



# Inclusive Development in Bihar: The Role of Fiscal Policy

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# Introduction



- Fiscal policy is a means to achieving inclusive growth.
- Despite impressive growth performance, uneven regional spread.
- Two way relationship between lack of development and poor law and order and poor governance and lack of development.
- What factors determine the growth performance of different regions is an issue that needs to be understood better.
- It is important that for inclusive growth political and economic stability, lagging regions must catch up with the rest of the country in accelerating growth, creating employment and reducing poverty.
- Inclusive growth is a function of policies, institutions and resources. In some ways, resources depend on policies and institutions. In a federal set up, policies and institutions of both centre and states are important. The issue is, what can the state do in this constrained situation?

# Growth Performance in Different States



- Large differences in per capita GSDP and increasing disparity. In 1980-81, difference between the highest and lowest per capita income in states was 3 times. In 2009-10, it is more than 4 times; Bihar: Rs. 15038; Maharashtra: Rs. 63000.

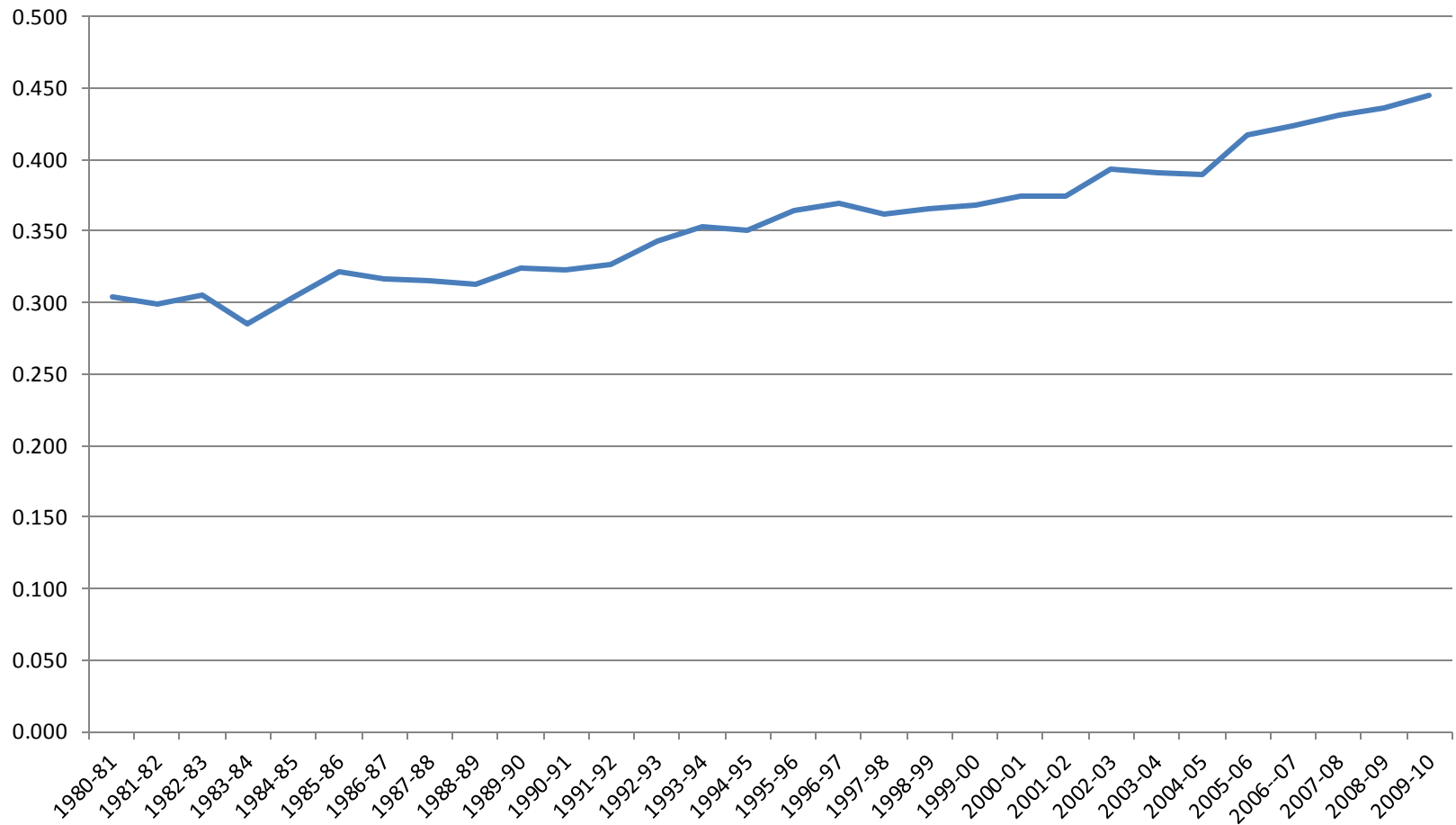
## Growth of per capita GSDP

Year	All States	Bihar
1981-1994	4.6	3.6
1995-2003	4.9	4.7
2004-2010	8.7	9.7

- Acceleration in growth: Positive correlation with per capita income throughout 30 years; CV increased from 0.31 in 1981-82 to 0.45 in 2004-05.



# Coefficient of Variation in Per Capita GSDP Among States: 1980-2009.



# Determinants of Growth



- Institutions, Policies and Resources.
- Institutions:
  - Minimalist State: Olson's roving bandits, stationary bandits and encompassing governance.
  - Institutions determine the structure of incentives: First stage is ensuring law and order; Second stage is to streamline the administration to deliver the services and to ensure competitive infrastructure to minimise transaction costs of conducting business.
  - Competitive governments – preconditions for stable intergovernmental competition.

# Determinants of Growth: Policies

- Policies:
  - Abundance of labour is an advantage if the right policies are made;
  - Central policies are presumed to be neutral across regions. Freight equalization scheme; pricing and subsidy; labour laws.
  - States' policies should be to attract investments into the state.
  - Prioritization to human development is an important means of ensuring inclusive growth. Particular focus should be on education and skill development.
  - Competitive infrastructure is critical for inclusive growth.



# Determinants of Growth: Resources

- Resources:
  - Need to find sufficient capital to enhance economic activity by harnessing the resources.
  - Attracting private investment requires minimizing transaction cost of conducting business (governance);
  - States have predominant role in the provision of social and co-equal role with the centre in the provision of physical infrastructure.
  - States' fiscal policies should ensure adequate spending on essential social and physical infrastructure.

**Table 2**  
**Per Capita Development Expenditures in Major States in 2009-10 (in Rs)**

<b>States</b>	<b>Per capita GSDP (2009-10) (at 2004-05 current prices)</b>	<b>Per capita Education Expenditure (2009-10)</b>	<b>Per capita Health Expenditure (2009-10)</b>	<b>Per capita Social Service Expenditure (2009-10)</b>	<b>Per capita Economic Service Expenditure (2009-10)</b>	<b>Per capita Development (Economic + Social Service) Expenditure (2009-10)</b>
Andhra Pradesh	56869.88	1222.47	507.27	3786.84	4441.80	8228.63
Assam	30821.58	1551.34	686.17	2998.23	2129.45	5127.67
Bihar	17616.45	809.78	243.37	1495.07	1360.71	2855.78
Chattisgarh	46213.23	1412.88	491.89	3713.79	2646.45	6360.24
Gujarat	74240.65	1313.68	642.89	3407.70	3738.28	7145.98
Haryana	87182.73	2214.02	1031.88	4180.91	5330.21	9511.12
Jharkhand	34503.39	1133.68	371.07	2707.61	1460.68	4168.29
Karnataka	57400.06	1466.25	598.87	3863.60	3567.07	7430.67
Kerala	67363.42	1748.98	661.43	3167.82	1736.32	4904.14
Madhya Pradesh	30785.78	1795.30	363.69	1885.82	1983.26	3869.07
Maharashtra	81689.91	2126.58	449.48	3487.37	3491.60	6978.98
Orissa	40372.91	1373.76	543.06	2587.29	2156.66	4743.95
Punjab	73308.84	1260.73	557.25	2803.61	2576.00	5379.61
Rajasthan	38586.16	1319.42	851.89	2870.10	1694.60	4564.70
Tamil Nadu	69473.92	1560.12	665.60	3996.08	3190.94	7187.02
Uttar Pradesh	26590.97	1774.52	347.33	1984.81	2166.99	4151.80
West Bengal	45387.25	965.32	229.71	2368.06	2387.53	4755.59
Corr. Coefficient of Per capita GSDP with Developmental Heads		0.487	0.545	0.763	0.739	0.796

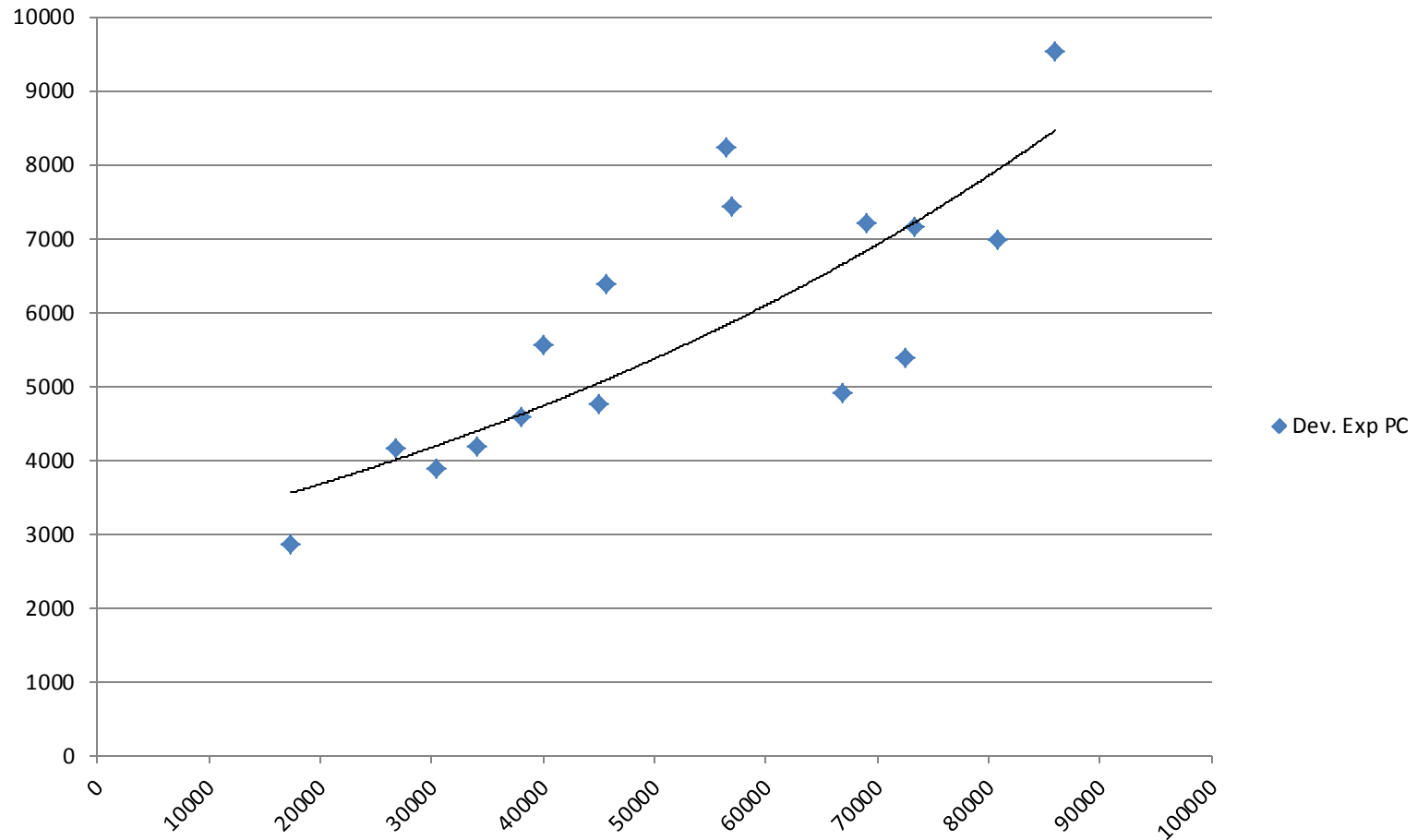
Note: Health Expenditure includes Medical and Public health, Family welfare and water supply and sanitation







## Per Capita Development Expenditures in States: 2009-10



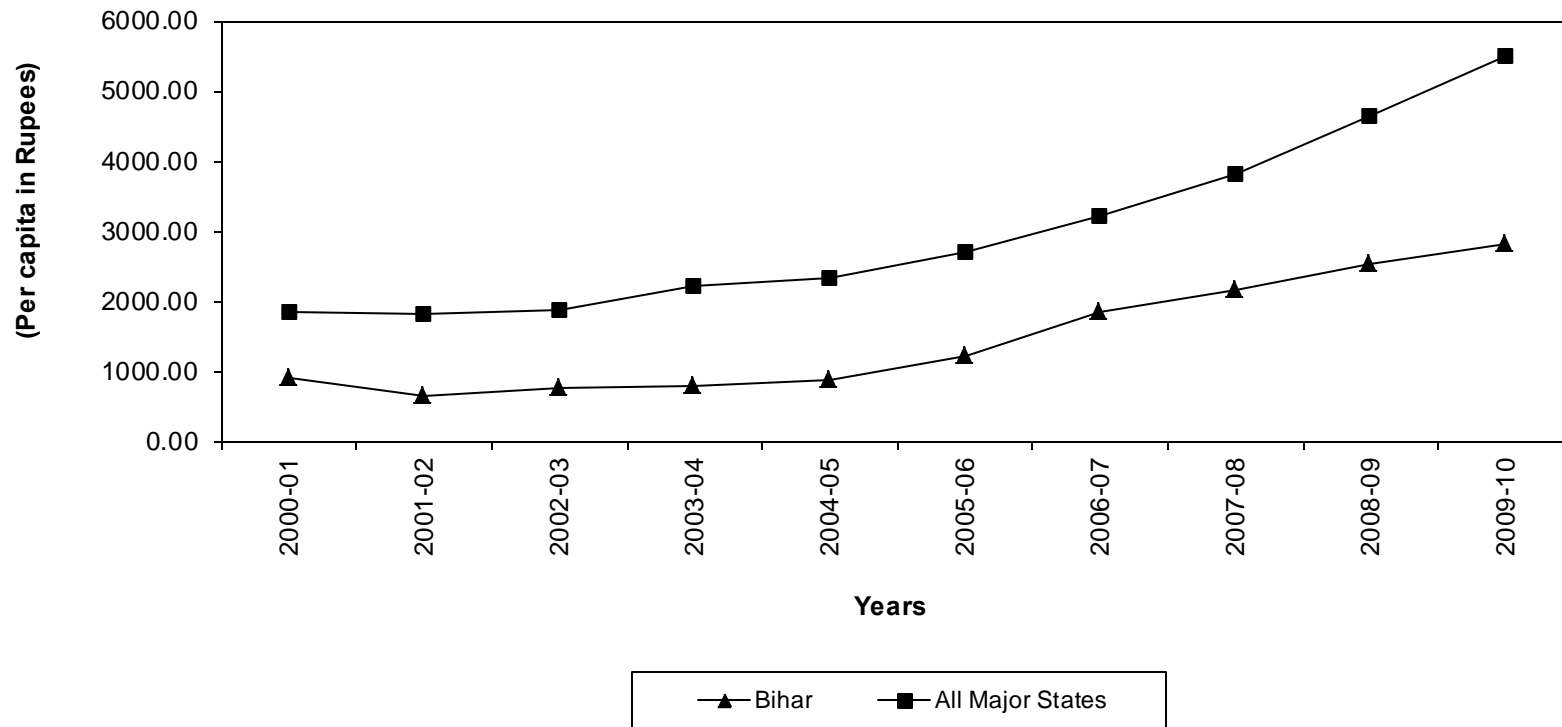


# Strengthening Infrastructure

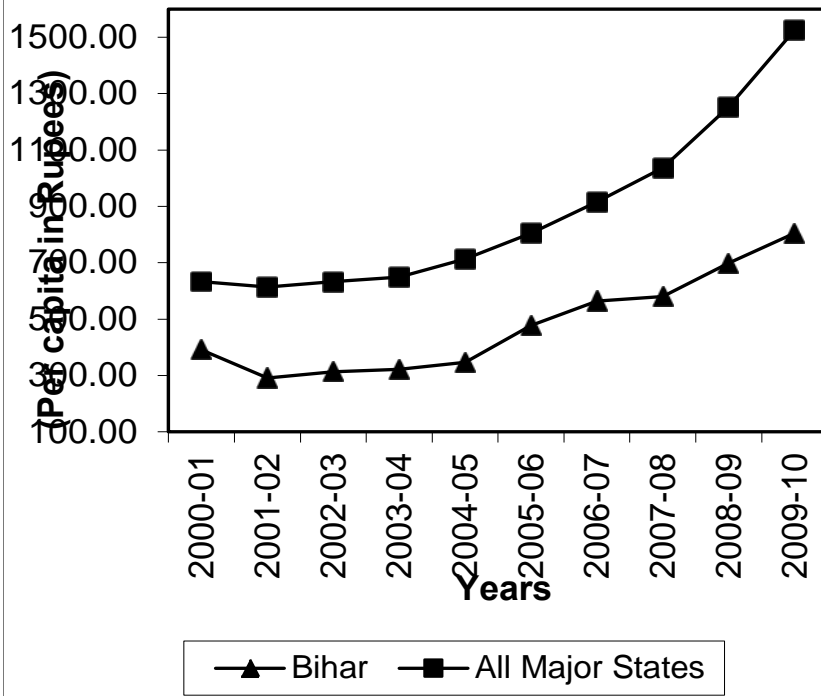
- Central initiatives have been meager in strengthening social and physical infrastructure; To a considerable extent, this shows the lack of priority of political parties in the state.
- Expenditure levels are low; more and better spending is needed.
- There is considerable need to augment infrastructure for production, storing and marketing of farm products.
- Need to strengthen educational institutions, healthcare in rural and urban areas and skill development; The state has to devise policies to enhance skill development in collaboration with the private sector to ensure that MGNREGA does not condemn the poor to perennial poverty.
- Improving the quality of government schools and health centres is critical.
- The state has been rightly focusing on roads which is important for inclusive development. Another area with great potential for inclusive growth is tourism. This requires infrastructure development, regulation and skill development in services.

# Pattern of Development Expenditures in States

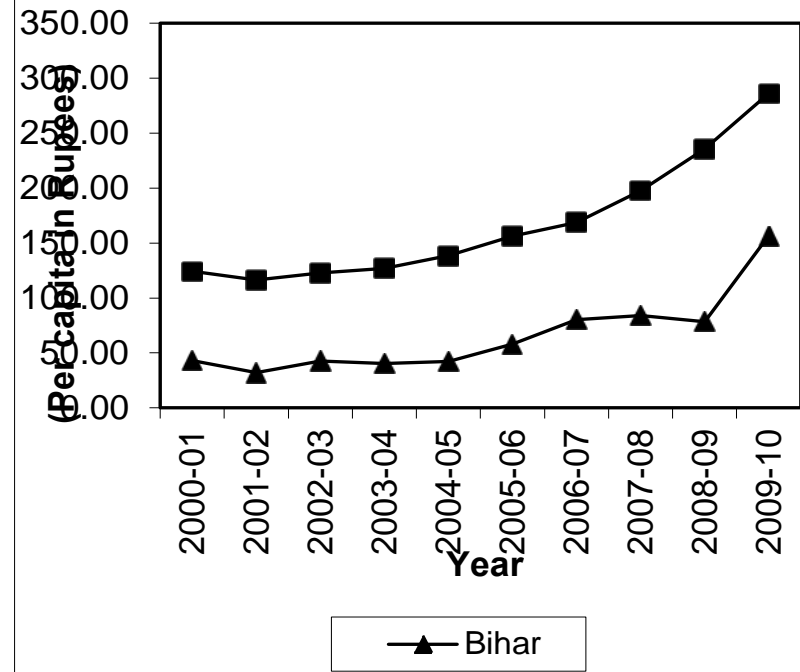
Figure 1: Per capita expenditure on Developmental Expenditure for Bihar and All General Category States



**Figure 1: Per capita expenditure on Education for Bihar and All General Category States**

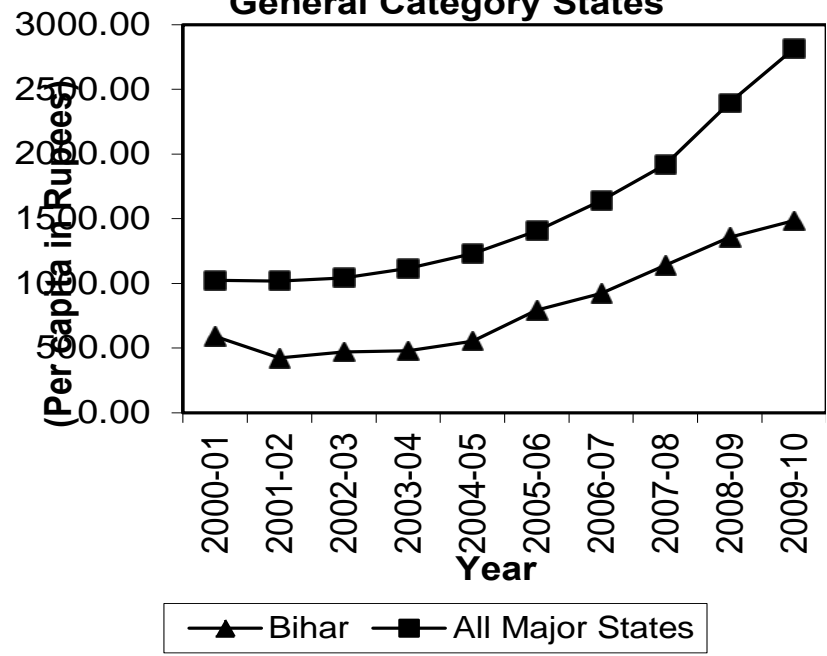


**Figure 2: Per capita expenditure on Medical and Public Health for Bihar and All General Category States**



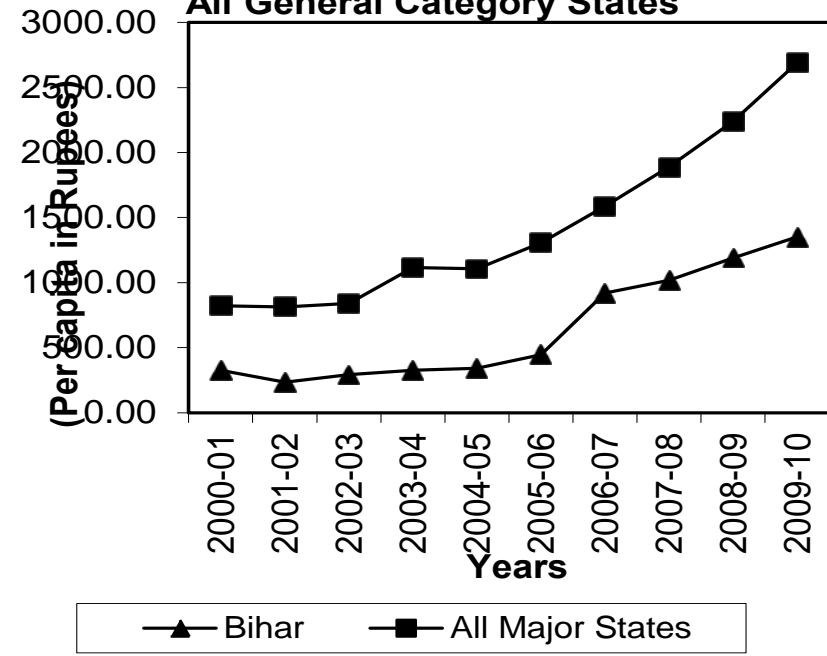
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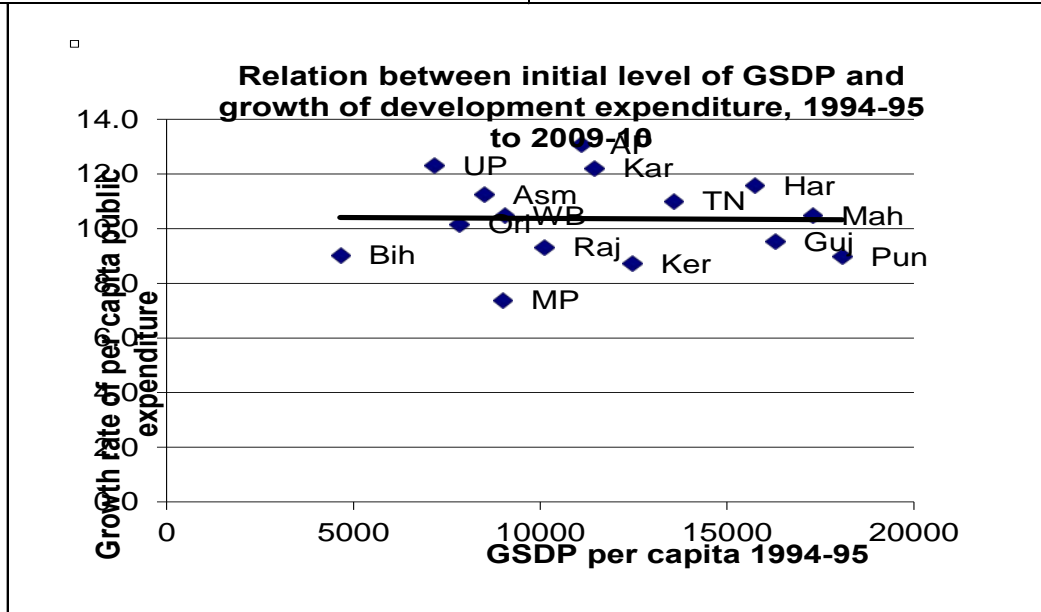
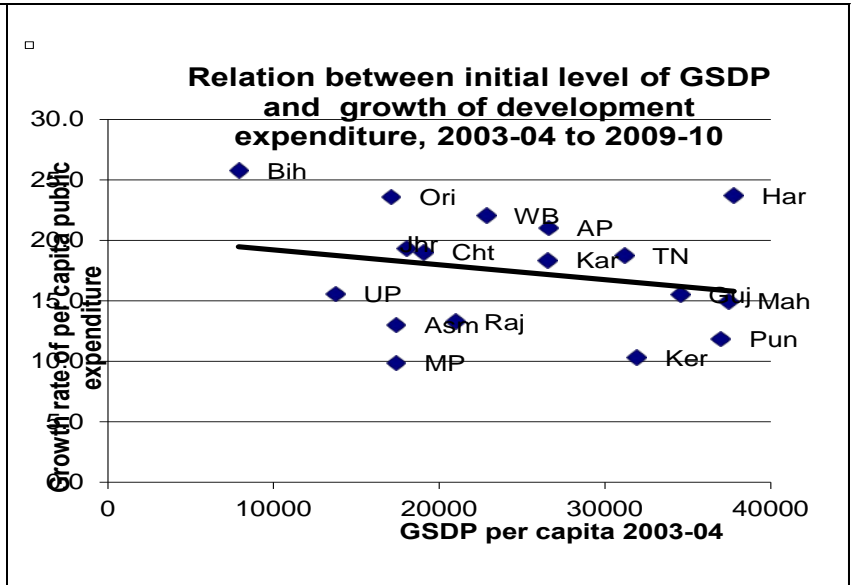
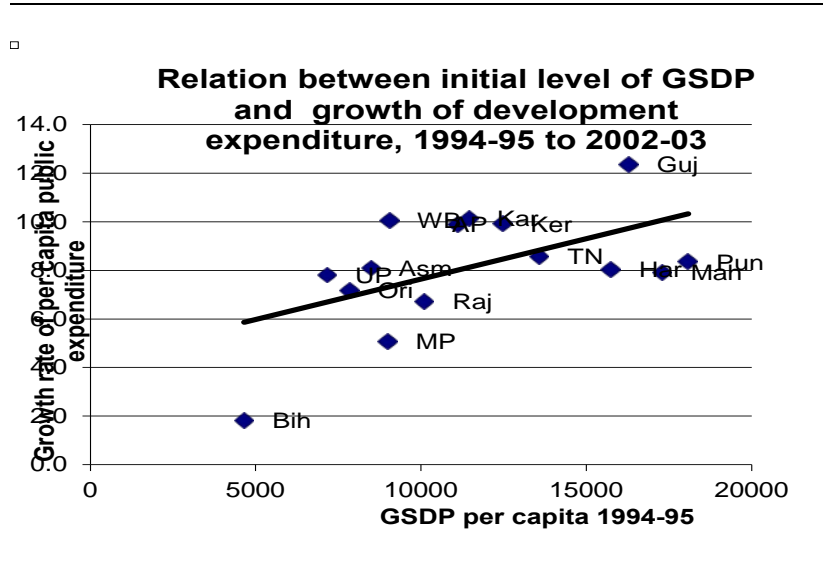
**Figure 3: Per capita expenditure on Social Services for Bihar and All General Category States**



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**Figure 4: Per capita expenditure on Economic Services for Bihar and All General Category States**





# Reasons for Low Development Expenditures

- Own Tax revenue is not high: 4.8% of GSDP. (Average: 6.7%0. West Bengal: 4.2%: Karnataka: 8.7%; Tamil Nadu: 8%.
- Intergovernmental Transfers are equalizing, but do not fully offset fiscal disabilities. Not designed to enable the states to provide comparable level of public services at comparable tax rates.
- The share of poorer States in investment and employment central enterprises is lower.



## Tax - GSDP Ratios in General Cat. States

1.Andhra Pradesh	8.6
2.Bihar	4.8
3.Chhattisgarh	6.1
4.Goa	7.4
5.Gujarat	6.1
6.Haryana	6.5
7.Jharkhand	4.9
8.Karnataka	8.7
9.Kerala	7.6
10.Madhya Pradesh	8.0
11.Maharashtra	6.2
12.Orissa	5.5
13.Punjab	6.9
14.Rajasthan	6.5
15.Tamil Nadu	7.6
16.Uttar Pradesh	5.8
17.West Bengal	4.2
Total: Gen. Cat	6.7







# States' Own Tax Revenue

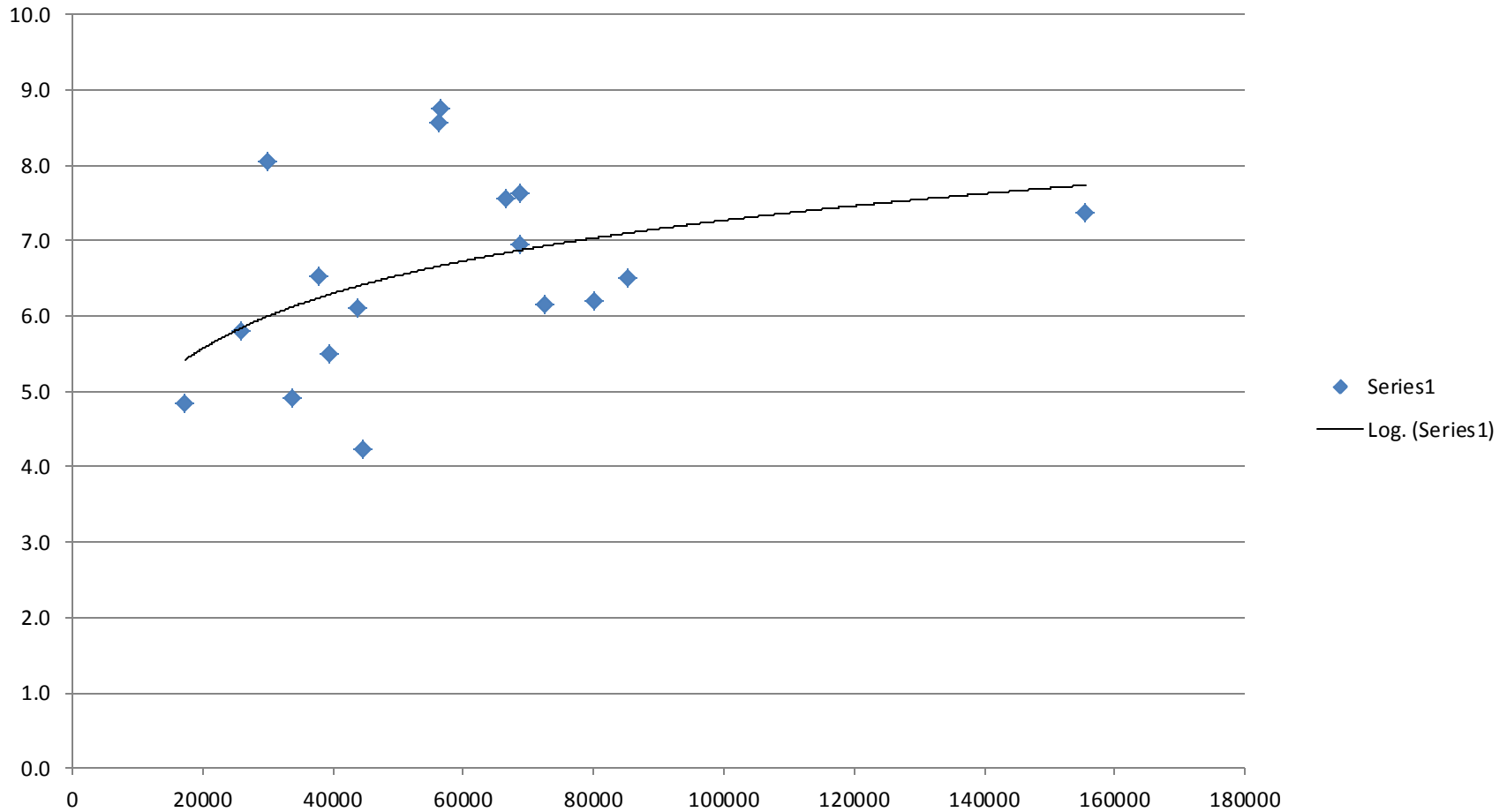
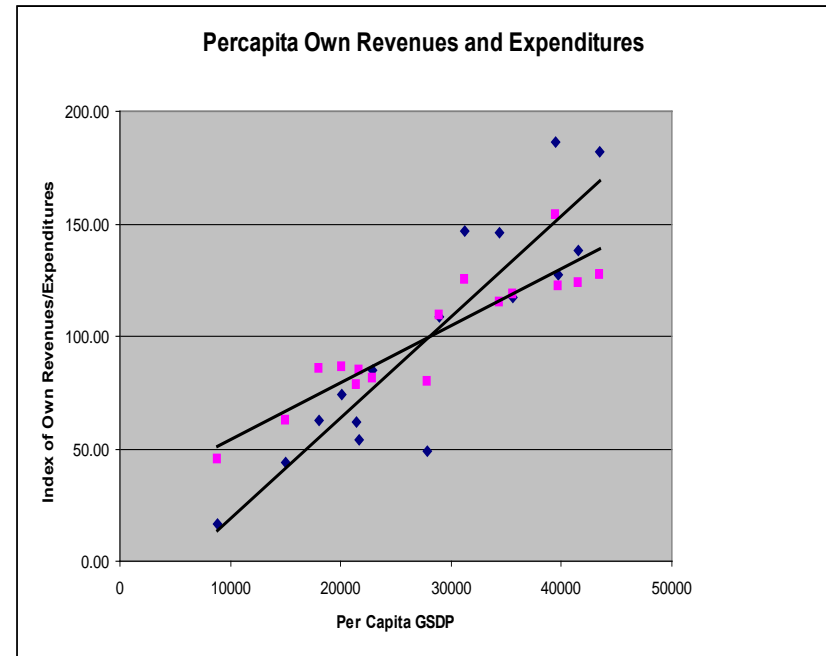
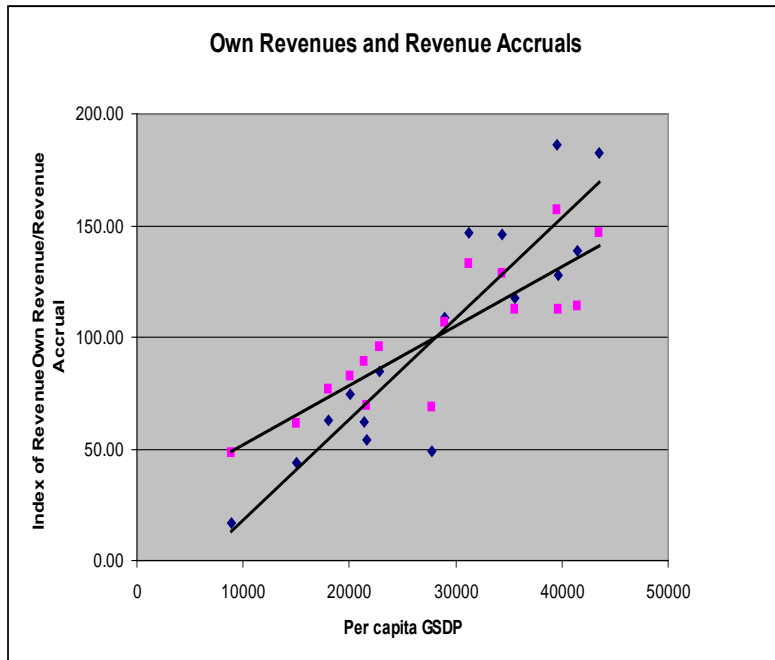


Figure 2  
Extent of Equalization in Central transfers to States





# Distribution of Centre's Subsidies

	Petroleum Subsidy	Food	Fertilizer	Agri. Marketing and Insurance	Central Road Fund	School and Higher Education	Total	Per cent of GSDP
General Category States	450.25	170.11	243.47	11.52	12.83	<b>25.65</b>	913.84	3.90
Andhra Pradesh	489.01	276.17	361.93	25.13	5.80	<b>24.34</b>	1182.37	<b>4.00</b>
Bihar	226.82	68.22	149.45	8.32	2.50	<b>10.18</b>	465.49	<b>4.94</b>
Chattisgarh	335.58	291.00	245.87	0.38	9.97	<b>14.81</b>	897.62	<b>3.64</b>
Goa	1646.55	52.20	60.69	0.00	0.00	<b>50.28</b>	1809.72	<b>2.42</b>
Gujarat	632.93	79.08	294.58	16.32	17.41	<b>13.09</b>	1053.42	<b>3.19</b>
Haryana	867.49	59.02	610.53	52.70	24.00	<b>26.14</b>	1639.88	<b>3.90</b>
Jharkhand	320.80	145.23	55.11	17.97	3.47	<b>14.56</b>	557.13	<b>3.41</b>
Karnataka	550.83	248.73	297.86	2.35	19.21	<b>16.94</b>	1135.91	<b>3.81</b>
Kerala	520.09	199.83	69.85	0.55	9.16	<b>27.18</b>	826.67	<b>2.55</b>
Madhya Pradesh	334.12	141.45	211.54	4.66	12.11	<b>36.41</b>	740.28	<b>4.79</b>
Maharashtra	623.71	141.82	243.92	2.13	20.33	<b>21.93</b>	1053.84	<b>2.92</b>
Orissa	339.81	288.18	129.31	0.61	12.90	<b>22.82</b>	793.63	<b>4.48</b>
Punjab	842.46	18.38	791.04	0.54	23.09	<b>39.45</b>	1714.97	<b>4.67</b>
Rajasthan	429.15	61.71	177.21	73.46	21.31	<b>21.81</b>	784.66	<b>4.33</b>
Tamil Nadu	624.63	396.61	194.25	7.60	19.67	<b>31.64</b>	1274.40	<b>4.13</b>
Uttar Pradesh	317.99	149.26	245.96	1.34	10.42	<b>37.46</b>	762.44	<b>5.73</b>
West Bengal	350.84	185.78	183.13	3.82	7.80	<b>28.67</b>	760.04	<b>3.10</b>

## Inter-State Allocation of Investments in Central Government Enterprises – 2003-04

	Population Share	GSDP Share	Investment Share	Employment Share
Goa	0.14	0.44	0.07	0.12
Punjab	2.41	3.97	1.56	1.72
Maharashtra	9.57	15.09	19.38	12.80
Haryana	2.08	3.24	2.34	1.29
Kerala	3.15	4.09	2.75	2.77
Gujarat	5.00	6.86	7.04	3.26
Tamil Nadu	6.16	7.94	6.92	5.42
Karnataka	5.23	6.34	5.32	5.11
Andhra Pradesh	7.53	8.66	7.63	6.34
West Bengal	7.91	8.40	5.28	13.48
<b>High Income States</b>	<b>49.19</b>	<b>65.02</b>	<b>58.30</b>	<b>52.31</b>
Rajasthan	5.58	4.98	2.77	1.91
Chhattisgarh	2.05	1.71	2.17	6.40
Madhya Pradesh	5.97	4.67	4.97	6.77
Jharkhand	2.67	1.79	4.11	15.32
Orissa	3.64	2.42	5.65	4.18
Uttar Pradesh	16.42	10.38	7.18	5.48
<b>Bihar</b>	<b>8.20</b>	<b>2.99</b>	<b>1.87</b>	<b>1.17</b>
<b>Low Income States</b>	<b>44.53</b>	<b>28.94</b>	<b>28.72</b>	<b>41.23</b>
Special Category States	6.28	6.04	12.98	6.46
<b>Total</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>

# Political Economy of States' Development



- In the changed political context, are long term development policies sustainable?
- How do we make the development policies systemic?
- Erosion of federal value and its long term ramifications.
- Failure of the finance Commissions.

# Concluding Remarks

- Bihar needs more and better spending. Need to create fiscal space to increase developmental spending. One of the few states containing revenue expenditures to increase capital expenditures.
- Tax administration reform is the key to increasing own revenues. The most important measure is to improve the information system.
- Development expenditures will have to increase substantially: Education, teachers' training and skill development; healthcare; roads; agricultural production, processing and storage, small irrigation works.
- Power sector needs a closer look. Per capita consumption is the lowest.
- Need to harness central schemes better; Good information system is the key.
- Strategic relationship with the centre to ensure greater central investments.