

Institute of Development Policy and Management
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India:
Public Finance and Development 1980-2005

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Comparative Country Profiles 2000



	USA	Brazil	Russia	China	India
Population	282 M	166 M	145 M	1260 M	1000 M
Area	9.4M Sq Km	8.5M Sq Km	17M Sq Km	9.6 M Sq Km	3.3M Sq Km
% area cropland	21% (1.9M)	6% (.5M)	8% (1.4M)	10% (1M)	57% (1.8M)
% area forest	32%	66%	45%	13%	16%
Agriculture/GDP	2%	8%	7%	21%	29%
GDP(PPP)	\$ 9870 Bn	\$ 1200 Bn	\$ 722 Bn	\$ 5900 Bn	\$ 2233 Bn
GDP per capita	35000	7710.8	4979.3	4682.5	2038
Gini Index	0.34	0.58	0.5	0.41	0.34
Trade/GDP	20%	21%	60%	43%	27%
S&P Credit Rating	AAA	BB-	B	BBB	BB
Life Expectancy	77 years	67 Years	65 Years	69 Years	62 Years
Adult Literacy	100%	84%	100%	81%	52%



China-India: Similarities



- Amongst the **five biggest** countries in the world in terms of geographical extent, population, market-size and economy (PPP)
- **Ancient** prosperous civilizations, economically ahead of Europe before the Industrial revolution.
- **Colonized** by western powers, and attained independence in mid twentieth century.
- Amongst the **fastest growing** major economies today: China's growth industry led, India's services led.
- Followed a **socialist, ISI** model of development before opening up: China late 70's, India early 90's.
- The **State sector** continues to dominate economic activity even today, although role of private enterprise is expanding fast.
- In both China and India rapid economic growth has widened regional **economic disparities**: in China, the coastal areas versus the interior; In India, the south and west versus the north and east.



China-India: “Simi-rences”



- Big **Diaspora** a major factor in big foreign currency reserve build-up. Chinese Diaspora more entrepreneurial (FDI), Indian more professional (Invisibles). External liquidity situation very comfortable.
- China very competitive in **visible exports** (manufactures), India in **invisible exports** (software services)
- Both face serious **fiscal problems** and ballooning domestic debt and would need to carry out a major public sector adjustment in the foreseeable future. India has a weaker fisc, China, weaker banks.
- Both countries face major future **developmental threats**: for India it is economic growth, whereas for China the threat is more institutional, as these are not in synch with the needs of a market economy.
- **Corruption** endemic in both China and India. In China it is more centralized around the entrenched party which practically guarantees quick action. In India corruption is more dispersed, and outcomes less certain. Because corruption in India is subject to legislative, press and judicial oversight, it is less of a systemic risk than in China.



China-India:Differences I



- Pre-reform, China had made much greater investment in the social infrastructure such as health and education and agricultural infrastructure than India, thereby mostly eliminating absolute **poverty**. India has the single largest mass of poor people in the world.
- China has shown greater urgency for **public sector restructuring**, and WTO accession is expected to intensify the process, with an unpredictable impact on political institutions.
- China is a **closed society** run by a tightly knit communist party (bereft of socialist ideology); India is an open, democratic society, with an independent judiciary and press.
- Local government in China have effective economic decision making powers, whereas India's **centralized control** is loosening only gradually.
- China has low **trade barriers** (custom tariff collections only about 3% of value of imports); India's customs tariffs still amongst the highest in the world.



China-India: Differences II



- Domestic **savings** about one-third higher in China (40%)
- China at the outset had an aggressive **FDI policy** for attracting investment in the labour intensive manufacturing sector in coastal SEZs insulated from the domestic policy environment. Gradually moving up the technology chain. India initially encouraged FDI in high technology and infrastructure sectors, which were difficult to absorb, and is only now liberalizing down the value chain.
- China invested huge amounts of public funds in developing its **infrastructure**; India relied relatively more on private funding, which has been slow to fructify, with a negative fall-out on growth.
- China has a very strong **political commitment** to reform at the top and in the regions. India has a weak, though growing, consensus.
- Political dissent not aired in the public domain which gives China **overt political stability** arguably difficult to sustain during a severe economic downswing/public sector restructuring. India has a long history of frequent transfer of political power through the ballot box at both the federal and State levels, an overt instability which nevertheless underscores the inherent stability its political institutions.

Indian Economic Development: Overview

- Major policy **shift in 1991** de-regulating the economy
 - Industrial delicensing; Interest rates left to market forces; Capital markets freed; Rupee floated on current account; openness to Foreign investment; trade barriers lowered;
- Tax reforms sustained over last 15 years: VAT introduced in 2005
- Still a **relatively closed** economy by global standards.
- **External** payments position **comfortable**
- National Income **growing by about 6%** over the last 20 years
- **Govt. sector** in heavy **deficit**
- **Agriculture and Labour** markets relatively **untouched** by reform.
- Fast growing services sector, esp. **IT and ITES**
- Weak physical and social **infrastructure major constraint** on growth.
- **Slow reduction in poverty**, mainly trickle down of enhanced growth rates.
- **First round** of reforms (Federal level) crisis driven and **swift**; **second** round (mostly State level) consensus driven and **staggered**.

Reform Outcomes – External

(March 92 versus March 05)

- **External debt ↑\$85B to \$ 123 B but ratios improve**
 - EDT/GDP ↓ from 36% to 21%
 - FE Reserves ↑ from \$ 2.2 B(1M import cover) to \$ 142 B (13M import cover)
 - EA/Capital flows ↓ 25% to 6%; FI/Capital Flows ↑ 37% from Nil.
- **Manageable CAD because of Invisibles**
 - TB/GDP ↑ from -3 to -6.4%; CAD/GDP ↓ from -3.5% to -1.1%
 - Greater eastward orientation of merchandise trade
 - Invisibles trade westward oriented
- **Stable rupee:**
 - No sharp variations in real exchange rates
 - Nominal depreciation against US\$ about 3.5% PA over last 10 years
 - Float takes wind out of hawala market
- **Economy more open: CA/GDP ↑ 23.8% to 54.4%**

Reform Outcomes – Domestic

(Indicators averaged for 1980-81 to 1990-91 and 1992-93 to 2004-05. Crisis year of 1991-92 excluded)

- **Average Growth Rates constant at 5.8%**
 - Agriculture declined from 4.48% to 2.6% (Unreformed, monsoon linked)
 - Industry: ↓ from 7.4% to 5.9%
 - Growth led by services ↑ from 6.4% to 7.5%
 - GDP Composition
 - Share of services in GDP ↑ from 48% to 58%,
 - agric. ↓ 31% to 20%
 - industry K at 21-22% between 1992 and 2005
- **Poverty and employment - Outcomes contested.**
 - Poverty ↓ 55% in 1973-74 to 36% in 1993-94 and 26% in 1999-2000 (World Bank: 29% under \$1/Day/PPP)
 - Employment growth ↓ from 24% in the 80's to 15% in the 90's. (Decline in both organized and unorganised sectors)
- **Fiscal management weak**
 - Consolidated GFD of Centre and States K at around 9% of GDP. Centre ↓ States ↑
 - Combined liabilities of Centre & States ↑ from 51% (1980) to 87% (2005) of GDP
- **Big backlog in Infrastructure investment remains**
- **Inflation**
 - Price inflation ↓ from 9% to 6.9% (double digit unacceptable politically)
 - Differential between US inflation and Indian ↑ from 3.6% to 4.6%.
 - Asset (BSE) inflation ↓ 24.3% to 11.6%.
- **Interest Rates**
 - Nominal (SBI Bank) rates ↓ from 16.5% to 13% (10.5% presently), Real rates ↓ from 7.5% to 6.1%
 - Real differential between US Prime and SBI Bank Rate ↑ from 1.5% to 1.7%.

Savings, Investment & Taxes

(Indicators averaged for 1980-81 to 1990-91 and 1992-93 to 2003-04. Crisis year of 1991-92 excluded)

- **Savings/GDP ↑ from 20% to 24%**
 - Public sector savings ↓ 2.8% (to negative)
 - Household savings ↑ 5% (to 20%)
 - Corporate savings ↑ 2.1% (to 3.9%)
- **Foreign savings/GDP ↑ from 1.3% to 2.4%**
 - Substantial proportion sterilized by the Central Bank
- **Domestic capital formation ↑ 1.8% (to 22.3% of GDP)**
 - Private capital formation ↑ 4.5% (to 15.4%)
 - Public sector ↓ 2.7% (to 6.9%).
- **Tax/GDP Ratios still to return to pre-reform levels**
 - ↓ from average of 16.8% to 16%
 - Federal tax ratios ↓ while State taxes ↑ modestly



Regional Growth and Fiscal Parameters



%	Nat.Inc. 2002-03	NSDP Growth (%)		2002-03 Audited Accounts				
		1993-2003		NSDP Per Capita	Soc.Ser.Exp	GFD	Debt	Own Tax Rev.
		<i>Real</i>	<i>Per Capita</i>	<i>Rupees</i>	<i>% of GSDP</i>	<i>% of GSDP</i>	<i>% of GSDP</i>	<i>% of GSDP</i>
8.1%	Andhra Pradesh	59	43	18820	7.1	4.8	28.2	7.9
6.2%	Karnataka	73	51	18251	7	4.7	24.9	9
8.0%	Tamil Nadu	57	43	21433	6.4	3.7	22.6	8.9
3.5%	Kerala	55	43	21853	7.2	5.3	35.6	8.3
6.8%	Gujarat	77	48	22838	7.2	5.6	29.2	7.4
14.4%	Maharashtra	51	27	26113	5.9	4.2	19.8	8
0.4%	Goa	96	70	52277	7	5	32.2	7
47.4%	Average Peninsular	67	46	25940.7	6.8	4.8	27.5	8.1
3.8%	NCT Delhi	113	54	47477	4.7	2.8	13.4	7.2
3.7%	Punjab	39	20	26032	4.8	6.2	45.3	7.2
3.1%	Haryana	65	33	26974	5.5	3.6	26.3	8.2
10.6%	Average High Income Northern	72	36	33494.3	5.0	4.2	28.3	7.5
8.4%	West Bengal	86	62	18756	6	7.2	38	4.2
2.2%	Orissa	35	19	10340	9.8	8	60.1	5.9
3.0%	Bihar	66	33	6015	12.7	8.9	75.5	5.3
2.1%	Jharkhand	65	32		9	4		4.6
4.7%	Madhya Pradesh	29	7	11483	8.5	4.3	38	6.9
1.5%	Chhattisgarh	22	8		6.8	2.1		7
4.9%	Rajasthan	54	23	12753	9	6.3	42.8	6.7
9.6%	Uttar Pradesh	35	11	10289	6.8	5.4	41.2	6.1
36.4%	Average Low Income Northern	49	24	11606.0	8.6	5.8	49.3	5.8
	Federal liabilities/GDP						69	
	Federal & State Liabilities/GDP						83	

REGIONAL DEVELOPMENT INDICATORS	HDI Ranking	% BPL	Total Literacy	LE at Birth	Infant Mortality	Sex Ratio	Per capita Consumption	Per Capita Elect. kWh	Percentage Unemployed
	1991	1999-00	2001	92-96	1991	2001	1999-00	1996-97	1999-00
Andhra Pradesh	23	15.8	61.1	62	55	978	551	346	1.4
Karnataka	19	20.0	67.04	62.9	74	964	639	340	1.4
Tamil Nadu	14	21.1	73.47	63.7	54	986	681	468	2.6
Kerala	3	12.7	90.9	73.1	42	1058	816	241	8.6
Gujarat	17	14.1	66.43	61.4	78	921	678	694	0.8
Maharashtra	15	25.0	77.27	65.2	74	922	697	556	2.9
Goa	4	4.4	82.32		51	960	1015	724	13.6
Average Peninsular	14	16.2	74.1	64.7	61.1	970	725	481	4
NCT Delhi	2	8.2	81.8		54	821	1316	577	3.6
Punjab	12	6.2	69.95	67.4	74	874	792	792	2.1
Haryana	16	8.7	68.59	63.8	52	861	768	504	1.2
Average High Income Northern	10.0	7.7	73.4	65.6	60.0	852	959	624	4
West Bengal	20	27.0	69.22	62.4	62	934	572	194	4
Orissa	28	47.2	63.62	56.9	125	972	414	309	2.6
Bihar	32	42.6	47.53	59.4	75	921	417	138	2.4
Madhya Pradesh	30	37.4	64.08	55.2	133	920	479	367	1.1
Rajasthan	27	15.3	61.03	59.5	87	922	611	301	0.8
Uttar Pradesh	31	31.2	57.36	57.2	99	898	517	197	1.4
Average Low Income Northern	28.0	33.4	60.5	58.4	96.8	928	502	251	2
National Average		26.1	65.2	60.7	77	933	591	334	2.3

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SWOT Analysis

- **STRENGTHS**

- **Robust, services driven growth**
- **External sector**
 - High reserves
 - Invisible flows
 - ↓Debt service ratios
- **Fiscal Deficit**
 - No external spill
 - Limited crowding out effect
- **Big domestic Market**
- **Young labour force**
- **Limited external contagion**
- **Knowledge based eco.activity**
- **Agricultural potential**
- **Limited long-term pol.risk**

- **WEAKNESSES**

- **Fiscal position**
 - power
 - privatization
 - public employment
 - State deficits
- **Big POL deficit**
- **Agriculture growth rates**
- **Inflexible labour market**
- **Infrastructure**
 - physical
 - social
- **Emerging North-Peninsular divide**
- **Governance**
- **Poverty, Social Security and Pensions**

India 2005: Ten Imperatives

- **Fiscal consolidation** in the Centre and States
- **Privatization** and Roll-back of the State
- Redirecting public expenditure to substantially improve the **Infrastructure** – transport, power, urban, rural, social.
- Carrying forward **domestic and external (Tariff) Tax** reforms
- **Labour** market reforms
- Deepening **financial sector** reforms, including Capital Account convertibility
- Reforming the **agricultural** regime
- **Social security and pensions**
- Improving **governance**
- Pushing up **growth** to over 8% to absorb growing labour force.



Kerala Model: Indicators



Amartya Sen and Jean Dr'eze: HDI comparable to developed countries despite relatively low per capita income. National HDI Rank # 3 (NHDR 2001)

	Kerala	India
Settlement Pattern	Rurban	Urban - Rural
Land reforms	Successful	Partial
Growth Rate	6%	6%
Income Poverty (99-00)	12%	26%
Per capita consumption (99-00)	Rs. 816	Rs. 591
Telephone density per 1000	68	32
Literacy (2001)	91	65
Sex Ratio (2001)	1058	933
Life Expectancy (92-96)	73	61
Infant Mortality (1991)	42	77
Per capita elect. Consumption (96-97)	241 KwH	334 KwH
Unemployment (99-00)	8.6%	2.3%
Services Sector	64%	58%



Kerala: Remittance Economy

1999-00: State per capita Net income 13% and consumption 38% above National Average

- Pros

- Safety valve for high chronic **unemployment**
- **Counter-cyclical** effect
- Increases **consumption**:
 - lower poverty
 - higher expenditure on health, education etc.
- Higher **growth** through more investment (construction boom)
- Improves **public finances**
 - Sales tax, VAT and excise revenues
 - Contains potential fiscal expenditures arising out of high unemployment, poverty, etc.

- Cons

- Depresses **domestic savings** by creating illusion of household financial stability
- Vulnerability to external **shocks**
- **Wage inflation** has negative impact on investment and growth
- **Moral hazard** – diminishing pressure for reform

Kerala: Fiscal & Growth Parameters

	1987-92	1992-97	1997-02	2002-05
Debt/Revenue Receipts	189%	187%	245%	306%
Debt/GSDP	32%	28%	32%	41%
RR/GSDP	17%	15%	13%	13%
Own revenue/Total Revenue	69%	69%	72%	74%
Own Tax/GSDP	9.8%	8.9%	8.5%	9.0%
Revenue Deficit/GSDP	-2.1%	-1.4%	-4.0%	-4.3%
GFD/GSDP	-4.7%	-3.5%	-5.5%	-5.6%
Revenue Receipts/Total Expenditure	81%	84%	72%	73%
Total Expenditure/GSDP	21%	18%	18%	18%
Salary & Pensions/Revenue Receipts	70%	56%	67%	63%
Salary & Pensions/Total Expenditure	57%	47%	48%	45%
Salary & Pensions/GSDP	11.8%	8.3%	8.6%	8%
Salary, Pensions & Interest/Revenue Receipts	84%	73%	90%	90%
Salary, Pensions & Interest/Total Expenditure	68%	62%	64%	65%
Salary, Pensions & Interest/GSDP	14.2%	10.9%	11.6%	12%
Real Growth Rate	6.7%	7.7%	5.4%	6.4%
Agriculture/GSDP		30%	23%	15%
Industry/GSDP		21%	22%	22%
Services/GSDP		48.50%	55%	62%



Kerala: The Roadmap Ahead

- **Fiscal** correction
- **Redirect public expenditure** to maintain/upgrade Infrastructure
- Target **high unemployment** by:
 - Leveraging \$ 8-10B of major **PPP/BOT** infrastructure investment taking place over next 5 years.
 - Creating **investor friendly climate** to crowd in more private investment, especially in the booming services sector
 - Tourism
 - IT and biotechnology
 - Healthcare
 - Addressing **skills mismatch**
 - High white collar unemployment rate
 - Export of labour: remittance economy
 - Import of blue collar labour
- Address crisis in **traditional** and Plantation sectors

Thank-you for your patience



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