

Ethics & Values in Public Governance

ISB, Hyderabad
08th February, 2024

“The **purpose of a government** is to make it easy for people to do good and difficult to do evil.”

– *William Gladstone*

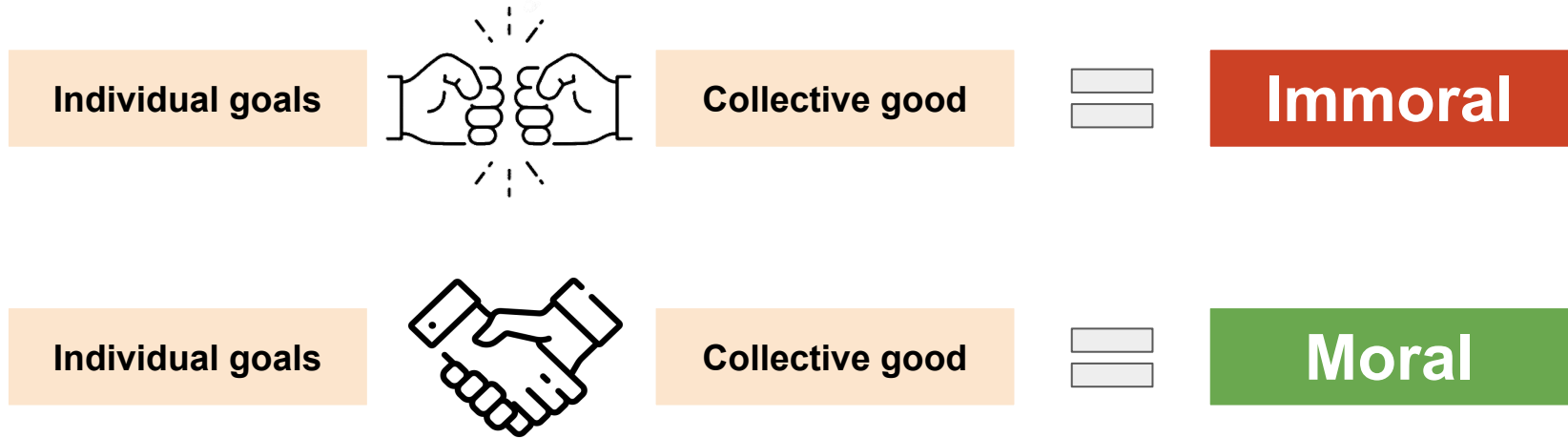
Three central questions

- Do we **lack morals and values**?
- Are we **even capable** of democratic governance?
- What is the roadblock – **values or institutions**?

What is morality?

- That which **reconciles** individual goals with public good

Central Principle of Morality



Calculus of Risk & Reward

WHEN GOOD BEHAVIOUR IS NOT REWARDED
AND **BAD BEHAVIOUR IS REWARDED**



WHEN **GOOD BEHAVIOUR IS REWARDED**
AND BAD BEHAVIOUR IS PUNISHED

Institutions that determine the calculus of risk & reward

Religion

- Most Indians are God-fearing

Society

- Strong family bonds
- Fear of social sanctions / loss of face
- Sense of Dharma beyond faith
- Acceptance of multiple faiths / belief systems
- Contentment
- Sense of community

State

- The real challenge is failings of the Indian state
- With increasing urbanisation and lives becoming more impersonal, the state assumes greater importance

Dr. Carolyn Elliott summed up the societal flaws as **absence of a sense of equality, trust and common fate.**

Equality

- Suffer from **moral neutrality to inequity by birth**
- Can be corrected by **movements within civil society, and political institutions**

Trust

- Better-off sections of society **instinctively reject the capacity of all citizens** for self-governance
- Trust that binds family, caste group must be **extended in all social interactions across diverse groups**

Sense of common fate

- Vital to bind people to create an orderly society
- Citizens should recognize that **rights and duties coexist**; one's rights are translated as duties of others, and vice versa

Regulating Human Behaviour: A Virtuous Cycle



- Changing **incentives alter behaviour** that results in **better outcomes**
- Better outcomes create an **ethical society** that further strengthens the **institutions**
- Institutions that **reward good behaviour** and **punish bad behaviour**

Institutions and Incentives Shape

Outcomes

Where institutions and incentives are in place, corruption has declined

- Railway Reservation – Technology and Transparency
- Telephone services – Competition and Choice
- Spectrum allocation – Competition and Transparency through competitive bidding
- Passport – Technology; Transparency; Predictability

Value System or Perverse Incentive?

- **Corruption** - most visible symptom of **dysfunctional governance**

Extortory Corruption

Citizens subjected to extortion for myriad services;
a cruel choice - comply with bribe and get work done or resist the demand and suffer delays and harassment

Citizens become **victims** of extortory corruption; racked by guilt and an oppressive feeling of moral compromise

Citizen's Charter with penalties for non-delivery of services; digitalisation; transparency, and empowerment of local communities

Collusive Corruption

Both bribe-taker and bribe-giver **act in collusion** and undermine public interest; example - awarding of contract, transfer of officials, recruitment in public service, interference in crime investigation

Competition is eroded, public resources swindled, **injustice** done, and monopolies are created.

Needs to be treated on a higher footing and impose **rigorous punishments**

Concerted efforts to build **institutions and practices** to ensure prompt delivery of services is needed.

- **Inefficient** state apparatus →
 - Red Tapism & **unresponsive** bureaucracy →
 - Failure of **Rule of Law** →
 - **Money & muscle-power** in elections
- Substandard **public amenities**
 - **No decent education** in government schools
 - **Poor health care**
 - **All pervasive corruption**

 - **Criminalisation** of Politics
 - Vicious **cycle of corruption**
 - Even honest public servants are **passive and helpless**

Positive power restricted — Negative power unchecked

A system of alibis — Victims of a vicious cycle

Change of players — No change in the rules of the game

***Political process ought to be the solution;
But has become the **problem** itself***

Political Crisis in India: Interlocking Vicious Cycles

Inexhaustible demand for illegitimate funds

Direct and indirect cost of political activity driven up by informal political machinery

Most expenditure incurred for vote buying

Poor service delivery and vote delinked from consequence

Rise of political fiefdoms

Entry barriers as money, caste and local clout become critical

Vote delinked from public good

Centralised polity drives voter to maximise short-term gain

Taxes delinked from services

Deeper fiscal crisis as raising taxes or de-subsidizing or reducing public sector wages is disincentivized

Political survival and honesty incompatible

Dependence on legislator support for survival makes corruption and misgovernance endemic

Social divisions are exacerbated

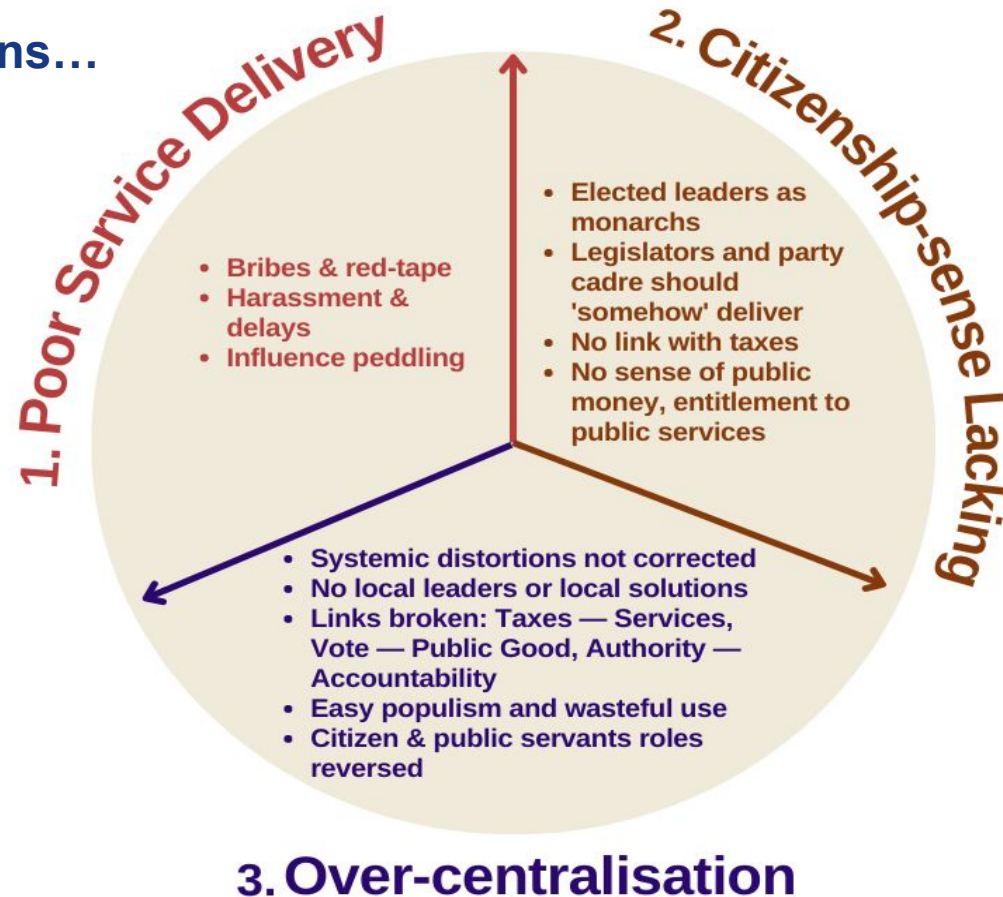
Vote bank politics – marginalisation and ghettoisation based on primordial loyalties

Competence & integrity excluded

Need for money & caste-clout excludes competent elements from public policy & governance

How did we get here?

The initial conditions...



How did we get here?

& choices made at the time of independence...

**System of Rule of
Law**

Weak instruments

**First-past-the-post
System**

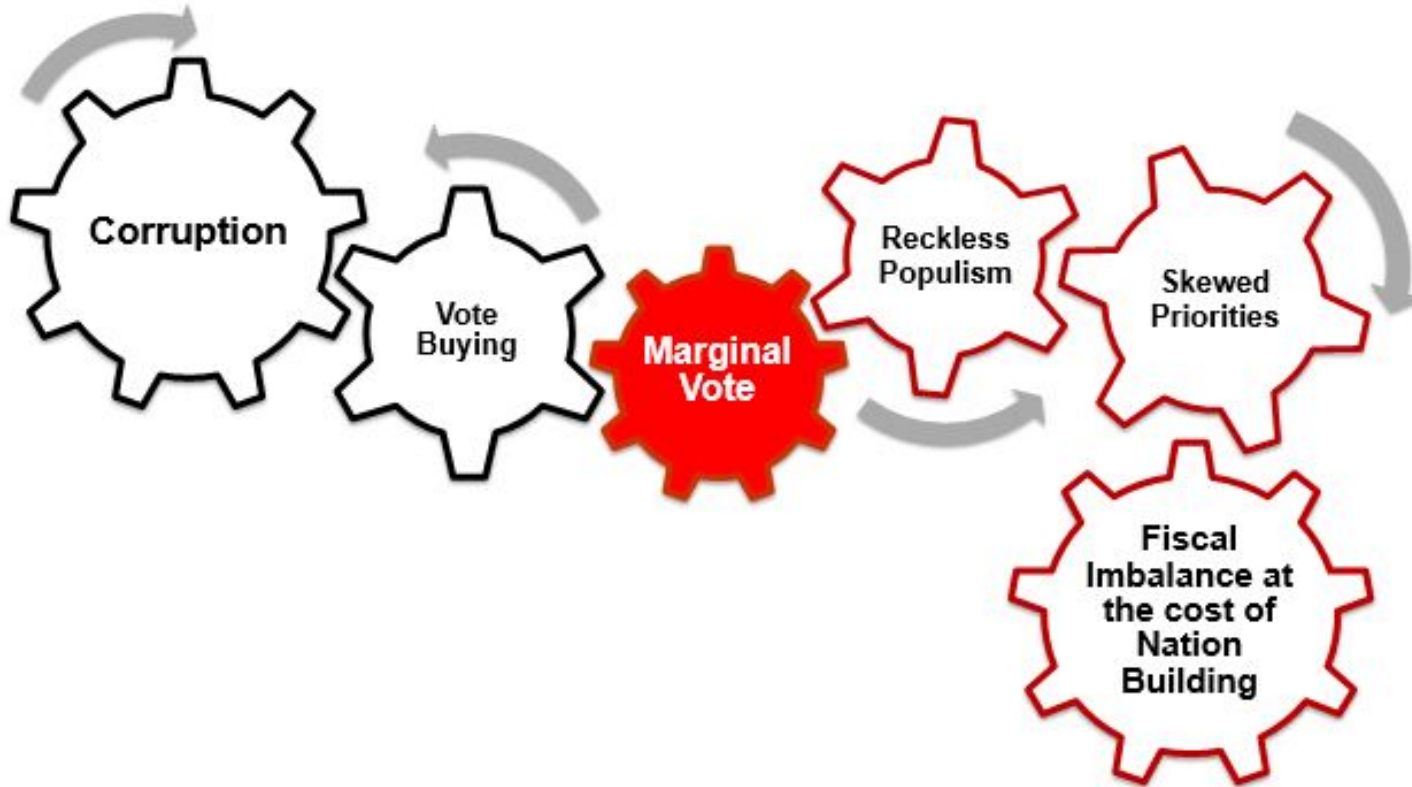
**Unsuitable for poor
societies**

**Economic
Socialism**

**Embracing state
monopoly**

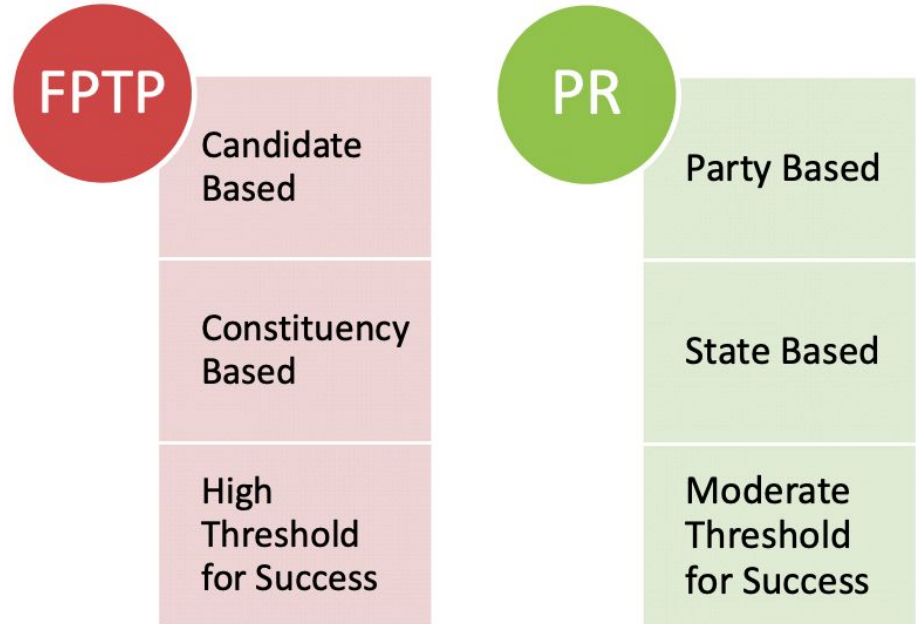
**The challenge then is to alter incentives
to alter behaviour...**

Consequences of Marginal Vote in the Current System



A Case for Proportional Representation

- There is a need for an alternative electoral system that –
 - is fair
 - is broadly acceptable
 - is easy to achieve
 - corrects most of the present distortions
 - has minimal negative impact



Altering Incentives – Proportional Representation

First-past-the-post (FPTP) system

Winner-take-all system

Leading to **divisiveness** and **political fragmentation**

Dominance of zero-sum-game issues like *reservations*

Vs.

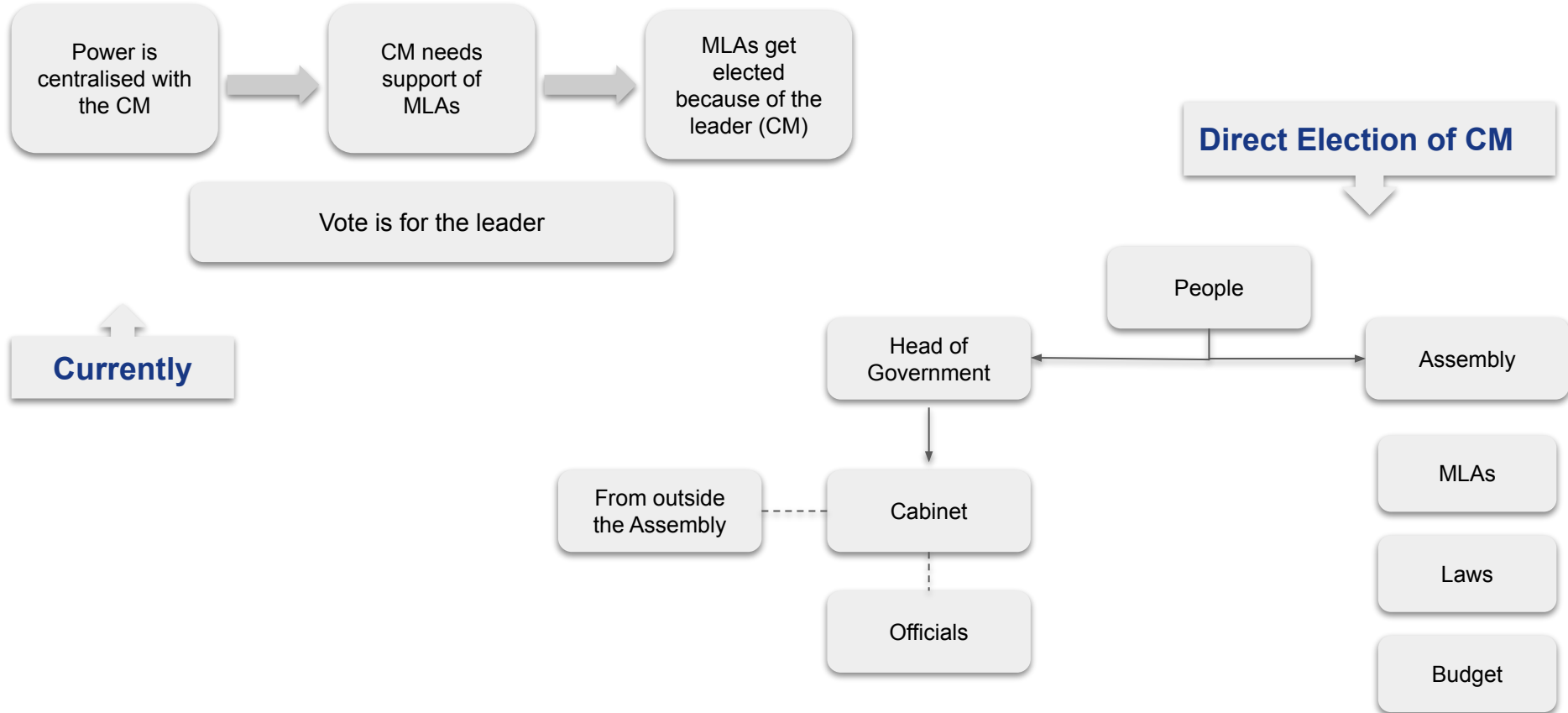
Proportional Representation

Marginal vote no longer all-important – no incentive to buy votes

Reduction in **competitive populism**
Political fiefdoms will disappear

Representation to small parties, scattered minorities and legitimate reform groups, not money power

Altering Incentives – Separation of Powers



How will Direct Election of the CM help?

From a vicious cycle to a virtuous cycle...

- **Stability of government** is assured as it is not dependent on MLAs' support
- Executive is **free from vested interests**; no scope for interference in general governance by MLAs
- Can appoint **competent ministers** from a wide pool, excluding legislators
- **Increased democratisation** as tenure of a Chief Minister can be limited to two terms
- **Local governments** can be strengthened
- **Illegitimate expenditure** during election will come down
- Appeal of the MLA office will fade.
 - MLA has **no 'disguised executive' role**; political fiefdoms become irrelevant
 - Those with merit and ambition will become **leaders in the local governments**

Core State Functions – Where does India stand?

Comparison of Various Development Indicators Among 50 Large Economies											
Rank	GDP Per Capita (PPP, 2019)	Life Expectancy (2019)	IMR (2019)	MMR (2017)	Out-of-Pocket-Expenditure on Healthcare (2018)	EYS (Expected Years of Schooling, 2019)	MYS (Mean Years of Schooling, 2020)	HDI (Human Development Index, 2020)	Power Consumption (Kwh Per capita, 2019)	Employment in Agriculture (% of total employment, 2019)	LFPR (Labor Force Participation Rate - female, 2018)
1	Switzerland	Hong Kong	Hong Kong	Hong Kong	South Africa	Australia	Germany	Norway	Norway	Singapore	Sweden
2	Ireland	Japan	Japan	Italy	France	Belgium	Canada	Ireland	Canada	Argentina	Switzerland
3	Norway	Switzerland	Finland	Norway	Netherlands	Sweden	Switzerland	Switzerland	Sweden	Hong Kong	Vietnam
4	Singapore	Spain	Norway	Poland	United States	Finland	United States	Hong Kong	UAE	Belgium	New Zealand
5	United States	Singapore	Sweden	Czech Republic	Thailand	Denmark	United Kingdom	Germany	United States	Israel	Netherlands
6	Denmark	Italy	Singapore	Finland	Ireland	New Zealand	Israel	Sweden	Finland	United Kingdom	Finland
7	Australia	South Korea	Czech Republic	Israel	Germany	Ireland	Norway	Australia	Taiwan	Germany	Denmark
8	Netherlands	Sweden	Spain	UAE	UAE	Netherlands	Finland	Netherlands	Saudi Arabia	United States	Norway
9	Sweden	Australia	Italy	Denmark	Japan	Norway	Japan	Denmark	South Korea	UAE	Canada
10	Austria	Norway	South Korea	Spain	New Zealand	Argentina	New Zealand	Finland	Australia	Canada	Germany
11	Finland	Israel	Belgium	Sweden	Denmark	Spain	Australia	Singapore	New Zealand	Sweden	Peru
12	Hong Kong	France	Austria	Austria	Sweden	United Kingdom	Czechia	United Kingdom	Singapore	Norway	Australia
13	Germany	Ireland	Ireland	Belgium	Czech Republic	Germany	Ireland	Belgium	France	Netherlands	United Kingdom
14	Belgium	Canada	Israel	Ireland	Norway	Hong Kong	Denmark	New Zealand	Switzerland	Denmark	Portugal
15	Canada	Netherlands	Australia	Japan	Saudi Arabia	Czechia	Austria	Canada	Israel	Saudi Arabia	Japan
16	Israel	Austria	Portugal	Netherlands	Canada	Turkey	Poland	United States	Austria	France	Austria
17	UAE	Finland	Germany	Switzerland	Colombia	Taiwan	Sweden	Austria	Czechia	Australia	Czech Republic
18	New Zealand	Belgium	Denmark	Australia	United Kingdom	South Korea	Netherlands	Israel	Japan	Switzerland	Singapore
19	United Kingdom	New Zealand	Netherlands	Germany	Turkey	Portugal	Hong Kong	Japan	Belgium	Czech Republic	Israel
20	Japan	United Kingdom	Switzerland	United Kingdom	Australia	Singapore	South Korea	South Korea	Netherlands	Japan	Spain
21	France	Denmark	United Kingdom	France	Austria	Chile	Russia	Spain	Russia	Austria	Russia
22	Italy	Germany	France	Portugal	Finland	Switzerland	Belgium	France	Germany	Finland	China
23	South Korea	Taiwan	Poland	Singapore	Belgium	United States	UAE	Czech Republic	Ireland	Italy	France
24	Spain	Portugal	Taiwan	New Zealand	Romania	Poland	Taiwan	Italy	Spain	Spain	United States
25	Taiwan	Chile	New Zealand	Canada	Poland	Canada	Singapore	UAE	China	Ireland	Ireland
26	Czech Republic	Czech Republic	Canada	Taiwan	Israel	Israel	France	Poland	Portugal	Taiwan	Thailand

Comparison of Various Development Indicators Among 50 Large Economies											
Rank	GDP Per Capita (PPP, 2019)	Life Expectancy (2019)	IMR (2019)	MMR (2017)	Out-of-Pocket-Expenditure on Healthcare (2018)	EYS (Expected Years of Schooling, 2019)	MYS (Mean Years of Schooling, 2020)	HDI (Human Development Index, 2020)	Power Consumption (Kwh Per capita, 2019)	Employment in Agriculture (% of total employment, 2019)	LFPR (Labor Force Participation Rate - female, 2018)
27	Portugal	United States	Russia	South Korea	Spain	Austria	Romania	Portugal	Malaysia	South Korea	Hong Kong
28	Saudi Arabia	UAE	United States	Chile	Italy	Italy	Argentina	Saudi Arabia	Denmark	South Africa	Belgium
29	Poland	Poland	Saudi Arabia	Russia	Brazil	Saudi Arabia	Chile	Chile	Hong Kong	Portugal	Poland
30	Chile	Turkey	Romania	Saudi Arabia	Argentina	France	Italy	Argentina	Italy	Russia	Brazil
31	Romania	Colombia	Chile	Turkey	Switzerland	Brazil	Malaysia	Romania	United Kingdom	New Zealand	Colombia
32	Russia	Thailand	UAE	Uruguay	Peru	Japan	Spain	Russia	Poland	Chile	South Korea
33	Malaysia	China	China	Romania	Portugal	Russia	Saudi Arabia	Turkey	Chile	Brazil	Argentina
34	China	Argentina	Malaysia	China	Singapore	Peru	South Africa	Malaysia	South Africa	Poland	Romania
35	Mexico	Peru	Thailand	Malaysia	Hong Kong	Thailand	Peru	Mexico	Turkey	Malaysia	Chile
36	Argentina	Malaysia	Argentina	Mexico	South Korea	Mexico	Philippines	Peru	Argentina	Mexico	Italy
37	Turkey	Brazil	Turkey	Egypt	Chile	Colombia	Portugal	Thailand	Romania	Colombia	Indonesia
38	Brazil	Romania	Peru	Thailand	Indonesia	UAE	Mexico	Colombia	Brazil	Turkey	Malaysia
39	Thailand	Vietnam	Colombia	Argentina	Malaysia	Romania	Colombia	Brazil	Vietnam	Egypt	South Africa
40	Peru	Mexico	Mexico	Vietnam	Taiwan	China	Viet Nam	China	Thailand	Romania	UAE
41	Colombia	Saudi Arabia	Brazil	Brazil	China	South Africa	Indonesia	Indonesia	Mexico	Philippines	Taiwan
42	South Africa	Russia	Vietnam	Colombia	Russia	Malaysia	China	Philippines	Egypt	China	Nigeria
43	Indonesia	Bangladesh	Egypt	Peru	Mexico	Indonesia	Turkey	South Africa	Peru	Peru	Philippines
44	Philippines	Egypt	Indonesia	South Africa	Vietnam	Egypt	Brazil	Egypt	Colombia	Indonesia	Mexico
45	Egypt	Indonesia	Philippines	Philippines	Philippines	Philippines	Thailand	Vietnam	Indonesia	Thailand	Bangladesh
46	Vietnam	Philippines	Bangladesh	Pakistan	Pakistan	Vietnam	Egypt	India	India	Nigeria	Turkey
47	Nigeria	India	South Africa	India	Egypt	India	Nigeria	Bangladesh	Philippines	Pakistan	Saudi Arabia
48	India	Pakistan	India	Bangladesh	India	Bangladesh	India	Pakistan	Pakistan	Vietnam	Pakistan
49	Bangladesh	South Africa	Pakistan	Indonesia	Bangladesh	Nigeria	Bangladesh	Nigeria	Bangladesh	Bangladesh	India
50	Pakistan	Nigeria	Nigeria	Nigeria	Nigeria	Pakistan	Pakistan	*Taiwan	Nigeria	India	Egypt
*Taiwan is not included in UNDP's HDI rankings											

Failure of Rule of Law

- Large pendency and inordinate delays in courts.
 - Trial courts pendency – **3.4 crore and 1.1 crore** criminal & civil cases respectively.
 - About **60%** of the cases are more than an year old.
- Criminal cases **outnumber** civil cases
- Lowest **conviction rate** – 50.4%

Avoidable Suffering & Unfulfilled Potential

- Failure in **healthcare delivery**
 - About **5.5 crore people fall into poverty every year** because of healthcare costs
 - **26% of deaths** are caused by mostly **preventable** communicable, maternal, neonatal & nutritional diseases
- School education – **abysmal learning outcomes**
 - **60% of Std. V students** cannot read a Std. II level text
 - **55% of Std. VIII** students cannot **divide**

Core Functions of the State

Rule of Law

Public Order

Justice

Basic Amenities

Infrastructure

Education

Healthcare

**Sustainable
Natural Resource
Development**

Unfinished Tasks

**Core functions still
neglected**

**Doing business in India is
still difficult**

**Local Governments are
still weak**

**Opportunity denied to
most people – education,
healthcare, rule of law**

**Minimal productivity
increase**

**Service delivery is still
poor**

**Deepening rural & agrarian
crisis**

Shifting corruption

**Growing distortions in the
political process – money
power, populism,
polarisation**

Emerging fault lines in electoral politics

- The most important faultline *emerging* in our electoral politics is **long-term growth vs individual, short-term welfare measures (ISW)**.
- In a country with large numbers of poor, **ISW has a strong political appeal**. Even in wealthy, mature democracies voters are attracted to ISW. Hence, challenge is to **balance ISW and pro-growth expenditure in a manner that the public finances remain healthy and economic growth prospects are not hindered**.
- A frontal clash between ISW and growth may be **counterproductive**.

Why growth matters?

- The difference between sustained 7% growth rate versus 8% growth rate over ten years for an economy of India's size would mean **a difference in GDP of \$600 billion or about Rs. 50,00,000 crores of GDP lost per year after 10 years.**
- Our Tax-to-GDP ratio is about 18-19%, this implies that the **Union and states lose over Rs. 9 lakh crores revenue every year**, which could have been deployed for more ISW promoting welfare, and better infrastructure to promote further higher growth and employment.
- Hence, to ensure the right **balance** between short-term welfare and long-term growth, a **minimalistic, pragmatic framework** is vital to preserve the growth momentum of the economy
- However, **fiscal profligacy** has gripped various states and the situation is **alarming!**

Telangana:

The projected additional expenditure on electoral promises, including guarantees, is approximately ₹ **1.2-1.3 lakh crore annually.**

Recurring Annual Expenditure	~ ₹ 60,000 crore
Farm Loan Waiver	~ ₹ 10,000 crore
₹ 12 lakh each to SC/ST households	~ ₹ 2.7 lakh crore over a period of five years

Constituting **60% of the projected State's revenue (FY 2023-24)**, this additional expenditure, when added to current spending, drives **overall cost to unsustainable levels.**

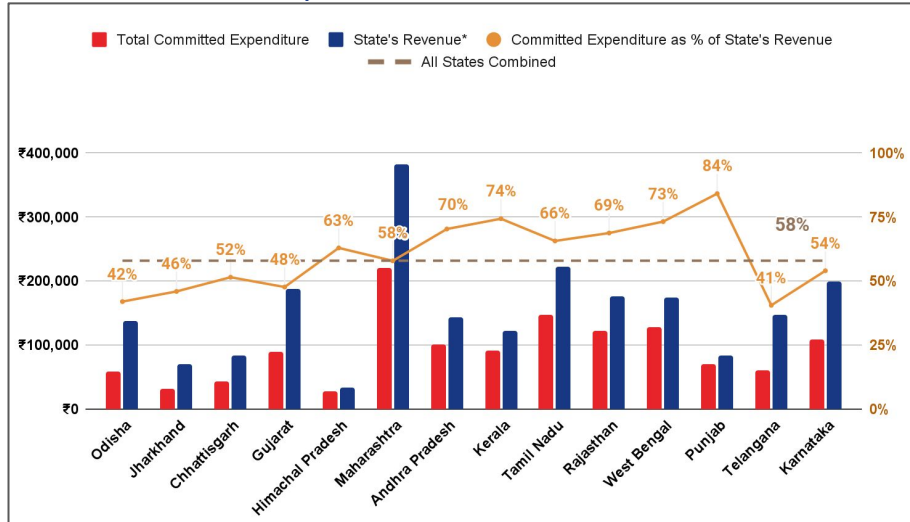
Karnataka:

The estimated annual expenditure of electoral guarantees stands at ~ ₹ **52,000 crore, of which ₹ 39,825 crore has been earmarked for the current year (July 2023 - March 2024).**

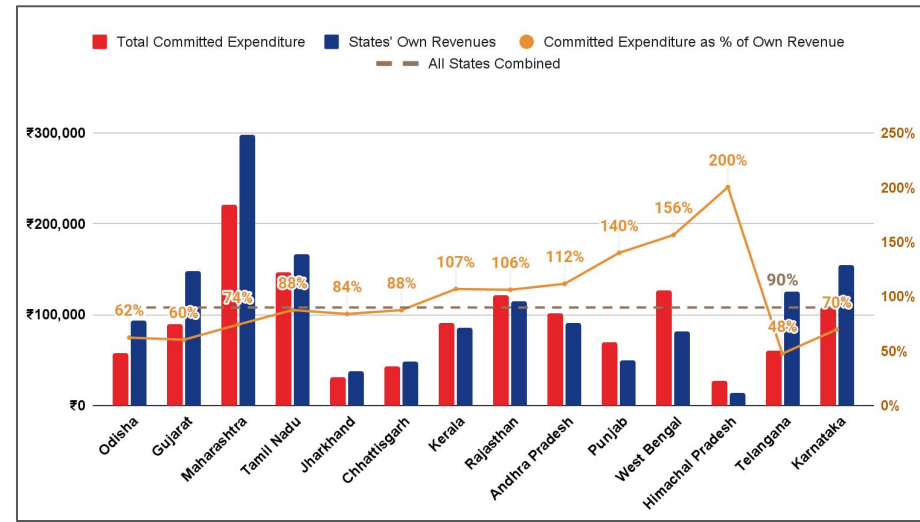
The current year's expenditure accounts for **16.7% of the projected State's revenue (FY 2023-24).**

High Committed Expenditures*

Committed Expenditure vs. States' Revenues (including Transfers) in Select States, FY 2022-23 RE



Committed Expenditure vs. States' Own Revenues in Select States, FY 2022-23 RE



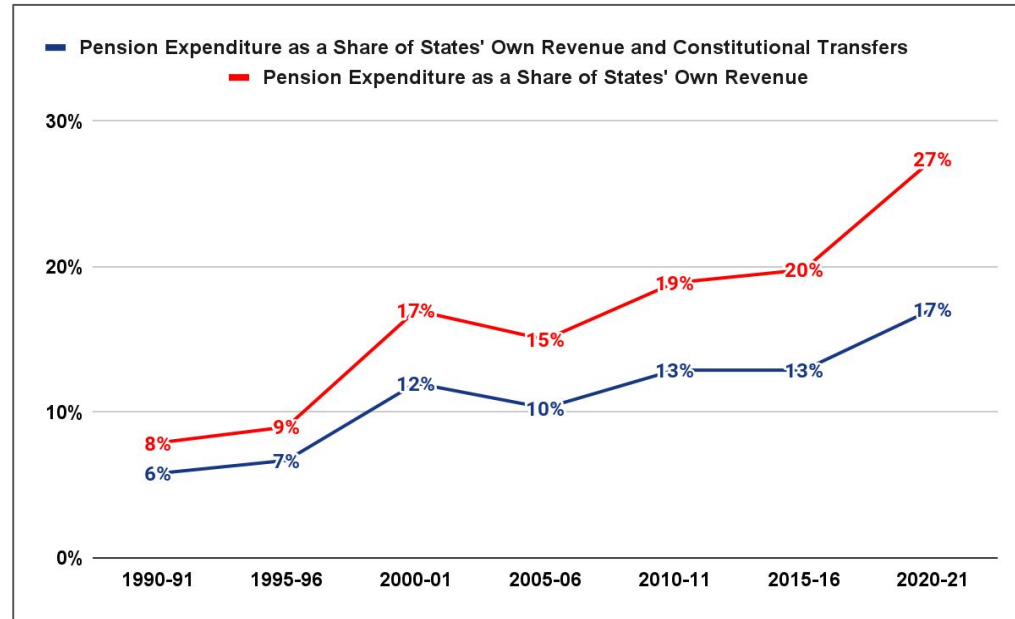
Committed expenditure accounts for **58%** of **total revenues of states including Union transfers**, and **90%** of the states' own revenue receipts, leaving little room for core governance functions

*committed expenditure includes salaries & wages, pensions and interest payments

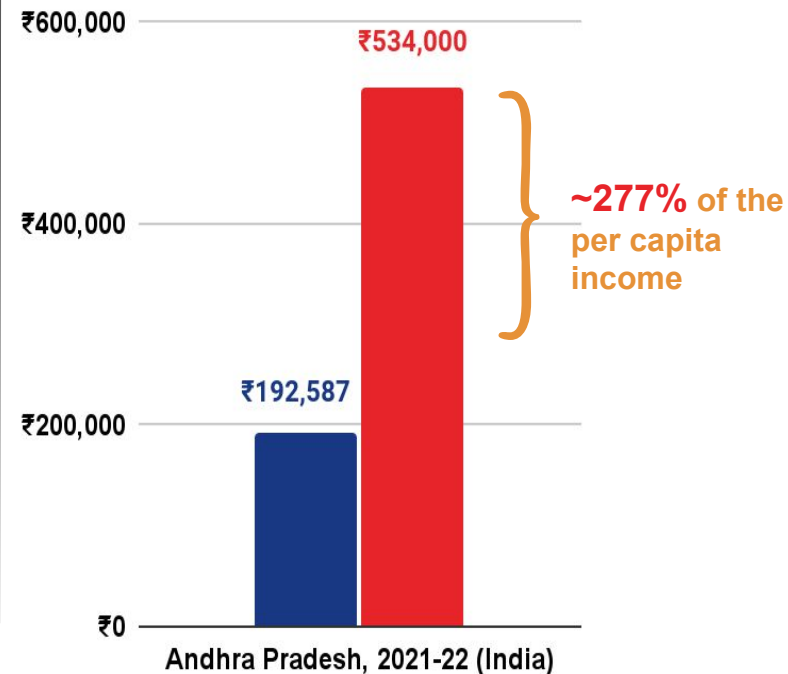
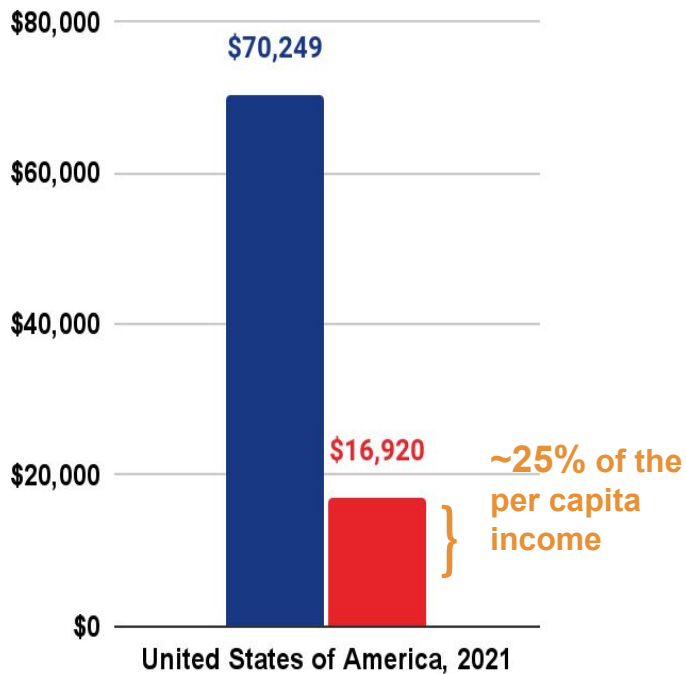
Rising Pension Burden

- The pension liability of state governments has more than **trebled in three decades from FY1991 to FY21**, which is **17% as a share of all state revenue receipts**, and **27% of own tax revenues of states (FY 2021)**.
- Currently, 18% of the Government Revenue is spent by the government, union and states combined, on pensions to its employees only, whereas the developed countries like USA spend around **~15% of its Government Revenue on Social Security** for *all workers* in the public and private sectors and it is **contributory**.

Pension Expenditure of All States as a Share of Revenues



Comparing Pension Benefit – United States (Funded) vs. India (Unfunded)

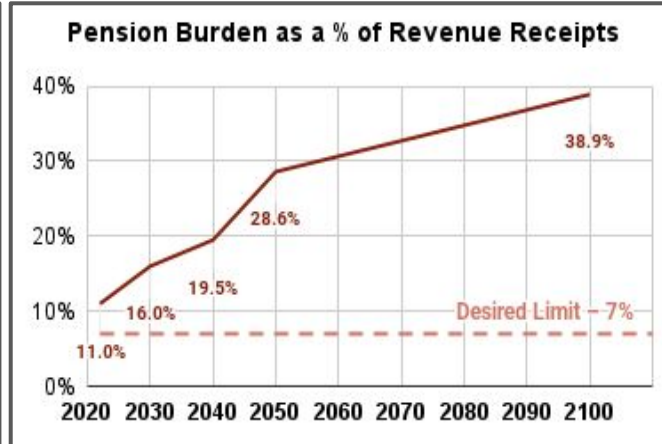
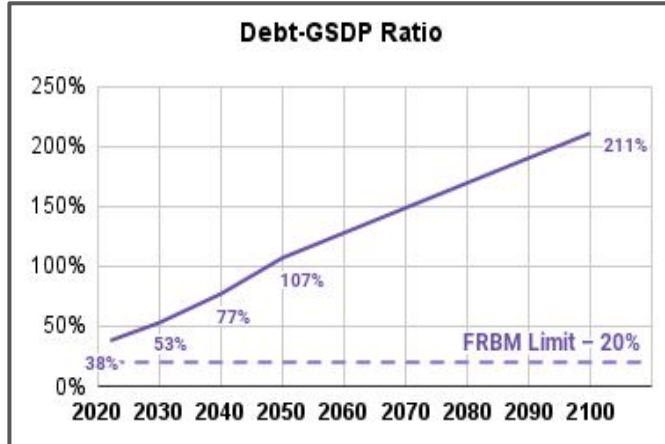
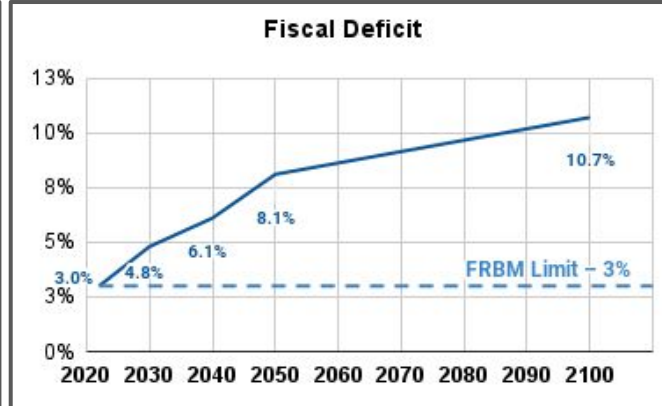
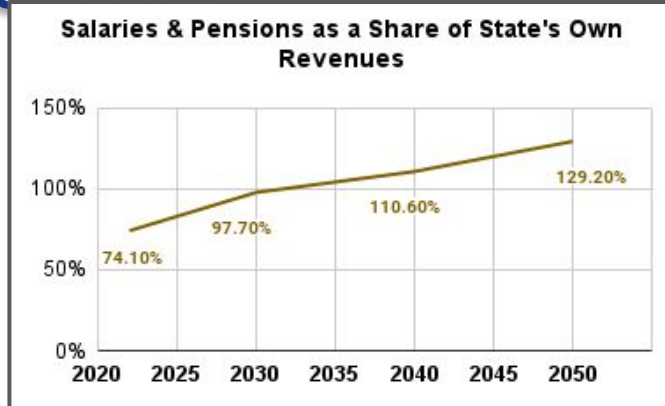


■ Annual per capita income

■ Average annual pension per beneficiary

Horrendous Price with Old Pension Scheme

Scheme



← Andhra Pradesh's projections of key fiscal indicators upon reverting to Old Pension Scheme (OPS)

Chattisgarh, Punjab, Rajasthan, Himachal Pradesh, Jharkhand have gone back to OPS. West Bengal did not join the NPS.

Rising Debt Burden of States

Debt Burden of Select States

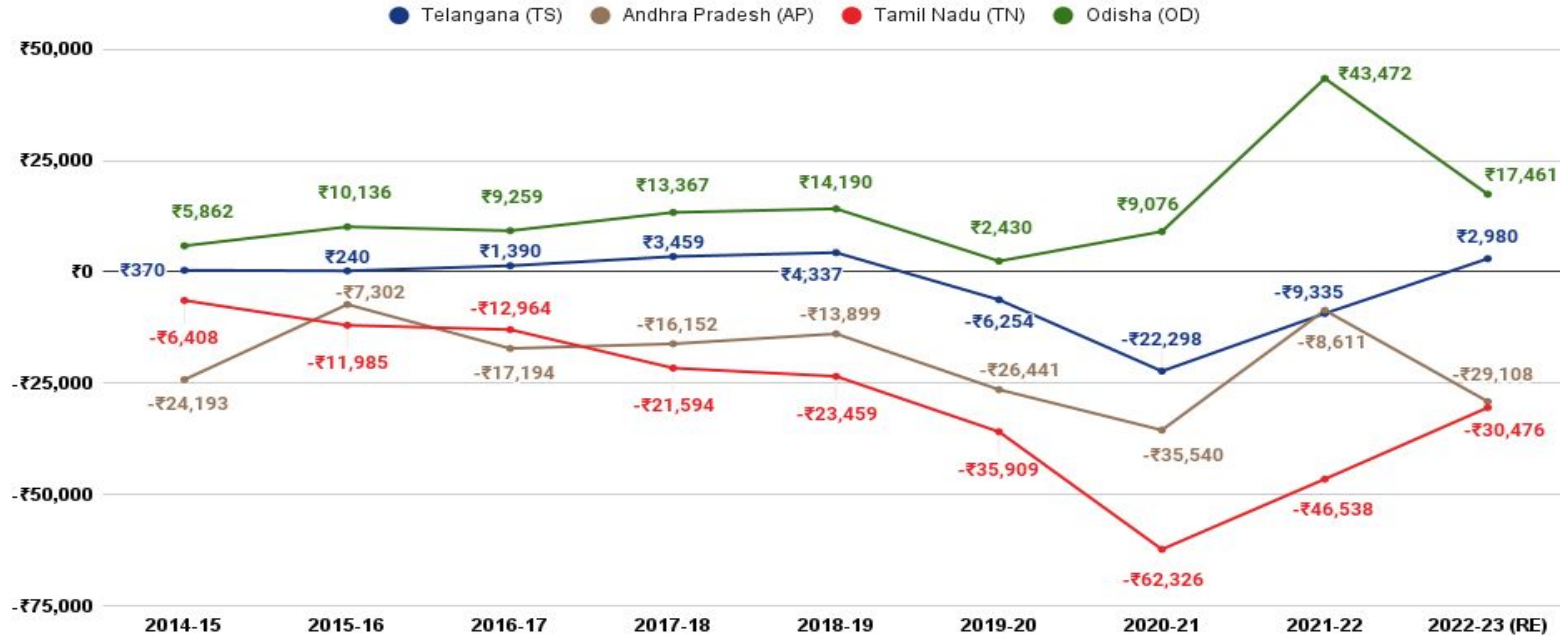
State	Outstanding Liabilities (2022) (Rs. Crores)	Government Guarantees* (Rs. Crores)	GSDP at Nominal prices (2021-22) (Rs. Crores)	Outstanding Liabilities to GSDP (exclusive of Government guarantees) (in %)	Total Liabilities to GSDP (inclusive of Government Guarantees) (in %)
Andhra Pradesh	398904	117503	1201736	33.19	42.97
Telangana	312191	135283	1148115	27.19	38.97
Tamil Nadu	659869	91818	2065436	31.95	36.39
Punjab	282865	22261	584042	48.43	52.24
Rajasthan	477177	84896	1196137	39.89	46.99
Kerala	335989	31714	901998	37.25	40.77
Uttar Pradesh	653308	153836	1863221	35.06	43.32
Madhya Pradesh	317737	34992	1169004	27.18	30.17
Odisha	167206	7068	642087	26.04	27.14
Himachal Pradesh	74686	1880	175173	42.64	43.71
Chhattisgarh**	114201	19611	400061	28.54	33.44
Jharkhand	117790	1553	343178	34.32	34.77
West Bengal***	528833	6593	1536681	34.41	34.84

GSDP: Gross State Domestic Product

- The **real debt-GDP ratio of States**, including off-budget borrowings, is of the order of **34%** by end of fiscal year 2022-23.
- There are instances of **repeated deferrals and postponements of bills** in States to the order of tens or thousand of crores, putting the actual liabilities of States at an even higher level.

From Surplus to Deficit: Impact of Populist, Unviable Projects

Revenue Balance over the Years of Select States – TS, AP, TN & OD (₹ Crore)



- Once a top-ranking state with the highest revenue surplus, **Telangana** slipped into a revenue deficit position due to the implementation of **populist projects**.
- **Odisha**, a relatively less developed state, has consistently generated healthy revenue surpluses, showcasing that **balancing** political stability, electoral viability, and healthy public finances is possible.

- Sound Fiscal policies and good health of public finances are not necessarily politically costly. The governing party in Odisha has been politically stable and popular, consistently winning elections since 2000.

- **Telangana** - highest surplus resources of Rs 1,18,000 crores between 2014-15 and 2019-20 - **but** revenue deficit of Rs 22,298 crores in 2020-21
- **Andhra Pradesh** - suffered on account of loss of revenue from Hyderabad with the division of state - started with revenue deficit - **but** mounted substantially despite support of Union government
- **Tamil Nadu** - prosperous state with high degree of urbanisation - **but** fiscal profligacy in the form of ISWs and relatively low revenue mobilisation - so high revenue deficits
- **Odisha** - less developed state with low per capita income, low urbanisation - **but healthy revenue surpluses**

- Ensuring **zero Revenue Deficits** - **curb borrowing for current expenditures**
Realistic that all states can meet a zero revenue deficit target within 1-3 years, but the **Union may need upto 5 years on account of its *structural deficit***
- **Articles 293(3)** - union's consent required for states to borrow and **Article 293(4)** - union to impose conditions for granting consent
 - States should be required to meet and **maintain zero revenue deficit targets and later revenue surplus targets under Article 293(4) as a condition** for consent to borrow.
 - In case of states shifting to OPS, establishing a **sinking fund** to provide for government pensions should be mandatory.
- **Independent, credible institution to exercise functions under Article 293(3)** given the political sensitivity of the issue.

Can be entrusted to **Finance Commission making it a permanent body under Article 280** or establishing a **Fiscal Council** as recommended by FRBM Review Committee headed by N K Singh
- **Discontinuation of Revenue Deficit Grants** by the Finance Commission

- UK's **Office for Budget Responsibility (OBR)** like body for independent, accurate and credible analysis, forecasts and costings of government's fiscal policies and programmes.
An equivalent body can be created under **the Comptroller and Auditor General (C&AG) under Article 150.**
- The Office of C&AG should be empowered to **seek data on public debt of the state and its agencies from public and private banks**, and it must be made **mandatory** that the said data be made available to the C&AG.
- In case of large capital expenditure, there should be a proper **cost-benefit analysis and approval of loans should be contingent upon reasonable returns or benefits from investments**, as per the conditions imposed under **Article 293(4).**

“Never doubt that a small group of thoughtful, committed citizens can change the world. **Indeed, it’s the only thing that ever has.**”

– Margaret Mead