
State	Revenue Expenditure				Capital Expenditure			
	Average 1974-80	Average 1980-85	Average 1985-91	Growth Rate(%)	Average 1974-80	Average 1980-85	Average 1985-91	Growth Rate(%)
<b>High Income States</b>	<b>24.8</b>	<b>31.0</b>	<b>40.6</b>	<b>5.7</b>	<b>1.6</b>	<b>1.6</b>	<b>3.6</b>	<b>6.6</b>
Punjab	24.0	24.7	30.8	2.6	0.8	-1.5	2.7	n.c.
Haryana	22.4	30.4	38.5	5.7	0.0	-0.9	0.1	n.c.
Maharashtra	39.0	52.4	64.8	5.9	3.0	3.0	5.3	5.3
Gujarat	13.6	16.5	28.1	7.2	2.7	5.6	6.3	32.1
<b>Middle Income States</b>	<b>15.3</b>	<b>18.5</b>	<b>24.9</b>	<b>4.5</b>	<b>2.4</b>	<b>2.0</b>	<b>1.8</b>	<b>-0.2</b>
Karnataka	18.9	22.9	29.7	4.1	1.0	1.1	0.4	-7.4
West Bengal	14.2	16.4	20.2	3.9	3.9	1.6	1.2	-12.3
Andhra Pradesh	12.5	14.0	19.5	3.9	2.7	0.2	0.9	n.c.
Tamil Nadu	14.9	19.5	30.7	6.1	1.4	3.4	3.2	n.c.
Kerala	16.2	19.7	24.3	3.7	3.0	3.5	3.4	-0.2
<b>Low Income States</b>	<b>15.1</b>	<b>18.3</b>	<b>23.9</b>	<b>4.7</b>	<b>0.9</b>	<b>0.5</b>	<b>1.0</b>	<b>2.2</b>
Rajasthan	12.4	13.7	22.2	5.9	0.7	0.3	0.4	-2.8
Madhya Pradesh	28.9	35.5	42.1	3.9	1.5	0.9	1.2	-1.8
Uttar Pradesh	8.5	9.9	15.6	6.2	0.7	0.5	1.1	n.c.
Orissa	17.4	21.0	27.5	4.5	1.5	0.6	1.7	-11.4
Bihar*	8.3	11.2	11.9	5.1	0.3	0.3	0.8	8.1
<b>14 Selected States</b>	<b>16.9</b>	<b>20.9</b>	<b>28.3</b>	<b>4.9</b>	<b>1.7</b>	<b>1.4</b>	<b>2.0</b>	<b>2.3</b>

n.c. Not computed due to wide fluctuations in the figures.

\* Averages for the period 1985-91 and the growth rates do not include figures for 1990-91.

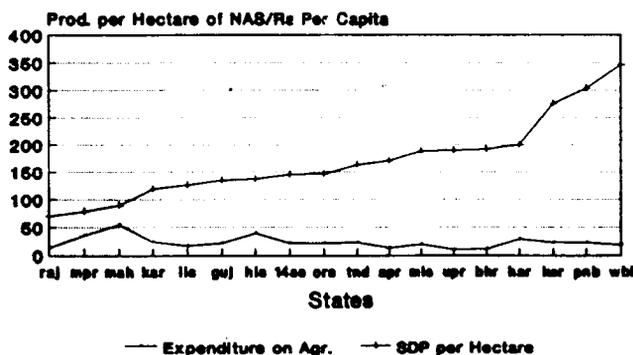
# Figure 4.6

## Agricultural Productivity and Government Expenditure : 1974-80



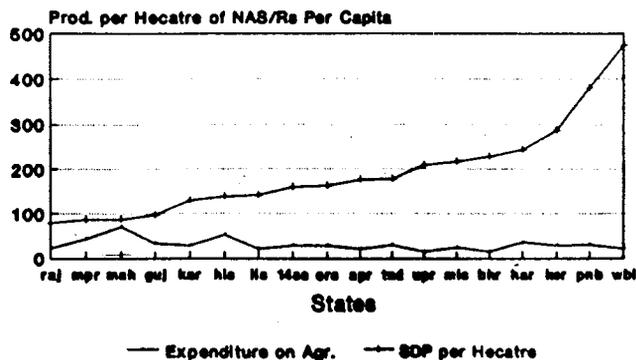
ke: Low Income States; hie: High Income States; mie: Middle Income States; 14ee: 14 Selected States

## Agricultural Productivity and Government Expenditure : 1980-85



ke: Low Income States; hie: High Income States; mie: Middle Income States; 14ee: 14 Selected States

## Agricultural Productivity and Government Expenditure : 1985-89



ke: Low Income States; hie: High Income States; mie: Middle Income States; 14ee: 14 Selected States

Table 4.32 indicates that per capita real government expenditure on agriculture and allied activities have been rising, but mostly in the revenue account. Gujarat, Uttar Pradesh and Tamil Nadu exhibit the highest growth in revenue expenditures under agriculture and allied services (7.2, 6.2 and 6.1 per cent per annum respectively). Real capital expenditures have actually grown in only three States: Maharashtra, Gujarat and Bihar. This trend, coupled with declining private investment in agriculture (C.H.H. Rao, 1992), should be viewed with concern. Further, the per capita expenditures were the least in the States needing them most. Rath (1989) discusses the issue of low agricultural productivity in some States (the four Eastern States of Assam, Bihar, Orissa and West Bengal in particular), and links it to inadequate capital formation in the public sector, aggravated by a distribution of agricultural credit skewed against these States. Figure 4.6 shows that broadly, per capita real expenditure on agriculture and allied activities varied inversely with agricultural incomes (defined as the SDP from agriculture and allied activities per hectare of gross cropped area), but greater governmental effort is needed in States where value added per hectare is low.<sup>20</sup> It must, however, be noted that public spending on the agricultural sector is captured only partially in the figures cited above. Expenditures on irrigation, on procurement of agricultural output (both foodgrains and non-foodgrains), on interest subsidies and loan waivers, and on other input subsidies probably have a greater impact on the agricultural sector, although not all of the above come out of the State resources. A major problem with the government expenditures in this area has been the perception of their inherent inequity; it is felt that the beneficiaries of government expenditure "are mostly rich and middle income farmers who created the Green Revolution, reduced the country's food deficit, and gave her much needed food security. In the process, however, these farmers have not only become used to subsidies (which were necessary early on) but also more and more demanding in these matters. The importance of their leaders as powerbrokers who control vote banks makes political parties vie with each other in promising more advantages" (Dhar, 1991).

**b. Irrigation:** This is actually an element of expenditure on agriculture as mentioned above, but given the size of the government expenditure under this head, it merits a separate analysis. It should be noted that the data reported here on expenditure on irrigation are different from the data given in the budget documents in one important respect -- our figures *do not* include the notional interest payments on capital invested by the government department as these are only book entries cancelled out by a corresponding entry on the receipts side.

The three major issues in public expenditure on irrigation are: (a) adequacy of maintenance of existing assets, (b) adequacy of capital investments, and (c) pricing of the water supplied. The third is not directly relevant for the analysis of government expenditures, but has a bearing on the other two due to its impact on resource availability, apart from the distortions

20. It may be argued that spending larger amounts in States with higher marginal productivity is an appropriate strategy to maximise output. However, the larger productivity itself is probably the consequence of better infrastructures and therefore from a long-term point of view, greater spending in States with lower productivity is called for.

**Table 4.33**  
**Government Expenditure on Irrigation**

(Rs.)

	<u>Revenue Expenditure (81-82 prices)</u>				<u>Per Capita</u>		<u>Net Irrigated Area/ Net</u>		
	per hect. of net area sown			<u>Per</u>	<u>Capital Expenditure</u>		<u>Area sown (per cent)</u>		
	<u>Average</u>	<u>Average</u>	<u>Average</u>		<u>Capita</u>	<u>(in 1981-82 prices)</u>		<u>Average</u>	<u>Average</u>
	1974-80	1980-85	1985-90	<u>Growth</u>	<u>Growth</u>	<u>Growth</u>	1974-80	1980-85	1985-90
<b>High Income States</b>	<b>160.5</b>	<b>216.3</b>	<b>319.6</b>	<b>5.4</b>	<b>11.2</b>	<b>-1.4</b>	<b>24.3</b>	<b>27.8</b>	<b>28.7</b>
Punjab	73.8	87.2	146.7	5.1	17.3	-4.4	77.6	83.7	89.2
Haryana	77.6	92.0	95.5	4.6	18.3	-10.5	52.2	61.5	69.4
Maharashtra	224.1	422.8	565.9	7.8	10.4	0.2	10.1	10.7	10.4
Gujarat	354.4	369.7	688.9	2.9	7.6	-0.2	17.6	22.9	21.7
<b>Middle Income States</b>	<b>201.3</b>	<b>223.0</b>	<b>232.9</b>	<b>1.4</b>	<b>9.1</b>	<b>-2.3</b>	<b>26.2</b>	<b>28.1</b>	<b>29.8</b>
Karnataka	213.5	265.9	290.5	4.4	8.2	-2.3	13.2	14.7	17.7
West Bengal	381.2	322.0	329.1	1.0	6.5	-1.5	26.8	32.8	35.8
Andhra Pradesh	191.6	215.0	187.5	-1.4	9.6	-1.9	31.0	32.9	35.0
Tamil Nadu	94.4	107.5	125.2	0.9	3.0	-1.7	44.1	45.7	42.8
Kerala	402.4	559.9	702.0	7.2	16.2	-5.8	12.1	11.7	13.8
<b>Low Income States</b>	<b>144.3</b>	<b>173.7</b>	<b>219.1</b>	<b>4.2</b>	<b>9.6</b>	<b>-2.7</b>	<b>26.2</b>	<b>30.2</b>	<b>33.2</b>
Rajasthan	153.9	154.8	263.0	2.7	4.4	-2.3	18.9	20.0	23.2
Madhya Pradesh	66.7	193.7	185.8	37.9	13.2	-1.3	10.8	13.9	17.3
Uttar Pradesh	141.8	160.3	198.0	3.7	7.5	-4.7	48.5	56.7	58.4
Orissa	355.9	172.8	158.7	-3.4	18.7	-4.0	17.8	26.2	27.6
Bihar	119.3	236.2	309.9	7.8	7.4	-0.2	33.5	34.9	41.1
<b>14 Selected States</b>	<b>163.1</b>	<b>196.4</b>	<b>246.7</b>	<b>3.8</b>	<b>9.9</b>	<b>-2.1</b>	<b>25.7</b>	<b>29.1</b>	<b>31.2</b>

introduced in the demand for irrigation. Table 4.33 throws some light on the first two issues. Revenue expenditure on irrigation per hectare of net irrigated area broadly indicates the level of maintenance of existing facilities; these are clearly inadequate in general and more so in the low income States. Further, per capita revenue expenditure in Orissa and Andhra Pradesh actually fell in real terms. Per capita capital expenditure on irrigation shows a fall in the Eighties as compared to a fairly high growth rate in the Seventies (10 per cent per annum in real terms) in all the States. Also, the need for capital expenditure on irrigation can be presumed to be more in the States with lower percentages of irrigated area to gross cropped area; actual capital expenditures do not follow the pattern of need in this sense.

One of the reasons for (and to some extent the effect of) even the stagnant capital expenditures not translating into actual irrigation facilities is the commitment of State governments to several projects simultaneously without being able to complete most of them in time, resulting in serious cost overruns. There are irrigation projects taken up more than 20 years ago and still not completed. This is, to a large extent, due to the tendency to appease the politically strong large farmers' lobby by starting irrigation projects indiscriminately, as they stand to benefit the most from these projects. Funding from international agencies like the World Bank have also caused commitment to more projects than the State machineries can handle at a time, as the prospect of incoming foreign exchange forces the Centre to persuade the States -- formally or informally -- to take up such projects.

**c. Rural Development:** This head primarily consists of the poverty alleviation programmes besides other programmes like community development, Panchayati Raj, and land reforms. In terms of the amount of expenditure involved, the first is, of course, the dominant category. Until recently, all poverty alleviation programmes were aimed at the rural poor and there were several schemes with different objectives. Now all the rural employment oriented Centrally Sponsored Schemes have been combined into one scheme (Jawahar Rozgar Yojana or JRY). The other major programme in operation is Integrated Rural Development Programme (IRDP), which again subsumes several schemes in it. The objective of IRDP is to enhance the income earning capabilities of the rural poor by giving them assets/ skills.

While the objectives of the programmes are noble enough, the pros and cons of the actual administration have been discussed widely. To begin with, these programmes are partly funded by the Centre with matching grants. This type of grant falls between stools as the mechanism is open to the charges of distorting State priorities without achieving spending in the desired area to an extent a specific grant would (Rao and Das-Gupta, 1990). There have been persistent charges of corruption, diversion and leakage of funds meant for these schemes. More serious than all these charges is the fact that given the allocations and the number of the poor, per poor expenditure is simply too small to make any dent. This is borne out by the figures of expenditure on rural development per rural poor reported in Table 4.34, although total expenditures on this head have increased very fast over the reference period. One may recall that Galbraith had made this point earlier (Galbraith, 1979) and had criticised the target oriented

approach strongly; he felt that the right way was to concentrate on a few poor persons and demonstrate that it was not inevitable that the poor should remain poor. This followed from his basic premise that the problem of poverty was to a large extent due to the lack of initiative and motivation on the part of the poor themselves (caused by a complex set of socio-economic factors) to shake off their poverty. Thus, if the funds availability for these programmes do not improve greatly, it may be necessary to reconsider the current approach to poverty alleviation.

**Table 4.34**  
**Expenditure on Rural Development**

(Rs.)

State	Expenditure in 1981-82 prices		Growth Rate (1974-91)
	per rural poor 1982-83	1987-88	
<b>High Income States</b>	<b>109</b>	<b>147</b>	<b>9.6</b>
Punjab	77	72	10.8
Haryana	84	141	12.5
Maharashtra	112	169	8.5
Gujarat	115	119	11.3
<b>Middle Income States</b>	<b>52</b>	<b>81</b>	<b>12.3</b>
Karnataka	62	93	15.7
West Bengal	27	52	14.2
Andhra Pradesh	73	142	15.9
Tamil Nadu	72	72	7.3
Kerala	43	70	8.3
<b>Low Income States</b>	<b>42</b>	<b>74</b>	<b>10.7</b>
Rajasthan	38	186	13.7
Madhya Pradesh	31	59	15.6
Uttar Pradesh	62	84	8.8
Orissa	27	43	13.3
Bihar	35	49	14.0
<b>14 Selected States</b>	<b>55</b>	<b>87</b>	<b>10.9</b>

*Note:* (i) The growth rate for Bihar is for the period 1974-90.  
(ii) The number of rural poor are as estimated by B.S. Minhas, L.R. Jain and S.D. Tendulkar (1991), "Declining Incidence of Poverty in 1980s: Evidence versus Artefacts", *Economic and Political Weekly*, Nos 27 and 28, pp. 1673-82.

**Table 4.35**  
**Expenditure on Industries and Minerals**  
**(1981-82 Prices)**

State	Per capita expenditure			(Rs.)	Expenditure on minerals/SDP from mining		
	1974-80	1980-85	1985-90	Growth Rate(%)	1974-80	1980-85	1985-90
<b>High Income States</b>	<b>6.9</b>	<b>8.2</b>	<b>9.7</b>	<b>3.8</b>	<b>0.02</b>	<b>0.01</b>	<b>0.01</b>
Punjab	11.2	9.4	14.4	2.7	0.37	0.16	0.19
Haryana	6.1	8.8	7.9	2.6	0.01	0.01	0.02
Maharashtra	6.2	7.0	6.3	1.0	0.04	0.02	0.01
Gujarat	6.4	9.5	14.6	9.8	0.01	0.01	0.01
<b>Middle Income States</b>	<b>8.7</b>	<b>10.2</b>	<b>12.8</b>	<b>4.0</b>	<b>0.03</b>	<b>0.04</b>	<b>0.04</b>
Karnataka	18.5	16.9	20.8	1.3	0.06	0.05	0.02
West Bengal	4.3	5.6	7.8	6.3	0.00	0.00	0.00
Andhra Pradesh	7.9	8.4	10.9	3.2	0.06	0.05	0.05
Tamil Nadu	6.9	12.7	14.7	7.5	0.03	0.06	0.02
Kerala	8.8	9.9	12.7	4.4	0.29	0.34	0.50
<b>Low Income States</b>	<b>4.5</b>	<b>7.3</b>	<b>8.9</b>	<b>6.0</b>	<b>0.03</b>	<b>0.04</b>	<b>0.05</b>
Rajasthan	8.3	9.3	9.8	2.1	0.15	0.16	0.14
Madhya Pradesh	3.6	5.0	6.2	9.0	0.01	0.03	0.05
Uttar Pradesh	5.5	8.9	10.2	4.7	0.06	0.04	0.11
Orissa	4.5	9.7	14.9	11.6	0.02	0.03	0.03
Bihar	2.7	4.6	5.2	6.2	0.01	0.00	0.01
<b>14 Selected States</b>	<b>6.4</b>	<b>8.5</b>	<b>10.4</b>	<b>4.7</b>	<b>0.03</b>	<b>0.03</b>	<b>0.04</b>

**d. Industries and Minerals:** The major part of expenditures on this head are incurred on village and small industries. The share of this in economic services is not very large as such (Table 4.30), and per capita expenditure on this head in constant prices does not show any significant increase except in low income States. In fact, even in States where a relatively larger share of SDP comes from minerals, the expenditure on minerals is very small. This is borne out by Table 4.35, showing expenditure on mines and minerals in constant prices as a ratio of SDP from mining; in mineral-bearing States like Bihar, Orissa and West Bengal, these figures are quite small.

The expenditure on industries ought to be mostly promotional, but this is not always the case. There are several State-level non-infrastructure public enterprises (often producing consumer goods like beer, soap etc.) running at losses which are financed by the respective State governments through budgetary support. Even the promotional enterprises have not in general served the purpose for which they were created. In fact, many of the State level public

enterprises have become fiefdoms of favoured bureaucrats and less active politicians. The public sector has "spawned a number of economic interests and political constituencies which wield formidable power....Public sector undertakings project the power of the Government, the Minister, his ministry and his political party over large groups of men and large amounts of money. This is particularly true in the case of the public sector in the States, where it provides an arena for the distribution of sinecures and patronage in return for political support" (Dhar, 1991). Given such trenchant criticism of the public sector enterprises, the relatively low growth of real per capita expenditure on industries is probably a welcome trend.

**Table 4.36**  
**Government Expenditure on Energy: in 1981-82 Prices**

State	Revenue Expenditure/Installed Capacity (Rs. per kwh)		Per capita Energy Consumption (kwh)		Per capita Capital Expenditure (Rs.)		
	1980-81	1991-92	1980-81	1990-91	1974-80	1980-85	1985-91
<b>High Income States</b>	<b>88.4</b>	<b>87.8</b>	<b>230.4</b>	<b>437.1</b>	<b>2.3</b>	<b>2.4</b>	<b>4.0</b>
Punjab	68.7	1.4	297.7	631.3	0.0	0.0	0.4
Haryana	67.9	85.5	197.8	413.5	3.1	1.1	1.8
Maharashtra	148.2	117.5	223.6	397.0	4.1	4.6	5.2
Gujarat	3.9	91.1	222.0	427.7	0.0	0.1	4.2
<b>Middle Income States</b>	<b>100.7</b>	<b>117.9</b>	<b>124.5</b>	<b>243.4</b>	<b>2.1</b>	<b>1.3</b>	<b>2.6</b>
Karnataka	2.1	50.2	139.1	295.4	1.3	0.0	5.0
West Bengal	14.3	51.1	104.0	154.4	0.0	0.0	5.4
Andhra Pradesh	123.1	60.0	95.0	267.7	7.6	5.2	1.3
Tamil Nadu	247.9	309.8	177.6	310.8	0.2	0.0	0.0
Kerala	2.8	5.4	108.3	185.9	0.0	0.0	0.0
<b>Low Income States</b>	<b>58.0</b>	<b>54.6</b>	<b>73.5</b>	<b>232.6</b>	<b>0.0</b>	<b>0.1</b>	<b>3.1</b>
Rajasthan	50.7	51.4	85.7	208.8	0.0	0.0	0.0
Madhya Pradesh	176.4	156.3	87.5	202.0	0.0	0.2	2.4
Uttar Pradesh	2.3	6.3	70.8	148.5	0.0	0.0	2.4
Orissa	44.9	20.2	94.0	200.5	0.2	0.0	17.0
Bihar	85.5	77.7	53.7	102.9	0.0	0.2	0.6
<b>14 Selected States</b>	<b>83.2</b>	<b>88.2</b>	<b>122.1</b>	<b>282.3</b>	<b>1.2</b>	<b>1.0</b>	<b>3.1</b>

Note: Installed capacities refer to the year given in the column heading; revenue expenditures refer to averages for the years 1979-82 and 1988-91, except for Bihar where the latter average was for the period 1988-90.

**e. Energy:** The four basic issues in the energy sector, as far as the State governments are concerned, relate to (a) maintenance of existing assets, (b) adequacy of capital investments, (c) operational efficiency, and (d) pricing of energy supplied, just as in the case of other infrastructural services. Almost every State has an autonomous public undertaking for the purpose of production and supply of power, and these are expected to generate a minimum rate of return. The minimum rate of return required, however, is only of academic interest as almost none of these undertakings generate any positive rate of return. They are sustained by budgetary support, the form of which is irrelevant as most of these ultimately become grants. Technical efficiency in production and distribution varies across States considerably, but uneconomic pricing causes even the otherwise efficient agencies to incur substantial losses (Chelliah, Rao and Sen, 1993). As far as the other two issues are concerned, an indication can be had from Table 4.36, which shows the revenue expenditure on energy (an approximation for the government expenditure on maintenance and/or current transfers to the State Electricity Boards) per unit of installed capacity<sup>21</sup> and also gives the figures of per capita consumption to be compared to per capita capital expenditure on energy. While the former clearly shows the pitifully small amounts for maintenance in most States (except Maharashtra, Tamil Nadu, Andhra Pradesh and Madhya Pradesh), the latter shows that even in the States where power availability is very low (e.g., Bihar), not much is being done by way of investment in the power sector. The trend of gradual withdrawal of the States from investments in the power sector, and the inadequate compensatory increase in Central investment has been pointed out earlier (Bagchi and Sen, 1992). The exceptions were Orissa, West Bengal, Maharashtra, Karnataka and Gujarat, which invested above average (Rs. 3.10 during 1985-91) amounts in this sector in recent years.

**f. Transport:** The expenditure under this head contains two major elements: the expenditure on roads and bridges, and the budgetary support to State road transport services. As far as the former element is concerned, the issues are the same as in the case of irrigation or power with one difference: there is no direct pricing mechanism. Table 4.37 gives the level of per capita expenditure on this head; these figures again show the constraint of resources in operation. But more important are the issues relevant to public transport which are: (a) the need for continuing government provision of the service at the same scale, (b) efficiency issues, and (c) pricing.

As far as roads and bridges are concerned, even National Highways are not properly maintained, although practically all expenses are reimbursed by the Central government (Mahalingam, 1990); the condition of State Highways and other roads can then be easily imagined. The construction and maintenance of roads is usually entrusted to the Public Works

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21. The institutional setup related to the figures make them difficult to interpret. The calculated ratio could be high due to either inefficient functioning of the SEB involved or greater maintenance. While the former would be a bad sign, the latter should be viewed positively. In fact, even the mix of current and capital expenditure requirements for *existing* capacities would depend on technical factors like the ratio of hydro-electric generation in the total.

**Table 4.37**  
**Per Capita Expenditure on Transport**  
**(1981-82 Prices)**

State	Average 1974-80	Average 1980-85	Average 1980-85	Growth Rate(%)
				(Rs.)
<b>High Income States</b>	<b>26.7</b>	<b>33.2</b>	<b>32.3</b>	<b>2.1</b>
Punjab	50.6	53.7	49.8	0.2
Haryana	60.5	74.9	78.8	2.5
Maharashtra	15.1	18.9	19.6	2.2
Gujarat	23.6	33.6	29.7	2.4
<b>Middle Income States</b>	<b>13.6</b>	<b>15.5</b>	<b>15.3</b>	<b>1.7</b>
Karnataka	12.3	15.5	17.5	3.6
West Bengal	11.4	15.1	13.0	2.8
Andhra Pradesh	14.8	12.7	11.3	-1.3
Tamil Nadu	14.6	17.5	16.0	1.0
Kerala	15.7	18.7	24.5	4.2
<b>Low Income States</b>	<b>10.8</b>	<b>14.5</b>	<b>16.6</b>	<b>4.0</b>
Rajasthan	14.0	20.6	22.6	4.3
Madhya Pradesh	13.2	17.8	19.1	3.3
Uttar Pradesh	10.5	15.0	17.4	5.0
Orissa	13.2	15.7	18.4	3.6
Bihar	7.0	7.8	8.3	3.1*
<b>14 Selected States</b>	<b>14.9</b>	<b>18.6</b>	<b>19.4</b>	<b>2.8</b>

\* Growth rate over 1974-75 to 1988-89. It changes to -2.069 when figures for 1989-90 are included.

department of the respective States. But the complaint of not getting value for the money spent is becoming quite loud in recent years, and some States have started contracting out construction of roads. The money spent on maintenance is small in most States to begin with; leakages involved cause this amount to shrink further. Proposals about handing over construction and maintenance of roads and bridges to private parties, allowing them to collect road tolls at fixed rates for a specified period of time have been made; no concrete policy in this regard has emerged so far. Collecting tolls on a busy road may not be administratively easy, as the experience of the Second bridge on Hooghly river in Calcutta has shown. Increasing frequency of natural calamities due to environmental degradation causing extensive damages to roads and bridges have preempted routine maintenance to a large extent; ad-hoc maintenance has become the rule rather than the exception.

With respect to provision of public transport, the situation differs among the States. Not all of the State road transport undertakings are making losses, nor are their services required in all States to the same extent. States with relatively better road network and greater demand for public transport can afford to withdraw from this sector gradually, as is being done in some States like Punjab. But States where neither of these conditions are fulfilled cannot afford to do so, as in their case withdrawal of the government would imply no provision of the service at all. Prices also cannot be raised much in these States due to the fear of further reducing already low occupancy rates. Efficiency issues, however, are universal and there is ample scope for improvement; in general, fuel efficiency is low and consumption of stores and spares high in these undertakings, due to improper maintenance of vehicles, and leakages.

**g. Other Economic Services:** Among the other economic services, relatively large expenditures are made only on cooperation. Food and civil supplies also claim a small share, but it is the Central government which really does the spending in this area through food subsidies. Some States have their own additional subsidies, but these were small and are dwindling. The expenditures on cooperation shows no such tendency. Most of the critique of State level public sector industrial undertakings is applicable to co-operatives also, with important exceptions. Given the realities of the agricultural scene of most of the States in India, cooperatives can play a very significant role in increasing productivity and raising the income of the farmers, particularly small and medium ones. That they have not done so in the past is due to the imperfections in the implementation rather than the concept itself. Further, there seems to be no other viable method to achieve the desired objectives. Sugar cooperatives in the sugarcane belt of Maharashtra are also examples of how successful the cooperative system can be in changing the entire rural scene. The milk producers' cooperatives in Gujarat is another notable example of successful cooperative movement. But such exceptions apart, cooperatives have become completely politicised and under the facade of noble objectives, conduits for diversion of public funds by dominant groups. The sorry state of accounts of the majority of cooperatives in which the State has a stake bears testimony to the widespread misuse of this excellent concept.

#### **4.5.6 Net Loans and Advances**

We have already remarked on the tendency of loans and advances growing in amount and in relative importance with the growth of SDP, while discussing net capital disbursements and its components with reference to Table 4.12. The figures given in Table 4.38 below confirms the trends noticed there. While per capita net loans and advances grew at a rate of -0.6 per cent over the reference period in the low income States, the growth rates for the middle and high income States were 1.3 and 3.7 per cent respectively. The highest growth rate was observed in the case of Rajasthan (11 per cent) with Punjab following at 7.6 per cent per annum; however, even in the period 1985-86 to 1990-91, average per capita net loans and advances in Punjab was almost eight times that of Rajasthan. Three States -- West Bengal, Madhya Pradesh and Uttar Pradesh -- exhibited negative growth. The smallest per capita loans and advances were in Orissa in all the three periods. Thus, there are clear indications of loans and advances gaining

importance with increasing resource base; there cannot be any economic explanation for this phenomenon; our hypothesis is that it probably increasingly gets used as a channel to divert public resources through the State public enterprises for private gains.

**Table 4.38**

**Per Capita Net Loans and Advances in 1981-82 Prices**

State	(Rs.)			
	Average 1974-80	Average 1980-85	Average 1980-85	Growth Rate(%)
<b>High Income States</b>	<b>43.1</b>	<b>55.3</b>	<b>59.1</b>	<b>3.7</b>
Punjab	67.1	93.5	161.6	7.6
Haryana	52.7	54.4	71.0	2.7
Maharashtra	38.7	48.9	36.5	1.6
Gujarat	35.8	48.9	46.7	3.6
<b>Middle Income States</b>	<b>23.8</b>	<b>24.9</b>	<b>26.0</b>	<b>1.3</b>
Karnataka	26.3	32.2	30.3	1.1
West Bengal	27.2	16.8	21.1	-11.6
Andhra Pradesh	19.3	12.8	20.6	2.3
Tamil Nadu	28.9	49.1	37.9	3.1
Kerala	12.5	11.6	20.0	6.0
<b>Low Income States</b>	<b>21.9</b>	<b>24.4</b>	<b>17.7</b>	<b>-0.6</b>
Rajasthan	14.7	21.7	20.2	11.1
Madhya Pradesh	26.8	34.1	11.4	-5.6
Uttar Pradesh	29.8	30.8	19.7	-3.1
Orissa	7.9	4.0	6.9	4.0
Bihar	14.4	15.9	22.5	5.3
<b>14 Selected States</b>	<b>26.7</b>	<b>30.7</b>	<b>28.9</b>	<b>1.7</b>

\* In 1985-86 per capita Net Loans and Advances were Rs.-18.7. This Figure is substituted by a very small positive number to calculate the compound growth rate.

@ In 1984-85, per capita Net Loans and Advances were Rs.-0.1. This figure is substituted by a very small positive number to calculate the compound growth rate.

#### **4.6 Summary and Conclusions**

A look at the broad trends in aggregate government expenditures at the State level shows that they have been increasing at about 16 per cent per annum in nominal terms throughout the reference period (1974-75 to 1990-91) fairly steadily, but in real per capita terms the growth rate works out to 5.6 per cent. There are inter-State variations, with Bihar exhibiting the highest growth and Orissa exhibiting the lowest; in general, however, both level of per capita

government expenditures and their growth seem to be related to the level of per capita SDP. The steady increase in nominal expenditures as opposed to the fluctuations around a rising trend for the expenditures in real per capita terms appears to lend some empirical support to the hypothesis of 'incremental budgeting' in nominal terms. When total expenditures are broken up into revenue and capital, the relative stagnation in capital expenditures immediately becomes apparent, particularly in the Eighties. Revenue expenditures show unabated growth, however, and as a result, have come to dominate the trends in total expenditure. An inter-State comparison shows wide differences in the growth of per capita capital disbursements; while West Bengal shows a negative growth rate and Tamil Nadu exhibits very low growth, in Orissa and Punjab, the capital disbursements have grown more or less in line with revenue expenditures. Increased Central transfers at the beginning of the Eighties fuelled increase in revenue expenditure which was not matched by the growth in revenue receipts including Central transfers. This resulted in a resource crunch in all the selected States by the mid-Eighties. The committed nature of some of the expenditures -- primarily fast growing debt-servicing liabilities -- and pressure from interest groups to maintain many other categories crowded out capital disbursements to a large extent, net loans and advances in particular.

Government employees as a group maintained their share in total expenditures. Given a rising share of the government in SDP, this meant that an increasing proportion of the State incomes were appropriated by them. Rising subsidies, probably due to pressure group activities, also contributed significantly to the increase in public expenditures at the State level. The share of maintenance expenditures (including government purchase of goods and services) fell over the reference period as a result. The link between expenditure on wages and salaries, and maintenance expenditure (which ought to be complementary) appear to be weakening over the years.

The relationship between per capita SDP and per capita government expenditure appears to be quite strong in the context of the States. Even the share of government expenditure in total SDP seems to be related to the level of per capita SDP. The relationship (probably working through the resource availability) shows up repeatedly at the disaggregated level also. The observed relationship constitutes an indictment of the system of inter-governmental transfer mechanism in India, as it implies a failure to enable the poorer States to raise the standard and coverage of the publicly provided services. There are exceptions like Kerala (with reference to education in particular), but the basic problem is undeniable. Intergovernmental transfers have, however, not been totally ineffective, as is indicated by the lower coefficient of variation for public expenditures in all years as compared to the C.V. for per capita SDP. Another worrisome trend is the rise in all the C.V.s during the second half of the Eighties after a fall in the first half. Considering all the broad trends, the prognosis that emerges is that of a widening gap between rich, middle income and poor States if present trends continue.

Disaggregation of the C.V.s reveal that the variations in total expenditures can be attributed to broad budgetary groups more or less according to their shares. Thus, expenditure on

social and economic services, which account for more than 70 per cent of total expenditures need to be equalised for an equalising impact of sufficient magnitude. Between these two, the variation in economic services is greater and hence equalising efforts should be directed more at these.

Examination of trends in various components of general administration reveal that the largest part (almost one-third) is claimed by police. But the fastest growing component is pensions and retirement benefits, particularly after 1984-85, probably as a result of the Supreme Court judgement in 1984 enhancing these substantially. While expenditures on police have kept pace with the increase in total expenditures on general administration, those on justice and jails have not, leading to an imbalance in the law and order machinery. Tax collection costs exhibit economies of scale, which all States are reaping with increasing tax revenue.

Most of the government expenditure on social services in India (85 per cent) are incurred at the State level. These also directly affect the well being and the capacity to earn of the vast majority of the population. Education claims half of these expenditures. Other categories of expenditures with significant shares are health, family welfare, and sewerage and sanitation, direct social welfare and water supply. In per capita terms, the expenditure on the last two categories are too small to have any significant impact. Expenditure on water supply, in any case, appears to be determined by the cost factors.

Within education, about half of the expenditure is on primary education. In high income States, this ratio is lower, probably reflecting better availability of primary education. But the differences in per capita amounts are glaring and clearly show the inability of the poorer States to spend sufficiently large amounts to tackle their typically more widespread illiteracy. A similar trend is noticed in the case of health expenditures (broadly defined); the States with the worst health status indicators are the poorer ones and therefore do not have the resources to make a dent on this problem through sufficiently large public expenditures. Additionally, the increasing share of wages and salaries at the cost of maintenance and capital expenditures could be further reducing the effectiveness of the expenditures incurred.

In the case of economic services, capital expenditures are vital; the cutback in capital expenditures affected these the most as a large part of the total is on economic services. Since this category of expenditures represents public supply of infrastructural facilities, long term economic growth should be closely linked to these expenditures. The most important among these are expenditures on the agricultural sector including irrigation. Along with rural development, these account for about 65 per cent of government expenditures on economic services. These are marked by low capital formation and inadequate maintenance expenditure. Capital expenditure on irrigation actually show a fall in real terms in all States in the most recent period. Rural development, dominated by the rural poverty alleviation programmes show fairly high growth probably due to the incentive provided by the Central transfers on this account, but the expenditure per rural poor is hopelessly small and the policy in this respect must be

reconsidered for effective use of resources. Expenditures in the area of energy are dwindling in most States, even as the per capita consumption of power of several States with lower per capita GDP are stuck at a low level. Orissa seems to be an exception to this trend. Expenditures on transport also show only a small growth over the entire period. While some of the higher income States can now afford to reduce public provision of transport due to higher ability to pay of their residents and private provision of the service, the lower income States cannot do so. Naturally, the growth of government expenditure is higher in poorer States. Loans and advances constitute a large part of the expenditure on economic services, but their share is falling steadily in almost all States. Subsidies, however, are rising fast and so are transfers (revenue and capital).

## CHAPTER V

### CONCLUDING REMARKS

This study analyses the trends in government expenditures in India over the last one and a half decades. In undertaking this task, our endeavour has been to make an attempt at examining the role of special interest groups in influencing the size, growth and changes in the composition of government expenditures in India. Admittedly, it is difficult to precisely identify the special interest groups and the exact mechanism with which they influence public expenditure policy. We have tried broadly to associate the trends in public expenditures with the working of special interest groups.

The special interest groups influence public expenditure policies in either of the two ways. First, the groups involved in selling their outputs/services to governments organise themselves to charge oligopolistic prices, thereby shifting governments' cost curves. They may also influence the policy makers to purchase quantities larger than that is required at higher prices. Second, the beneficiaries may organise themselves to 'free-ride' or gain a larger share of the benefits without commensurately sharing in the costs. In the first case, expenditure increases will occur mainly due to cost increases and fall in productivity. In the second, expenditure increases will take place due to increase in the level of public services which benefit mainly the special interest groups.

Our analysis reveals that the effect of special interest group action on public expenditure outcomes is different when the resource position of the government is comfortable, from that when it faces a hard budget constraint. When the resource position is flexible, there is a general buoyancy in expenditures. It is relatively easy to get higher prices on goods and services sold to the government by the sellers. Similarly, during this period, interest groups can obtain higher allocation on the quasi-public and private goods provided by the government benefiting them without having to reduce allocations on other items. The outcome is analogous to the Peacock-Wiseman (1965) 'displacement effect' wherein, the upward shift in the revenue function created during the war years, helps in financing the expansion of other public services after the war.

However, the effect of special interest groups on public expenditure outcomes will be different when the government is faced with a hard budget constraint, particularly when expenditure compression is attempted to stabilise the economy. At such times, increase in the allocation to goods and services beneficial to the special interest groups or higher payment to the sellers of goods and services to the government is possible only by 'crowding out' expenditure on other services which are not demanded by the powerful coalitions. The general experience has been that the capital and maintenance expenditures are likely to receive the maximum cut during the period of fiscal compression.

The analysis of the trends in government expenditure in India brings out the effect of special interest groups on expenditure policy quite clearly. It is interesting to see that the size and composition of government expenditures vary with the nature of resource constraint. Flexible resource position during the first half of 1980's led to the fiscal expansion wherein, there was a general buoyancy in expenditures, but expenditures on wages and salaries, subsidies and transfers besides interest payments increased at rates faster than capital and maintenance expenditures and net loans and advances. On the other hand, when the resource constraint hardened in the latter half of the 1980's, the expenditure on wages and salaries, subsidies and transfers continued to increase at fairly high rates whereas, socially productive capital expenditures particularly on infrastructural sectors in per capita terms (at 1981-82 prices) declined even in absolute terms. The negative growth rates seen in the capital expenditures would have adverse implication on both growth and equity.

The above finding has important implications on the strategy of fiscal compression that has been initiated as a part of the stabilisation programme. Satisfactory levels of social and economic infrastructure is an important precondition for the large inflow of foreign direct investment into the economy. It is therefore necessary to maintain if not increase allocation to the infrastructural sectors at the time of structural adjustment. Unhindered interplay of special interest groups will only result in the situation wherein the macro-effects of stabilisation programme will not be consistent with the micro objectives of structural adjustment.

Our analysis also shows that the nature of resource constraints at the Central and State levels are different and consequently, the behaviour of public expenditures at the two levels do not strictly follow a consistent path. Nevertheless, in India, Central government is able to influence the expenditures at the State level in significant ways. As it is, the States face a harder budget constraint for, they do not have independent powers to borrow and when the Centre reduces transfers to the States due to its own resource constraint, additional problems are created. As the type of services provided by the States are more labour intensive, the cost escalation arising from the organisation of workers has more adverse effects on the States' ability to provide public services, this necessarily causes displacement of capital expenditures on items like agriculture and irrigation, energy and transport. This is precisely what seems to have happened in India during the 1980's.

Our analysis also shows, *albeit* indirectly, the failure of the federal transfer policy in equalising the levels of public services. The richer States with already higher levels of public services are able to spend larger amounts per capita on various social and economic services and vice-versa, in the case of poorer States. It is also seen that the inequalities in expenditure levels has not shown any trend towards convergence and the residents in richer States continue to enjoy higher levels of public services.

The above finding has important implications at a time the country has embarked on the policy of liberalisation. When the market forces determine the investment pattern, the flow of private investment to poorer regions will be hindered by the paucity of infrastructural facilities. This, in fact, may accentuate inequalities in the living standards further. In such a situation, the poorer regions may become poorer not because they are poor in resources - but merely due to want of infrastructure to harness the resources. If our observation is correct, the need for redesigning the federal transfer policy is of paramount importance now, than it was ever before. Of equal importance is the need for poorer States to plan their fiscal allocations to ensure cost-efficient utilisation of the scarce resources. It is another matter, however, that the distributional coalitions tend to exercise greater influence in poorer regions (Olson, 1992).

While the special interest groups attempt to enhance their share of benefits by influencing public expenditure policy, it must be stated that, it is not the only mechanism through which they can maximise their gains. The interest groups can enhance their benefits by influencing a host of economic policies - like the tax policy, industrial policy or the tariff policy, - to name only a few. The actual methods by which each distributional coalition maximises its gains is by equating marginal costs and benefits from each policy measure. Therefore, it is incorrect to conclude that if a coalition succeeds in gaining larger share of benefits from government expenditure policy, it is necessarily the most powerful. There may be other coalitions obtaining greater benefits for other policy measures.

We must conclude by stating that our exercise is only preliminary and conclusions tentative. A lot more work needs to be done to understand the influence of special interest groups on economic policies in general and public expenditure policy in particular. We have, in this study, only tried to take the first step in the direction of systematically analysing the influence of these groups on government expenditure policy. We must, however, indicate that the path is difficult but it would be rewarding to take the risk. On our part, we would have succeeded in this endeavour, if we have generated more discussion on the subject towards forging a better understanding of the mechanics of government expenditure determination.

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