India's Fiscal Management Post-Liberalisation

Impact on the Social Sector and Federal Fiscal Relations

An exclusive focus on deficit reduction has had the adverse fallout for public spending on health and education in several states, forcing a shrinkage of the public sector's involvement in the social sector. Policy-makers are now seeking an escape route by getting the fiscal and revenue deficit targets relaxed. While there can be valid arguments against inflexible targets, abandoning the discipline underlying fiscal responsibility legislation, as has been suggested, is questionable. For, at base, the fiscal problems of democracies have their origin in the short time horizon of governments and their penchant for promising the moon to the electorate while showing an extreme reluctance to tax.

AMARESH BAGCHI

I
Remembering Panchanan Babu

If I were to name to whom among the teachers, in my college days, I owe the greatest debt for intellectual development, Panchanan Chakraborty comes first to mind. I came in contact with him only in my postgraduate years. He taught us Keynes. Within a short period the contact developed into a close and affectionate relationship that lasted as long as he lived. Although I do not count myself as one of his worthy students, his affection never diminished and I had the benefit of interacting with him for many years after I ceased to be in academia. I had the privilege of visiting him in his house starting with his elder brother's residence at Chakraberia Road South where he lived alone for many years, his family residing at Jiaganj in Murshidabad district. I, like his other students, had free access to him wherever he lived thereafter. The "civilised" practice of calling on people only by prior appointment was not there then and anyone could drop in at his place any time without notice. But seldom was any time wasted in trivial gossip. Sipping interminable cups of tea in no time would he plunge into discussing some intricate issue in economics mostly macroeconomics that he was preoccupied with at the time or some latest development in the field brought up in the leading journals.

Anyone who had come in touch with him at those sittings would have remembered how well informed he was, keeping abreast as he did of the developments in theory through journals and latest publications and how insightful his observations were. It may not be an exaggeration to say that several of the later developments in macro theory were anticipated by him. How a theory of trade cycles could emerge through the interaction of the multiplier and the accelerator was expounded by him at those sittings well before Hicks had come out with his neat construct. That the consumption function of Keynes needed some modification or qualification had also occurred to him before Duesenberry came out with his thesis of relative income. Unfortunately he did not care to put down his thoughts on paper to make a journal article. He did write on the strategy of First (or perhaps the second and third) Five-Year Plan but seldom did he expound his thoughts on macro theory in a journal article. What he did find attractive enough to put down in ink was his ideas on history of economic thought. He used to read out to us, visitors at his house, bits and pieces from those notes on the history and how illuminating those were, only those who were fortunate to have listened to him reading out from his handwritten notes would vouchsafe. I believe he had finally pieced those notes together and used it for a presidential address at an annual conference of the Bengal Economic Association and it was published subsequently.

As a teacher Panchanan Chakraborty was not one who would impress by his oratory. But he was extremely thorough in whatever he took up. (There was a joke among his students that when teaching Public Finance – and that was what he taught before moving over to General Theory – he had read the entire medical literature on Malaria in order to comprehend the likely fallout of a tax on quinine). But those who listened or read the notes he used to dictate, mostly extempore, would remember how illuminating they were. It may sound naïve to say so after so much has happened in the theory of macroeconomics, but a few things he taught us in the class have stuck in my mind. One is, why money does not always serve as a mere veil. Another was what marked the point of departure for Keynes from neoclassical economists. At base, he taught us, it was bringing "uncertainty" into reckoning. When I was working for a PhD thesis, the subject being 'The Concept of Income for Taxation', it was he who drew my attention to the article by Samuelson that opened my eyes into the nature of income and the problems of defining and measuring income. It was this article by Samuelson that trivialises the distinction made between capital gains and income, attributing the distinction to be the penchant among accountants and "aboriginals" for treating the calendar year as fundamental!

His discourses were not always confined to economics. They ranged over a wide field. He had clearly anticipated the computer revolution and that was in the early 1950s when few in India had seen a computer. He used to talk about "cybernetics" and its likely fallout. Information economics about which we hear so much these days was also anticipated by him. Although

his interest was primarily in theory, he was well aware of the problems and issues in Indian economics. He used to comment on the changes in tariffs and their likely impact on India's economy. He complimented Bhoothalingam for his report on the rationalisation and simplification of direct tax laws (that was in 1966) which showed that his interest was not confined to theory.

II
The Backdrop

For the first 30 years after independence macroeconomic management in India was concerned mainly with maintaining price stability and managing the balance of payments. The fiscal situation presented no problem. Budgets were in reasonable balance. Current expenditures were met mostly out of current receipts. Borrowings were used mainly to finance capital expenditures comprising government's capital outlay and loans. Borrowing was on a modest scale and the combined deficit of the centre and the states seldom went beyond 4 per cent of GDP. The budgets remained in balance even when the expenditures of the government as a proportion of GDP more than doubled following the growth of the public sector under the strategy of planning adopted for development; in fact often there used to be some surplus, though small, in the revenue budget. This was because in step with expenditures, revenues of the government had gone up. The debt-GDP ratio had moved up but remained below 45 per cent of GDP.

It was only in the 1980s that the budgetary situation started causing worry. With the public sector expanding fast, growth of government expenditures outstripped revenue growth. Both deficits and the debt ratio went up. Things came to a head at the end of the 1980s. In 1990-91, the combined fiscal deficit of the centre and the states exceeded 9 per cent of GDP and the debt-GDP ratio increased to nearly 62 per cent. Interest payments as a proportion of GDP had gone up from less than 2 per cent earlier to over 4 per cent preempting almost one quarter of revenue. Primary deficit also measured almost 5 per cent of GDP raising alarm about a debt trap. Nearly one-fourth of the deficit was monetised. Despite appreciable improvement in growth there was chronic inflation (7-8 per cent) a year. In the absence of a commensurate increase in domestic saving, the deficits tended to spill over to the external sector. The current account deficit, that is foreign borrowing, widened to unsustainable levels with forex reserves dwindling to barely 14 days cover for imports. As is well known, the crisis that overtook the economy at the beginning of the 1990s forced the government to go to IMF and undertake wide-ranging reforms to stabilise the economy immediately. Fiscal stabilisation figured prominently in the reform agenda. The focus was on reducing the deficits in the government budget quickly.

The strategy was to act on both sides of the budget, raising more revenue and reducing expenditures. But revenue could not be raised quickly; in fact with liberalisation and opening up, the revenue-GDP ratio went down as the role of customs as a source of centre's revenue sharply diminished and the taxes on domestic income and trade were inadequate to compensate for the revenue lost. So the stabilisation was brought about largely by cutting expenditure that could be cut easily and quickly. The axe fell mainly on capital expenditure and also on expenditure on social and economic services with consequences that unfolded later and are still unfolding. The government at the centre also undertook through an agreement with the RBI to discontinue the practice of borrowing against treasury bills, which had meant an end to automatic monetisation of the debt. The states too felt the pinch though their fiscal situation did not come under much attention initially as the level of deficit in the state budgets remained at reasonable levels at the time. However, as will be seen presently, the states too came under the scanner not long after and various measures designed to get them to obey the rules of fiscal discipline were initiated. While the fiscal situation has improved, the result has not been too wholesome for the social sectors or for federal fiscal relations, the states losing a good bit of their fiscal autonomy in the process. This note seeks to draw attention to some salient points of these developments.

Fiscal Consolidation at the State Level: Salient Features

The stabilisation measures launched in the initial phase of the reforms helped to bring down the combined deficits significantly (to less than 7 per cent) but the improvement was short-lived. The deficits started moving up again in 1997-98, crossing the 9 per cent mark in 2000-01, raising alarm all round. This time a good part of the deficits originated from the state budgets accounting for almost one half of the combined deficits which was not the case earlier. The focus now shifted to the states. If the country's fiscal situation was to be stabilised on a sustained basis, the states too, it was argued, needed to be brought under some discipline to rein in their deficits. It was not, however, simple for any state to reduce its deficit. As the adverse turn in state budgets had resulted from several factors not within their control, particularly the rise in the interest rates following financial liberalisation and the fallout of the central pay commission report raising the emoluments of employees heftily apart from the fall in transfers from the centre mentioned earlier.

To bind the states to some discipline in budgeting the Eleventh Finance Commission (EFC) was asked to recommend a restructuring plan to restore fiscal balance both at the centre and the states. The plan formulated by the EFC (in its majority report), however, did not help. A fund carved out of the grants-in-aid recommended by the EFC to "incentivise" the states to follow the path of fiscal rectiude – "the medium-term fiscal reform facility fund" – proved to be of no avail either. Between 2000 and 2003 things deteriorated further. In another attempt to impose fiscal discipline the Twelfth Finance Commission (TFC) was also asked to review the finances of the centre and the states and formulate another restructuring plan.

The TFC's review revealed an alarming state of the states' finances and how they had deteriorated between 1993-96 and 2000-03. Table 1, extracted from the TFC report, brings this out succinctly. Briefly, taking the major states together, their revenue deficit that averaged 0.86 per cent of GDP during 1993-96 went up to 3.19 per cent; their fiscal deficit from 2.93 per cent to 4.97 per cent; debt ratio from 24 per cent to 36 per cent and interest payments as proportion of total revenue receipts from 16.7 per cent to 25.4 per cent. The fiscal situation of all states had deteriorated, but there were wide interstate variations. Most stressed of all in many respects was West Bengal. The state's fiscal deficit was the highest next only to Orissa. A particularly worrying aspect of the fiscal situation was that an increasingly large proportion of the fiscal deficits was on account of the revenue deficits.

After reviewing the finances of the states, the TFC came out with some radical recommendations to ease the budget problems

of the states. The share of the states in the centre's tax revenues was raised from 29.5 to 30.5 per cent. Also a scheme of debt consolidation and debt restructuring for the states was put forward. The benefit of these schemes however were anchored heavily on the states' undertaking to enact a fiscal responsibility law (FRL) – on the lines of the Fiscal Responsibility and Budget Management Act (FRBM) passed by Parliament for the centre in 2003. The FRLs are required to be designed to commit the states to eliminating the revenue deficit and bringing down the fiscal deficit to 3 per cent by 2008-09. Most states (not West Bengal, to my knowledge) have passed the law of fiscal responsibility. But since the revenues could not be raised by all states to the level required to meet the FRL targets of deficits, cuts were imposed on both capital and social sector expenditure. Some states had approached international aid agencies, the World Bank and the Asian Development Bank, who too had imposed conditionalities while extending structural adjustment loans (SAL) that required pledging to take action in many directions to reduce deficits. The central transfers flowing through the Planning Commission also came to be tied to conditionalities aimed at inculcating fiscal discipline.

There has been some improvement in the fiscal position of the states since 2003 and some states have even achieved revenue surplus. But the result has not been very wholesome for the social sectors particularly for the poorer states. On the other hand, an increasing tendency on the part of the centre to use the transfer system to get the states to fall in line is casting a long shadow on the states' fiscal autonomy and thus India's federal structure. First we take a look at the fallout on the social sector mainly comprising health and education.

Impact on Social Sector

While the burden on deficit compression at the centre fell on the government's, investment expenditure, in the states it was the social sector that bore the brunt. With salaries, pensions and interest payments accounting for nearly 80 per cent of their revenue receipts (in some states, notably West Bengal, the proportion exceeded 100 per cent) little fiscal space was left to the states to undertake any worthwhile new development expenditure or even maintain their social sector spending at the same level. (Of course salaries paid to teachers and doctors count as development expenditure but expenditure on new programme was not possible on any significant scale). Besides, with salary, pension and interest payments eating up most of their revenue receipts the allocations for complementary expenditure on materials fell. Taking all major states together, development expenditure as a percentage of revenue expenditure fell from 68 per cent in 1990-91 to 54 per cent in 2003-04. In West Bengal the proportion went down from 67 to 43 per cent, well below the all states average (Table 2).

Reviewing the results of the efforts of the states towards fiscal consolidation in recent years, a paper presented at a WIDER conference at Helsinki in June authored by Govinda Rao and Pinaki Chakraborty, concludes:

> The analysis of revenue and fiscal deficits show significant interstate variations. … The performance of West Bengal in terms of both the size of deficits and their change over time is worrisome. Other badly performing states are Punjab and Gujarat, the latter mainly due to the fiscal fallout from the earthquake in 2001. At the other end of the spectrum Haryana and Tamil Nadu have performed well in terms of containing their deficits. Curiously, some of the low income states such as Bihar and Uttar Pradesh too have contained their deficits raising serious doubts about the appropriateness of making these measures to understand fiscal stress in the states. Given the structure of incentives many of the poorer states have preferred to reduce their expenditure particularly on social and economic services with adverse growth implications for the future as a route to contain the deficit.

Some states like West Bengal have of course tried not to cut expenditures much but with a poor tax effort (lowest among all major states) deficits have persisted at a high level. Whether that has helped to maintain the level of social services is, however, not clear especially since there has been a compression of government employment in most states and a tendency to replace regular employees with contract workers (para-teachers on very low salaries). Even so, as is public knowledge, many schools are going without teachers and health centres without doctors and nurses. And even if there are doctors there is no medicine, the laboratories go without essential chemicals; many primary schools have no building much less other facilities like drinking water.

To ease the rigour of deficit reduction targets, the Approach Paper to the Eleventh Five-Year Plan suggests a reclassification of education and health as capital expenditure. While it may help the governments at both levels to wriggle out of the rigours of the FRLs, whether that will be the right course is a matter of debate. For while it will allow the governments to use a part of their borrowing to

Table 2: Developmental Expenditure as Percentage of Revenue Expenditure
(in per cent)

	1990-91	1997-98	1999-00	2003-04
Bihar	64.01	57.52	57.66	49.45
Haryana	67.03	50.72	58.24	56.36
Karnataka	67.95	64.59	62.26	54.58
Tamil Nadu	72.31	63.20	57.70	52.25
West Bengal	67.40	56.93	57.52	43.02
All states	68.07	60.97	57.98	54.18

Source: Handbook of Statistics on State Finances, 2004, RBI.

Table 1: Trends in Revenue and Fiscal Deficits in States

	Average Revenue Deficit		Average Fiscal Deficit		Ratio of Revenue Deficit in Fiscal Deficit	Increase in Revenue Deficit	Increase in Fiscal Deficit
	1993-96	2000-03	1993-96	2000-03	2000-03	1993-2003	1993-2003
1	2	3	4	5	6	7	8
Andhra Pradesh	-0.5	-2.03	-3.16	-4.57	44.42	-1.53	-1.41
Bihar	-1.83	-1.87	-2.85	-4.52	41.37	-0.04	-1.67
Gujarat	0.1	-4.66	-1.82	-5.74	81.18	-4.76	-3.92
Haryana	-0.75	-1.32	-2.5	-3.69	35.77	-0.57	-1.19
Karnataka	-0.07	-2.21	-2.71	-4.37	50.57	-2.14	-1.66
Kerala	-1.18	-4.17	-3.32	-5.13	81.29	-2.99	-1.81
Madhya Pradesh	-0.61	-2.05	-2.16	-3.94	52.03	-1.44	-1.78
Maharashtra	-0.09	-3.09	-2.16	-4.12	75.00	-3.0	-1.96
Orissa	-2.0	-4.91	-4.63	-7.84	62.63	-2.91	-3.21
Punjab	-1.88	-4.53	-4.37	-6.14	73.78	-2.65	-1.77
Rajasthan	-1.09	-3.87	-4.51	-6.05	63.97	-2.78	-1.54
Tamil Nadu	-0.71	-2.5	-1.99	-3.75	66.67	-1.79	-1.76
Uttar Pradesh	-1.77	-2.98	-4.04	-5.07	58.78	-1.21	-1.03
West Bengal	-1.53	-5.47	-3.18	-7.31	74.83	-3.94	-4.13
Major States	-0.86	-3.19	-2.93	-4.97	64.19	-2.33	-2.04

Source: Report of the Twelfth Finance Commission.

meet some of the expenditures that are classified as "current" at present, so long as the limit for fiscal deficit remains at 3 per cent, the result will be smaller room for investment in physical infrastructure. However, there can be no gainsaying that something needs to be done to get more funds for the social sector than are available for them now. For the fact remains that exclusive focus on deficit reduction has had an adverse fallout on public spending on health and education in several states, particularly the poorer ones and perhaps others too forcing a shrinkage of public sector's involvement in provision of healthcare and education and inviting the private sector to fill the space.What has been or will be the impact of all this on the level and quality of education and healthcare only the future will tell.

Another stark fact of the fiscal situation is that faced with acute fiscal stress, the states have turned more and more to the centre for funds to run their affairs. For almost any development scheme they look up to the centre for they have no funds to spare even to run their existing facilities. In "national interest" the centre too is coming out with schemes accompanied with grants to get the schemes implemented. Inevitably this has affected the fiscal autonomy of the states. How this has come about is explored briefly in the remaining part of the note.

Impact on Federalism

Transfers from the centre are a common feature in all federations. This is because economies of scale and other factors predicate assignment of mass based taxes to the national government, while because of their proximity to the people expenditure responsibilities are cast on the lower level governments thereby creating what is called a vertical gap. Anticipating this and in order that it did not make the states subservient to the centre our Constitution makers had ordained the appointment of a finance commission (FC) periodically. The role envisaged for the finance commission in the Constitution as a mechanism for mediating the transfer of funds from the centre to the states has however been undermined in many ways. How this has come about and is happening cannot be gone into in any detail in a note like this. Only a few salient points may be noted:

– Right from the beginning a good part of the transfers from the centre is being routed through the Planning Commission bypassing the FC in the form of assistance for state plans. In order that this did not widen the scope for discretionary grants from the centre, the National Development Council had decided in 1969 that plan assistance from the centre to the states should be mainly in the form of untied block assistance allocated on the basis of a formula (Gadgil formula) and centrally sponsored schemes (CSS) which are discretionary should be limited to only one-sixth of such block transfers. This decision has been thoroughly compromised by now as much of the Plan grants are flowing outside the Gadgil formula. There has been an enormous expansion of the CSS which has enabled the centre to expand the scope of discretionary transfers and impose its own priorities on the states.

– While there can be a case for specific purpose transfers to take care of "externalities" or to promote objectives of national interest such as the Sarva Shiksha Abhiyan, proliferation of such grants unavoidably undermines the states' role as fiscally empowered units of responsible government and creates a dependency syndrome that is sacrcely conducive to either true federalism or fiscal discipline. The CSS and special purpose grants are now assuming large proportions with the government at the centre embarking on what is called Bharat Nirman pumping in large funds, reducing the states to mere spending agencies.

– What is more, a large part of the CSS transfers is flowing from the centre bypassing the states. They are being routed directly to various agencies and local bodies. An incisive paper by Subhash Garg (forthcoming in *EPW*) analysing the central budget 2005-06 shows that as much as Rs 34,325 crore out of a CSS outlay of Rs 54,580 or 62.9 per cent of CSS funds are going directly to various agencies bypassing the state budgets. Whatever be the justification, this clearly undercuts the states. No state seems to be protesting as they are all in dire need of funds.

– Following the recommendations of the National Advisory Council of the UPA government, a proposal has been mooted now by the Planning Commission to set up an "incentive fund" to "incentivise" the states to compete among themselves in good governance by rewarding the good performers. In a democratic system, it is the voters and investors who vote with their feet and states that do better are rewarded through this process. The idea of the centre rewarding the states that perform better even if based on the judgment of an "independent panel" is totally repugnant to the federal idea in which the constituents are supposed to be independent in their spheres.

– No doubt, the centre has a responsibility to enforce fiscal discipline among subnational governments and that "represents the most serious challenge for decentralising countries" as Jonathan Rodden puts it in the opening sentence of a book on the subject edited by him. But the best way to enforce that discipline, it is now well acknowledged, is to compel the constituents to go to the market for their borrowing coupled with a hard budget constraint. There must also be a credible commitment on the part of the centre to a "no bailout" policy. The centre assuming the role of a superior authority to reward the states for "good governance" is something unknown in any established federation of the world. How the states are reacting to the proposal is not known.

– Pursuit of a "no bailout" policy is becoming increasingly hard for the centre with the emergence of coalition governments and regional parties aligned with centre exerting pressure all the time to tilt the scales of fiscal transfers in their favour. As Rao and Chakraborty (2006) observe this is going to have serious implication for the states' response to fiscal stress. For it may mean softening of their budget constraint depending on their relationship with the centre. And there are many ways in which such softening can be secured. Maintaining the integrity of the transfer system is going to pose a big challenge for fiscal policy framers.

– To inculcate a market-based discipline, the TFC had proposed that the practice of the centre lending to the states should stop and they should be encouraged to go to the market. While stopping lending to the states, the centre is dragging its feet in following the other proposal. On the contrary the centre is now compelling the states to borrow heavily from the National Small Savings Fund (NSSF), a high cost borrowing source carrying an interest rate of 9.5 per cent. The states as a result have a huge cash surplus, which they are investing in low return (5 per cent) central government treasury bills. The finance minister of Kerala complained bitterly about it in his recent budget speech. "The fact is that", he said, "as a result of this new dispensation the centre was able to

improve its fiscal position at the expense of the state governments". It seems a committee of state ministers has been set up to look into the matter. One can only hope that, the matter will be resolved amicably but the way it has been handled by the centre shows insensitivity to the states' needs.

– One of the important recommendations of the TFC was to set up a loans council to help the states to move over to a market-based regime for borrowing. The centre has so far been lukewarm to the idea.

Concluding Observations

As mentioned earlier, faced with the challenge of honouring the commitment contained in the FRBM Act of 2003 and those in the common minimum programme entailing large public expenditure in several fields, policy-makers are now seeking an escape route by getting the RD and FD targets relaxed. While there can be valid arguments against inflexible deficit targets year to year (it would perhaps be more sensible to require the deficit targets to be met over a cycle) – whether giving the discipline underlying the FRLs a total go by as is suggested now by some is questionable. For at base, the fiscal problems of democracies have their origin in the short time horizon of periodically elected governments and their penchant for promising the moon to the electorate at the time of elections by expanding expenditures while showing extreme reluctance to tax.

The assumption underlying this tendency is that money will somehow be found through borrowing, off-budget if need be, and in the case of the states, through transfers from the centre. The states often assume heavy expenditure liabilities (by handing to existing employees hefty pay rises and so on) on the presumption that ultimately the centre will come to their rescue by giving more grants or remitting their loans. West Bengal taking pride in being at the top among the states in mobilising small savings (which essentially constitutes borrowing from the centre) while being at the bottom in tax-raising is a case in point. The argument often advanced that West Bengal is an agriculture-dependent state does not wash the state has ample powers to tax agriculture and agriculture now offers good scope for taxation especially after the advent of corporate contract farming. In any case, if the farmers of the state are doing so well, there is no reason why they cannot pay some tax to the exchequer. Instead the state goes on relying heavily on borrowing in the expectation that the centre will write it off, that is to say, other states will share the burden. Maharashtra, asking for money from the centre to renew Mumbai's civic infrastructure while sitting over the huge taxable pool that Mumbai contains (according to experts, the city's land alone can fetch more than Rs 50,000 crore) is another case in point. The scope for raising non-tax revenue also remains unexploited, on the plea of subsidising the poor although here is ample evidence that it is the better-off sections who benefit more. Reluctance to tax to match expenditure requirements even when there is ample room is not peculiar to the states, as is evidenced by the exemption of long-term capital gains tax from equity and dividends. Neither the centre nor the states now tax purely cotton-based textiles. It seems the states are reluctant to take over the power to tax textiles under their VAT for fear of "popular" resistance.

Given this reality, some institutional checks on the borrowing powers of governmnts may not be altogether wrong. Rules based market discipline are perhaps the most effective and efficient way to ensure responsible fiscal behaviour of governments in democracies. That alone can compel governments to exploit the available revenue sources to the maximum extent. At the same time it is necessary (i) to enlarge the tax powers of the states and lower level governments so that the expenditure decisions are linked to decisions to tax (the Wicksellian link). The ceiling imposed on the level of VAT that the states can levy, though evolved through a "consensus" is scarcely conducive to the strengthening of this link, particularly in the absence of any compensating augmentation of the states' tax powers; (ii) transfers will still be needed to meet the remaining vertical and horizontal imbalances but the entitlement of a state to transfers should be based strictly on quantifiable norms of its revenue capacity and expenditure need. Specific purpose transfers should be limited only to correct glaring externalities and promotion of universally acknowledged national objectives; (iii) once the transfers are so determined there should be a firmly enforced hard budget constraint and the states should be compelled to go to the market for borrowing.

Ideally the market would be the best judge of a state's repaying capacity but martkets are seldom perfect and can misjudge a state's fiscal potential. Hence, given the national government's responsibility for maintaining macro-stability and the need to take care of the weak states, some oversight by the centre on the states' borrowing cannot be avoided at least in the initial stages. But in order that this does not give undue discretion to the centre there should be a loans council as suggested by the TFC.

What is missed out in the current discussions of the fiscal problems is that for a sustainable and satisfactory cure for fiscal ills the proclivity of politicians to go for borrowing even when there is clear room for taxation must be curbed. It is also imperative for the people to be prepared to pay for the services they want from the government through taxes or user charges. It is the responsibility of economists to educate the people of the root causes of our fiscal malaise and the weakening of our federal fabric and make them aware of their responsibility.

Eminent economist Amit Bhaduri has suggested that the RBI should fund rural development projects by printing money and handing over the cash to the panchayats. One wonders whether Panchanan Babu for all his allegiance to Keynes would have approved of such an idea, especially, given the absence of effective mechanisms of checks and balances against misuse of public money. As it is, on the average panchayats meet very little of their expenditures (less than 10 per cent) out of moneys raised on their own. Should they be given more money to spend or more powers to raise revenue?

One also wonders how many among the economists in West Bengal – and the state can boast of quite a few very brilliant ones – bother to go into the fiscal problems of their state and local bodies. The drop in the share of West Bengal in tax devolution by over one percentage point under the TFC's dispensation went virtually unnoticed in the state. Panchanan Chakraborty might have his first love for macro theory but he had multidimensional interests. I am sure these developments in the field of fiscal discipline and fiscal federalism would not have escaped his attention. EPW

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