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# CID at Harvard University :: Budget and the Development Decade

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## Budget and the development decade

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NEW DELHI has proclaimed the new decade as a Decade of Development, during which India will meet bold targets for economic growth and social development. What are the challenges in meeting these goals? We suggest that the 2001-02 Budget should be the operational policy document for the Decade of Development:

### The fiscal strategy

The Centre must undertake a fundamental review and reorientation of fiscal policies to support the Decade of Development. There are three goals. First, the overall fiscal deficit must be reduced sharply. Second, the expenditure should be shifted from economic sectors (infrastructure), where the private sector can carry the investment burden, to social sectors (health and education) where increased public spending is vital. Third, social programme should be redesigned to make maximal impact per rupee spent. This can best be accomplished by replacing generalised subsidies (such as the Public Distribution System or free electricity for farmers) with targeted programmes (such as school meal programmes).

The Centre's fiscal deficit is around 5 per cent of GDP, and this should be reduced significantly to ensure macroeconomic stability, and to prevent an unmanageable buildup of public debt. At the same time, social spending should rise, including on health and education. Most of this should come

from cuts in current expenditure rather than from increases in taxation as a per cent of GDP. Current government spending (of the Centre and the States) is already around one-third of GDP, which is quite high compared with other developing countries in India's income range. If India were to increase expenditure further as a per cent of GDP, it would have a very difficult time raising the internal tax revenues to cover the spending programme.

We can identify the following prime areas of potential expenditure reduction over a three-year period, beginning with the upcoming Budget:

### Central expenditure:

- 1) Disinvestment of PSUs (with revenues used to reduce the public debt): The net worth of Central PSUs is estimated to be Rs 1,32,400 crore, a little over 13 per cent of GDP. The capital employed is placed at around Rs 2,23,000 crore. (Estimated savings 1.5 per cent of GDP.)
- 2) Closure of loss-making PSUs: Of the 236 Central PSUs, 104 are loss-making that account for roughly Rs 4000 crore in annual losses to the Central exchequer. (Estimated savings 0.4 per cent of GDP.)
- 3) Reduced bureaucracy: A freeze on new employment matched by normal attrition through retirement and death. On an average, about 1.25 lakh Central employees are taken off government payroll each year due to these reasons. Implementation of such an approach over four years could result in a reduction in the Central government employment by 12.3 per cent, or a reduction of around half-a-million employees from the present total of about four million. On an average, the Government could

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save about Rs 1000 crore every year on account of reduced wages and salaries, and the associated reduction in the operating expenses. Over a three-year period, this would imply savings of roughly 0.3 per cent of GDP. (Estimated savings 0.3 per cent of GDP.)

4) Central power sector undertakings support to SEBs: The SEBs owe huge sums to the Central power sector undertakings, such as the National Thermal Power Corporation (NTPC), the National Hydro Power Corporation (NHPC), Damodar Valley Corporation (DVC), and the Power Finance Corporation (PFC), etc. It is estimated that as of September 1998, the SEBs owed Rs 16,800 crore to these Central power sector undertakings. (Estimated savings 1 per cent of GDP.)

5) Reduction in subsidies, including PDS and transport. (Estimated savings 0.5 per cent of GDP.)

6) Reduced infrastructure investments, taken over by private-sector projects: Annual infrastructure investment for the country is placed at around Rs 60000 crore (\$13 billion) which is roughly 6 per cent of GDP. We figure that a little less than quarter of this amount can be reduced (1.3 per cent of GDP at the Centre) in investments per year if the private sector were to take on large-scale investments in the infrastructure sector.

(Estimated savings 1.3 per cent of GDP.)

We estimate expenditure saving that could be achieved by each of these line items to a total of approximately 5 per cent of GDP over three years. Perhaps, these bold cuts could be augmented by 1 or 2 per cent of GDP in increased tax collections, though credibility in collecting more taxes would depend firmly on making sharp cuts in major areas of waste.

It may seem politically impossible to proceed with such bold cuts, but it should be remembered that

these cuts would be combined with substantial increases in public and private spending. Public spending would rise in health and education, including some highly visible and politically popular programmes such as school meals and increased availability of primary health

facilities. Private spending in infrastructure would also be politically popular, as it will mean the much faster diffusion of new technologies (cellular phones, Internet connectivity) to the rural areas.

#### Setting development targets

The starting point for the Decade of Development is the setting of development targets for India. One key target is the rise in national income – the Prime Minister had announced two key targets in his Independence Day speech, one to achieve a doubling of the per capita income by 2010 and the other to achieve universal primary education by the same time frame. But targets should also include improvements in health and education, as well as political participation. We, therefore, recommend the following targets for the Decade of Development:

First, a doubling of the per capita income between 2000 and 2010. This requires average per capita growth of the Gross National Product of 7 per cent per year. In the light of population growth of around 2 per cent per year, the total GNP should increase by around 9 per cent per year.

Second, a decline of infant mortality rates from around 80 per 1000 live births to below 30 per 1000 live births by 2010. This should be combined with explicit targets for halting the AIDS epidemic, and treating key diseases such as malaria, tuberculosis, and other major killers.

Third, reduction of adult illiteracy from around 45 per cent to less than 20 per cent by 2010.

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Fourth, universal primary education for ages 5-14 for girls and boys by 2010, with a school for all within 5 km of home. Finally, all villages possessing electricity, a trunk road, telephone and Internet connectivity, a school, clean water and sanitation, a village health worker, and local self-government by 2010.

### Two pillars of development

There are two basic pillars of economic development. Broadly speaking, these are human development and economic growth. Human development signifies the ability of every individual to reach their full potential as healthy and educated citizens. Economic growth signifies the broad-based and sustained increase in per capita GNP. Sustained economic growth depends on favourable business conditions, high levels of private sector investment, technological upgrading, and successful integration into global markets.

There can be no sustained economic development without strong successes in both human development and economic growth. Development strategy, therefore, requires major public commitments to social sectors (especially health and education) and to improvements in the business environment in order to promote large-scale private investments needed for economic growth.

From a budgetary point of view, government resources need to be shifted towards investments in human development, leaving the private sector with the major responsibilities for increased economic growth. The Government at both the Centre and the State should commit much greater resources to public health and education. At the same time, the government should turn over major infrastructure investments (in ports, airports, telecommunications, Internet, electricity, large-scale water and sanitation facilities, and major roads) to private investors who can finance these projects using private capital.

The major budgetary challenge is to shift government spending away from low-priority areas (such as untargeted subsidies, excessive bureaucracy, and investments that can better be left to the private sector) towards high-priority areas such as health and education that can only be met by public spending. India should also mobilise international financial support for the decade of development. This includes larger aid flows for human development as well as much greater flows of private investment to speed economic growth.

### Meeting the human development challenge

India has not yet met the human development challenge. Adult illiteracy remains almost 50 per cent, and up to 60 per cent for women. Almost half of all children do not finish primary school. Only around 20 per cent are in secondary school. Infant mortality rates are high by international standards, and life expectancy at around 63 years is much lower than in China, other countries in East Asia, and the advanced economies. Fertility rates are still very high, and the population continues to grow rapidly, pressing hard on India's fragile ecosystems and natural environment.

There is a severe under-investment in both public health and education. The Government (the Centre and the States) spends less than 1 per cent of GNP for health, compared to an average of around 3 per cent for all developing countries, and more than 5 per cent for high-income countries. The public health services are in bad shape, especially at the primary level. Study after study shows that the primary health centres (PHCs) fail to provide an adequate set of services for the population. The poor are left with almost no health services, besides the very meagre services that they can pay for out of pocket.

The situation in health will get worse, not better, if there is no increase in public investment in health. The AIDS epidemic threatens to rise dramatically

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in the coming years. Malaria is resurgent, as is tuberculosis linked especially to AIDS.

India needs a similarly bold strategy for universal education, at least through age 14. Special attention is needed to ensure the education of girls on the same basis as boys, and to ensure the continuation of children in school through the ninth year.

Public spending in education should rise from the current level of around 3 per cent of GNP to at least 5 per cent of GNP (and probably more) to meet these goals. This money should be spent mainly by State Budgets, but with local responsibility for overseeing the effective operation of schools.

Studies have shown that more parents would like to send their children to school, but are dissuaded from doing so because of school fees, the poor quality of education in many schools, and great distances from home to school in the rural areas.

One of the most effective ways to increase student enrollments is through the provision of free school meals (school breakfasts or mid-day meals, or both). Tamil Nadu has been very successful in implementing a mid-day meals programme, and this example should be generalised throughout the country. School meals not only improve enrollments and attendance, but also childhood nutrition. Regular school meals can be augmented with nutritional supplementation, such as Vitamin A tablets on a six-month basis.

The social agenda should focus most urgently on health and education, but it should also include other social initiatives, such as increased political participation at the village-level (through village councils or panchayats), and greater social and political equality for girls and women.

[\(To be concluded\)](#)

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