Chapter-II
SOURCES OF FINANCING THE FIVE-YEAR PLANS

2.1 Brief Review of Theoretical Framework / Background
Importance of Management of Financial Resources

The basic objective of economic planning is to carry out an adoption of the production to social needs and thereby to have a rapid and accelerated economic development of the country. A planned economy is not an end in itself. Its usefulness lies in mitigating the evils of the free enterprise system and spreading the activities to non-traditional forms as quickly as possible. The concept of planning includes the two main constituents which are i) a system of ends to be pursued ii) knowledge regarding the available resources and their optimum allocation. India suffers from resource constraints and therefore, it has to use the resources judiciously and therefore the very basis or pivot of economic planning is the management of financial resources and this particular aspect of economic activity is very important because it includes resource growth, resource appraisal and resource mobilization which determines the very process of capital formation that consists of investing current resources to add to the economy's stock of physical assets, which largely make possible the growth of income and productivity. The fund for investment is the financial resources, investment determines the growth of this fund and the Indian Plans lays down investment targets for both the public and the private sectors. In the case of private sector, the major
responsibility for resource mobilization lies with the private production units which raise either equity capital or obtain loans from banks and other financial institutions the role of the state in this case is subsidiary as it merely facilitates mobilization of savings for investment in the private sector. The funds for public sector outlay are obtained by the Government from both the domestic and external sources. Taxation, market borrowings and surpluses from public enterprises are the major sources of finance from domestic sources. If all the sources are unable to fulfill the investment requirement in the public sector, then India seeks external assistance for its development plan and as a last resort it takes recourse to deficit financing. Since India suffers from resource constraints it has to use the resources judiciously and therefore finance is not only one of the important instrument for resource mobilization but it is also essential for the purpose of removing the maladjustment between supplies and demands of goods and services in order to avoid problems like inflation and balance of payment difficulties. If sufficient funds are not available, the achievement of physical targets becomes impossible because the most difficult part of planning in India or for that matter in any country of the world lies in the management of financial resources. The targets specified in the plan should be in accordance with the resources, if targets specified in the plan are higher, larger resources will be needed to achieve them because if the financial resources
are not adequate simply laying down targets will be unrealizable on account of shortage of fund. Therefore the management of financial resources has been given an important place in India’s Five Year Plans.

2.2 General Constraints in the raising of adequate resources from expected sources

The Indian Planning Commission makes every effort to ensure that the plans are a consistent in financial terms. Yet the Government has failed to raise adequate resources for the plans from the expected sources, which can be attributed partly to the fact that there was errors in estimating the availability of funds from different source and partly on account of uncertainties caused by instability which is inherent due to economic, social and political factors which acts as a constraints in the way of raising of adequate resources from expected source firstly the public sector enterprises as a source of financing and the constraints associated with it is discussed. Public sector unit as a source of financing has its own importance because in a developing economy like India, for ensuring the rapid growth of economy some industries will have to be brought under Governments control, however the contribution from public enterprises has always been less than what has been anticipated. Most of the Central Government enterprises has been running on losses and contribution of such departmental undertakings as the
Railways and Posts and Telegraph have always been minimal because in many situations political factors influence decision about location of projects. The ministers in their own vested interests, make promises about the future location of projects without keeping in mind the results of feasibility of state-about costs consequently leading to a considerable wastage of capital resources. Not only this the costs of project was also raised upwards which can be attributed to poor and inadequate project planning. There is also a policy of deliberate under pricing which has two adverse effects “Firstly, a policy of under-pricing may result in distortion of choice of technique by the user industries. Thus for example under-priced steel can result in excessive and sub-optimal use of it as against other materials whichever choice is available, secondly even where no such choice is available the fact that, in many cases there is no de-jure regulation of the prices of the end products of the user industries implies that the profits foregone by the public sector enterprises wind up with the users who eventually find to be in the private sector”. The effect of under pricing of public sector enterprises is thus substantially to redistribute revenue in favour of the private sector which in turn, comprises of the effort of the Government at raising real savings in so far as it leads to additional consumption in the private sector. According to Bimal Jalan “The most conspicuous failure of public sector enterprises has been in the financial area. An important
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shortcoming has been relatively low level of capacity utilization in many enterprises. This has increased the capital - output ratio and reduced efficiency in the use of capital. The poor financial performance of several enterprises is traceable to a large extent to poor investment decision. These are reflected in factors such as inappropriate technology, an irrational product mix and imposed marketing management. Moreover large scale employment generation by public enterprises has over the years led to a situation where some of the enterprises are saddled with over employment or excess manpower resulting in low level of manpower productivity." 

External Assistance is a capital inflow or assistance to a country, which is not the resultant of natural market force Foreign aid serves the purpose of supplementing domestic saving, so that in the early stages of economic development there would be availability of additional resources apart from what is available internally through budgetary sources or deficit financing. However the first constraints is in the of magnitude and character of foreign aid which is likely to become available over a period of time "The most important factor which limits the absorptive capacity is the country's capacity to repay in future the loans currently contracted. Till, the country reaches the stages of self sustaining growth its needs for larger volume of imports will ever grow. The problem becomes more serious in view of the fact that the country has not built large exportable potential
so the burden of repayment becomes more acute". At the moment the problem has assumed such severe proportion that a substantial part of the gross foreign aid is being utilized for meeting these obligations.

Taxation – Is the most important instrument in curbing the increased demand for consumer goods generated by the development process. Although the Government has been relying heavily on this source but still they have not been able to live upto their expectation and if today the government feels that its resources are inadequate. It is due to the following weakness with the tax structure which acts as constraint.

Inadequate Tax Revenue - The demerit is that tax revenue has all along being a small figure despite the fact that this has been a rising trend.

Lopsided and Regressive - Since the tax structure have rather relied too heavily on indirect tax, it is lopsided and this tendency has increased over a period of time, with the share of direct tax declining and that of indirect tax rising. moreover there is administrative inefficiency. Both direct as well as indirect tax are highly complicated and there are enough loopholes for the unscrupulous elements to avoid as well as to evade tax. Another inherent weakness in direct taxes have been its unequal treatment meted out to different people with more benefits for people with higher income and wealth for e.g. income from certain specific
investments like those in Unit Trust of India were exempted up to a certain amount. Moreover there are grave intersectoral imbalances in India’s tax structure as agricultural incomes are almost tax free. Prior to independence, there were not many people engaged in agriculture whose income could be made liable to pay income tax and agriculture being out of bound of taxes offers plenty of scope for camouflaging black money and evading tax. Moreover services sector has been untaxed which leads to distortion. According to Economic Survey (2001-02) "First as the share of industry in GDP decreases while that of service expands the tax base shrinks, aggregate buoyancy of excise revenue declines and the excise tax\GDP ratio fall. Second, failure to tax services distorts consumer choices, encouraging spending on service at the expense of goods and savings".

Deficit Financing – Is considered to be the most useful method of promoting economic development in a developing country because, the nature of developing countries is such that sufficient private investment is not forthcoming due to the various social, economic and institutional factors. However there are certain constraints in the raising of adequate resource. Dr. V.K.R.V. Rao, “attributes four reasons as to why the danger of the initial rise in prices taking on the character of inflation is greatest in the case of deficit financing by government.
i) Expansion of currency brings with it the possibility of a greater expansion of money supply through the expansion of credit

ii) Absence of direct return i.e. absence of supplies of goods and services resulting from the outlay and saleable by the government to the public, lessens the possibility of mopping up the additional incomes created by additional outlay.

iii) Absence of saleable securities against which the government outlay is undertaken lessens the chances of mopping of additional income created by the additional outlay.

iv) Great possibility of waste and failure to promote greater productivity associated with government investment in the absence of an exceptionally competent and honest standard of public administration leads to a failure of output to rise and compensate the additional purchasing power created by the additional outlay. Because of these reasons deficit financing by government has always been looked upon as containing inflationary possibilities even when it is undertaken for development.⁵

2.3 Relative Merits and Demerits of Each Source

The source of financing available to the government may broadly be divided into two categories
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(i) Internal
(ii) External

The internal sources include taxation, public or market borrowings including small savings, surplus of public enterprises and deficit financing. The external sources comprises of foreign aids from governments and the international institutions and commercial loans raised in the world market at prevailing rates of interest. The relative merit and demerit of each one of these sources is analyzed below.

Taxation in India provides the main base for current revenue balance and is invariably relied upon for additional resource mobilization because of many reasons. Firstly it is an effective method of organizing savings out of the incremental incomes. In a developing country like India with low per capita income little can be achieved by way of savings from the existing incomes. The way out is to plough the maximum proportion of additional income for development. “Taxation is an effective instrument to take away a part of additional income before it is distributed. It is for this reason that plans have been providing much under this head. Two it can reach the maximum number of people and make them pay for development. This can be achieved through a judicious combination of various taxes, Direct taxes, for instance can be so arranged that while the rich pay more the not-so poor also pay, though less. Similarly,
through Indirect taxes a large many, including even those who do not pay direct taxes, can be reached for their contribution to development. The rich can of course be asked to part with more through heavy taxes on the luxury goods". As compared to deficit financing which if used, in excess results in raising the prices taxation does not do so unduly if properly designed. The importance of taxation is that the state enforces an act of savings, whereas the act of investment can be public, private or as a mixed institutional arrangement. Secondly it is also the most important instrument for ensuring social justice both in equitably distributing the burden of development as also in reducing the inequalities of income. Compared to other sources such as borrowing and deficit financing it is preferable because with borrowings it involves no interest burden and unlike deficit financing it does not result in rise in prices. However most of the people in this country are too poor and hence they fall outside the ambit of direct taxes they can no doubt be taxed by the levy of indirect taxes on commodities of mass consumption but apart from other things it results in raising prices. and meets with public opposition which is not the case for public borrowings. Moreover taxation implies forced saving, borrowing is voluntary the tax payer is never happy in paying a tax, for he does not expect to get his money back. A lender on the other hand gives his money on loan of his own record to receive it back along with the interest after a stipulated period unlike taxation borrowing
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does not adversely affect incentives to save and invest. The lure of interest is always there to increase the incentives instead. As the Economic Bulletin for Asia and the Far East states "Taxation therefore remains as the only effective financial instrument for reducing private consumption and investment, and transferring resources to the government for economic development".?

Small Savings: -

Generally the principal agency through which the masses can be reached for the mobilization of resources is through that of small savings, which it does by tapping the genuine savings of the people and also by providing capital to the government without aggravating inflationary situation in the economy. Moreover it has a psychological appeal in providing an opportunity for the ordinary people to participate in the national effort for development. By tapping the genuine savings of the people, encouraging thrift on the part of the people, restricting their consumption and thereby helping in arresting price rise. While mobilization of public savings for development purpose is really useful and in certain respect better than taxation but it has one serious disadvantage as compared to taxation, the government has to pay interest and return the principal also at a future date. These burden have to borne by the future generation in the form of higher taxation. This is described by economists as internal debt trap. However
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the basic advantage is that it voluntary and does not meet with public opposition as in the case of taxation.

The advantage of saving as a source of capital formation, when compared with other forms of resource mobilization is that firstly it is non-inflationary in character and is the only ultimate form of the source of capital formation secondly a developing economy will not be able to increase the supply of consumer goods at the required rate during the initial stage of its development. Therefore unless consumption is restricted, scarcities of consumer goods inflationary pressure and the associated problems are bound to arise in the initial stages of development and these problem often retard the process of development of the economy. A high rate of domestic savings avoids the emergence of such problem by restricting the consumption expenditure in the economy.

Public Loans:

It has an important place in the list of internal sources. Taxation as a method of raising resources is not adequate in particular for a big plan. Moreover taxation cannot be pushed beyond a certain limit because it is neither possible nor desirable and also because of the fact that people do not react favourably to the imposition of taxation of incomes because this reduces their incomes however, this is not the case with public loans. Secondly it has an edge over taxation because when the government borrows from
the public by issuing bonds or securities, provision is made for the payment of interest. This raises the income of the people instead of reducing it, further “public borrowing is an effective instrument for mobilizing private saving. Often private savings get invested in few special industries or sectors where prospects for private profit are great. The resulting pattern of investment may not be comparable with rapid and balanced development from the national viewpoint. This malinvestment can be corrected, if through public borrowing private savings is transferred to the government. Public borrowing, not only brings about the transfer of savings from the private to the public sector, but under certain circumstances it can even increase the pool of savings”. Since this method of financing does not involve the compulsory burden that taxation implies, the Government is tempted to use this method for wasteful expenditure. Moreover unlike taxation the repayment of maturing debt creates problem of its size which is indeed large and its timing coincides with recessionary conditions in the economy.

Contribution from Public Enterprises:

Prior to independence there was virtually no public sector in Indian economy, however in the post independence period the expansion of public sector was undertaken as an integral part of the industrial policy 1956 and with the
passage of time the public sector has come to occupy an increasingly important place in the Indian economy.

The justification for public enterprises in India was based on the fact that the rate of economic development planned by the Government was much faster than can be achieved by the private sector alone. In other words, the public sector was essential to realize the target of high rate of development deliberately fixed by the government. The public sector is an important source if used for development. The surplus of public enterprises can be invested in the same industries or can be used for the establishment and expansion of other industries. It plays an important role in bringing about optimum allocation of resources in the country so that economic development is promoted in desirable channels. The expansion of public sector has become necessary to bring under State control the essential industries. This helps the Government to make those industries free from the control of the monopolies in the private sector. In Professor Ramanadham's words “The main reason for the expansion of the public sector lies in the pattern of resources allocation decided upon under the plans”.

Explaining the importance of the public sector in a mixed economy and its role in the establishment of a Socialist pattern of society Professor V.K.R.V. Rao opined “Sectors of economic activity which involve either
monopoly conditions of strategic economic power or possession of large resources in private hands should be publicly owned and operated as public enterprises, it also means that public enterprise should make itself responsible for the building of the economic overheads on the external economies like transport, power, fuel and basic capital goods without which increase in the production of consumption goods and services either on the required scale or necessary economic basis will not be possible irrespective of whether it is to be in the private or public sector. Unfortunately the performance of these enterprises not been satisfactory. Many of the Central Government enterprises has been suffering losses and even the contributions of such departmental undertakings as the Railways and Post and Telegraph have been minimal. The State Electricity Board and the State Road Transport Corporation which are the two major state enterprises have been running on losses throughout the planning period. Further states incur annual losses of Rs.700 crores on commercial irrigation.

Deficit Financing:

It is resorted to when the government is unable to raise finances from other sources, so much so that the state government frequently succumbs to the temptation of deficit financing. Moreover it is used when the efforts to raise tax revenues remain low as a proportion of national income.
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According to the Indian Planning Commission "The term deficit financing is used to denote the direct addition to gross national expenditure through budget deficits, whether the deficits are on revenue or on capital account. The essence of such a policy lies, therefore in Government spending in excess of the revenue it receives in the shape of taxes, earning of state enterprises, loans from the public, deposits and funds and other miscellaneous sources. The Government may cover the deficit either by running down its accumulated balances or by borrowing from the banking system (mainly from the Central Bank of the Country) and thus creating money". It is used when the efforts to raise tax revenues does not yield the desired amount. This together with large-scale evasion causes revenues to remain low as a proportion of national income. Secondly borrowing programmes at the domestic level leaves much to be desired keeping in view the thinly spread incomes among the vast masses. There to yet no massive movement to mobilize resources. According to G. Patterson "With the help of deficit financing, unutilized or under utilized resources of the community can be shifted to productive channels; especially the skill formation in the economy can be augmented". Deficit financing is useful too, if adopted in small doses for, it will raise the money supply in the country and raise the demand for goods and services. In fact deficit financing does help to arise the demands for goods and services and increase production if it is kept within safe
limits. However it has an inherent danger as compared to other sources, if once deficit financing is adopted by the government it becomes cumulative with every passing year, the volume of deficit financing increases. By raising money supply, deficit financing creates imbalance between the demand and supply of consumption goods. Hence there is a great danger of inflation. Further although these economics generally have a large supply of unemployed manpower, they have shortages of critical inputs and technical skill. Hence, the limit to which increased money supply can lead to the utilization of unutilized resources is reached before time. Moreover, as the multiplier in such economies operates more with respect to money incomes than with real incomes, price rise faster price inflation may in turn, lead to cost-push inflation and wage induced inflation. Therefore much of the inflationary pressure in India in recent years is due directly to deficit financing and the government has stopped relying on this source.

External Assistance: -

The importance of external assistance in financing the plan is visualized because developing economy are unable to mobilize adequate resources internally because for creating any principle dent on poverty and unemployment it becomes necessary to go in for big development plan but because of the poverty of the people developing countries are unable to mobilize adequate resources internally to
finance such a plan because under a democratic set-up it is difficult to push up domestic savings beyond a certain level. This inadequacy of domestic savings in the initial stages can be made up through recourse to foreign capital. According to Prof. Lewis "nearly every developed state has had the assistance of foreign finance to supplement its own meagre savings during the early stages of its development". Unlike internal source it is a very uncertain source when from where, and how much external assistance would be available it is difficult to say in advance with much degree of certainty. This source also creates the problem of repayment. Moreover the lending countries may exert pressure of a political nature on the aid receiving countries. Also the debtor country will have to find resources later on to pay off interest and principal.

2.4 Plan Versus Non – Plan Expenditure – A Comparison

In the Pre-independence period the range of the government activities was influenced by classical thinking. the classical economists did not support the idea of entrusting many activities to the Government. But after attaining independence, the Government has been widening its activities in economic and social spheres and is trying to help the country in its economic growth and is participating in an ever-increasing measure in the capital formation, saving and investment and other economic activities.
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The Central Government has adopted a new classification of public expenditure from 1987-88 budget under this new classification all public expenditure is classified into

(a) Plan expenditure (b) Non-plan expenditure

2.4.1 Plan Expenditure:- The first major item of Central Government expenditure is plan expenditure.

This is to finance

a) Central Plan such as agriculture, rural development, irrigation and flood control, energy, industry and minerals, transport and communication, science and technology, environment, social sectors and others

b) Central Assistance for plans of the states and union territories.

The data given shows the plan outlay by Heads of development.
### Table A-1

Plan outlay by Heads of Development – Centre State and Union Territories

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<td>5.1</td>
<td>4.4</td>
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<td>7.4</td>
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<td>6.5</td>
<td>6.7</td>
<td>7.6</td>
<td>7.2</td>
<td>8.5</td>
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<td>2.50</td>
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<td>10.1</td>
<td>7.9</td>
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<td>6.1</td>
<td>8.63</td>
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<td>56.7</td>
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<td>100.0</td>
<td>62.49</td>
<td>15.25</td>
<td>24.40</td>
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<td>(b)</td>
<td>State plan</td>
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<td>38.3</td>
<td>41.2</td>
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<td>NA</td>
<td>2</td>
<td>0.8</td>
<td>10.80</td>
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**Sources:** Government of India, Ministry of Finance Economic Survey, various issues
The table A-1 shows that in the total plan expenditure, the highest allocation of fund was made for the energy sector. In 1991-92 the total fund allocated to this sector was 30.5 percent of the total Planned expenditure. The dominance of this sector continued to remain over the total planned expenditure during the 1990s however in 2000-01 the expenditure over this head was 21.5 percent of the total. The expenditure over this head has been constant during the study period. The sector that managed greater share in the planned expenditure of the Government over the years in social services. It confers a positive advantage on the community and the more developed these services are, happier and better off would be the people in the country. It aggregated 15.9 percent of the total planned expenditure in 1991-92. This sector registered a slow gain and absorbed 21.2 percent of the planned expenditure in 1996-97. After a gradual decline in 1997-98, once again it convinced the planners of the need for greater allocation of funds for it in 1998-99 which was 25.9 %, highest among all these years as seen in the table A-1, but in 2001-02 this sector failed to register its importance in reducing the social deprivation and got a share of only 20.7 percent in the total plan expenditure.

The two important sectors that decides the destiny of more than 60 percent of population are agriculture & allied activities and rural development. In 1991-92 only 5.2 percent of the total planned expenditure was allocated to
this sector, the share of agriculture and allied activities in the planned expenditure has declined slowly and reduced to 4.6 percent in 1997-98 as seen in table A-1 the exception being in the year of 1997-98. this declining trend of the share of agriculture and allied activities in the total planned expenditure continued and became 2.6 percent in 2001-02. Contrary to this, the Government expenditure on rural development formed an inverse U-Shape. Its share in the total planned expenditure firstly increased, then reached to its maximum and then declined. Its share was 6.9 percent in 1991-92 that reached to its maximum of 8.0 percent in 1996-97 and then declined. At the end of the fiscal year 2001-02, the share of the rural development expenditure in the total expenditure shrunk to 3.4 percent. The reason for this decline in expenditure on agriculture and rural development is the result of squeeze on capital expenditure apart from the problems created by the squeeze and capital expenditure there are some other areas of concern. Firstly, it is often alleged that the Government has generally violated the canon of the economy, which can be attributed to the fact that the public funds are recklessly squandered under plans and this in fact is the reason why in spite of targeted money spending being realized, physical targets are seldom achieved.

The statistical analysis of plan outlay of centre, state and union territories explains that on an average the highest amount of resources is allocated to energy sector followed by the social services during 1990-91 to 2001-02 the value of standard deviation and coefficient of variation show that there is consistency in the pattern of financing these sectors.

The lowest amount of resources is allocated to special area, general services, Science and technology and general economic services. However pattern of financing these sectors are comparatively more consistent than the energy sector and social services sector for the same period.

It can be seen from the table (A-2) that outlay on plan expenditure has almost been less than half of that of non plan expenditure while in the year 1990-91 it was 5% of the
GDP while from 1996-2000 it hovered around to 4%. Such a development is the result of the pressure of forces originating from policies pursued by the Government.

Table A-2

<table>
<thead>
<tr>
<th>Year</th>
<th>Plan expenditure</th>
<th>Non-Plan expenditure</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990-91</td>
<td>5.0</td>
<td>12.3</td>
</tr>
<tr>
<td>1996-97</td>
<td>3.9</td>
<td>10.0</td>
</tr>
<tr>
<td>1997-98</td>
<td>3.9</td>
<td>10.3</td>
</tr>
<tr>
<td>1998-99</td>
<td>3.6</td>
<td>10.8</td>
</tr>
<tr>
<td>1999-00</td>
<td>3.9</td>
<td>11.5</td>
</tr>
<tr>
<td>2000-01</td>
<td>3.9</td>
<td>11.3</td>
</tr>
<tr>
<td>2001-02</td>
<td>4.0</td>
<td>12.0</td>
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<tr>
<td>Average</td>
<td>4.04</td>
<td>11.17</td>
</tr>
<tr>
<td>Std. Dev.</td>
<td>0.44</td>
<td>0.85</td>
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<tr>
<td>Coeff. of Var.</td>
<td>10.89</td>
<td>7.60</td>
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</table>


Policies which inflates non plan expenditure at the cost of planned expenditure because the three major components of non-plan expenditure that is interest, payment subsidies and defense expenditure consume away an alarmingly large proportion of non-plan expenditure and as a result they have generated self feeding process of their own which has been supported by numerous economic, social and political compulsions.

The Central Government on an average made a plan expenditure of 4.04 percent of GDP during 1990-91 to 2001-02. Since the value of standard deviation is less than one, we can say that there is consistency in the plan expenditure. In comparison to plan expenditure on an average non-plan expenditure has been more. As far as the level of consistency is concerned, non plan expenditure is also consistent however it is less than plan expenditure.

2.4.2 Non-Plan Expenditure:-

Its concept can be understood by the explanation given in the expenditure budget, which are as follows "Non-
Plan expenditure is a generic term used to cover all expenditures of the government not included in the plan. It includes both developmental and non-developmental expenditure. Part of the expenditure is obligatory in nature e.g. interest payment, pensionary charges, and statutories to states part of the expenditure is an essential obligation of the state e.g. defence and internal security. Then there is a special responsibilities of the centre like external affairs, currency and mint and cooperation with other developing countries expenditure on maintaining the assets created in previous plan is also treated as non-plan expenditure similarly expenditure on continuing services and activities at level already reached in a plan period is shifted to non-plan in the next plan e.g. education and health facilities, continuing research projects and operating expenses of power station. Thus as more plan are completed, a large amount of expenditure on operation and maintenance of facilities and services created gets added to non-plan expenditure besides the interest on borrowings to finance the plan.14

The major component of non-plan expenditure are

Interest Payment: This item has grown both on account of growing debt obligation of the Government of India and rising level of interest. According to Economic Survey 2001-02. “This has been the single largest component of the non-plan revenue expenditure over the
years and is the outcome of past borrowings. The rising level of fiscal deficit coupled with the changing pattern of its financing in the favour of market borrowings has led to a higher interest burden.\textsuperscript{15} The only way to contain the growth in this item is to scale down the borrowing programmes of the Government which in turn necessitates greater resource mobilization on the one hand and the economy in expenditure on the other. Economic Survey 2001-02 mentions “interest payments entail a large claim on public resources and severely impair the Governments capacity to spend on social sectors and infrastructures”.\textsuperscript{16}

Subsidies: Holds an important position in public expenditure and it amounts to negative taxation. A subsidy by implication helps one section of the community by procuring resources from the rest of the society. Subsidies assumes significance when the market fails to bring about a change, because in a developing economy where the market system has not developed properly and where the distribution of income is extremely uneven and skewed the forces of supply and demand cannot be allowed to operate unfettered, in this background, subsidies are a powerful instrument in the armoury of the government exercising control over the functioning of the economy, however as revealed by the study on subsidies conducted by the National Institute of Public Finance and Policy (NIPFP), the indirect cost of subsidies is much greater than the direct budgeted subsidies. Now a days unfortunately, the volume
of subsidies have been accelerating with time mainly because of vested political interests – a fact which goes against the very objective for which they are being given, over – protection through subsidies has prevented the potential competitiveness of the system from being realized. Beyond a point, however the fiscal system cannot absorb such subsidies. In principle though the government decided to cut down subsidies, in practice it failed to do that. The Government has reduced the export subsidy, but is finding it difficult to cut down the fertilizers and food subsidies it is due to resistance from the big farmers lobby. As far as food subsidy is concerned it should be provided to the lower strata of the society.

Defence: Another important component of non-plan expenditure is the allocation for the defence sectors. No attempt at containing non-plan expenditure can succeed if defence is to be excluded. Containment of the growth of defence expenditure involves some security risk. There is general agreement in the fact that there is considerable scope to enhance the cost effectiveness of the defence expenditure. Defence preparedness is one aspect of the country’s existence which has to be accorded top priority at all cost and therefore the desirability part should not be taken into account. Prime Minister Dr. ManMohan Singh in his capacity as the Finance Minister in his First Budget speech stated. “It is absolutely essential to ensure that a quest for economy in expenditure does not in any way
compromise national security we must therefore, seek to limit expenditure without diluting the efficiency and effectiveness of our defence services".¹⁷
REFERENCES

9. Ramandham V.V.; The Structure of Public Enterprises in India, p.56.


