

FISCAL HEALTH OF MAHARASHTRA: A STOCK TAKING EXERCISE

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ABSTRACT

This paper provides a brief overview of the economic environment in Maharashtra including the socio-economic development of the state as a backdrop. Within this context we assess and analyze the fiscal situation in Maharashtra. We, examine both, the relative performance vis-à-vis other major states of the Indian union and look at its temporal performance over a ten year period. The power sector has been discussed as a bottleneck to growth of Maharashtra's economy thereby adding to the fiscal woes of the state. Cotton Monopoly Scheme and Sugar co-operatives have also been touched upon. For the reform package to be comprehensive we would like to see policy measures being initiated at three levels: policies at the level of the state, which are financial and administrative in the main; policies that the central government must pursue in its dealing with the states and the third type that are overarching in a sense that they concern the governments at all levels and have to do with capacity building as well as having pragmatic regulatory framework in place.

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1. Introduction

The Indian federal setup has traditionally been loaded in favor of the center. It was hoped the passage of the 73rd and 74th Constitutional Amendments Acts in 1992 and 1993 would result in a transformation in the fiscal scenario of the economy. However, a decade down the line when one takes stock of the situation, *de facto* decentralization is conspicuous by its absence. *Functional and expenditure responsibilities lack clarity and neither the matching resources nor resource raising powers have been adequately devolved.* At each of the three tiers of government i.e. the center, the state and local level, it is of utmost importance that the role of the State and its areas of intervention be *delimited and well defined.* For a comprehensive reform package, the problems faced by each of the three tiers of government will need to be tackled. This paper attempts to understand the fiscal problems being confronted at the level of state governments, with the state of Maharashtra being our focus.

Although the focus of this paper is to look at the fiscal health of the state of Maharashtra, we would like to begin with broad strokes on a wider canvas and look at the economic environment in Maharashtra. Section 2 of the paper assesses Maharashtra's growth performance. Both size and pattern of growth are important to examine in order to yield a proper perspective. Section 3 discusses the demographic pattern and socio-economic development of the state and provides the backdrop in which we examine and analyze the fiscal situation in Maharashtra. The fiscal scenario in Maharashtra is examined in the context of its relative performance vis-à-vis other major states of the Indian union as also its temporal performance over a ten year period is studied in section 4 of the paper. Section 5 takes a closer look at the performance of Maharashtra since the Medium Term Reform package was initiated. The Power sector represents one of the bottlenecks to growth of Maharashtra's economy. Problems confronting this sector and reform measures initiated have been discussed in Section 6. Also discussed here are the Cotton Monopoly and Sugar Co-operatives. Finally in section 7, we discuss governance

issues and required policy initiatives by way of capacity building that suggest the road ahead to usher in the growth process. We conclude in section 8.

2. Assessing Maharashtra's Growth Performance

The state of Maharashtra, occupying 3.08 lakh sq. km i.e. approximately 9% of the territory of India, is home to 9.67 crore people, which constitutes 9.4% of India's total population (2001 census). It is the second most populous state of India after Uttar Pradesh. Despite the fact that Maharashtra constitutes less than 10% of the total population of the country, it accounts for nearly one-fourth of the gross value of India's industrial sector. At current prices the per capita income (Net National Product at Factor cost) of Maharashtra stood at Rs.26,386 as compared to a national average of Rs.18,912 in 2002-03. Such being the scale of Maharashtra's contribution to the Indian economy, it has earned the reputation of being the '*Power House of India*'. Despite these facts and figures, which seems to suggest that Maharashtra is one of the more progressive states of the Indian federation, the World Bank has branded it as a state with "*an impressive past but an uncertain future*" (World Bank, 2002). Fiscal deterioration of Maharashtra is the prime reason for this view.

A look at annual growth rates of GSDP (at 1993-94 prices) tells us that Maharashtra experienced a high real growth rate in 1995-96, when the secondary sector registered the highest growth rate. Since then a steady decline has been noticed. (Annexure A: Table A1). In terms of per capita GSDP (93-94 prices) Maharashtra has maintained its second rank (from amongst 15 non-special category states) since 1993/94 with the happy exception of two years of 1997/98 and 1999/00 when it ranked first.

The sectoral contributions of the three sectors reveal a very telling story. The contribution of the tertiary sector has risen and stands at 56% in 2002-03, that of secondary sector was 28% and that of primary sector was 15% (Annexure A: Table A1). Clearly, *the secondary sector's contribution to Maharashtra's growth has been far from satisfactory with detrimental effect on its own taxable capacity*. The general point to be made here is that, for any economy, service sector expansion without commensurate increase in other sectors is unsustainable. This *lopsided development* can only be self-

limiting and potentially crisis prone. The change in the structure of production has clearly a worrisome implication that the tax revenue potential is severely limited. This is particularly noteworthy as Maharashtra is one of the most industrialized states. Clearly, any further impetus to growth in Maharashtra requires that an enabling environment be put in place for the secondary sector to perform to its potential.

Two distinguishing characteristics of the economic growth in Maharashtra are its regionally skewed pattern and its dependence on the performance of Mumbai. The contribution of Mumbai alone to per capita GSDP has never fallen below 36% in the last ten years. The state of Maharashtra has never fallen below the 2nd rank in case of per capita GSDP, but if we exclude Mumbai from Maharashtra, its rank slips to 3rd in 1993-94, to 4th between 1994-95 and 1998-99 and further to 5th position in 2000-01 and 2001-02 (Annexure A: Table A2).

As a backdrop to any economic analysis of a state of the Indian federation, it is important to understand its demographic features. This is especially true of the state of Maharashtra where regional variations are sharp and where in-migration contributes significantly to population growth. The next section takes a quick look at demographic features and social attainment of Maharashtra.

3. Demographic Status and Social Attainment of Maharashtra

Census 2001 points out that from 1901 to 1961 i.e. in 60 years the state merely doubled its population but only within the last 40 years it has multiplied by 2.5 times. However, the decade of 1991-2001 has witnessed the lowest ever decadal growth rate of 22.57% since 1961 and this is certainly a welcome sign. Undoubtedly it still lies above the national average of the decadal growth rate being 21.34% but clearly there has been some progress on this front.

Regional variations in population size in the five divisions of the State have been tabulated (Table A3). That the coefficient of variation has risen from about 29% to 35% is indicative of regional variations having increased on the population front. The five largest districts in Maharashtra each with a population exceeding 4 million are from Western Maharashtra. Mumbai, Thane, Pune, Nashik and Ahmadnagar occupy only 19%

of the area of Maharashtra and account for one third of the total population of Maharashtra state.

A characteristic feature of Maharashtra's demographic pattern is that *in-migration contributes significantly to the increase in population of the state*. With the 2001 census migration figures not yet available for Maharashtra, the Economic Survey (2003) has worked it out as the difference between actual and natural growth rates. The estimate so obtained shows that migration contributed as much as 23% to the population growth during 1991-2001. In other words one out of every five additions to Maharashtra's population was a migrant. Statistics show that not only has migration contributed significantly to Maharashtra's population, but that its contribution has further increased in the last decade. The contribution of migration to Maharashtra's population over the last two decades has been tabulated in Table A4

In addition to being the second most populous state, Maharashtra is also the second most urbanized state of India. The urban population of Maharashtra at 42.4% is one and a half times that of the national average of 27.78% as per the 2001 census. This figure emphasizes the fact that any analysis of Maharashtra requires that a special effort be made to analyse the issues and problems specific to the urban sector in Maharashtra. Further, it may be worth noting that as per the 2001 census, among the fifteen most populous agglomerations in India, Maharashtra alone has three with Brihanmumbai (1st rank), Pune (8th rank) and Nagpur (13th rank). The strong trend towards urbanization and limited housing stock has led to the development of large slum areas. 2001 census reports that 10.6 million people reside in slums in Maharashtra, with 5.82 million in Mumbai city and suburbs alone. An inter-state comparison of the percent of population residing in slums as per the 2001 population shows that of the 14 major states, Maharashtra ranks 12th i.e. it has the third largest proportion of slum population. (see Table A5)

What is important to understand from these statistics is that growth in slum population of Maharashtra is – at least in part – a natural consequence of the large-scale in-migration that takes place into Maharashtra. The fact that Kerala is ranked first with only 1.81% of its population in slums is not necessarily suggestive of its having done remarkably well on the front of housing or welfare of the poor. Contrary to the state of Maharashtra, Kerala and many other states of India have people migrating away in search

of better jobs. Hence the point that one is trying to emphasise here is that *large slum population is inherent to a highly urbanized state like Maharashtra and it cannot be compared to others like Kerala in this respect. Another important offshoot of this is that by implication the social sector requirements of a state like Maharashtra are likely to be quite peculiar .In particular water-sanitation requirements as well as type of education required will need to be tailor made for specific situation.*

Obtaining the exact numbers of people below the poverty line has become a subject of research in its own right, and not something that we would like to delve into in this study. Hence we confine ourselves to the official estimates of poverty published by the Government of Maharashtra in its Economic Survey, which are listed in Table A6

Figures show that the percent of people below the poverty line has declined from 53.24% in 73-74 to 36.86% in 93-94 and further to 25.02% in 1999-00. The poverty reduction rate for rural areas is seen to be higher than that for urban areas. While the above figures would suggest that significant strides have been made in poverty reduction in Maharashtra, the Economic Survey of Maharashtra (2003) points out that in relative terms Maharashtra has been outperformed by its contemporaries. Punjab and Haryana, which had the about the same per capita income during 1999-00, had a much lower incidence of poverty. Also, Karnataka and Kerala had the same level of the incidence of poverty in 1973/74, but in 1999/00 their poverty levels were much lower than that of Maharashtra. 1999/00 estimates show that of the 16 major states with more than 1 crore of population, 10 states had an incidence of poverty lower than that of Maharashtra. Thus Maharashtra has undoubtedly improved on the poverty reduction front when compared to its own past but in relative terms it hasn't done as well as some its counterparts.

On the education front, Maharashtra with a literacy rate of 77.3 per cent is 12 percentage points above the all India level (65.38%). Maharashtra has shown a two fold increase from the 35.1% literacy rate in 1961. A 12.4 percentage point increase in the decade of 1991-2001 in literacy rate is the maximum decadal rise in the last four decades. In the year 2001 there were 27 districts with a literacy rate exceeding 60% as compared to only 7 in 1961. As compared to 1961 the *enrolment* in primary education has tripled, in secondary education it has increases ten fold and in higher education there is a 8.5 times increase. Hence, compared to its own past, Maharashtra has come a long way in

increasing the spread of education in the state. On a relative scale, Maharashtra stood *second amongst the 14 major states* in 2001 on this count.

However, the *high dropout* levels are disturbing. Data reveals that by Standard IV only 85 per cent of boys and 86 per cent of girls remain in school. These figures dip further for the higher classes and by Standard X only 47 per cent of boys and 40 per cent of girls remain in school. Another area that Maharashtra has not done well is the area of *adult literacy*. More than 80% of female agricultural labourers and more than 60% of women from landholding families are illiterate (Human Development Report: Maharashtra,2002).

Another important point to take note of in this context is that simply looking at literacy rates is not a sufficient indicator in a highly urbanized state such as Maharashtra. A clear indicator to this is observed from the fact that if we look at slum literacy rates we will find them to be as high if not higher sometimes than the non-slum literacy rates. Slum literacy for Mumbai is seen to be as high as 80% as per 2001 census. This clearly suggests that success of the state on the education front needs to be looked at not only in terms of conventional indicators such as literacy rates, but in terms of the extent of *vocationalisation* that has occurred in the state. The number of vocational institutions and enrolments in such institutions are important as job oriented training is provided here. Here is an important policy initiative in waiting!

Improvement in *health profile*, access to healthcare, and higher life expectancy are just as important indicators of human development. On two counts Maharashtra has done fairly well – reducing the infant mortality rate and raising life expectancy at birth. From 105 in 1971, the IMR declined to 48 per 1000 births in 1999 with a marginal differential between males and females. Though the overall gap is steadily closing the difference between the urban and rural levels remains a cause for concern. Life expectancy at birth is 67.7 years and 61.7 years for urban and rural males respectively, and it is 71.2 years and 63.9 years for urban and rural females respectively. This is due to improved access to healthcare and facilities like immunisation and nutrition. However, despite this improvement, the new challenge of HIV and AIDS constitutes one of the biggest hurdles for Maharashtra, which has among the highest incidence of this disease in India. HIV needs to be addressed as a regular development issue as its prevalence is

closely related to poverty, migration, patterns of labour, urbanisation and child mortality. It represents a formidable task that needs focused efforts by clinics supplying blood, community education /awareness campaigns and family welfare bodies.

There is a wide gap in the healthcare infrastructure available in the rural and urban areas. Public investment and health expenditure is not only inadequate but has declined since the 1990's, lowering Maharashtra's position vis-à-vis the other States of India. The private health sector in Maharashtra is the largest in the country and better developed, especially in Mumbai, but the issues of quality and minimum standards need to be addressed. As far as the public sector is concerned, the non-availability of doctors and medicines, lengthy bureaucratic procedures and inadequate medical staff add to the problems. More resources are required, therefore, in the public domain to achieve better reach and equity in health services with a special focus on women and childrens' needs. Wide discrepancy in rural and urban Maharashtra are indicated in the statistics provided in the Human Development Report: Maharashtra, 2002 (Table A7).

We find that there are 140 doctors in urban areas per lakh population while there are only 24 doctorss per lakh population in rural areas. Similar disparities are noticeable in case of hospitals, dispensaries, beds and nurses. Thus intra-state variation is a cause for concern on the health front in Maharashtra.

The broad story that emerges out of the above analysis is that in terms of conventional socio-economic indicators there is no doubt that poverty eradication, education and health status have improved in the state of Maharashtra, but it would not be out of place to say that firstly, the *performance in the social sector has certainly not matched growth performance of the State*. Secondly, *the wide disparities within the state, especially between rural and urban areas are a major cause for concern in the socio-economic development of Maharashtra*. The Human Development Report of Maharashtra observes that the benefits of growth have not been shared evenly across Maharashtra. It is common knowledge that growth is non-homothetic, but the State must step in and iron out the regional disparities to avoid potential socio-political strife that will endanger the very fruits of success.

Having got a broad picture of the socio-economic development of Maharshtra, it would be pertinent to point out at this juncture that although direct links between the

financial state and socio-economic indicators cannot be uncovered in a statistical or econometric sense. Nonetheless, given that the government is a major provider of public health, education and physical infrastructure, problems in its delivery systems due to inadequate finances are bound to adversely impact the socio-economic indicators. Thus, having got an overall picture of the socio-economic development in Maharashtra, we proceed to a detailed discussion of the fiscal scenario in the state, which forms the major thrust of the present paper.

The broad story that emerges from the above analysis is that in terms of conventional socio-economic indicators, there is no doubt that as far as poverty eradication, education and health status is concerned, there has been an improvement in the state of Maharashtra over time. In terms of conventional indicators its relative position is reasonably good but hasn't improved on the education front (consistently 3rd rank), but presents a mixed picture on the health side. However, as mentioned previously, for a highly urbanized state like Maharashtra, these conventional indicators are inadequate. *The performance of Maharashtra in both, the education and the health sector must be deemed to have fallen short of the requirements.* Also, *wide intra-state disparity, between rural and urban areas,* is a major cause for concern in the socio-economic development of Maharashtra. Clearly, there are lessons to be learnt both at the policy design level as well as macro fiscal initiatives that we will draw in a later section.

Given that the main thrust of this paper is to trace the fiscal health of the state of Maharashtra, we have attempted to link this performance of Maharashtra on education and health front with expenditure allocations on education and health later in the paper after getting a feel of the macro picture of Maharashtra's fiscal performance.

4. Assessing Maharashtra's Fiscal Performance: The Macro Picture

The time period chosen for analysis spans the period 1993-94 to 2002-03 (RE) for inter-state comparison and 1993-94 to 2003-04 (RE) for Maharashtra alone. The budget estimate of 2004-05 for relevant variables too has been noted alongside so as to be able to take a view about its credibility. The choice of the beginning of sample period from 1993-94 can be justified on both, purely statistical and on economic grounds. From a purely statistical point of view the new GSDP begins from 1993-94 hence the chosen

sample would provide us with consistency in the data series. From an economic point of view one could say that the decade of the 90s began with the major macroeconomic crisis for the Indian economy. After the initial turmoil and volatility it was only from 1993-94 that the economy settled down.

Most recent studies (see World Bank, 2002) have suggested that Maharashtra slipped on the fiscal front after 1995-96. In order to judge the areas and extent of this slippage, we analyze Maharashtra's performance – as already noted – in two ways. First, we compare Maharashtra's performance vis-à-vis fourteen other major states of India³. We then look at the trend performance of Maharashtra since 1993-94. We have used both RBI data on State Finances as well as Financial Statements of the Government of Maharashtra (GoM). The RBI data has been used when analyzing Maharashtra's relative performance so as to get comparable estimates across states (available up to 02-03 RE) and the GoM data (available up to 2004-05 BE) has been used for the detailed analysis of Maharashtra's fiscal performance. On account of definitional variations, the figures presented in budget documents of the GoM do not conform to those in the RBI documents. Hence some data adjustments have been made in order to obtain comparable series over the entire sample period. These adjustments made have been detailed in Annexure B of the paper.

4 (A) Maharashtra's Relative Performance

To assess Maharashtra's relative performance we sub-divide this entire period into three sub-periods: *Period I* representing the first half of the 1990s (1993-94 to 1995-96); *Period II* reflects the period of so called 'setback' and spans the period 1996-97 to 2003-04 (RE) and *Period III* is the most recent performance i.e. 2000-01 to 2003-04 (RE). For each of these time periods we take simple averages of key macro fiscal indicators to assess the fiscal stress in the state and the improvement or deterioration of performance. This approach is advisedly simple, as given the data-size, it would be

³ The sample comprises of the same fifteen for which social attainment indicators were considered. In order to maintain consistency over time Bihar, MP and UP have been considered to be undivided. Specifically, Bihar and Jharkhand, MP and Chattisgarh; U.P and Uttaranchal have been clubbed together for the years 2000/01 to 2002/03(RE).

foolhardy to put an unbearable burden on it with sophisticated tools of statistics/econometrics.

Six key indicators were identified by us (see table A8) to rank the fifteen states in each of the three periods mentioned below. The ranks have been given so that the best performing state in each of the cases has been awarded a rank of 1.

The picture that emerges from the relevant table is that when GFD/GSDP is used, Maharashtra does not seem to be a poor performer in the latter half of the 90s in comparison with 14 major states of the Indian Union. The changing structure and composition of the deficit, however, is a cause for worry. The ratio of Revenue Deficits to GFD shows its rank to have slipped from 3rd in period I to 6th in period II and further to 11th in period III. Thus, fiscal deterioration has sharply increased in the years 200-01 to 2002-03, at least in relative terms. When considering the budget, the ratio of capital disbursements to total expenditures the state, Maharashtra has slipped from its 3rd position in period I, to 9th in period II and even further to 13th in period III. On the own tax revenue front as per cent of revenue expenditure (tax effort measure used by the EFC), the state was seen to be a star performer in a relative sense in the first half of the nineties. It has been over taken by Tamil Nadu in the latter half of the 90s in period II (slipped to 2nd rank) and by Haryana and Tamil Nadu in period III (slipped to 3rd rank). However, despite this relatively good tax effort, Maharashtra finds itself at the bottom of the table in the devolution of grants. Grants given by the Finance Commission and Planning Commission are criteria based and hence it is often pointed out in official circles that no state can be deliberately victimized. However, we believe that efficiency has not been given its due weight in the criteria used to devolve grants. It is our contention that there is no problem if Maharashtra receives nothing on some criteria, coming under the 'need based' category, but it must get its due share from the kitty on efficiency grounds (see Pethe and Lalvani, 2004).

It has been pointed out that the tax effort measure need not necessarily suggest efficiency as tax competition amongst states has led to large scale tax exporting and hence is not a precise efficiency measure⁴. For Maharashtra specifically, Rao and Sen (1996) find that in 1987/88, tax exportation contributed as much as 43% of Maharashtra's

⁴ We thank Dr. Govinda Rao for drawing attention to this point.

own tax revenue. We do recognize that our tax effort measure suffers from the limitation of not factoring in tax exportation. Even whilst keeping this caveat in mind, it continues to be our view that in the absence of any alternative measure that is simple, transparent and easily computable, this measure does serve its role as an indicative measure proxying efficiency in tax performance, especially in the incremental sense. This is especially so if tax exportation is temporally reasonably stable across states. Indeed, it needs hardly be mentioned that all indicators, especially ratios, suffer from some obvious limitations.

Having used some macro fiscal indicators to compare Maharashtra's fiscal performance to that of others, in the next sub-section we undertake a more detailed examination of the fiscal performance of Maharashtra since 1993-94. In other words the next sub-section attempts to assess Maharashtra's performance vis-à-vis its own past.

4(B) A Trend Pattern of Maharashtra's Fiscal Performance:

This section of the study is structured in the following manner:

- (i) We take a look at key deficit indicators, which show the *extent of fiscal stress* under which the economy finds itself.
- (ii) Trace the *cause of this stress* i.e. whether it originates from the expenditure or the receipts side of the budget.
- (iii) Attempt to see *how the government of Maharashtra has been trying to fund the fiscal deficits* i.e. we look at the debt profile of Maharashtra.

GFD/GSDP, Gross Fiscal Gap (GFG) and Primary Deficit to GSDP ratios, all indicators of fiscal stress, show a steady worsening in fiscal discipline. The extent of fiscal profligacy indulged in by any government is evident from revenue deficit. Only nine years ago i.e. in 1994-95 Maharashtra had registered a revenue surplus, but from then on the Revenue Deficit as a proportion of Gross Fiscal Deficit has risen rather sharply to reach 87% in 2000-01. The last two years show some improvement on this front but the ratio is still as high as 46% in 2003-04 (RE). The 2004-05(BE) shows this ratio to increase by 20 percentage points. This clearly signals that *no major effort to pull back revenue deficits is in the offing*. (Appendix A:Table A9)

The large increase in revenue expenditures has come at the expense of cuts in capital expenditures. We find a large increase in surpluses on capital account. Capital

surpluses have risen from -0.06% of GSDP in 1993-94 to reach a maximum of -2.51% of GSDP in 2003-04. In nominal terms the capital surpluses have risen from Rs. 63 crores in 1993-94 to reach almost Rs.10,000 crores in 2001-02. The last couple of years show some reduction on this front but it was still above Rs. 9000 crores in 2003-04(RE).

Expenditure Pattern

The broad story about the expenditure pattern of Maharashtra over the last ten years is that *it is the crucial developmental expenditures that have been axed in case of both the revenue and capital account.* The point that comes across very sharply from the above analysis of Maharashtra's finances is that *it is imperative that one looks at the fine print of budgets to know where exactly the burden of the adjustment falls.*

On the revenue expenditure side salaries, pensions and interest payments in a way represent 'committed expenditure' for the government. The share of these three in total revenue receipts constituted as much as 58% in 1993-94. This shot up to as much as 91% in 1999-00 on account of the Pay Commission revision. Since then there has been some effort to curb these expenditures but it continued to siphon off as much as 81% in 2001-02. The RE for 2003-04, which still is a mid-term figure, puts it at 74%. The budget estimate for 2004-05 puts it at 70% i.e. 4 percentage points lower than the RE of the previous year. *While the debt swap scheme does offer some scope for reduction of interest payments, with elections round the corner and budget announcements like D.A. hike by 6% in the 2004-05 budget this target does not appear credible.*

Delving a little further into details, in the (sub)sub-section that follows we take a closer look at specific expenditure heads of education and health and try to tell a story that relates the attainment indicators observed for education and health in section 2 above with expenditure allocations in these two sectors.

Expenditure Allocations for Education and Health

Earlier in the paper, we looked at a conventional measure of educational attainment viz., literacy. We are well aware that this measure of performance is only indicative, as a study of attainment in the education sector is in itself the subject matter of a large body of research. Be that as it may, looking at it from 'above', we find that the state has fared reasonably well temporally and also fared reasonably well among fifteen major states (3rd Rank). The financial side of this story is that in per capita terms the

expenditures on education, on revenue account, has shown a steady increase with sharp spike in 1999-00 and 2000-01. This is clearly on account of the Pay Commission award. However, per capita education expenditure on capital account shows a distinctly downward trend since 1999-00. If we consider the share of education in revenue expenditures, we find the shares to be fairly consistent till 1999-00, when there was a sharp rise in the share of education expenditures on revenue account. However, this has been seen to revert to its earlier level in the last two years. Since this very year the share of education in capital expenditure has been severely cut. Thus increasing expenditure allocations to education in per capita terms appear to be reflected in improved attainment till 2001 (the year for which latest attainment indicators are available).

In the health sector too attainment indicators suggest temporal improvement in conventional attainment indicators like IMR and Death rate (discussion in Section 3 above). On the fiscal side we find that health expenditure, both on revenue and on capital account, have shown a steady increase in per capita terms over the ten-year period under consideration. In terms of shares, however, we find a steadily declining trend in the share of health expenditures on revenue account in total revenue expenditures but an increase in the share of health expenditure on capital account in total capital expenditures. *A political economy explanation – that in a sense is generic – that one could possibly venture to provide for this result is that opening up of new public health center's (PHCs) and community health center's (CHCs) seem to be 'politically attractive' to incumbents to appease voters, but maintenance expenditures which are crucial for functioning of these PHCs/CHCs have been pulled back.*

Increasing social sector expenditures in per capita terms especially in revenue expenditures leads us to the conclusion that *there does not appear to be any disconnect between expenditures allocations for social sector and social sector attainment. However, the low and declining share of education and health in revenue expenditures clearly show that social sectors have not significantly contributed to the overall fiscal stress that the state finds itself in.*

To continue in this vein further, we once again draw on the previous discussion on social sector attainment, where we pointed out a highly urbanized state like Maharashtra needs to focus on issues such as vocationalisation of education and problems

of HIV and AIDS. Also, in both education and health sectors we need to bridge the sharp divide between rural and urban sectors on a priority basis. Undoubtedly, all these are extremely important issues, but they are matters of micro level design and cannot be addressed in a paper such as this, which attempts to provide the macro picture. However, these observations lead us to the policy prescription that *we need a re-adjustment of existing resources*. These *re-adjustments are needed at all levels* – from non-developmental to developmental, specifically towards social sector and even within specific category of education and health expenditures we need a re-adjustment of resources to address specific areas of concern. A better balance needs to be achieved between revenue and capital expenditures. *The challenge lies in achieving this whilst not allowing the macro-aggregates in fiscal/budgetary balance getting out of control.*

For tackling the existing problems and for gearing up to face future challenges, policies directed towards *re-adjusting of existing resources must be coupled with those which increase the size of the pie itself*. This brings us to the receipts side of the story.

Revenue Receipts

A measure of the efficiency in the government's functioning is gauged from the trend pattern of own tax and own non-tax revenues (as mentioned previously, own tax revenues do suffer from the limitation of not factoring in tax exportation by states). The share of own non-tax revenues from economic services has, however, dipped from 45% in 93-94 to a low of 28% in 2001-02. It has improved to about 46% in the RE of 2003-04 but is expected to fall to 38% as per the budget estimate of 2004-05. *This fall in non-tax revenues from economic services is indicative of subsidization of these services.*

The share of own tax revenues in revenue expenditure, the measure of tax effort used by the EFC shows the maximum to have been reached in 1994-95 and 1995-96. The measure has shown some reduction in the second half of the 90s and reached its minimum in 2000-01. However, an increasing trend is noticeable since then. The buoyancies for some of the important taxes have been computed. Our estimates show that sales tax, the most important contributor to state government treasury, contributing approximately 60% of the state's own tax revenue, has a buoyancy which is *lower* than stamps and registration duty, electricity duty, taxes on vehicles and even land revenue. Multiple rates have made the sales tax structure complicated resulting in loopholes,

which contribute to evasion. In addition to this, a number of tax exemptions have resulted in this source of tax revenue not contributing to a greater extent to the exchequer (Annexure A: Tables A13 and A14). Tax revenues can increase either by increasing tax rates or a widening of the tax base. The process of tinkering around with tax rates seem to have tapered off, hence a widening of the tax base must be actively explored coupled with improvements in tax administration to plug loopholes. A move towards VAT incentivizes correct reporting and, given the predominance of the service sector in Maharashtra, *getting more services into the tax net*. These are two measures, which are sure to cause the revenue receipts of the GoM to move to a higher trajectory. Both these decisions are politically difficult and dependent on the decisions at the central government. Although, technically, the state can introduce VAT within its boundaries⁵, for it to be successful, a nation-wide VAT would need to be put in place.

Yet another reason why the state of Maharashtra needs to look towards the center for improving its fiscal health is the design of intergovernmental transfers. The share of grants from the center in revenue receipts has declined from 11% in 1993-94 to reach its lowest of 5% in 1998-99. Subsequently there has been some increase but it stood at about 8% in 2003-04(RE) (Annexure A: Table A13). Here we would like to reiterate the point made in the previous section about increased weight being accorded to the efficiency criterion. In a previous study we have suggested a set of principles (FAIR PLAN approach) that should guide the devolution by Twelfth Central Finance Commission (see Pethe and Lalvani 2004a). What it urges in the main is to have an element of incentive compatibility in the devolution process. Such a move is mandated by the emerging context of party (coalitional) politics and the reality of different political interests at the Center and the State. As a logical corollary it follows that a similar scheme must prevail when it comes to the transfer from the State to Local Bodies (see Karnik et al 2001). The Fiscal Reform Facility of the Eleventh Finance Commission, which has instituted an incentive fund is a positive move in this direction. However, the package of rewards and penalties (incentive compatibility) needs to be instituted in the devolution criteria. Thus,

⁵ Maharashtra did experiment with a subtraction type VAT between 1995-99 but the experiment did not succeed.

what we are arguing here is for a more meaningful and a mandated/statutory interaction between various levels of governments.

Thus the story from the receipts side of the budget is that Maharashtra has fared reasonably well on the tax front. However, there is scope for improvement. For substantial improvements to occur some measures could be adopted at the level of state government itself, but for others it must depend on a comprehensive package including reform measures at the level of the central government. *Improvement at the level of the state government can occur by reducing exemptions and improving administration in case of taxes such as sales tax. For additional improvements such as bringing in more services into the tax net and implementation of VAT the initiative needs to come from the central government.* (This has happened since we wrote this piece and the jury is out on its success).

Since resources raised thus far have fallen far short of expenditure needs, the state has been compelled to borrow. Unlike the individual level, borrowing at the level of governments is not necessarily a vice. The use to which these borrowings are put is crucial. Given the large scale borrowings resorted by all state governments, questions of debt sustainability have once again come to the fore. While the rule of thumb measure of debt to GDP ratio exceeding the interest rate can be used to get a feel for its sustainability, to our mind a careful analysis of the structure and composition of debt assumes greater importance from the point of view of debt restructuring.

Debt Position and Composition

The GoM defines total debt as having three components viz., (i) Public Debt i.e. internal debt and loans from central government (ii) Borrowings from small savings and provident fund and (iii) other interest bearing obligations i.e. from reserve fund and deposits and advances. Total debt of the state of Maharashtra as per cent of GSDP has gone up from 14% to 25% in 2004-05(RE) i.e. an increase of 11 percentage points (Annexure A: Table A15). In nominal terms the expenditure on interest payments has increased over five times. The share of loans and advances constituted as much as 88% in 93-94. This share reduced but continued to stay as high as 81% till 2001-02. On account of the debt swap scheme the share of loans from centre has declined to reach 51% in 2003-04 (RE) (Annexure A: Table A15).

The debt problem of the state of Maharashtra is further compounded on account of *extra-budgetary operations*. Many PSUs in Maharashtra have raised money in the domestic capital market backed by unconditional and irrevocable guarantees by the GoM. These borrowings do not need to figure in the budget as they do not need the approval of the state legislature. These operations constitute (i) off-budget borrowings through the creation of new public corporations called Special Purpose Vehicles (SPVs). These are serviced through the budget. Borrowings through SPVs provide an easy way to bypass the GOI restriction placed on state government borrowings via Article 293, Clause (3)⁶ and (ii) guarantees or contingent liabilities which are serviced by the borrowing agencies. While off budget borrowings have been a feature of Maharashtra's finances only since 1996/97, it has been issuing guarantees on extra-budgetary borrowings since the 1980s. *During the period 1996-97 to 2003-04 (RE) the stock of off-budget borrowings has shown a fifteen fold increase. The amount outstanding by way of guarantees has increased seven fold between 1996-97 and 2001-02 (Annexure A: Table A16).*

A point that we would like to make at this juncture is that off-budget borrowings, while 'gimmicky' and used as an instrument for circumventing government restrictions, cannot in a logical sense be deemed to be necessarily wasteful as they are borrowings for infrastructure projects. Like all other forms of borrowing the use to which these funds are put, the returns from those projects vis-à-vis the cost of these borrowings however, will determine its viability. In Maharashtra's case most of the funds borrowed via SPVs have gone into irrigation projects and have not been have not utilized appropriately⁷. However, if infrastructure funding is not to suffer, alternative sources/strategies of funding these projects need to be explored. One such alternative is the public-private partnership where the government acts as a provider of seed money and /or enabling regulatory environment. The other alternative that could be explored is the access of local bodies to capital markets via municipal bonds. The experience thus far shows that only bigger municipal corporations are in a position to take the advantage of the resources available

⁶ Article 293 Clause (3) of the Indian Constitution states that "A state may not without the consent of the GOI raise any loan if there is still outstanding any part of the loan which has been made to the GOI or by its predecessor government, or in respect of which a guarantee has been given by the GOI or by its predecessor government".

⁷ We would like to thank the Finance Secretary of Maharashtra, Ms. Chitkala Zutshi for drawing attention to this.

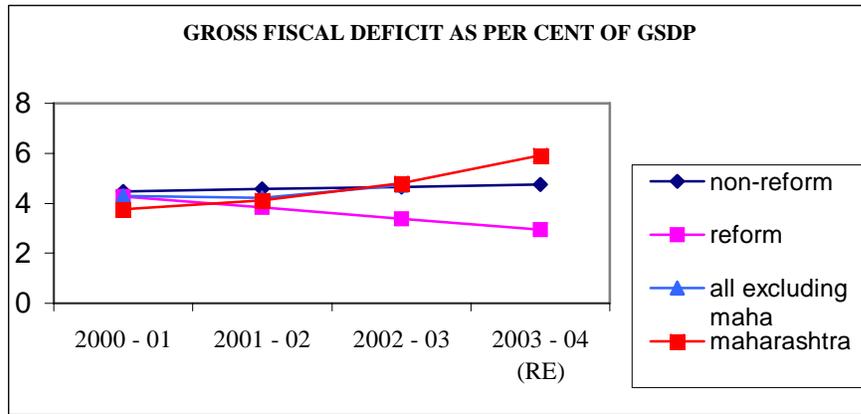
in capital market. Medium and smaller municipalities are unable to do so due to weak financial position and lack of capacity to prepare viable project proposals. Some suggestions that will enable small and medium local bodies to access the capital market have been provided in Pethe and Lalvani (2004b).

While there is no denying that the fiscal health of Maharashtra is far from enviable and has deteriorated significantly over the last decade, it would be unfair not to credit the government of Maharashtra (bureaucracy included) for recognizing the problems and putting it down in the form of reports and documents. In October 1999 a White Paper on the State's finances was presented and discussed in the State Legislature. The National Institute of Public Finance and Policy (NIPFP) was engaged to do a study of state finances and it submitted its final report in September 2001. A one-man committee was then appointed to suggest ways to improve the transparency in budgetary processes (Godbole July 2001). Under the States' Fiscal Reform Facility the GoM drew up the Medium Term Fiscal Reform Programme for Maharashtra. Like 14 other states the GoM too signed an MOU with the central government. *However, the fact that the MOU and the MTFRP document have not been put on the public domain defeats the very purpose of any such reform initiative. If reform commitments are to be institutionalized then it must be made mandatory that such documents be put in public domain. Such publicly made commitments have a greater chance of tying the hands of political parties and ushering in accountability on the part of governments.*

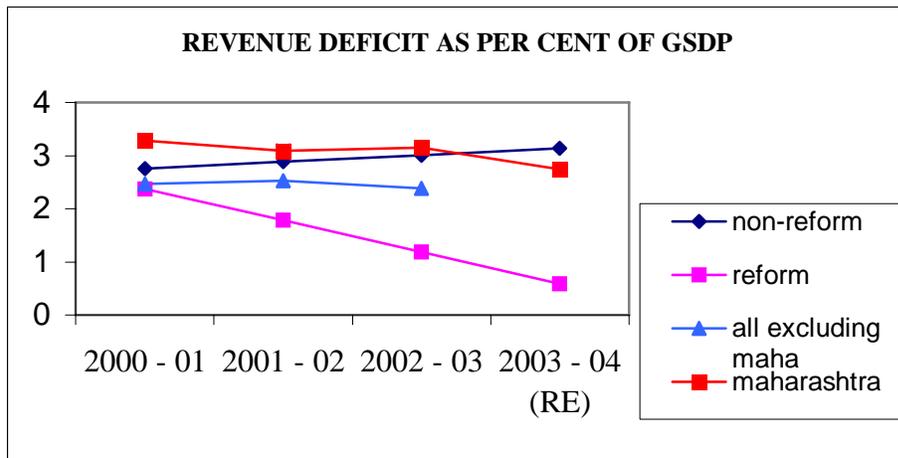
5. Assessing Maharashtra's Performance during MTFRP period: 2000-01 to 2003-04 (RE):

Since the origins of the MTFRP goes back to the EFC and also since the MTFRP document of the GoM was not available in public domain we have chosen to assess Maharashtra's performance on some key parameters in the 'reform' scenario vis-à-vis the 'base' or 'no-reform' projections for all states made by the Eleventh Finance Commission (EFC) and also vis-à-vis the actual performance of all states other than Maharashtra (this refers to the aggregate of all 28 states). The performance of all states could be traced only up to 2002-03 (RE) as the RBI State Finances make inter-state comparisons possible only till this data point. The 'no-reform' and 'reform' graphs are as projected by the EFC of GFD/GSDP is shown below. We find that Maharashtra started

off as being better than even the reform projections made by EFC but ended up being worse than even the no-reform scenario.

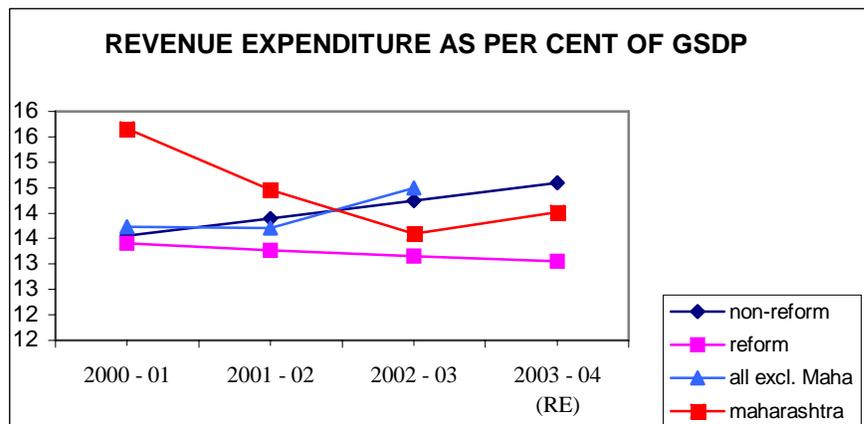


Maharashtra shows up in poor light as far as the ratio of revenue deficits to GSDP is concerned. The state was worse than the no-reform projection and the performance of all states in the beginning stages. Some improvement on this front, however, is noticeable in 2003-04 (RE) where it is better than the no-reform projection but way off target from the reform projection.

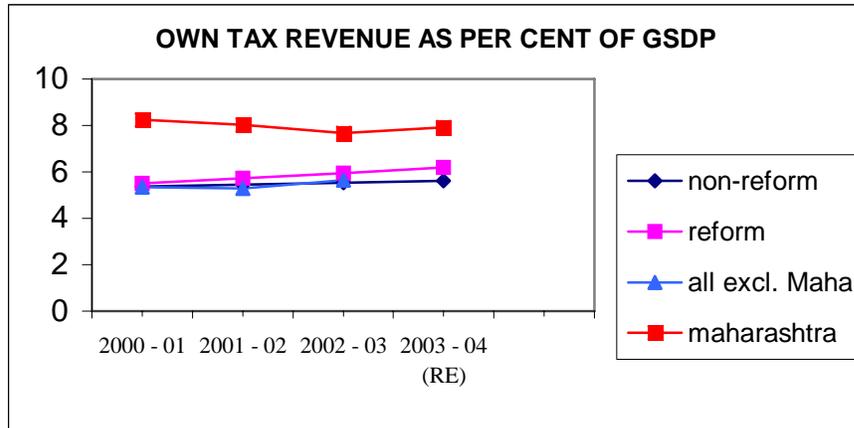


Delving a little further into the structure of revenue deficit we find that revenue expenditures as per cent of GSDP has shown a steady reduction. In 2002-03 its performance has shown an improvement. It has bettered the collective performance of other states and the non-reform projections. This improvement, however, must be

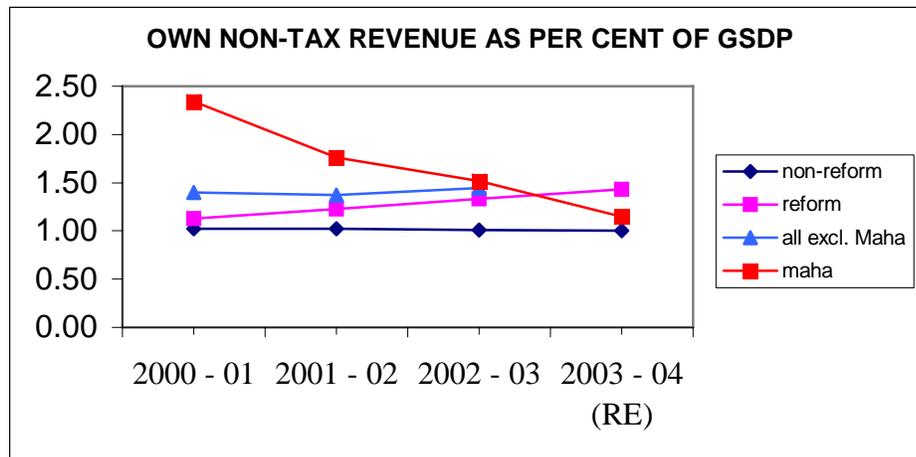
juxtaposed with our observations in the previous section where we analysed revenue expenditures in detail. The observation made was that it is the ‘developmental’ category of expenditure has been axed. This finding serves to draw attention to the potential danger of target setting without charting out the road map for attaining these targets. In the context of this lacunae in the FRBM. Karnik (2002) observes that *in the absence of any checks and balances along a well defined path, our politicians would be sure to try and attain the goal of deficit reduction by axing the politically convenient expenditures on social sector.*



Having taken stock of the expenditure performance we proceed to examining the receipts side of the budget. Maharashtra’s performance on the own tax front has been substantially better than even the reform projections of the EFC .



On the front of own non-tax revenues, Maharashtra's performance was substantially better than that of other states and the reform projections of EFC. However, there has been a steady decline on the performance on this front. The ratio of non-tax revenue to GSDP, however, the ratio for Maharashtra declined to come to par with the combined performance of other states in 2002-03. The revised estimate for 2003-04 shows it to have slipped even further to almost reach the non-reform projection.



The overall impression is that while Maharashtra's performance has bettered the reform projections made by the EFC, on the revenue front, it has fallen short of the target on the expenditure front. The more detailed analysis of the previous sections reveal that structure of the deficit and the direction of expenditure pruning that has occurred is a cause for concern. Some of the welcome reform initiatives that have been initiated

include the introduction of the Fiscal Responsibility (FRB) and Social Responsibility Bills (SRB) in the Assembly.

Moving a step forward from the macro picture of the fiscal scenario of Maharashtra, if we were to identify one specific sector, which has added significantly to fiscal woes of Maharashtra, the prime accused is the '*Power Sector*'. The section that follows provides a somewhat more detailed discussion of sectoral issues, specifically the power sector and the cotton and sugar markets.

6. Sectoral Issues

6(A) Power Sector in Maharashtra

Maharashtra has the highest installed capacity, both private and public, and the largest market among the Indian States. Three power utilities, TATA Electric Company, Bombay Suburban Electric Supply (BSES) and Bombay Electric Supply & Transport (BEST) serve the Mumbai area. The first two are private, and the third one is municipality-owned but operates with considerable autonomy. Outside Mumbai, the Maharashtra State Electricity Board (MSEB) – a public body created under the Electric Supply Act (1948) of the Government of India – is the sole supplier of power in Maharashtra.

Until 1999-2000, MSEB's financial performance was guaranteed by the state. In August 1999 Maharashtra Electricity Regulatory Commission (MERC) was established and has become effective since 2000-01. It sets electricity tariffs based on tariff filings submitted by MSEB. This has resulted in MSEB's financial and other data becoming public and subject to considerable scrutiny. MERC has set strict performance targets for MSEB and has issued tariff orders predicated on efficiency improvements together with tariff adjustments such that the state will no longer have to subsidise the utility. MSEB required a manageable subsidy of Rs 300-650 crore until 1998-99. Since 1999-00 when Dhabol came into existence MSEB has become a loss making enterprise without subsidy. The net loss without subsidy was to the tune of Rs. 1149 crores for the year 2000-01. *The budgetary support to the power sector which constitutes (i) subsidy and (ii) capital outlay and net lending has risen from Rs. 450 crores in 1993/94 to Rs. 1122 crores in 2003-04 (RE) i.e. an increase of 2.5 times* (Annexure A: Table A17). The point about the Dabhol episode is that while it may be considered an isolated instance that did not come off, the

ill effects have a tendency to cast their spell wide and long. Indeed, not only will this lead to financial losses to the state economy, and the consequent loss of face vis-à-vis foreign investors, it will be a while before such a momentous initiative will be conceptualised again let alone actually taken.

The power sector in Maharashtra, as in many other parts of the country, has been characterized by a total lack of commercial orientation. Tariffs for domestic and agricultural segments are lower than the average cost of supply of power, and are cross-subsidized by the commercial, industrial and the railway traction consumers. It can be seen that even though the average cost of generating electricity is 357.54 Ps. per unit, the average realisation is only 270.02 Ps. per unit i.e a loss of 87.52 Ps. per unit.

Table A18 shows that even though the agricultural/irrigation sector consumed about 25% of the total electricity sales it only contributed only a dismal 7.7% of the total revenues. The distorted tariff structure has led to an increase in high-paying industrial consumers setting up their own generating stations which currently have generating capacity of about 641 MW. In addition, NOCs for an additional 1181 MW captive capacity have been given. While consumption of power from the MSEB grid by high-paying industrial consumers has been on the decline, consumption by subsidized consumer categories has grown over the past few years. Further, the low tariff for subsidized consumers has not only led to lower revenues, but also to sub-optimal consumption from these consumers (*GoM's white paper on Maharashtra Power Sector Reforms*). The T&D losses are high at about 39.4%.

Despite the problems confronting MSEB, a study done in 2002 by the Department of Power, GOI, of various electricity boards and electricity departments where scores were given according to the several factors that they listed out, Maharashtra was ranked 5th. Here the point that we wish to make is that despite the fact that the MSEB is not performing so badly in relative terms there is no room for complacency. Maharashtra is a highly industrialized state and its performance hinges crucially on the power sector, hence problems confronting this sector are likely to affect the economic well being of the state of Maharashtra to a greater extent than would be felt in other less industrialized states of India.

The new Electricity Act 2003 has come into force from June 2003. An important aspect of the Act is that the provisions related to subsidies and cross-subsidies are well spelt out⁸. It clearly states that if the state government requires any specific category of consumers, such as farmers, be given a subsidy then the subsidy amount should be paid in *advance* to MSEB in the manner as specified by MERC. However, the new government has asked for the Act to be reviewed, hence a sense of uncertainty prevails. Speedy action in this context is called for, as it must be recognized that problems confronting the power sector are huge and there are no quick fixes. The White Paper on power sector reforms makes it clear that the GoM recognizes the significance and the urgency of undertaking reforms in this sector on a priority basis.

6(B) Fiscal Implication of Interventions in Cotton and Sugar Markets

The populist Cotton Monopoly Scheme of the Government of Maharashtra is only too well known. The Maharashtra State Marketing Federation operated the scheme as the chief government agent till 1984, when it was taken over by the Maharashtra State Co-operative Cotton Growers Federation Ltd. The scheme made profits for ten years. Since 1994-95 the two factors that have contributed to its downfall are falling market prices and rising minimum support price. In the year 1994-95 the total cost rose by 40%, of which 70% was due to higher procurement price. The accumulated losses of the Federation in 2000-01 were nearly Rs. 28,000 crores. This scheme has resulted in benefiting financial institutions and intermediary traders rather than the cotton farmers (World Bank, 2002).

Sugar Co-operatives are the other major problem that has added to the financial burden on the state exchequer. The rationale behind government support to sugar co-operatives was to promote rural development. However, a majority of sugar co-operative mills in Maharashtra are sick. This is a consequence of a lack of proper cost-benefit analysis before setting up of the mill. The proliferation of new mills has resulted in underutilization of existing ones. The outstanding stock of guaranteed loans at the end of the year 2000 was Rs.3300 crores. Given the sickness of a large number of sugar

⁸ "If the State Government requires the grant of any subsidy to any consumer or class of consumers in the tariff determined by the State Commission under section 62, the State Government shall, notwithstanding any direction which may be given under section 108, pay, within in *advance* in the manner as may be specified, by the State Commission the amount to compensate the person affected by the grant of subsidy in the manner the State Commission may direct, as a condition for the license or any other person concerned to implement the subsidy provided for by the State Government. Provided that no such direction of the State Government shall be operative if the payment is not made in accordance with the provisions contained in this section and the tariff fixed by State Commission shall be applicable from the date of issue of orders by the Commission in this regard".

factories many of these guarantees are likely to be invoked. This will add substantially to worsen the existing precarious fiscal health of the state. In the 2004-05 budget the Government has given default guarantee to the 51 co-operative sugar factories pre-seasonal loan amounting to Rs. 39.57 crore during the crushing season 2003-2004 and also gave guarantee for the working capital term loan of Rs. 786.50 crore to 31 co-operative sugar factories. This measure is sure to add to the already strained fiscal health of the state. But given the political economy considerations in general, reforms in this arena are fraught with difficulties.

After all the financial and fiscal data and ratios are computed and lacunae are identified, policy initiatives need to be suggested and taken. These cannot be operationalised in a vacuum. The framework of policy regimen is constructed through principles of governance. This forms the subject matter of discussion in the section that follows.

7. Governance Issues

Governance is a generic term. It has to do with *the strategies that deal with identification of the lacunae and operational policy initiatives to be undertaken given the objectives of the government in order to infuse greater efficiency, transparency and accountability in its processes*. The framework of strategic regimen is constructed through principles of governance. Given the objectives of the government, ‘good governance’ is concerned with systemic design that leads to better and efficient practices being adopted by administrative machinery – in some sense divorced (sanitized) from partisan political considerations – in the conduct of governmental policies. In a country like India, it is essential that polity, bureaucracy, private sector and civil society forge synergistic relations in order to create an environment conducive to good governance.

One of the chief concerns in this area is denoted by the umbrella term of *capacity building*. This term has several connotations. The change in the macroeconomic ethos has implied that state level policy design and implementation have to be carried out in a different manner. The best management practices need to be borrowed from private sector and inculcated by the state government machinery even in the highest echelons. Implementation at times will be seriously impinging on the vested interests of groups in the society and will require tact and political will to see such a transformation through.

Capacity needs to be built in this arena with the instrumentality of state administrative schools like the YASHADA. Similar capacity needs to be built in accessing capital markets or taking bank exposure or indeed designing the enabling regulatory framework thereof. This requires considerable economic skills, something that many a public servant will need to work at building the capacity for. Design of specific courses for government employees is a task that requires urgent attention.

At a higher level of governance (perhaps even at the political level) serious attention has to be paid to creating an incentive compatible structure in government service from top to bottom. In-service training and recognition of achievement through monetary and other compensation needs to be institutionalized. Thus, the *public servants must perceive themselves as stakeholders in the process of governance*. It is clear that service conditions have to be adjusted to be in tune with the changing times. This is clearly recognized but nothing concrete has yet emerged in the state of Maharashtra.

Allied considerations have to be given to the question of political interference. In particular, transfers have to be rational and transparent, so that they sub-serve the goal of enhancing systemic efficiency rather than being an instrument of petty political vendetta. Maharashtra has taken some steps in this regard. The administrative reforms commission headed by Shri. Sukhtankar, and the Godbole committee report have taken pains to focus on this very aspect (of non-transparency and arbitrary transfer process). The reports are comprehensive and have been accepted and much appreciated but nothing really has moved on the ground. The trick here – the crucial next step – is to have in place a mandatory requirement on part of whichever government is in place to follow certain procedures that would stop ‘politicization’ and consequent emasculation of bureaucracy.

Perhaps the time has come to have a fresh look at the role of the state in the present circumstances and redefine it. Apart from recognizing the difference between the traditional role of government to the more modern – enabling role – delimited and well-defined multi-level hierarchical structure with obvious technology application in terms of e-governance, it must be recognized that the older regime has been carrying considerable extra baggage for too long. *The time has come to trim down the responsibilities of the state and focus on catering to bare socially essential services*. This will serve two purposes, one, the financial provisioning will come down and two, the quality of services

to be provided will be focused so that it will become altogether more possible to monitor the quality of service delivery in an accountable way. Thus, what we are stressing here is the need to *build a conducive and enabling environment that will accept changes in the institutional settings*. There is an obvious scope for considerable capacity building here. The initiative here has to come from the ‘political process’ perhaps with help from civil society, because the perception of both the politicians as well as the bureaucracy will be that they will lose the domain of influence both in extent and magnitude.

Thus, governance issues emerge at various levels and should be dealt with as such. These involve training of staff in specific skills apart from procedures and protocols, the changes in service conditions so that incentive compatible system is in place. There are changes required at the level at policy and regulation to keep in step with the changing environment. Finally, there is need to bring about a change in the institutional substructures and their interaction modes not to mention involvement of expert external agencies. All this requires a massive capacity building exercise requiring a change in mindsets, creation of a feeling on the part of all the agents of being real stakeholders with the end result of improved governance.

8. Conclusion

Now the unenviable task of concluding this somewhat long paper must be faced. We have provided a backdrop of the state of Maharashtra in its various economic facets. We have then zeroed in on the fiscal situation and performance both in the relative (to other states) as well as the temporal (stand alone) aspects. In doing this we have gone into the structural details in order to gain insights and policy implications for improvements. Apart from illustrative treatment of Power sector – in some sense the *pons asinorum* – for Maharashtra’s progress, we have also dealt briefly with governance issues. The paper points to many specific problems and contains some specific suggestions that we briefly recapitulate.

- The role of the State and its areas of intervention must be *delimited and well defined*.
- An *enabling environment* must be put in place for the *secondary sector*, which is currently lagging behind, to perform to its potential.
- Policy initiatives must address the question of *regional imbalance*.
- With 42% of the population residing in urban areas, special effort must be made to analyze the issues and problems specific to the urban sector in Maharashtra.

- Vocational education must be given greater attention.
- Serious consideration must be given to rectify the *structural lacunae* in the budget.
- Intra-state variation is a cause for concern on the health front and needs to be addressed.
- Improvement on the expenditure side of the budget requires a *re-adjusting of existing resources*, coupled with policies directed towards increasing the size of the pie itself.
- Improvement on the receipts side requires a reduction in exemptions and an improvement in tax administration. Additional improvements such as bringing in more services into the tax net and implementation of VAT where the initiative needs to come from the centre.
- Mechanisms – such as legislative changes and the pooled fund approach – for smaller and medium municipalities to access the capital market must be designed.
- If reform commitments are to be institutionalized then it must be made mandatory that *relevant documents be put on public domain*. Such publicly made commitments have a greater chance of tying the hands of political parties and ushering in accountability on the part of governments.
- A more meaningful and a *mandated/statutory interaction* between various levels of governments must emerge.
- Finally, for effective service delivery to happen, *capacity building and governance issues* must be tackled at all levels of government.

The policy suggestions – the solution set if you like – can be partitioned into three types of policies. One that deals with what the state can do on its own. The other that deals with what needs to be done by the Central government to create an enabling environment. And the third that deals with governance issues. The first type requires policies to be implemented by the state have to do with financial matters in the main but also deal with creation of meaningful and viable substructures. They also are concerned with having a properly worked out implementation mechanisms/ schemes. The second type deal with policies that the central government must pursue in its dealing with the states. The third type are overarching in a sense that they concern the governments at all levels and have to do with capacity building as well as having pragmatic regulatory frameworks in place.

The political space throws up many contradictions and compulsions so that techno-economic feasibility is never sufficient. Yet our hope lies in the fact that through all this muddle, politics continues to be an art of the possible!

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Annexure A

**TABLE A1
Gross State Domestic Product 1993/94 prices**

Year	Annual Growth Rates				Sectoral Contribution (As per cent of GSDP)		
	GSDP	Primary	Secondary	Tertiary	Primary	Secondary	Tertiary
1993-94	-	-	-	-	20.16	32.77	47.07
1994-95	2.55	-1.37	2.34	4.38	19.39	32.70	47.91
1995-96	11.49	4.81	15.43	11.51	18.23	33.86	47.91
1996-97	5.08	15.58	4.59	1.43	20.05	33.70	46.25
1997-98	5.56	-12.97	11.85	9.02	16.53	35.71	47.76
1998-99	2.92	4.84	-4.17	7.56	16.84	33.24	49.92
1999-2000	9.76	9.01	6.14	12.42	16.72	32.15	51.13
2000-2001	-3.75	-4.15	-12.63	1.96	16.66	29.18	54.16
2001-2002	5.17	5.14	1.33	7.25	16.65	28.12	55.23
2002-2003	6.13	-1.70	6.36	8.37	15.42	28.18	56.40

Source: Economic Survey of Maharashtra, various issues

**TABLE A2
Regional Variation in District Domestic Product**

	Relative Contribution to Per Capita Gross District Domestic Product (93-94 prices)		C.V across 5 admin. divisions	Relative Rank of Maharashtra among 14 states based on Per capita GSDP (93-94 prices)	
	Mumbai	Mumbai+ Nasik+ Pune		Maharashtra including Mumbai	Maharashtra Excluding Mumbai
1993-94	36.51	74.77	50.78	2	3
1994-95	36.13	75.82	50.70	2	4
1995-96	36.46	76.70	51.80	1	4
1996-97	36.06	78.19	49.04	2	4
1997-98	38.82	78.23	56.25	2	4
1998-99	37.50	76.94	53.15	2	4
1999-2000	37.92	78.16	51.00	1	4
2000-2001	37.79	78.20	51.10	2	5
2001-2002	37.70	78.18	50.66	2	5

Source: District Domestic Product Series, GoM

TABLE A3
Population (Division-Wise)

(in lakhs)

	<i>1971</i>	<i>1981</i>	<i>1991</i>	<i>2001</i>
Konkan	116	152	194	248
Pune	107	131	164	200
Nashik	84	104	129	158
Aurangabad	81	97	128	156
Nagpur	52	74	90	107
Amravati	65	69	84	99
MEAN	84.17	104.5	131.5	161.33
COFF. OF VAR.	28.84	30.88	32.19	34.94

TABLE A4

Contribution of Net Migration to Population Growth in Maharashtra

(%)

	Annual Net migration rate	Net Migration as per cent of population growth	Estimated Net Migrants per year (million)
1981-1991	0.23	10.0	0.16
1991-2001	0.39	19.1	0.34

Source: Maharashtra Human Development Report, 2002.
Based on the difference between crude birth and death rates from Sample Registration System data

TABLE A5
Slum Population (2001 Census)

<i>STATE</i>	<i>% OF SLUM POPULATION</i>	<i>RANK</i>
Kerala	1.81	1
Bihar	10.53	2
Karnataka	11.50	3
Gujarat	11.79	4
Rajasthan	16.18	5
Tamil Nadu	17.85	6
Punjab	20.38	7
Uttar Pradesh	22.12	8
Orissa	22.54	9
Madhya Pradesh	24.31	10
West Bengal	26.82	11
Maharashtra	31.66	12
Andhra Pradesh	32.69	13
Haryana	33.07	14
INDIA	22.59	

Source: Census 2001

TABLE A6
Incidence of Poverty in Maharashtra

	1973-74	1993-94	1999-00
Rural	57.71	37.93	23.72
Urban	43.87	35.15	26.81
Total	53.24	36.86	25.02
Source: Economic survey of Maharashtra 2002-03			

TABLE A7
Availability of Medical Care Facilities

	<i>No. Per 1,00,000 population</i>		
	TOTAL	RURAL	URBAN
Allopathic hosp (1995)	5.9	1.0	13.2
Allopathic Dispensaries (1995)	9.9	2.6	21.3
Beds(1995)	153.9	44.7	324.7
Doctors-allopathic (2000)	72.5	23.7	139.8
Nurses (2000)	140.5	65.4	244.3
Source: Maharashtra Human Development Report, 2002			

TABLE A8
Relative Rank of Maharashtra

	Ranks*		
	93/94-95/96	96/97-02/03	00/01-02/03
	Period I	Period II	Period III
Gross Fiscal Deficit / GSDP	3	3	4
Revenue Deficit / GFD	4	6	12
Revenue Expenditure / Rev. Receipts	3	6	7
Capital Disbursements / Total Exp.	3	10	14
Own tax / Rev. Exp.	1	2	3
Grants / Rev. Rec.	13	15	15
*Note: Rows 1, 2 and 3 smallest ratio has been given a rank of 1. In Rows 4, 5 and 6, the largest ratio has been given a rank of 1			

TABLE A9
Measures of Fiscal Imbalance

(%)

	<i>Gross Fiscal Deficit as % of GSDP</i>	<i>Gross Fiscal Gap as % of GSDP</i>	<i>Primary Deficit as % of GSDP</i>	<i>Revenue Deficit as % of Gross Fiscal Deficit</i>	<i>Capital Deficit as % of GSDP</i>
1993 - 94	2.00	2.64	0.67	5.38	-0.06
1994 - 95	2.20	3.80	0.85	-9.69	-0.25
1995 - 96	2.63	3.05	1.33	14.67	-0.51
1996 - 97	2.76	3.21	1.40	32.11	-0.80
1997 - 98	3.32	3.79	1.82	40.05	-1.45
1998 - 99	3.49	4.01	1.77	52.61	-2.19
1999 - 00	4.81	5.34	2.81	36.47	-1.02
2000 - 01	3.76	5.29	1.57	87.28	-3.39
2001 - 02	4.12	4.68	1.69	75.14	-2.76
2002 - 03	4.80	5.41	2.41	65.58	-3.35
2003-04 (RE)	5.91	7.72	3.39	46.40	-2.18
2004-05 (BE)					
	4.06	4.92	1.28	66.07	-2.51
<i>Note: Gross Fiscal Gap (GFG) is a measure based on Karnik (2001). It does not exclude discharge of internal debt and repayment of loans to the center since both these involve a commitment of resources for the states and factoring them out would wrongly suggest a reduced requirement of resources.</i>					

TABLE A10
Expenditures on Revenue Account and its Components

	<i>Revenue exp. as % of Total Exp.</i>	<i>Devt. Exp on rev. acct. as % of revenue exp</i>	<i>Social services on revenue account as % of revenue expenditure</i>	<i>Economic services on revenue account as % of revenue expenditure</i>	<i>Non-dev. Exp on revenue account as % of revenue expenditure</i>
1993 - 94	82.02	61.79	34.76	27.03	37.87
1994 - 95	73.96	60.37	35.29	25.08	39.33
1995 - 96	80.31	60.71	37.86	22.85	39.02
1996 - 97	83.37	61.86	35.49	26.37	37.72
1997 - 98	82.73	59.46	37.54	21.92	39.91
1998 - 99	84.65	57.96	36.74	21.22	41.36
1999 - 00	77.24	55.65	37.85	17.80	42.45
2000 - 01	88.61	58.84	38.37	20.47	39.31
2001 - 02	90.12	52.28	36.93	15.35	46.32
2002 - 03	85.72	53.99	35.13	18.87	44.34
2003 - 04 (RE)	73.79	52.43	36.37	16.06	45.20
2004-05 (BE)					
	86.05	46.43	32.66	13.77	52.26
<i>Source: Financial Statements, GoM and Budget in Brief, GoM, various issues</i>					

TABLE A11
Select Expenditure Categories on Revenue Account
(As % of Revenue Receipts)

	<i>Interest Payments</i>	<i>Salaries</i>	<i>Salary+pension & retirement benefits + interest payments</i>
1993 - 94	11.63	43.35	58.31
1994 - 95	11.66	40.82	55.73
1995 - 96	12.41	42.63	58.69
1996 - 97	12.71	41.08	57.89
1997 - 98	14.29	43.51	62.33
1998 - 99	16.90	46.14	67.43
1999 - 00	19.33	65.81	91.43
2000 - 01	17.67	45.49	70.34
2001 - 02	21.36	50.77	80.74
2002 - 03	22.92	49.88	80.93
2003 - 04 (RE)	22.35	44.45	74.29
2004-05(BE)			
	25.00	38.10	69.86

TABLE A12
Capital Expenditure

	<i>Capital expenditure as % of total expenditure</i>	<i>cap. Exp. On soc. Serv as % of capital exp..</i>	<i>repayment of int. debt & of loans & adv to Centre) as % of capital exp</i>
1993 - 94	17.98	3.37	19.28
1994 - 95	26.04	1.98	9.72
1995 - 96	19.69	3.02	12.84
1996 - 97	16.63	2.92	15.18
1997 - 98	17.27	2.88	16.19
1998 - 99	15.35	5.98	19.82
1999 - 00	22.76	2.08	12.54
2000 - 01	11.39	2.51	23.22
2001 - 02	9.88	3.17	29.27
2002 - 03	14.28	2.36	20.68
2003 - 04 (RE)	26.21	2.17	33.13
2004-05(BE)			
	13.95	2.65	33.19

TABLE A13
Composition of Revenue Receipts
(as % of revenue receipts)

	<i>Tax Revenue</i>	<i>Own Tax revenue</i>	<i>Own Non-tax revenue</i>	<i>Grants</i>
1993 - 94	71.13	59.26	18.35	10.52
1994 - 95	74.05	62.66	19.24	6.71
1995 - 96	76.16	66.03	16.76	7.08
1996 - 97	72.66	60.84	19.50	7.84
1997 - 98	76.05	67.53	17.92	6.03
1998 - 99	78.78	65.34	16.44	4.79
1999 - 00	78.65	68.32	15.58	5.77
2000 - 01	76.13	66.71	18.93	4.95
2001 - 02	78.94	70.74	15.47	5.59
2002 - 03	87.88	73.35	14.52	7.28
2003 - 04 (RE)	78.34	70.17	10.16	8.17
2004-05 (BE)				
	79.48	70.46	11.74	9.02
<i>Source: Computed from Financial Statements, GoM and Budget in Brief, GoM, various issues</i>				

TABLE A14
Buoyancies of Major State Taxes

	<i>1993/94 to 2003/04 (RE)</i>
Tax Revenue	1.107
State's own Tax Revenue	1.138
Sales Tax	1.081
Stamps & Registration fees	1.381
State excise duties	0.933
Electricity duties.	1.435
Taxes on vehicles	1.311
Taxes on goods & passengers	0.320
Land Revenue	1.362
<i>Source: Computed from Financial Statements, GoM and Budget in Brief, GoM, various issues</i>	

TABLE A15
Debt Profile of Maharashtra

(%)

	Dept as % to GSDP	Share of Loans & Advance from Central Government to total debt	Share of Internal debt of the State Government to total debt	Share of Provident Fund, Small Savings etc.
<i>1993-94</i>	13.55	88.16	11.84	11.61
<i>1994-95</i>	13.44	86.12	13.88	11.67
<i>1995-96</i>	12.66	84.52	15.48	11.67
<i>1996-97</i>	13.21	83.84	16.16	11.56
<i>1997-98</i>	14.48	83.72	16.28	10.96
<i>1998-99</i>	15.99	84.00	16.00	10.86
<i>1999 - 00</i>	17.55	83.54	16.46	13.60
<i>2000 - 01</i>	21.07	83.02	16.98	12.94
<i>2001 - 02</i>	22.61	81.19	18.81	11.93
<i>2002 - 03</i>	23.17	68.27	31.73	10.44
<i>2003 - 04 (RE)</i>	25.23	50.91	49.09	10.88
<i>2004-05 (BE)</i>				
	25.66	44.88	55.12	10.51

TABLE A16
Extra Budgetary Operations
(Rs. Crores)

	Stock of Off budget borrowings	Sum of guarantees outstanding
1993 - 94	0	-
1994 - 95	0	-
1995 - 96	0	-
1996 - 97	975	7636**
1997 - 98	1621	9933
1998 - 99	4146	19729
1999 - 00	6494	32146
2000 - 01	9534	45979
2001 - 02	12664	52922
2002 - 03	13833	n.a
2003 - 04 (RE)	14181	n.a.
<i>Source:</i>		
<i>Off budget borrowings:</i> World Bank (2002). Data from 2001-02 onwards have been obtained from Finance Dept. of GoM, hence figures may not be strictly comparable.		
<i>Guarantees:</i> CAG report 2001-02		
http://www.cagindia.org/states/maharashtra/civil/index.htm		
as viewed on June 13 th 2004.		
** sum of guarantee outstanding up to 1996-97		

TABLE A17
Budgetary Allocations for Power Sector

	Power subsidy (Rs. Crs.)	capital outlay & net lending (Rs. Crs.)	Budgetary Support to power sector (Rs. Crs.)
	(1)	(2)	(3) = 1 + 2
1993 - 94	0	450	450
1994 - 95	0	730	730
1995 - 96	0	350	350
1996 - 97	0	760	760
1997 - 98	0	690	690
1998 - 99	0	510	510
1999 - 00	0	450	450
2000 - 01	2371	220	2591
2001 - 02	629	719	1348
2002 - 03	712	439	1151
2003 - 04(RE)	835	287	1122
2004-05 (BE)			
	713	161	874

TABLE A 18
Sales and Revenue Receipts of MSEB for the year 2001-02

	Sales		Revenue	
	Mn. Kwh.	% of total	Rs. Mn.	% of total
Domestic	9771	20.76	2423.4	19.07
Commercial	2023	4.30	923.28	7.27
Agri/Irrign	11911	25.31	980.04	7.71
Industry	17927	38.09	6864.68	54.02
Railways	1110	2.36	466.12	3.67
Other States	700	1.49	182	1.43
Others	3621	7.69	868.56	6.83
Total	47063		12708.08	
<i>Source: Annual Report (2001-02) on The Working of SEB's & Electricity Departments</i>				

Annexure B

Data Adjustments

1. Capital Receipts

Maharashtra Budget document gives capital receipts inclusive of Ways and Means Advances and Cash Balance Investment.

RBI classification = Cap. Receipts of Maharashtra Govt. - [ways & means + cash balance investment (net)].

(We conform to RBI def.)

2. Capital Expenditure.

Maharashtra Budget document gives capital receipts inclusive of Ways and Means Advances RBI classification = Capital Expend of GoM. - ways & means advances

(We conform to RBI def.)

3. Development Expenditure (on revenue account)

RBI classification = Social Services + Economic services

GoM budget Social Services + Economic services + compensation to local bodies

(We conform to RBI def.)

4. Non-development Exp (on revenue account)

RBI classification = Exp. on general services.

GoM budget defines non-devt. revenue expenditure as expenditure on general services + expenditure on debt services

(We conform to RBI def.)

5. Development Expenditure (on capital account)

RBI classification = Expenditure on Economic services + Social Services

Maharashtra Budget = Expenditure on Economic services + Social Services + loans by state governments

6. Non-Development Expenditure (on capital account)

RBI classification = expenditure on general services

Maharashtra Budget = Discharge of internal debt + repayment of loans to the Centre (including Ways and Means Advances)

In our study we do not analyse capital expenditures in terms of development / non-development. Instead we look at specific expenditure categories.

7. Gross Fiscal Deficit

Gross Fiscal Deficit = Budgetary Deficit + Borrowings and Lendings (While the definition remains the same the nos. in our study are based on RBI definition, hence the figures differ from budget documents of GoM)

(Specifically we deducted ways and means advances from capital expenditure and ways and means advance and net cash balance investment (CBI) from capital receipts)

8. Primary Deficit

The Budget in Brief of GoM for 2004-05 has defined

Primary Deficit = GFD - (interest payments and appropriation for debt servicing).

We have conformed to previous def. Of Primary Deficit = GFD- Interest Payments

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