Budgetary Constraint's and Growth Scenario in Uttar Pradesh

Manoj Kumar Agarwal

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Introduction

There is a growing concern that inter-state disparities in India have been increasing since the advent of economic reforms in India whereas economic performance at the country level has been improving. At the national level, as K.C. Pant observes, "…the process of economic reforms taken up in earnest by us since 1991 has yielded rich dividends from a situation of crisis at the turn of the decade, today India is one of the ten fastest growing economies in the world…" (Howes *et. al.,* 2003, p. 27). He also argues that for the reforms to pick up momentum, states would have to take the lead. The mid-term appraisal of the Ninth Plan as well as the Tenth Plan showed concern about disparities among states. The Tenth Plan argues that "A major task that the country has to undertake in response to this challenge during the Tenth Plan is to narrow down these disparities" (GoI, 2002b; Vol. III; p. 123). Acharya (2002) puts it differently and argues that fiscal strain in states and lack of reforms are speed-breakers in the way of India's medium-term growth prospects. It has been highlighted by Ahluwalia (2002) and later endorsed by Shetty (2003) that inter-state inequalities have been increasing in India. Agarwal (2004) has noted that food-surplus states like Uttar Pradesh are growing at slower pace while food-deficient

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states are growing at higher and accelerated pace since the 1990s. Dholakia (2003) has also stressed the regional disparity in economic performance and argues that in terms of economic and human development there has been decline in regional disparities.

On the whole, the focus has been on orienting and implementing economic reforms at the state level in such a manner that lagging states are also able to develop quickly. It has been felt that reforms at the state level were ignored initially. This needs to be corrected with the participation of the centre and other concerned agencies. Fiscal position of the states has deteriorated since late nineties as indicated by the revenue deficit of all the states, which remained at less than 1 percent of GDP up to the mid-nineties and started increasing to reach more than 2 percent in recent years. Similarly, gross fiscal deficit of the states as a ratio of GDP increased from below 3 percent to above 4 percent in the same period. In the face of growing fiscal crisis across the states, it was realised that this must be given importance over other issues so that particularly backward and more crisis-ridden states like Uttar Pradesh can orient their fiscal strategies to put their finances in order and provide support to growth. This could also be used to energise the dormant economic forces that can be instrumental in attracting private investments at a pegged-up level.

Uttar Pradesh is a huge state having one-sixth of the population of the nation. By virtue of being the top-ranking state of India in terms of population, it has the maximum representation in Parliament of 80 members, i.e., it constitutes almost 15 percent of the Lok Sabha. Uttar Pradesh is also politically privileged as it has given eight prime ministers to the nation so far who have ruled the country for more than four decades in the parliamentary history of more than five decades. However, it is also true that Uttar Pradesh has been lagging behind the other states of the country. Its economic prospect is not very encouraging. Even the role of the state does not seem to be defined with sufficient force and direction. Evidence of this ambiguity can be found in the internal structural constraints of the fiscal measures being pursued by the Government of Uttar Pradesh. This paper endeavours to establish a relationship between budgetary constraints and poor economic growth in Uttar Pradesh. The present paper comprises five sections. In section-II, we try to present a broad growth scenario of the state economy as well as the status of socio-economic development. Section-III attempts to deal with the fiscal scenario of Uttar Pradesh wherein broad trends are analysed regarding pattern of expenditures, resource mobilisation, and indebtedness while in section-IV indicators of fiscal discipline and efforts to introduce reforms for better results are reviewed. The last section tries to derive growth imperatives of the fiscal scenario and also reach some policy conclusions.

II. Economic Performance of Uttar Pradesh

Indicators of Development

Since any effort through planning or fiscal strategies is aimed at raising the level of development, both social and economic, it is desirable to begin with a discussion of the status of development in Uttar Pradesh, *vis-à-vis,* all India and the most progressive states. We are not comparing it with other parts of world for the simple reason that targets established by the progressive states of the Indian economy itself would require a great deal of sustained effort for the state to match. Table-1 illustrates the backwardness of Uttar Pradesh in absolute as well as relative terms. Demographically, Uttar Pradesh is one of the most backward states of India as birth rate is very high; infant mortality rate is not declining at a desirable pace; literacy rate is still far from satisfactory; and life expectancy is low because of high IMR and high crude death rate. Going through economic parameters, it is discerned that per capita income in Uttar Pradesh is very low. It is 54 percent of the all-India average and only 38 percent of the highest per capita income among the states in 2001-02. The reason can be traced to both poor economic performance and high population growth in the state. Per capita consumption of electricity was less than half of the national average in 1999-2000 and is just one-fifth of Punjab. Area under commercial crops in Uttar Pradesh is around 16 percent of the total cropped area while it is as high as 59 percent in Gujarat. The situation is more unpalatable in the industrial sector, which is far behind the national average. At a time when other states are improving the growth rate of industrial sector, this sector shows signs of fatigue in Uttar Pradesh even before it could have any significant achievement. Thus, the state is characterised by poor social and economic infrastructure, low output, low human development index, and high incidence of poverty and unemployment. All these might be attributed to inadequate capital stock in the economy as well as lack of sustained investments through either public or private sectors.

Table: 1: Indicators of Development: Uttar Pradesh, Top State and India

Indicator	Period	Uttar Pradesh	Best performing major state	India
Literacy rate (%)	2001	57.4	90.9 (Kerala)	65.4
Life expectancy (years)	1993-97	58	73 (Kerala)	-
Crude birth rate	2002	31.6	16.9 (Kerala)	25.0
Crude death rate	2002	9.7	6.4 (Kerala)	8.1
Infant mortality rate	2002	80	10 (Kerala)	63
Urbanisation (%)	2001	20.8	43.9 (Tamil Nadu)	27.8
Per capita electricity consumption (KWH)	1999-2000	175.8	921.1 (Punjab)	354.7
Poverty ratio (%)	1999-2000	31.2	6.2 (Punjab)	26.1
Area under commercial crops(%)	2000-01	15.8	59.4 (Gujarat)	24.3
Per capita income at current prices (Rs.)	2001-02	9,749	25,652 (Punjab)	17,947
Industrial output (Rs.)	2000-01	3,948	25,496 (Gujarat)	9,111
Per capita value-added in industries (Rs.)	2000-01	587	3,360 (Gujarat)	1,417
Index of social & economic infrastructure	1999	101.2	187.6 (Punjab)	-
Per capita institutional investment (Rs.)	2001	619	1172 (Kerala)	-
Share in institutional projects in India (%)	September 2003	4.7	10.9 (Maharashtra)	100.0
Human development index	2001	0.388	0.638 (Kerala)	0.472

Table: 2: Trend Growth Rate of State Income in Uttar Pradesh
(At 1980-81 prices; per cent per year)

	Sectors	1980-81 to 1989-90	1990-91 to 1999-00	1993-94 to 2001-02#
1.	Agriculture & animal husbandry	2.74	2.27	2.52
2.	Forestry & logging	-23.79	-1.00	25.32
3.	Fishing	13.21	6.64	7.45
4.	Mining & quarrying	2.93	5.74	9.58
A.	**Primary sector**	**2.46**	**2.36**	**3.20**
5.	Manufacturing	10.40	7.04	2.02
(a)	Registered manufacturing	14.80	7.71	0.11
(b)	Unregistered manufacturing	5.49	5.90	4.71
6.	Construction	1.34	3.57	11.73
7.	Electricity, gas & water supply	16.43	-1.97	-4.61
B.	**Secondary sector**	**8.25**	**5.76**	**4.21**
8.	Transport, commu. & trade	4.12	4.38	4.35
9.	Finance & real estate	8.98	6.30	4.11
10.	Community & social services	8.05	4.69	6.02
C.	**Tertiary sector**	**6.33**	**4.94**	**4.76**
	Net state domestic product	**4.79**	**4.04**	**4.03**
	Population	2.36	2.15	2.33
	Per capita NSDP	**2.38**	**1.85**	**1.66**

\# At 1993-94 prices.
Source: Based upon data from the bulletins of State Income Estimates published by Economic & Statistics Division, State Planning Institute, Uttar Pradesh.

Pattern of Economic Growth

The year 1980-81 was a turning point in the Indian economy as the pace of economic growth and development picked up and a reasonable growth rate of well above 5 percent was realised. Annual growth rate of the national economy improved from 5.4 percent in the 1980s to above 6 percent in the following decade. Thus, it is obvious that at the national level growth prospect has improved. Surely, this aggregate performance must have derived its strength from various states that would have contributed to it. However, Uttar Pradesh seems to have moved in an unexpected direction. A review of the growth scenario of Uttar Pradesh since 1980-81 (Table-2) reveals that annual trend growth rate of the net state domestic product (NSDP) was 4.79 percent during the decade of the 1980s. This growth rate was lower than what was obtained at the national level. Even this growth rate could not be maintained afterwards. The trend growth rate at 1980-81 prices has been 4.04 percent during the period of 1990-91 to 1999-2000. If we estimate it at 1993-94 prices, the growth rate has been the same (4.03 percent) for the period

1993-94 to 2001-02. Consequently, growth rate of per capita income has also been lower at 2.38 percent in the 1980s and below 2 percent in the following period.[1] Here, the negative role of population growth is evident. More than half of the economic achievement in this slow growing economy is getting neutralised owing to high population growth rate of above 2 percent.

A comparison of performance during the last two five year plans reveals that the growth rate of the national economy was 6.7 percent in the Eighth Plan period (1992-97), declining to 5.5 percent in the Ninth Plan period (1997-2002). However, in the state economy, growth rates in the respective plans have been 3.2 and 3.0 percent only, i.e., half of the achievement of the national economy. In the opening year of the Tenth Five Year Plan, i.e., 2002-03, growth rate of the state economy has been just 0.3 percent[2] as against a target of 8 percent. In similar economic conditions, the Indian economy grew by 4.2 percent despite large slippages. This resulted in the ratio of per capita income of Uttar Pradesh to that in India deteriorating further from 65.9 percent in 1993-94 to 54.2 percent in 2001-02 and the contribution of the state to the national income declining from 10.3 percent to 8.8 percent during the same period. These facts can be further corroborated when we compare per capita income of Uttar Pradesh to the state with the highest per capita income. The distance is widening without interruption as the ratio declined from 53.3 percent in 1980-81 to 42.6 percent in 1996-97 and further to 38.0 percent in 2001-02. On the whole, performance of the state economy, *vis-à-vis*, Indian economy and other states has been a matter of disappointment because while some states have been improving their economic and social performance, Uttar Pradesh has been losing ground.

Table 3: Trend Growth Rate of Gross Domestic Product in India
(At 1993-94 prices; percent per year)

Sectors	1980-81 to 1989-90	1990-91 to 2000-01	1980-81 to 2000-01
Agriculture and allied	2.92	3.10	3.20
Primary	**3.22**	**3.40**	**3.40**
Manufacturing	7.34	7.07	6.87
Electricity, gas and water supply	9.21	6.26	7.87
Secondary	**6.60**	**6.71**	**6.52**
Transport, storage and communication	5.79	8.18	6.73
Tertiary	**6.85**	**7.93**	**7.13**
Gross domestic product	**5.38**	**6.11**	**5.69**

Note: Based upon data from **National Accounts Statistics of India: 1950-51 to 2000-01**; EPW Research Foundation, Mumbai; 2002.

Sectoral behaviour in Uttar Pradesh suggests that the adverse trends cut across the sectors. Sectoral composition of the state economy is such that in 2001-02, the share of the primary sector was 36.9 percent in the NSDP while the share of the secondary sector, stagnant since the mid-nineties, was 21.4 percent in 2001-02. The tertiary sector became the largest sector with a share of 41.7 percent. Structural backwardness of the state economy becomes clearer in comparison, as the three sectors shared 26.1, 24.4 and 49.5 percent respectively in the GDP of India in 2001-02. Moreover, weakening forces of growth are evident from Table-2 as the secondary sector's growth rate declined from 8.25 percent in the eighties to 5.76 percent in the nineties and further to 4.21 percent in the period of 1993-94 to 2001-02. This has been basically due to the fact that growth in the registered manufacturing sector came to a grinding halt and the infrastructure activities, mainly electricity, gas, and water supply, have been showing negative growth in recent years (-4.61 percent during 1993-94 to 2001-02) in contrast to a robust growth in the eighties (16.43 percent). Tertiary sector has also been showing weaker performance as the growth rate declined from 6.33 percent in the eighties to 4.76 percent during 1993-94 to 2001-02. In the primary sector, agriculture's performance remains poor and stagnant. However, fisheries, mining and quarrying do show some improvement. Contrary to state economy, in the national economy all the three sectors have shown better performance in the nineties as compared to the eighties (Table-3). On the whole, the growth process in the state economy is getting weaker leading to marginalisation in the national perspective as well as poor economic prospect within the state economy.

It is a matter of serious concern that the economy is not getting sufficient inducement to move on to a higher growth path, which becomes self-sustaining. This shows that there are bottlenecks in the economy that need to be removed through various initiatives of the government. Such efforts might take various shapes *viz.,* policy strategy, plan strategy, and fiscal measures. In fact, these are required to mobilise the forces of growth in the desired manner. This is equally relevant in the changed economic scenario in the country after 1991. Eventually, we have to look into the role of fiscal measures being adopted by the Government of Uttar Pradesh to energise the lagging economy. However, before going in to this issue we should examine plan efforts in Uttar Pradesh and other parameters where role of fiscal strategy becomes relevant, directly or indirectly.

Plan Expenditures in Uttar Pradesh

It is argued that the planning process has helped the Indian economy in accelerating its growth performance. As a consequence, larger private investment also flows in to supplement the initiatives of the plan investments. That is, plan and other public investments are expected to generate 'crowding in' effect. Therefore, in the plan strategy, public sector investment is kept at high level to have direct and indirect inducement effects. Keeping this in mind, we can also analyse the pattern of plan investments in the Uttar Pradesh economy. A brief examination of the per capita plan investment shows that it has always been lower than that for all states' average (Table-4). The ratio of per capita plan expenditure in Uttar Pradesh to that of all states taken together was around 65 percent in the first two plans and it increased rapidly to 93.0 percent in the Fourth Plan. But thereafter, there has been a decline in the ratio throughout and it came down to 73.0 percent in the Eighth Plan. In the Ninth Plan, the decline has been sharper (59.1 percent). What has been more alarming is the fact that the ratio declined to 54.0 percent in the Tenth Plan even though it has been estimated from outlay only. The same trend can be observed further if we estimate the share of total plan expenditure in Uttar Pradesh to that at the all-India level. This ratio was the highest at 7.8 percent in the First Plan and became 7.4 percent in the Fourth and Fifth Plans. But thereafter, there has been regular slippage and it has been the lowest in the Ninth Plan at 4.0 percent and in terms of even outlay, the ratio slipped further to a low of 3.7 percent when the state has one-sixth of the country's population.

Table 4: Plan Expenditures in U.P. and All States

Five year plans	Per capita plan expenditure in U.P. (Rs)	Per capita plan expenditure in all states (Rs)	Ratio of per capita plan expenditures in U.P. to all states (%)	Ratio of total plan expendture in U.P. to all states (%)	Ratio of total plan expenditure in U.P. to all India (%)	Ratio of total plan assistance to plan investments in U.P. (%)
First	25	38	65.8	12.3	7.8	
Second	32	51	62.7	11.0	5.0	
Third	72	92	78.3	13.3	6.5	
Fourth	132	142	93.0	15.2	7.4	
Fifth	329	361	91.3	14.5	7.4	
Sixth	588	718	81.9	13.3	6.0	35.5
Seventh	1077	1270	84.8	13.7	5.5	26.9
Eighth	1528	2144	73.0	11.5	4.5	59.6
Ninth	1766	2988	59.1	9.5	4.0	62.0@
Tenth@	3311	6126	54.0	8.9	3.7	59.3
Total (1951-2002)				**11.1**	**4.5**	

Note @ Plan Outlay.
Source Plan Documents and Statistical Diaries of Uttar Pradesh.

Thus, it is obvious that Uttar Pradesh has not been able to mobilise resources for plan investments and the relative share is deteriorating very fast. Now, if we look at Table-5, it is further affirmed that not only in relative sense, but also in absolute terms, plan investments in the state are not forthcoming to the extent it is claimed at the beginning of a plan. There has been a trend of big gaps. This trend is quite evident since the Ninth Five Year Plan (1997-2002). Plan investment envisaged for the Ninth Plan could not be realised fully as there was a huge gap of above 32 percent. As a result, in the last two years, outlays were reduced. However, the gaps persisted.

Table 5: Plan Expenditures in Uttar Pradesh

(Rs. crore)

Plan period	Approved outlay	Actual expenditure	Surplus deficiency (in %)
Seventh Plan (1985-90)			
1985-86	1751	1854	+ 5.9
1986-87	2150	2163	+ 0.6
1987-88	2630	2394	- 10.9
1988-89	2691	2665	- 1.0
1989-90	2971	2911	- 2.0
Eighth Plan (1992-97)	**21,000#**	**21,680$**	**+ 3.2**
1992-93	4040	3890	– 3.7
1993-94	4247	3433	- 19.2
1994-95	4760	4020	- 15.5
1995-96	5722	4436	- 22.5
1996-97	6774	5904	- 12.8
Ninth Plan (1997-2002)	**41,910##**	**28,386$**	**– 32.3**
1997-98	6,486	5,033	– 22.4
1998-99	9,235	5,648	– 38.8
1999-2000	10,260	5,843	– 43.1
2000-2001	8,122	5,897	– 27.4
2001-2002	8,400	5,965	– 29.0
Tenth Plan (2002-2007)	59,708*		
2002-03	7,250		
2003-04	7,728		
2004-05	8,500		

Source: Plan documents, Statistical Diaries and Budget documents of Uttar Pradesh.
***Notes:* *** Originally, the Tenth Plan outlay was fixed at Rs. 84,233 crore. But after assessment by the Planning Commission of India, it was found that due to resource constraint in Uttar Pradesh, it must be Rs. 59,708 crore. Still, the overall size of investment in the state economy was maintained at Rs. 3,64,645 crore,i.e., private investment level has been pegged up from Rs 2,80,412 to Rs 3,04,937 crore.
*#: At 1992-93 prices; ##: At 1996-97 prices; *: At 2001-2002 prices.*
$: At current prices.

The Tenth Five Year Plan (2002-07) has had to face rough weather from the stage of formulation. A total plan investment (public and private together) has been fixed at Rs. 3,64,645 crore. Out of this, initially it was proposed that the public sector investment would be at Rs. 84,233 crore. However, it got finalised at only Rs. 59,708 crore while not changing the overall plan investment. Indirectly, the private sector would have to accept the enhanced responsibility. Worse, the state plan outlays for the first three years of the Tenth Plan aggregated at only Rs. 23,478 crore, i.e., 39 percent of the total public sector outlay. Even these are unlikely to be realised. In such a situation, it is unrealistic to argue that the remaining investments would be forthcoming in the last two years of the Plan. Here, it needs to be pointed out that nominal plan outlays would go up if we adjust for price changes, as the plan outlays are determined at constant prices. Such a precarious situation in the state economy reflects upon growth and development mainly owing to paucity of funds. This is more pronounced since the mid-nineties or since the Ninth Plan. This is not helpful in even removing backwardness, social and economic; any discussion of taking the economy on a higher growth path remains largely academic.[3]

III. Fiscal Constraints

Since the decade of the nineties, fiscal health of almost all the state governments deteriorated with variation only in degree. The problem has a compounding effect, deeply scarring economies where fiscal health has not only become very weak and directionless but also economic growth has either been halted or highly moderated. These also tend to have low ranking in terms of human resource development, the major thrust area in the second leg of economic reforms. All these characteristics find simultaneous existence in Uttar Pradesh. Therefore, analysis of fiscal constraints operating in this economy assumes significance. In this section, we discuss the fiscal scenario in Uttar Pradesh, which shows regular deficits and lack of consistency in other areas over the years as far as its role in growth, development, and direction is concerned. The problem in the state economy seems to be deep-rooted while having structural overtones as well. These have their reflections in the budget formulation and fiscal strategy and we can analyse the issues accordingly.

Environment of the Budget Formulation

The significance of a budget lies in the seriousness and philosophy it embodies. There are various indicators to suggest that budget preparation is gradually becoming a mere ritual in Uttar Pradesh. There has been unprecedented political instability in Uttar Pradesh since the nineties; either there has been President's rule or frequent change of governments. In a situation of *ad-hoc* coalitions, the government tried to play safe and avoided all policies that might have gone against any section of population that was influential in the immediate context. The net result was that no meaningful strategy could be devised. Besides, lack of commitment about budgetary approach as a tool of economic development is reflected in presenting a budget as per convenience of the ruling party/coalition. Often, the budget in Uttar Pradesh is not presented in February or March. More than this, budget is not discussed adequately in the Assembly and passed without debate. Keeping in view developmental perspectives, it seems that political parties in Uttar Pradesh lack clarity of vision and commitment towards this annual exercise. Moreover, it is also becoming a practice not to appoint any full-fledged Minister to look after the finances of the state. As a tool of political power, most of the time budgets have been presented by Chief Ministers themselves who could not lend sufficient thought and time to the budget and state finances. There is no mechanism to properly monitor and enforce budgetary guidelines and the spirit of a budget often gets vitiated owing to lack of proper administrative system. On the whole, the scenario also reflects poor governance in Uttar Pradesh.

Fiscal Scenario

It is a common refrain that the fiscal scenario has worsened across states. However, the deterioration has been serious in Uttar Pradesh where even envisaged plan outlays are nowhere near being met. Despite tall claims and high targets, resource constraints have limited plan expenditures and this has resulted in continued slide down of plan expenditures/outlays in the national context. Therefore, it is obvious that in Uttar Pradesh, growth and development are seriously threatened on account of fiscal constraints. We now analyse fiscal trends mainly since the mid-nineties and try to find out how the situation can be reversed in this most populous and backward economy so that the budget plays a pivotal role in inducing investment realisations on a sustained basis.

Revenue Account

Table-6 reveals that revenue deficit has persisted in Uttar Pradesh for quite some time. Since the mid-nineties, the deficits have swollen, as they have been more than 3 percent of the GSDP. Since 2002-03, there seems to be some improvement but it is too early to be sanguine. In the year 2003-04, this ratio jumped up to 9.4 percent owing to an extraordinary situation of adjustment of government underwriting for a loan of Rs. 12,277.40 crore for the erstwhile UPSEB as a measure of power sector reforms. Even if this component is ignored, still the ratio of revenue deficit to GSDP is 3.6 percent. Therefore, it is difficult to suggest that sustained improvement in revenue deficit has been achieved in recent years. There are two broad components of revenue deficit, i.e., revenue receipts, and revenue expenditures. It can be seen (Table-6) that the receipts have been very low since the mid-nineties, but some improvements are visible in the present decade, subject to further analyses. As far as revenue expenditures are concerned, these have been at a higher level in the present decade after remaining relatively stable for most part of the 1990s (around 15 percent).

An examination of annual changes in revenue receipts points towards lack of consistent effort to mobilise resources in the state economy whereas growth of revenue expenditures could not be checked. In this context, while ignoring the amount of Rs. 12,277.40 crore mentioned earlier, the increase of expenditures by 23 percent in 2003-04 is a matter of concern. Nonetheless, it is to be acknowledged that since 1999-2000, the size of the revenue deficit has been shrinking. The Tenth Finance Commission had categorised Uttar Pradesh among the "high fiscal stress states" as its ratio of revenue deficit to revenue expenditure was above 17 percent. However, now it appears that the state has been making efforts to come out from the high stress category as the ratio has been 19.5, 15.5, 18.9 and 12.9 percent in the years 2001-02, 2002-03, 2003-04 and 2004-05 respectively, which seem to be getting below the threshold barring the year 2003-04 (even after ignoring the UPSEB loan adjustment).

Table 6: Revenue Receipts & Expenditures in Uttar Pradesh (Rs. crore)

Year	Receipts	Receipts / GSDP at factor cost (%)	Expendi-ture	Expendi-ture/ GSDP at factor cost (%)	Revenue deficit	Deficit as % of GSDP at factor cost	Revenue deficit / revenue expenditure (%)
1990-91	8310.2	15.0	9538.5	17.2	-1228.3	-2.2	-12.9
1991-92	9674.6	15.0	10399.2	16.1	-724.6	-1.1	-7.0
1992-93	11676.2	16.5	12690.7	17.9	-1014.5	-1.4	-8.0
1993-94	12131.4	13.8	13280.1	15.1	-1148.7	-1.3	-8.6
1994-95	13393.2	12.9	15396.0	14.9	-2002.8	-1.9	-13.0
1995-96	15215.2	13.1	17555.8	15.2	-2340.6	-2.0	-13.3
1996-97	16028.6	11.8	19207.7	14.1	-3179.1	-2.3	-16.6
1997-98	17571.1	11.7	22175.0	14.8	-4623.9	-3.1	-20.9
1998-99	17378.7	10.1	26074.9	15.2	-8696.2	-5.1	-33.9
1999-00	21495.1	11.6	28747.7	15.5	-7252.6	-3.9	-25.9
2000-01	24743.3	14.2	31032.6	17.8	-6289.3	-3.6	-20.3
2001-02	25597.9	14.9	31779.7	18.5	-6181.3	-3.6	-19.5
2002-03	27821.2	13.6	32938.5	16.1	-5117.3	-2.5	-15.5

Year	Receipts	Receipts / GSDP at factor cost (%)	Expenditure	Expenditure/ GSDP at factor cost (%)	Revenue deficit	Deficit as % of GSDP at factor cost	Revenue deficit / revenue expenditure (%)
2003-04 (RE)	32860.1	15.5	52798.1#	24.9#	-19938.0	-9.4	-37.7
2004-05 (BE)	37258.6	16.2	42785.7	13.0	-5527.1	-2.4	-12.9
CAGR 1990-2005 (%)	11.31		11.32		11.34		

Note: Receipts /GSDP and Expenditure /GSDP ratios since 1999-2000 have been estimated by the author. The GSDP figures have been obtained from budget documents where it was implicit in the revenue deficit / GSDP ratios.

#: Revenue expenditure includes adjustment of government underwriting a loan of Rs 12,277.40 crore for the erstwhile UPSEB.

Table 7: Annual Change in Revenue Receipts, Expenditures and Deficit in U. P. (percent)

Year	Receipts	Expenditure	Deficit
1990-91	…	…	…
1991-92	16.4	9.0	-41.0
1992-93	20.7	22.0	40.0
1993-94	3.9	4.6	13.2
1994-95	10.4	15.9	74.4
1995-96	13.6	14.0	16.9
1996-97	5.3	9.4	35.8
1997-98	9.6	15.4	45.4
1998-99	-1.1	17.6	88.1
1999-00	23.7	10.3	-16.6
2000-01	15.1	7.9	-13.3
2001-02	3.5	2.4	-1.7
2002-03	8.7	3.6	-17.2
2003-04 (RE)	18.1	60.3 (23.0)	289.6
2004-05 (BE)	13.4	-19.0 (5.6)	-72.3

Note: - Figures in parentheses represent annual change if we estimate after adjusting for Rs 12,277.40 crore in 2003-04 for government underwriting the loans of UPSEB.
Source: - Based upon Table 6.

Revenue Expenditures

Committed or contractual expenditures claim such a large part of total expenditures in Uttar Pradesh that it leaves almost no scope to pay attention towards more rewarding items. The worst was in 1998-99 when expenditures on salary, pension, and interest payment exceeded the total revenue receipts (Table-8). Thereafter, there has been some moderation. Nonetheless, the pattern of decline has not been smooth. Moreover, the pace of decline has been slow; as per budget estimates for 2004-05, the ratio is expected to be 80 percent. This may be broadly attributed to two factors: the first is the slow growth in revenue receipts and the second relates to the nature of the expenditure that cannot be brought down substantially in a short time.

It is noteworthy that in the last five years, annual increase in the salary expenditure has been much below 5 percent, a threshold outlined for states to control their revenue expenditure. However, in 2003-04, it went up by 16.2 percent, which could not be corrected in the ensuing budget as it is further expected to increase by 2.1 percent. However, there are reasons to believe that the salary burden is getting stabilised in the medium-run. Nevertheless, the state has been sweating it out to reduce the revenue deficit by at least 5 percent per year as required by the Eleventh Finance Commission to become eligible for incentive transfers in order to prune their revenue deficits. Pension and interest liabilities are unlikely to be reduced significantly in the medium-term. Pension liability is estimated to increase at a fast pace in future as it increased by 5 percent in 2000-01, and then 10.6 and 15.0 percent in the following two years. But the pace peaked in 2003-04 (29.9 percent) and still does not show any sign of comfort in the budget of 2004-05 (15.9 percent). Annual growth rate of interest payments on the borrowings by the state further accelerated and peaked in 2003-04 (52.7 percent). In 2004-05, interest burden is expected to further increase by 6.4 percent. Thus, instead of being contained as per expectation of several fiscal control devices, at least pension and interest payments are not showing any sign of moderation in the burden. Given this scenario, the state budget is not able to spend sufficiently on other priority items or for investments.

Revenue Receipts

Considering the inelastic nature of revenue expenditures prevailing in the last several years, it is stressed that to minimise and later eliminate revenue deficit altogether and to bring a situation of revenue surplus in Uttar Pradesh, revenue receipts of the state must increase rapidly. But it has already been seen that revenue receipts are not increasing consistently and with sufficient pace to realise the above objectives. Trends of receipts show that during the period 2000-01 to 2004-05, it is likely to go up by around 51 percent. In this, the credit goes mainly to contributions of the share in union government taxes and grants from the centre. These together are expected to increase by 64 percent in the above period while the increase of state's own revenue (tax + non-tax) is expected to be just 38 percent and that might have been just sufficient to neutralise changes in price level only.

Table 8: Various Indicators as Percentage of Revenue Receipts in Uttar Pradesh

Year	Revenue deficit	Salary, pension and interest	Debt service	Interest payments
1990-91	15	69	22	15.6
1991-92	7	64	23	17.7
1992-93	9	66	23	17.5
1993-94	9	63	24	17.4
1994-95	15	68	38	23.1
1995-96	15	69	29	21.9
1996-97	20	77	30	25.3
1997-98	28	85	33	26.7
1998-99	50	102	41	31.7
1999-00	34	93	39	30.5
2000-01	25	85	37	30.1
2001-02	24	84	44	32.1
2002-03	18	79	45	25.4
2003-04 (RE)	22	87	53	32.8
2004-05 (BE)	15	80	46	30.8

Source: Government of Uttar Pradesh, *Budget Documents*.

Table 9: Contribution of State & Union Governments in Revenue Receipts of U.P.

(Rs. crore)

Items	2000-01	2001-02	2002-03	2003-04 (RE)	2004-05 (BE)
Revenue receipts 1+2+3)	24743.3	25597.9	27821.2	32860.1	37258.6
	100.0	*100.0*	*100.0*	*100.0*	*100.0*
1. State's own revenue	12924.7	12106.4	14680.4	15574.1	17883.8
	52.2	*47.3*	*52.8*	*47.4*	*48.0*
(a)Tax revenue	10980.0	10319.3	12766.9	13707.7	16031.3
	44.4	*40.3*	*45.9*	*41.7*	*43.0*
(b)Non-tax revenue	1944.7	1787.1	1913.5	1866.4	1852.6
	7.9	*7.0*	*6.9*	*5.7*	*5.0*
2. Share in union taxes	9045.5	10200.0	10831.8	12595.3	15050.0
	36.6	*39.8*	*38.9*	*38.3*	*40.4*
3. Grants from the union Govt.	2773.2	3291.5	2309.0	4690.7	4324.8
	11.2	*12.9*	*8.3*	*14.3*	*11.6*

Note: Figures in italics are percent shares in total revenue receipts.

Consequently, the share of the state's own revenue in total revenue receipts in the next five-year period is to go down from above 52 percent to 48 percent and the share of central taxes and grants is expected to increase from 48 to 52 percent (Table-9). Therefore, expectation of the Medium Term Fiscal Reform Policy (MTFRP) of raising the state's own tax/GSDP ratio to 7.9 percent by 2004-05 is beyond reach as the budget for 2004-05 itself aims to achieve only 6.8 percent. Further, it was targeted in the MTFRP to maintain the state's non-tax revenue/GSDP ratio at 1.1 percent in these five years. There are many factors responsible for the declining amount and share of non-tax revenues in Uttar Pradesh. Net return from public sector units is only a fraction of 1 percent of the total investments in these PSUs. Secondly, there are not only low user charges but also, due to political expediency, being slashed further. This also lowers the quality of service and the morale of the concerned authorities. At the same time, it is not helpful in raising the quantity and quality of such services. As Table-9 suggests, during the period 2000-05, in absolute terms non-tax revenue has declined from Rs. 1,945 crore to Rs 1,853 crore. This is clearly against the expectation of the Eleventh Finance Commission, which had hoped that the states would be more successful in collecting non-tax revenue than the centre (2000; p. 25). Instead, the ratio of central transfers to GSDP was higher at 8.2 percent against a target of 7.1 percent. Overall, revenue receipts/GSDP ratio targeted for 2004-05 at 16.0 percent is budgeted to increase to 16.2 percent. Surprisingly, the state government has not resorted to measures of resource mobilisation either by increasing tax rates or by widening the tax base. For many years, there has been no fresh tax strategy. Worse, due to administrative inefficiency, realisation of tax with the existing structure is not satisfactory. The number of traders registered under *UP Trade Tax Act*, the most important tax in the state in terms of tax revenue, increased from 2.93 lakh in 1990-91 to 3.99 lakh in 1999-2000 and further to 4.07 lakh in 2002-03. However, the number of taxable traders got reduced from 2.61 lakh to 2.00 lakh and further to 1.95 lakh in the respective years.

In this context, we may take note of the observation of B.M. Joshi that the causes of poor tax collection in the state are internal. He observes: "The average tax revenue of UP was only 50 percent of its level in the middle-income states. Since tax compliance in the state was relatively poor, the actual tax revenue realised was just about one-fourth that of the middle-income states" (Howes *et. al.*, 2003; p. 203).[4,5] This points to another dimension, i.e., of low growth and output in the economy as well as poor administrative machinery and weak institutional structure. Both aspects seem to form a vicious circle as there is a strong relationship between the two in Uttar Pradesh. Therefore, it can be safely argued that the state has failed to mobilise resources within the economy. Moreover, its resource base is shrinking instead of widening and covering more areas that lay emphasis on non-tax revenue within the state itself and attempts to employ new measures and policies to mobilise tax revenue are entirely missing.

Table 10: Fiscal indicators of Uttar Pradesh
(At current prices; in percent)

Year	Revenue deficit/ GSDP	Capital Expendi-ture/ GSDP	Net loans and advances/ GSDP	Fiscal deficit /GSDP	Revenue deficit/ fiscal deficit	Primary deficit/ fiscal deficit
1995-96	2.0	1.0	0.8	3.8	53.4	0.92
1996-97	2.2	1.0	1.0	4.3	53.6	1.37
1997-98	3.1	1.1	0.9	5.1	61.0	1.75
1998-99	5.1	1.2	0.5	6.8	74.8	2.97
1999-00	3.9	1.4	0.7	5.9	65.3	2.42
2000-01	3.6	1.9	0.4	5.9	61.8	1.58
2001-02	3.6	1.9	0.1	5.2	62.5	0.88
2002-03	2.5	1.9	0.3	4.7	53.9	1.21
2003-04 (RE)	9.4	5.4	-5.2	9.6	56.7*	4.53
2004-05 (BE)	2.4	2.1	0.0	4.4	53.2	-0.46$

***** Leaving Rs. 12,277.40 crore from revenue expenditure, Rs. 5,906.83 crore (power bonds) and Rs. 1,000.00 crore (Prime Minister *Gram Sadak Yojana*) from capital account outlay.
$: Shows primary surplus.

Deficits and Shrinking Capital Expenditure

The Tenth Five Year Plan of India (GoI, 2202b; Part-III, pp. 13-17) has recorded its concern for growing revenue and fiscal deficits that have been hindering the prospect of required plan expenditures and developmental expenditures among the states. Uttar Pradesh has been placed in `Group C' because of its low per capita income. Gross fiscal deficit (GFD) as a percentage of plan expenditure was 94.0 percent in the Eighth Plan. It has increased to 121.6 percent in the Ninth Plan. Thus, plan expenditure has been less than the GFD implying fully debt-financed plan expenditures. It also signifies strain on the state budget on account of poor resource mobilisation and uncontrolled fixed expenditures. Similarly, revenue deficit as a percentage of GFD increased from 44.1 percent to 57.9 percent signifying an increasing compulsion to meet revenue expenditures through enhanced borrowings. This ratio is estimated to be around 54 percent in the first three years of the Tenth Plan.

Analysis of Table-10 is indicative of the direction of fiscal drift in Uttar Pradesh and the need to discipline the fiscal *ad-hocism* persisting in the state for over one decade. Despite claims and efforts to trim the revenue deficit, it is still at 2.4 percent in the current year's budget. Revenue deficit has been accounting for more than half of the GFD in the economy. It peaked at 75 percent in the fiscally most strained year of 1998-99. But thereafter there appears to be a trend of moderation that could be capitalised upon through some increase in the capital expenditure. The ratio of capital expenditure to GSDP remained below 1.5 percent upto 1999-2000 but thereafter, it has averaged around 2 percent. Still, it remains grossly insufficient. Thus, the persisting high component of revenue deficit in the GFD obstructs the ultimate target of pruning fiscal deficit to around 2.4 percent. This does not permit the state to resort to high capital expenditures and net loans and advances to its other organs to generate greater productive capacity by way of investments in infrastructure etc. In fiscal distress, the soft but undesirable option of reduced capital expenditure to keep the fiscal deficit within "manageable limit" has been taken. Even so, the fiscal deficit is above 4 percent whereas in the budget of 2000-01, as a strategy of MTFRP, the ratio of GFD to GSDP was targeted to be 3.5 percent in 2004-05. However, the current budget itself claims it to be at 4.4 percent. At the national level, while fiscal deficit could not be reduced drastically, at least there is buoyancy in revenue receipts, control over expenditures, and sufficient diversification in terms of revenue receipts.[6] The net outcome of fiscal strain can be seen in the increased indebtedness of the state. Primary deficit is showing some sign of improvement as it is expected to change its direction from deficit to surplus after a grim situation in the late 1990s that got moderated in the ensuing years.

Indebtedness of the State

Almost inelastic nature of expenditures, particularly revenue expenditures, and that of revenue receipts of the state has been the immediate cause of persisting revenue deficits and negative BCR in Uttar Pradesh. Revenue deficits have resulted in fiscal deficits that require to be financed through borrowings. Therefore, all the borrowings cannot be used for expenditure on capital account. This in turn has resulted in deepening of indebtedness in Uttar Pradesh.

Although as shown earlier some fiscal indicators showed sign of improvement since 2000-01, no such improvement is noticeable in

Table 11 : Debt Indicators as percent of GSDP of U.P.

Year	Loans from market	Small savings	Loans from financial instit.	Loans from Govt of India	Provident and pension funds	Deposits and advances	Total debt stock of U.P.	Total debt stock of U.P. (Rs crore)
1995-96	5.6	7.5	0.2	9.1	5.8	3.1	31.2	
	(17.9)	(24.0)	(0.5)	(29.2)	(18.6)	(9.8)	(100.0)	*36144.98*
1996-97	5.4	7.1	0.2	8.7	5.6	3.2	30.2	
	(18.0)	(23.3)	(0.8)	(28.7)	(18.4)	(10.7)	(100.0)	*41767.91*
1997-98	5.8	7.7	0.4	9.2	6.3	3.3	32.6	
	(17.9)	(23.7)	(1.1)	(28.1)	(19.1)	(10.1)	(100.0)	*48364.99*
1998-99	6.1	8.5	0.4	8.5	6.5	2.8	32.8	
	(18.7)	(26.1)	(1.2)	(26.0)	(19.7)	(8.4)	(100.0)	*55952.23*
1999-00	6.6	9.5	0.8	8.7	7.2	1.9	34.7	
	(19.1)	(27.5)	(2.3)	(25.0)	(20.7)	(5.4)	(100.0)	*65135.18*
2000-01	7.7	11.7	1.3	10.0	8.7	2.5	41.9	
	(18.4)	(28.0)	(3.1)	(23.8)	(20.9)	(6.0)	(100.0)	*72765.64*
2001-02	8.3	12.6	1.4	10.1	8.7	3.0	44.0	
	(18.8)	(28.6)	(3.1)	(23.0)	(19.8)	(6.7)	(100.0)	*83010.85*
2002-03	8.5	12.0	1.0	9.6	8.0	2.5	41.6	
	(20.3)	(28.8)	(2.4)	(23.1)	(19.2)	(6.1)	(100.0)	*91182.12*
2003-04	10.7	12.2	3.7	10.7	8.8	2.7	48.8	
(RE)	(21.9)	(25.0)	(7.7)	(22.0)	(18.0)	(5.4)	(100.0)	*106434.21*
2004-05	10.6	12.6	3.6	11.0	8.9	2.6	49.1	
(BE)	(21.5)	(25.6)	(7.3)	(22.4)	(18.1)	(5.2)	(100.0)	*115254.69*
CAGR(% per year)	**16.1**	**14.5**	**52.9**	**10.4**	**13.4**	**6.1**	**13.8**	

Figures in parentheses are percent share in total debt stock of a year.
Source**:** Uttar Pradesh Budget 2004-2005 (Vol. 2(1)); February 2004.

the case of indebtedness. The ratio of debt to GSDP in Uttar Pradesh has increased consistently from 31.2 percent in 1995-96 to 34.7 percent in 1999-2000 (Table-11). But thereafter, there has been sharp increase, as it went up to 41.9 percent in the following year of 2000-01 and is expected to be the highest at 49.1 percent in 2004-05.[7]

In fact, the present debt burden is almost double that of around 26 percent in late-eighties. It remained below 30 percent in early 1990s. This clearly suggests that the growth of debt burden has been faster than the growth of the economy. However, it should be noted that the rate of annual increase in the debt stock is getting moderated in the years of the current decade. Thus, increase in debt-GSDP ratio may also be attributed partially to slow growth in the state income. Kripa Shankar (2002; p. 4902) argues that the growing indebtedness is due to the state not making efforts to raise additional resources; moreover, deployment of available funds is more for non-productive purposes than for investment in productive assets.

The structure of the debt stock in Uttar Pradesh indicates that the state government, faced with fiscal constraints and political pressures, is seeking loans from new and more manageable sources. As a result, although the ratio of all types of debt to state income has been increasing, it appears that loans from deposits and advances of state institutions, and borrowings from provident and pension funds have reached their peak and are not increasing much in the last five years. These are increasing roughly at the pace of increase in the state income only. Even the Government of India has not been a very generous supplier of debt in the above period, as ratio of borrowings from the Government of India to GSDP has increased from 10.0 percent in 2000-01 to only 11.0 percent in 2004-05. Similar has been the trend of small savings. In such a backdrop, the state has to fall back mainly upon either market borrowings or financial institutions (Table-11). For the Government of Uttar Pradesh, in a bid to find new sources of borrowings, financial institutions have become prominent with the fastest growth rate of almost 53 percent since 1995-96 and have now increased their share in total debt stock of the state from less than 1 percent to above 7 percent in recent years. In contrast, the central government loans have lost their predominant position. Although small savings still contribute the largest amount of debt, their share also is on the decline in recent years. The state has shifted focus to market borrowings that have been steadily increasing share and in the coming years, these are likely to get a further boost. However, the pattern of financing the GFD in Uttar Pradesh (as per RBI data) indicates that although securities issued to NSSF have been the largest contributor, their significance is much below that of the same in the case of all the states taken together. In Uttar Pradesh, against the trend relating to all states, the role of market borrowings and loans by the central government has been much larger.

Due to increased debt burden and borrowings in the past at high rates of interest, the problem of debt servicing is snowballing, as it has increased from 37 percent of revenue receipts in 2000-01 to a budget estimate of 46 percent in 2004-05. Due to increasing debt burden and contracting bulk of the debt at high rates of interest, the ratio of interest to revenue receipts has gone up to above 30 percent since the late 1990s. This ratio was only half of this at the beginning of the nineties. Average effective interest rate has increased from 12 percent in 1998-99 to 14 percent in 2003-04. However, due to participation of Uttar Pradesh in the debt swapping scheme, the effective rate is expected to scale down to 11 percent in 2004-05. It is hoped that at the end of the latter a total debt of around Rs 12,600 crore would stand swapped with new low cost loans. Debt swapping with NABARD is also under consideration to the extent of Rs 1,200 crore along with some other loans. MTFRP of the state had expected the ratio of interest payments to GSDP to be brought down to 4.6 percent by 2004-05. However, even by the latest budget estimates, it would be on the higher side at around 5.5 percent[8]. Significantly, a major portion of the market borrowings have to be repaid between 2008 and 2010 and these are on rates of interest varying between 10-14 percent per annum.

IV. Fiscal Reforms

The fiscal constraints in Uttar Pradesh have been such that the entire economy has been shaken, particularly since the late nineties. Similar problems, in varying degree, were noted across the states. As a result, since the late nineties, there has been increased thrust on state level economic reforms, of which fiscal reform forms an important component. According to the Tenth Five Year Plan of India, “The only way for states to relieve fiscal pressures is to increase all-round tax and non-tax resource mobilisation efforts, coupled with determined downsising of staff and administrative expenditure, and taking up fiscal reforms to sustainable basis” (GoI 2002b; vol. III; p. 125).

Uttar Pradesh has taken up the task of fiscal reforms during the preceding decade mainly as a result of the initiatives taken by various arms of the Government of India. In the recent context, fiscal reforms in the state may be acknowledged to have begun in March 1998 when the government came out with a *White Paper* on state finances. The central government also pursued the policy of carrot-and-stick with the states. In June 1999, a MoU was signed with the Government of India. Uttar Pradesh formulated its first MTFRP (Medium-term Fiscal Reform Policy) in 2000-01. Various targets had been set to be achieved by the end of 2004-05. These are given in Box – A along with the likely realisations. It is clear that the targeted level of GSDP could not be achieved with a substantial gap of more than 13 percent. Fiscal targets also could not be realised as the state's own revenue mobilisation remained behind the target. However, revenue expenditure has been capped to some extent. But the three incorrigibles (salary, pension, and interest) have remained beyond the defined range. These get manifested in higher revenue and fiscal deficits, and hence in higher debt burden.

The Government of India has also been making interventions for promoting fiscal reform among the states by way of providing incentive funds. The states would be eligible to receive the same if they met certain monitorable targets like reducing fiscal deficit to 2.5 percent; bringing down revenue deficit to zero; scaling down interest payments to 18-20 percent of the revenue receipts; containing increase in salary and wages within the increase in the consumer price index or 5 percent whichever is higher; contain increase in interest payments to 10 percent a year; and to eliminate subsidy altogether by 2009-10. It may be argued here that the state of Uttar Pradesh fails to be eligible to get incentives in respect of many criteria. Still, it appears that the salary component has been a source of some relief. The Tenth Finance Commission had placed Uttar Pradesh among the *High Fiscal Stress States* for its very high ratio of revenue deficit to revenue expenditures (above 17 percent). However, there has been some moderation now as the ratio has been brought below 13 percent in 2004-05.

Box A : Review of Major Targets of the MTFRP in Uttar Pradesh
(As percent of GSDP; at current prices)

Items	Target for 2004-2005	Budget estimate for 2004-05	Remark/ prospect
Revenue receipts	16.0	16.2	Very low & has potential to grow through tax reforms and economic growth
State's own revenue	8.9	7.9	Ignores potential of resource mobilisation
a. Tax revenue	7.9	6.8	Unexploited, mismanaged and poor collection
b. Non-tax revenue	1.1	1.1	Ignored; used as political arm; must get a boost
Revenue from the centre	7.1	8.3	Provides relief; *'May get more'*
Revenue expenditure	19.6	18.6	Cause of concern; Fiscal prudence needed
Interest payments	4.6	5.0	May be brought down through debt swapping and debt reduction in the medium term
Salary	3.7	5.0	Administrative expenditures are not being controlled sufficiently
Pension	1.4	1.8	Likely to go up further in near future
Salary, pension & interest payments/ revenue receipts	58.4	80.3	Together they leave little scope for reduction in revenue deficit
Debt service / Revenue receipts	35.0	46.0	Can be now managed only in the long run
Total debt / GSDP	40.6	49.1	Uncontrolled despite cut in capital account expenditure
Revenue deficit / GSDP	-0.8	-2.4	Borrowings for revenue deficit disturbs budget
Fiscal deficit/GSDP	-2.5	-4.4	Eating into resources for development
Interest / revenue	26.7	30.8	Can be controlled

Items	Target for 2004-2005	Budget estimate for 2004-05	Remark/ prospect
			through debt swapping and revenue increase
GSDP (Rs cr)	2,65,045	2,30,295	Growth of the economy needs to be taken care of properly on sustained basis

Box B : The Uttar Pradesh Fiscal Responsibility and Budget Management Act 2004

S.N	Items
1.	To prepare an MTFRP every year along with the budget with five year rolling fiscal targets
2.	To eliminate revenue deficit altogether by the end of 2008-09
3.	To bring down FD/GSDP to below 3 percent by the end of 2008-09
4.	To bring down the debt burden and reduce debt/GSDP ratio to 25 percent by 2017-18
5.	To manage prudently debt, guarantees and other contingent liabilities
6.	To reorient expenditure policies in such a manner that promote economic growth, human welfare and poverty reduction
7.	To disclose information regarding finances of the state for better public scrutiny and debate
8.	To review fiscal targets half-yearly and discuss the same in the Assembly
9.	To shift ultimately from discretionary fiscal policies to rule based fiscal policies

Uttar Pradesh has also taken recourse to several other measures of reform for fulfilment of the goal of taking the state out of serious fiscal imbalances. These are in the forms of institutional reforms, computerisation of important offices like treasuries, and presentation of budget documents as suggested by the Eleventh Finance Commission in such a manner that might be convenient for the public to understand and scrutinise. Notwithstanding poor resource mobilisation and imprudent fund management, Uttar Pradesh now appears to be more committed to fiscal reforms. This is reflected in the fact that the state is the fifth one among the states to begin the second phase of fiscal reforms by passing the *Uttar Pradesh Fiscal Responsibility & Budget Management Act, 2004* in

February, 2004. Its salient features are contained in Box – B. The latter indicates that Uttar Pradesh has been making efforts to streamline its fiscal affairs along with promotion of transparency, objectivity, and responsibility. However, the state is perhaps pursuing the path of fiscal reforms under compulsion and not of its own volition. There is lack of spontaneous and home grown reform strategy. This is evident from the fact that although some of the critical fiscal goals are realised, the real economy has failed to get energised; this is seen in the subdued overall economic performance. This implies that the State has not been able to implement fiscal reforms properly through careful blending of economic dynamism with fiscal reform. The latter has tended to move away from the ultimate goal of stirring up the state economy and uplifting the level of social and economic development in Uttar Pradesh.

V. Implications for Growth and Conclusion

An analysis of the state finances and of broad economic indicators in Uttar Pradesh suggests that adopted policies have not had the desired impact. The state has been struggling to restore its fiscal health through various measures of reforms. It is for this reason that some of the fiscal indicators seem to have now changed their course. For example, there are signs of:

- reduced quantum of revenue deficits in recent years;
- decline in GFD-GSDP ratio;
- decline in the rate of increase in salary and interest payments;
- reform in the energy sector;
- coming into force of the *Uttar Pradesh Fiscal Responsibility and Budget Management Act, 2004*; and
- constitution of the State Finance Commission twice and in time.

However, these are neither fully satisfactory nor sufficient considering the needs and targets of reforms in the economy. We can argue that there are certain other requirements to provide momentum to reform, but are beyond the scope of a monitorable programme of reforms. These include political stability, commitment, and vision of political leadership, administrative efficiency and stability, and good governance.

However, there are many important monitorable targets that have been framed in the context of Uttar Pradesh and several other states. Failure to meet these targets has been affecting the fiscal health of the state and has implications for growth and development (economic, social, and human development). Uttar Pradesh has failed to increase revenue collection to a desirable level, both tax and non-tax. It has also failed to expand the base of revenue collection, nor could it raise tax rates and user charges, resulting in relatively low per capita revenue and tax collection. It has been admitted by the state government that the tax buoyancy is less than one. Dependence on devolution of resources from the centre has been increasing because committed revenue expenditures on salary, pension, and interest payments are being met less and less from the state's own revenue receipts, nor could these be capped. Most of the fiscal indicators suggest that the state could not achieve the targets fixed for it in the Medium-term Fiscal Reforms Programme, as the ratio of fiscal deficit to GSDP is still very high. This has resulted in declining capital expenditures that represent investments. In this squeesed expenditure scenario that fails to meet targeted plan outlays on a regular basis, reprioritisation of the budget among various sectors to promote economic, social, and human development is hardly feasible.

Table 12 : Tax Collection and Economic Growth in India and U.P.

(At current prices)

Year	India					Uttar Pradesh				
	Gross tax revenue		Non-tax revenue		% change in GNP	Own tax revenue		Own non-tax revenue		% change in GSDP
	Rs crore	% change	Rs crore	% change		Rs crore	% change	Rs crore	% change	
1996-97	128762	-	32578	-	16.1	6306.0	15.3	1319.5	- 45.0	20.8
1997-98	139221	8.1	38214	17.3	11.9	6998.2	11.0	1291.2	- 2.6	7.1
1998-99	143797	3.3	44833	17.3	15.0	7910.1	13.0	1475.1	14.2	10.7
1999-00	171752	19.4	53211	18.7	10.3	9400.9	18.8	1964.0	33.1	8.4
2000-01	188603	9.8	55947	5.1	8.0	12924.7	37.5	1944.7	- 1.0	4.7
2001-02	187060	- 0.8	67774	21.1	10.2	12106.4	- 6.3	1787.1	- 8.1	8.7
2002-03	216266	15.6	72323	6.7	7.3	14680.4	21.3	1913.5	7.1	7.3
2003-04 (RE)	254438	17.7	76068	5.2	12.0	15574.1	6.1	1866.4	- 2.5	- 0.5[#]
2004-05 (BE)						17883.8	14.8	1852.6	- 0.7	7.6[#]

Obtained through debt stock and ratio of debt/GSDP in Uttar Pradesh.

Table 13: Composition of Revenue and Capital Account Expenditures in U.P.

(percent)

Year	2004-05 (BE)	2003-04 (RE)	2002-03	2001-02	2000-01
1. Total revenue expenditures	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
General services	54.4	39.3	47.3	50.9	48.8
Social services	27.1	22.4	31.3	29.4	29.7
Economic services	15.1	35.8	17.9	16.8	18.0
Compensation & assignments to local bodies & PRIs	3.4	2.6	3.5	2.9	3.5
Share of revenue expenditure in total expenditure	89.7	81.6	89.7	89.9	90.5
2. Capital expenditures	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
General services	5.4	3.0	8.7	3.6	3.3
Social services	9.3	3.5	7.6	5.9	8.0
Economic services	85.4	93.5	83.7	90.5	88.7
Agriculture & allied	1.0	0.1	15.7	27.8	12.6
Rural development	10.7	11.8	9.7	7.9	0.4
Special area programme	7.9	2.7	6.9	4.4	8.4
Irrigation & flood control	24.8	9.3	19.2	21.7	24.9
Energy	8.0	53.8	8.8	20.9	23.9
Industry & mining	0.0	0.3	0.2	0.9	0.4
Transport	33.2	15.4	22.4	6.1	18.1
Science, technology & environment	0.0	0.0	0.0	0.0	0.0
General economic services	0.1	0.2	0.9	0.8	0.1
Share of capital expenditure in total expenditure	10.3	18.4	10.3	10.1	9.5

Nonetheless, it is important to make at least a modest attempt to establish a link between poor budgetary measures and weak economic momentum in Uttar Pradesh with the help of some fiscal and economic parameters. As far as tax revenue is concerned, it is found that the relative growth has been better in Uttar Pradesh than in India (Table-12). However, mobilisation of non-tax revenue has been far better in the latter or to be more precise, it has been deteriorating consistently in Uttar Pradesh as it has declined even in absolute values in several years. Its adverse effect manifested through poor economic growth of the state economy for a period longer than the last decade, whereas it has been considerably higher at the national level. The pattern of expenditure incurred by the Government of Uttar Pradesh (Table-13) reveals its helplessness in providing any meaningful direction and thrust to the economy, as 90 percent of the total expenditure goes out as revenue expenditures and only 10 percent is left for capital expenditures to push the economy forward. Within the revenue expenditure, the share of general services is gaining way and has increased from 48.8 percent in 2000-01 to 54.4 percent in 2004-05. The share of economic and social services in the revenue expenditures, which are also considered as developmental expenditures, has shrunk. With limited share now available for capital expenditure, it is very difficult for the state government to provide any meaningful direction through its sectoral allocations. As a result, important activities like agriculture and allied services, industry and mining, energy, science and technology, and environment are being ignored.

Table 14 : Credit-Deposit Ratio, Investments in SSIs, & Investments/Loans by Financial Institutions in Uttar Pradesh

Item	1985-86	1990-91	1997-98	1998-99	2000-01	2001-02	2002-03
Credit-deposit ratio (%)	49.2	45.8	28.6	27.2	29.0	29.4	30.4
Investments in SSIs (Rs. crore)		153.5	403.9	399.4	293.5	31.8	272.2
IDBI#	13.0	-	5.2	5.8	3.7	2.0	
ICICI#	15.4	-	4.0	2.3	4.7	2.4	
IFCI#	-	-	9.1	5.9	3.4	2.5	
NABARD#	13.5	-	13.8	15.2	15.0	15.4	
REC#	25.2	-	8.5	6.4	-	6.6	
LIC#	9.6	-	7.2	10.7	38.9	-	

#: Shows percent share in all-India.

Overall impact of such vacuous budgetary policy on the economy may be seen through poor ‘crowding in’ effect on the private investments over which the state’s Tenth Plan has laid great emphasis. Some of the indicators are given in Table-14. Credit-deposit ratio has come down to around 30 percent from around 50 percent in the 1980s. This only shows that resources mobilised by the banking sector within the state economy are being drained out due to poor absorption capacity within the economy. Investments in the small-scale industries are also gradually dropping since the late nineties. Similarly, loans by prominent developmental institutions for carrying out various activities in the state economy have been scaled down significantly making Uttar Pradesh a poor destination for private investments. Surely, this should be attributed to poor demand for funds from the state economy. Among other reaons, poor budgetary policy on a sustained basis can be blamed for such a stagnant situation. In contrast, budgetary policy should have been an effective instrument to promote and sustain large private investments in this backward state economy of the nation.

All the fiscal problems have their impact upon economic performance. It is estimated that the expected GSDP (at current prices) in 2004-2005 would be Rs 2,30,300 crore against a target of Rs 2,65,045 crore in the MTFRP, showing a gap of over 13 percent. Already, as shown in the beginning, the Ninth Plan growth target of 7 percent has been missed by more than half. In the beginning of the Tenth Plan, growth rate of the economy seems to have dropped further, considering a target of 8 percent. It has been claimed in the Tenth Plan of Uttar Pradesh that the state is short of resources that can be compensated by private investments. But this does not seem to be on the cards. We have illustrated this gloomy prospect with the case of low credit-deposit ratio in the state persisting for several years now at around 30 percent, showing a net outflow of resources from the state due to lack of fiscal strength, prudence, and commitment. It is in this context that the Uttar Pradesh Budget for 2004-2005 did not speak of its achievements in terms of targets of fiscal reforms attained. In brief, weak budgetary initiatives have failed to encourage private investments in the economy leading to poor growth achievements. On the other hand, the bleak growth scenario has been limiting revenue mobilisation measures. Thus, it appears that a type of vicious circle has been operating in the economy of Uttar Pradesh between fiscal policy and economic growth and development. In fact, among the various fiscal targets set by the Government of India and other agencies, the state government managed to attain some of the targets. But in this process, the real sector of the economy has been further ignored making the budgetary process insensitive to economic and social development in Uttar Pradesh.

In such a scenario, it has become imperative to aggressively pursue fiscal reform that can help release forces of growth in the economy. To begin with, the administration must start the reform from within by pruning the size of staff and bureaucracy, gearing up the tax collection machinery and providing quality service through commitment to earn the confidence of the public. Expenditure efficiency should be enhanced. Only then can one embark upon revenue raising measures within the state itself by expanding the tax base and rationalising tax rates. Special emphasis had to be laid on increasing non-tax revenue by increasing user charges and gradually improving the quality of services to shift some of these to the private sector. To encourage the private sector to play an active role in the economy of Uttar Pradesh, the government has to effectively demonstrate its capabilities to reform itself and develop a sustainable economic environment with less of political interferences and more of vision and commitment.

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Endnotes

1. Despite having almost same growth rate of NSDP during 1990-91 to 1999-2000 (4.04 percent) and 1993-94 to 2001-02 (4.03 percent), growth of per capita income varied from 1.85 percent in the former period to 1.66 percent in the latter. This may be attributed to higher growth rate of population as it increased from 2.15 percent during 1990-91 to 1999-2000 to 2.33 percent in the period 1993-94 to 2001-02. In fact, such a discrepancy might also be due to population projections between the two census years.

2. Budget speech of the Chief Minister of Uttar Pradesh for the year 2004-05: 11 February, 2004.

3. In a very interesting and analytical study, it has been noted by Robert P. Beschel Jr. that decline in Uttar Pradesh has been more pronounced in the 1990s and its roots are many. He observes: "Chronic political instability and frequent changes in governments have placed tremendous demands upon politicians for money and patronage to assure their re-election. These pressures have in turn helped erode the boundary between political and administrative spheres and contributed to three major problems…" (in Howes *et al;* 2003: pp. 241-242). He also finds negative relationship between the growing size of civil service employment in Uttar Pradesh and its economic performance. He concludes, "Under such circumstances, it is difficult to articulate a common vision that can cross party and caste lines. It is also difficult to attain the stability and continuity in tenure necessary to take a reform agenda forward over time" (p. 245).

4. Taking this point further Kripa Shankar regrets that, "The state has not cared to mobilise resources and to put them to productive uses. Per capita tax revenue as a percentage of per capita income in UP is the lowest among all the states and successive finance ministers in UP have been taking pride in the fact that no new tax is being imposed' (2001: p. 1677). This also reflects lack of political will to increase the resource base in Uttar Pradesh.

5. By not making efforts to mobilise resources within the state economy, we cannot sit idle and expect to gain in terms of devolution from the centre as per recommendations of the Finance Commissions, as already states with better fiscal management and progressive trends find it inconsistent to reward states like Uttar Pradesh which either indulge in fiscal profligacy or ignore the need to discipline their fiscal management.

6. On this point, Ajit Karnik (2002: p. 831) disputes the suggestions of *Report on Currency and Finance, 2000-2001* and argues that "in the given scenario of growing combined fiscal deficit of the centre and states, it would be better if we emphasise drastic reduction in

revenue deficit and unchanged level of the gross fiscal deficit so that there is greater scope to invest in socially desirable expenditures such as investments in physical and social infrastructure."

7. Increasing debt burden of the states in India has become a source of concern in the country. Therefore, the Twelfth Finance Commission has been assigned the task of streamlining the management of government debts as one of the term of reference by the President of India.

8. For this again, we can blame the low level of output in Uttar Pradesh because the outline had targeted a gross state domestic product at current prices of Rs. 2,63,045 crore in 2004-05. But it is expected to be around Rs. 2,34,700 crore only, *i.e.*, a slip of above 11 percent. In this context, it can also be mentioned that proper attention is not being paid to projection of GSDP for budget purposes. As per *Budget Documents* of 2004-05, in Uttar Pradesh, implicit GSDP from various sources show differing values. It is estimated to be Rs. 2,30,295 crore from revenue deficit, Rs. 2,34,735 crore from the debt-ratio and Rs. 2,36,329 crore from fiscal deficit. Such variations make an analysis difficult to the extent various ratios and indicators become incomparable and result in misleading inferences.