

Public Expenditure: An Insight and Concern

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Introduction

The role of public expenditure in the fiscal policy goals of growth, equity and stability, has varied across different phases of economic development in India. The historical importance of public expenditure lies in the mixed economy model adopted after Independence in India whereby the government assumed the primary responsibility of building the capital and infrastructure base to promote economic growth. The concerns regarding equity and poverty alleviation added another important dimension to public expenditure in terms of redistribution of resources. The inadequate returns on capital outlays and the macroeconomic crisis of early Nineties arising out of high fiscal deficit shifted the focus of public expenditure to efficiency in its management for facilitating adequate returns and restoring macroeconomic stability. While the fiscal policy goal of stability could be achieved, the modus operandi of public expenditure management through curtailing capital expenditure raised concerns about infrastructure investment and its impact on the long-term growth potential of the economy. Furthermore, stagnating revenue mobilization in particular and some upward movements in expenditures led to a reversal of the fiscal stabilization process since the second half of the Nineties. Management of public expenditure has always been an issue. It may be more dominant at critical times than at times of relative stability and prosperity but it always has been, and will remain, a matter for concern. More recently, however with the persistent growth in fiscal problems in developing countries, net efficacy of public expenditure management has been increasingly discussed.

Traditionally public expenditure represents a form of government intervention designed to promote allocative efficiency through correction of market failures, redistribute resources equitably and promote economic growth and stability (Musgrave, 1959). The redistributive powers of the state, through public expenditure, emanates from the normative arguments in favour of greater equality (Marshall, 1950; Rawls, 1971).

Public expenditure has been witnessing a continuous increase over time in almost every country across the globe. However, the fact that public expenditure has grown over the period of time there are very areas in public expenditure which is largely unexplored. As Lowell Harris says 'the economist have generally concentrated their attention on the theory of taxation the theory of public expenditure has been more or less confined to that of generalities in terms of the effects of public expenditure on employment and prices'.

India's public expenditure is classified as development expenditure comprising central plan expenditure and central assistance and non-development expenditure. Increased defence Commitments, expansion of administration the working of the democratic institutions like the parliament, the government's international Commitment increase in government's participation in nation building activities like education and public health, rise in prices etc. All these are responsible for increased revenue expenditure of the Central Government.

Non-development expenditure still continues to be a large proportion of the total expenditure. Defence, debt services and administrative expenses are so large and so significant that they are responsible for keeping non-development expenditure at a high level.

The classification of expenditure into plan and non-plan although rooted in the constitution, has evolved with planning process. In the initial years of planning the emphasis was to direct capital investment in sectors according to priorities of each plan. The bulk of plan expenditure was capital expenditure and the aim was to increase the productivity capacity of the economy. However, the composition of the plan expenditure in both-centre and states have changed over time as the bulk of the Plan expenditure is now revenue expenditure.

Changing dimension in public expenditure

According to Wagner's law, the expansion of public expenditure is in proportion to the growth of the Gross National Product. According to Wagner, an increase in state activity is accompanied by an increase in government expenditure as a proportion of National Income. This is due to the fact that the government has to perform a number of functions more efficiently, which has led to an intensive growth in public activity thereby increasing government expenditure.

According to Peacock and Wiseman, public expenditure grows over time, not at a constant rate, but on an ascending spiral. Social emergencies like war and depression require a sizeable increase in their relative share of public expenditure. The growth of expenditure may also be owing to rise in prices. There was marked rise in the non-development expenditure due to the increasing welfare and developmental activities of the States, upward revision of pay scales and dearness Allowances and increasing law and order problems in the States.

At a time when the government thinking of ways to ensure four percent farm growth, the World Bank has asked India to restructure public expenditure in agriculture which is heavily tilted towards subsidies. "Agriculture spending in about four times greater on subsidies than on public goods. Moreover the return on subsidies in India has declined." The report said, adding there is a potential for significant efficiency gains from reallocating public expenditure in India.

According to 13th Finance Commission public expenditure through creation of funds outside the consolidated fund of the states need to be discouraged. Expenditure through such funds and from civil deposits should be brought under the audit jurisdiction of the C&AG. It also suggested a major Thrust of proposed expenditure reform is to improve the supply of public goods which is also inclusive by reducing existing untargeted and regressive subsidies.

The expenditure reforms Commission which looked into the working of 36 ministries/department has concluded that nearly 5 percent of the manpower is absolutely reluctant and its exist will provide a little elbow room to the government for carrying out some additional development activities outside the areas of infrastructural and human development. The government must not allow debt growth to become explosive and if it happens the economy will be in jeopardy.

Role of Public Expenditure

The link between public expenditure and growth depends upon the nature of expenditure. The government expenditures have to be balanced as to pursue the goals of growth and equity while at the same time keeping a vigil on the overall expenditure. Some of the major role are:

- Enhancing the quality of life of people.
- Allocating resources in accordance with national priorities.
- Affecting (i) the ability to work, save and invest; (ii) the desire to work, save and invest; and (iii) allocation of resources as between different uses (Dalton).
- Maintaining Economic stability.
- State firms often require subsidies or protected markets to survive.

Reason for Growth of public expenditure

- Increase in interest payments, defense and subsidies.
- Costs of civil administration has gone up considerably due to revision of pay scales, fringe benefits and liberalized scheme of pensions and other retirement benefit.
- Rapid growth of population is also responsible for increase in expenditure.
- The expenditure of state government particularly the maintenance expenditure has been expanding rapidly.
- The pattern of public expenditure management system in the initial phases stress on maximizing the growth through higher allocations towards capital formations. The concern of equity in the growth process induces more spending on social sector. The borrowed resources create a vicious cycle of debt, interest payment, deficit and further debt while managing expenditure responsibilities.
- The growth of non-plan expenditure at the State level depends on the state government. Under the existing system of federal financial relations, transfer of funds from the centre to the state takes place through the Finance Commission and Planning Commission and such transfers influence the size of non-plan expenditure of State Governments. But the impact of central transfers on different components of non-plan expenditure has not been assessed rigorously.
- Expansion of administration the working of the democratic institutions like the parliament, the government's international Commitment increase in government's participation in nation building activities like education and public health, rise in prices etc. All these are responsible for increased revenue expenditure of the Central Government

Review of Literature

According to **Raghabendra Jha**, for inadequate growth performance of the Indian economy is the (legendary) poor productivity of public expenditure in India. The seeds of such poor productivity are embedded in the very philosophy behind such expenditures. Public expenditure management systems in India have emphasized control and ignored achievement and have often served as avenues of easy and steady employment for many. As a consequence, government departments and programs have tended to expand uncontrollably irrespective of any rationale for their existence. Highly centralized decision-making and control systems have left bureaucrats unable to take initiatives to secure improved results even when they wished to do so. Hence, the public service has settled into a low-level equilibrium, in which low expectations, the dead weight of bureaucracy, lack of incentives, accountability and political interference combine to generate low performance, high waste and corruption. In the Indian case, this is typified by a high incidence of failure of public expenditure across the board: from large-scale public sector white-elephant type investments to anti-poverty programs that do not reach the poor.

Ranjit Kumar Pattnaik et.al. in this paper attempted to analyze the role of public expenditure in India as a key operating fiscal policy instrument in order to achieve the goals of growth, equity and stability and yet maintaining the intermediate targets of deficit indicators to ensure the sustainability of public finances. The Indian economy running “nearly at full steam”, there is a case of reaping the benefits by higher mobilization of revenue receipts. This can emanate in three ways. First, when the economy is on an upswing, there is more probability of mobilizing more taxes. Second, the increased capital expenditures would promote growth and enable higher tax collections. Thirdly, the user charges levied on the use of capital goods would boost non-tax revenue collections. Furthermore, given the fiscal policy transmission lag, there is a need to front load decisions on public investments, especially at a time when the Indian economy is on a high growth phase and industries have improved their efficiencies and increased their capacity utilization. The higher tax mobilization as well as recently increased share of their devolution to the states would be able to garner resources for implementation of schemes for provision of local public goods.

According to **Stephen Howes and Rinku Murgai (2004)**, there is necessary of expenditure saved by expenditure restructuring to reduce the gap between expenditure and revenue. There are significant savings which can feasibly be extracted from the salary bill, via both wage and hiring restraint, without sacrifice of expenditure quality. If real wage increases are avoided, the combined state-central government salary bill could fall by two percentage points of GDP over the next decade.

Trends In Public Expenditure: Major Heads of Developmental and Non-Developmental Expenditure of the Central Government

(Rs. in Billion)

Year	Developmental Expenditure	Economic Services	Social Services	Non-Developmental Expenditure	Total Expenditure (2+5)
1	2	3	4	5	6
1983-84	194.07	90.43	16.89	183.64	377.71
1984-85	273.75	120.21	21.46	185.25	459.00
1985-86	329.09	140.14	14.96	208.99	538.08
1986-87	354.98	162.75	21.61	260.60	647.78
1987-88	365.73	157.22	23.69	302.61	704.61
1988-89	415.36	180.22	27.69	355.19	815.29
1989-90	542.04	256.02	30.61	410.20	952.24
1990-91	586.45	245.88	32.74	493.49	1079.94
1991-92	593.13	236.81	35.69	551.70	1144.83
1992-93	654.79	262.48	40.09	605.84	1260.63
1993-94	724.64	275.71	48.30	735.86	1460.50
1994-95	828.03	338.97	58.73	824.02	1652.05
1995-96	844.27	350.29	76.55	986.32	1830.59
1996-97	941.97	372.53	96.72	1122.17	2064.14
1997-98	1109.94	442.46	118.45	1278.20	2388.14
1998-99	1372.57	543.75	146.56	1502.98	2875.55
1999-00	1291.51	609.56	172.21	1779.28	3070.79
2000-01	1393.86	717.31	176.79	1974.70	3368.56
2001-02	1593.64	808.68	151.30	2154.56	3748.20
2002-03	1841.97	1038.20	220.07	2427.49	4269.46
2003-04	1954.28	1080.71	238.59	2432.98	4387.26
2004-05	2149.55	1150.30	299.06	2629.04	4778.60
2005-06	2290.60	1330.53	382.64	2906.77	5197.37
2006-07	2557.18	1427.72	437.62	3412.78	5969.96
2007-08	3256.70	1729.55	616.48	4007.28	7263.98
2008-09	4713.99	2732.22	897.97	4281.45	8995.44
2009-10	5282.42	3044.40	1026.28	5141.01	10423.43
2010-11	6660.69	4043.12	1249.90	5514.71	12175.40
2011-12	7112.76	4504.12	1077.56	6361.94	13474.70
2012-13	7767.11	4586.86	1292.57	7385.14	15152.25

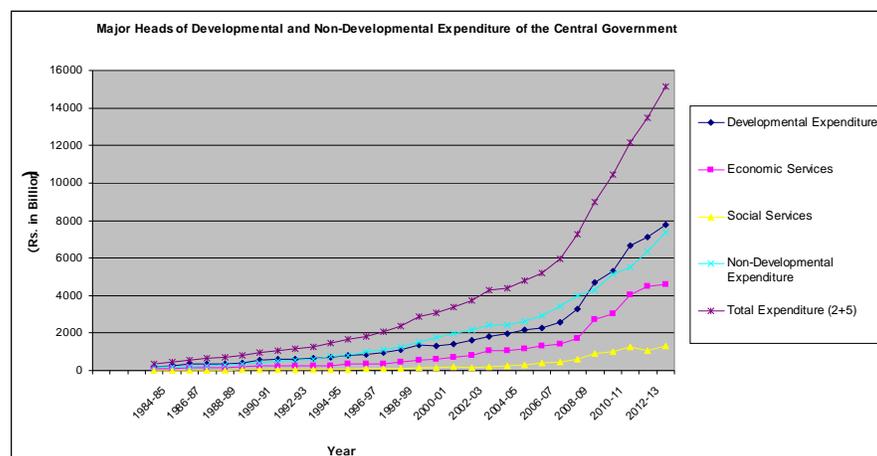
Notes:- 1. Data for 2011-12 are Revised Estimates and data for 2012-13 are Budget Estimates.

2. Total Expenditure and Developmental Expenditure of 2007-08 include an amount of Rs. 355.31 billion on account of transactions relating to transfer of Reserve Bank's stake in SBI to Central Government.

3. Data on development and non development gross expenditure are inclusive of commercial and postal departments.

Source: Budget documents of the Government of India.

Major Heads of Developmental and Non-Developmental Expenditure of the Central Government



Public expenditure has grown rapidly since independence and there has been change in the pattern and composition of public expenditure. The data given above in the table reflects that the total expenditure has grown from Rs. 377.1 bn in 1983-84 to Rs. 336856 bn and to Rs. 15152.25 bn for the year 2012-13 (estimates). Increasing participation of the government in economic life has caused the proportion of development expenditure to the total expenditure to increase rapidly however defence expenditure has also been rising rapidly due to threat to India's security. The graph depicted above also shows the trends.

Subsidies on food, fertilizers have become an integral part of Central Government and despite government's frequent promise to reduce them they are continuing to rise year to year. Recently in an effort to curb leakage of food grains meant for ration shops the central government is considering direct transform of food subsidy to ration card holders will launch a pilot project in 6 Union territories (UTs) from January, 2013. The other alternative model involve distribution of food grain at the rate closer to the market price through PDC and transfer of food subsidy to other beneficiaries bank account to minimize leakage and reducing the expenditure. The government's food subsidy given to run the public distribution system (PDS) is likely to be Rs. 91,000 cr in the current fiscal against Rs 72,823 cr in 2011-12.

The total expenditure on interest payments, defence, subsidies and General Services account for 80% of the current non planned revenue expenditure. While the development expenditure in the absolute terms has been higher than the non development component, the latter has been rising farther throughout the 80's and 90's.

In spite of continuously increasing development expenditure, economic growth has not risen to levels already achieved in many other less developed countries. Public fund are not used rationally and that is why inspite of targets are realized seldomely. In some industries unutilized capacity existed while some other industries find it difficult to meet existing demand with their present capacity. It relates to the outcome of inconsistencies in the Indian Planning System.

Main expenditure control measures in India

- Reduction of Non plan expenditure
- Reduction of Defence Expenditure
- Increment of administered prices like power, fertilizers.
- Restriction of provision of the major subsidies.
- Reduction of job in Government Departments, Public Sectors under taking (PSUS).
- A greater portion of expenditure is to be devoted to legitimate public goods.
- Some public goods are to be transferred to the local government.

- Increase in capital expenditure.
- Neutrality between present and future expenditure.
- A greater focus on public goods outcomes.
- Improvements in institutional mechanisms.

Recommendations:

- Decrease interest payment.
- Increase capital expenditure.
- Greater share should be transferred for developmental heads rather than to salaries and subsidies.
- Increase expenditure in social sectors.
- The return from the expenditure should be based on outcomes rather than outlays.
- To give attention to the productivity aspect of the public expenditure.
- Need for improvement in design and effectiveness of financing management information system.
- Objective of operational efficiency through better design and implementation of the programme should be achieved by the ministries and use of optimal mix of inputs for better output.
- Accounting heads are to be exhaustive as possible and any addition done should be after careful consideration of accounting principles.
- Distinctions between capital and current expenditure should be more clearly defined.
- An evaluation of the costs and constraint on financing and efficiency costs of different types of revenue is likely to cultivate a culture of accountability by ensuring that spending programs will be examined in terms of both their social benefits and social costs.
- The growth of non-plan expenditure at the State level depends on the state government. Under the existing system of federal financial relations, transfer of funds from the centre to the state takes place through the Finance Commission and Planning Commission and such transfers influence the size of non-plan expenditure of State Governments. But the impact of central transfers on different components of non-plan expenditure has not been assessed rigorously. It has to be taken care off.

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