

Taxation - Public Expenditure - Fiscal Prudence

5th September, 2023

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

William Gladstone

Irreducible Role of the State

Rule of Law

Public Order

Justice

Basic Amenities

Infrastructure

Education

Healthcare

Sustainable
Natural
Resource
Development

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 ₁
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											

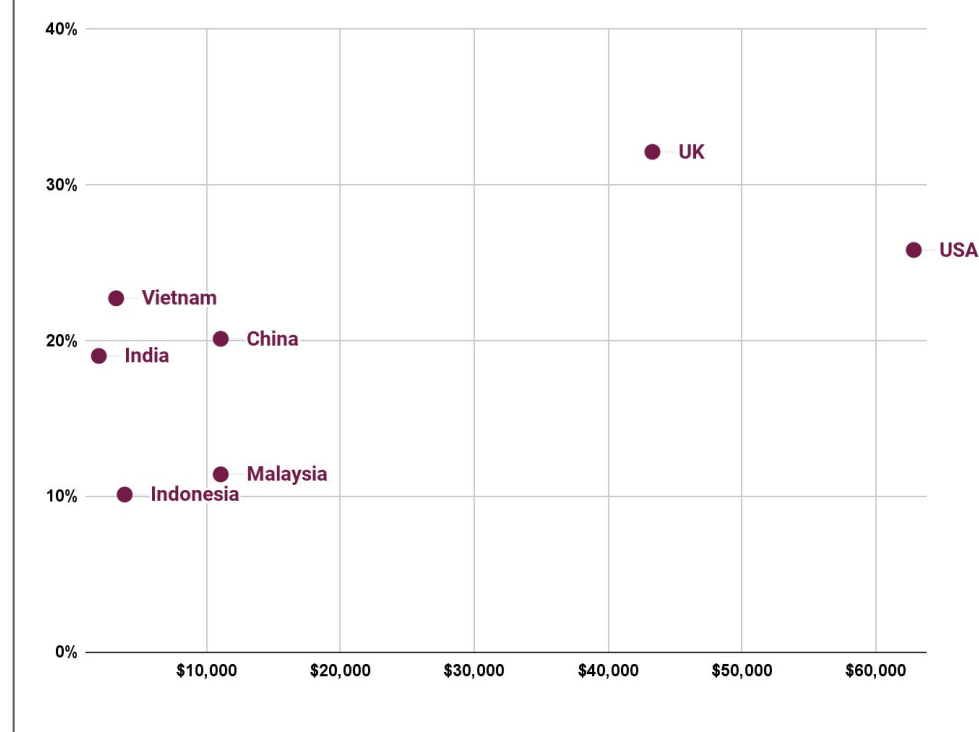
Tax-GDP Ratio and Per Capita Income of Select Countries

Tax-to-GDP Ratio and Per Capita Income of Select Countries

Country	Tax-to-GDP Ratio (%)		Per Capita Income (Nominal, in USD)	
	2018	2020	2018	2020
India	19.5	19	1,974	1,910
China	17.4	20.1	11,074	10,409
Vietnam	23.2	22.7	3,267	3,586
Malasiya	12.5	11.4	11,074	10,161
Indonesia	11.9	10.1	3,903	3,894
United States	24.9	25.8	62,823	63,531
United Kingdom	32.4	32.1	43,306	40,319

Source: OECD; World Bank; FDR’s calculations from Budget Documents and RBI data.

Tax-to-GDP Ratio vis-a-vis Per Capita Income (USD), 2020



High Degree of Centralisation

Local governments –

current scenario

- **Over-structured**
- **Underpowered**

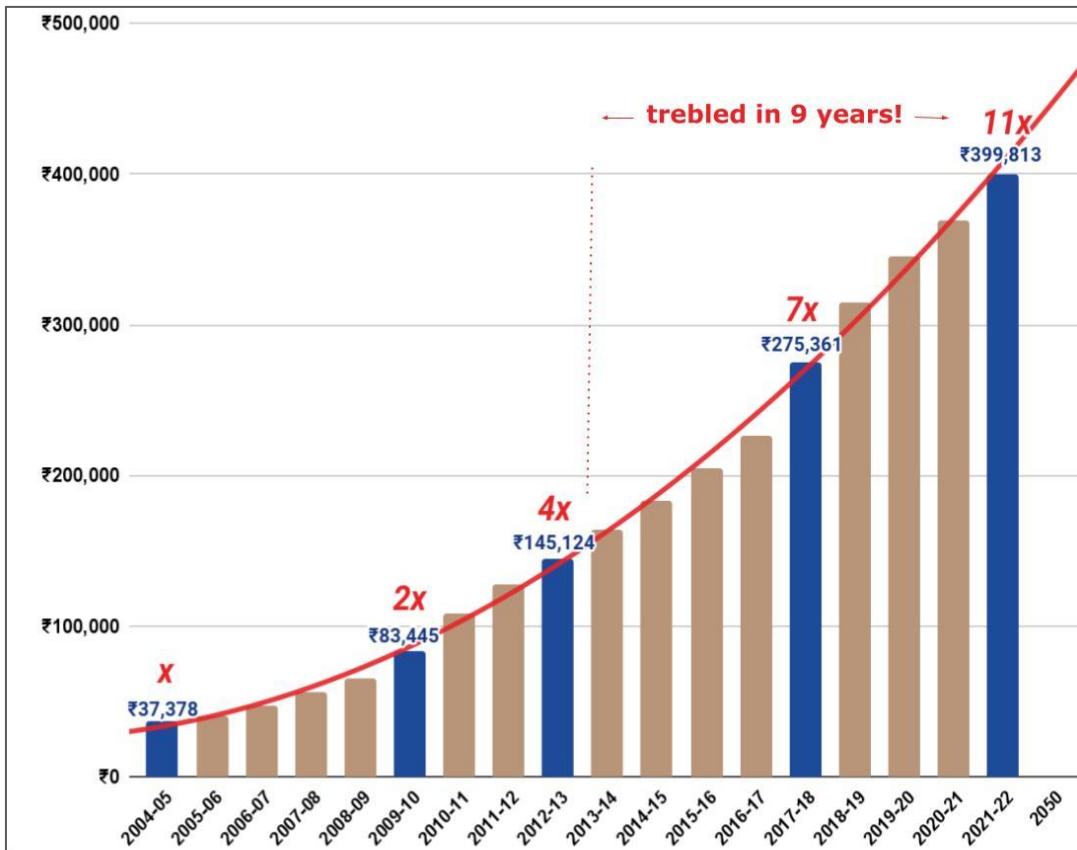


Resultant adverse consequences:

- No avenue for **leadership** to rise
- No proper **political recruitment**
- Inefficient and corrupt **service delivery**
- Absence of the following linkages –
 - **Vote and public good**
 - **Taxes and services**
 - **Authority and accountability**

*Vote becomes a **purchasable commodity** and **freebies** become endemic*

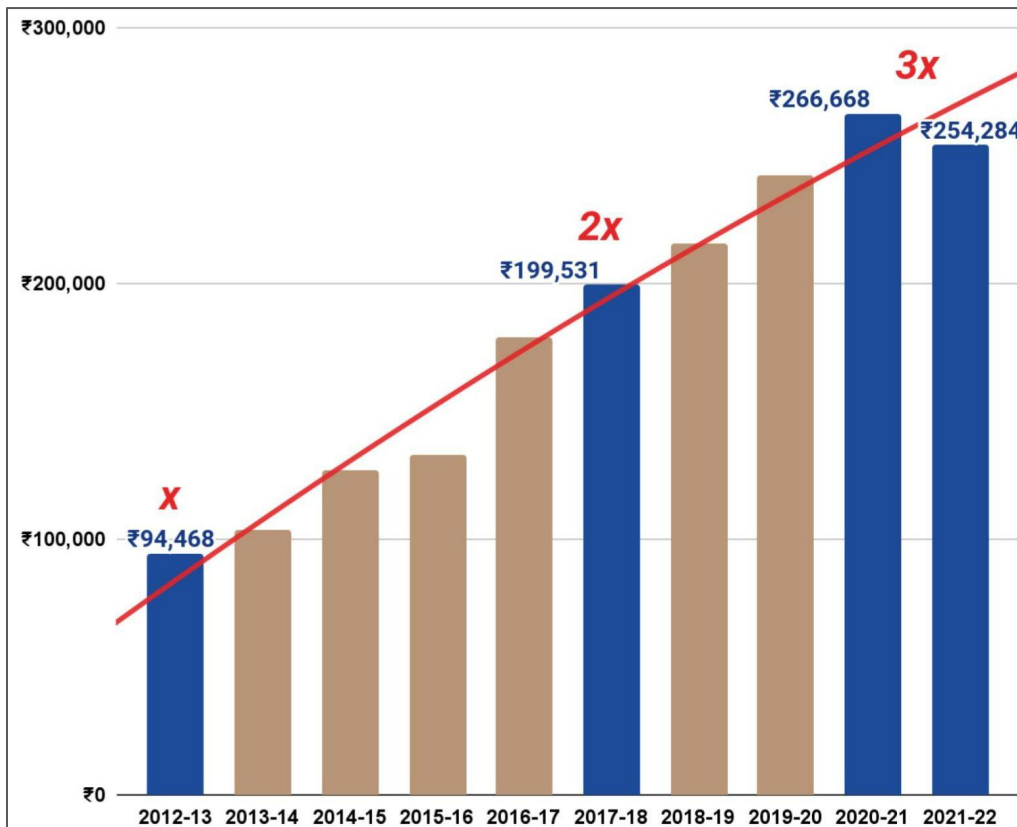
Public Finances: Short-term vs. Long-term



Mounting Pension Burden

Pension Outgo of all States and UTs

- The pension expenditure in States increased eleven times – from ₹ 37,378 crore in 2004-05 to ₹ 399,813 crore in 2021-22, and almost **trebled in nine years** – from ₹ 145,124 crore in 2012-13 to ₹ 399,813 crore



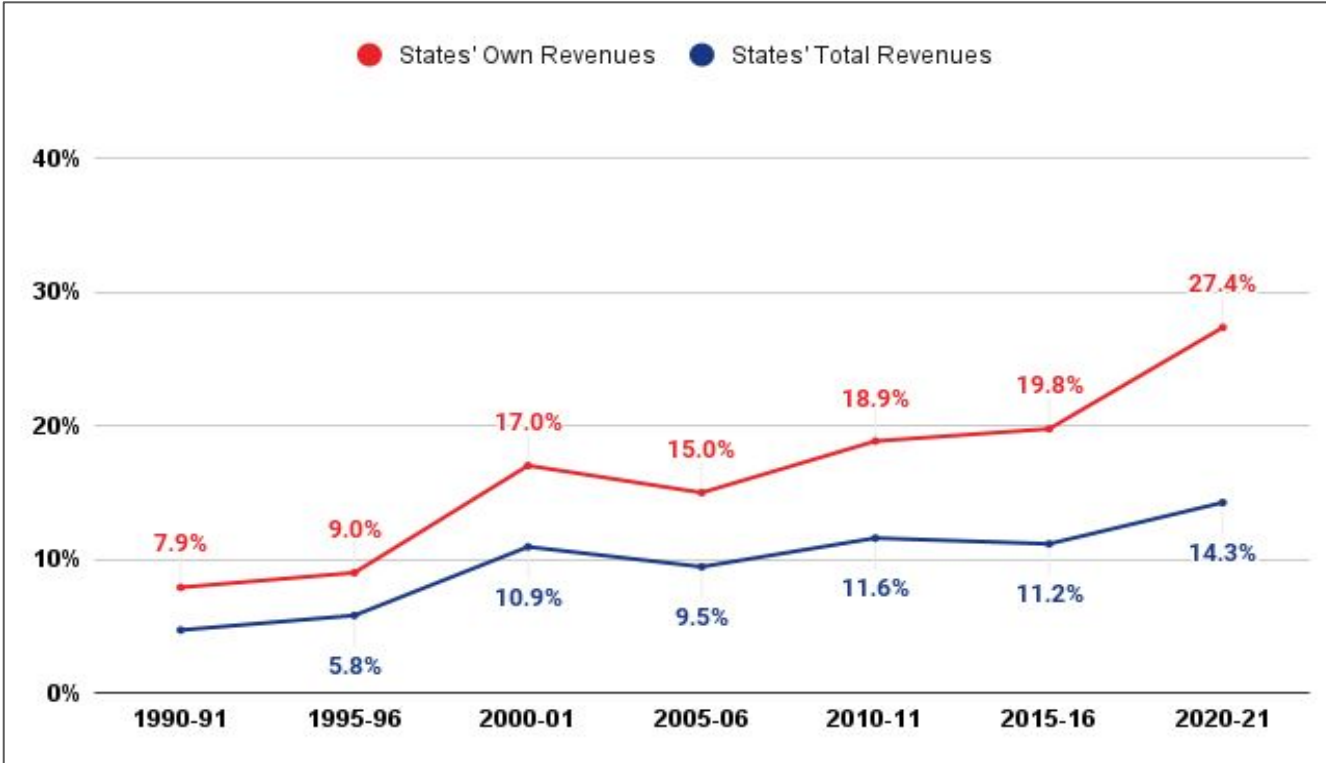
Mounting Pension Burden

Pension Outgo of the Union Government

- The pension expenditure of the Union increased **three times in nine years** – from ₹ 94,468 crore in 2012-13 to ₹ 254,284 crore in 2021-22

Pension Burden Depleting States' Revenues

Pension Expenditure of All States as a Share of Revenues



Note: States' Total Revenues include Transfers from the Union Government.

Source: Preserving Growth Momentum, A Politically Viable Framework for Fiscal Prudence, *Foundation for Democratic Reforms*

- Under the Old Pension Scheme (OPS), **pension constitutes both wage-indexed and price-indexed, open-ended liability.**
- The Compound Annual Growth Rate (CAGR) of pensions during the period 2004-05 to 2021-22 was 14.96%, while the States' own revenue grew at a compound annual rate of 12.60%.

Social Security Systems: The Global Norm vs. India

Overview of Contributory Pensions Programmes in Select OECD Countries and Comparison with India				
Country	Name of the program	Nature of Pension Liability	Coverage as a share of Workforce	Pension Expenditure as a Share of General Government Revenues
United States (2021)	Old Age, Survivors and Disability Insurance	Funded	94%	14.79%
United Kingdom (2020)	New State Pension	Funded	~100%	12.60%
France (2021)	Basic Scheme and Compulsory Complementary Scheme	Funded	~100%	22.70%
Sweden (2020)	Income Pension (Inkomstpension)	Funded	~100%	13.10%
India (2021)	Old Pension Scheme (OPS)	Unfunded	1.84%	18.20%
	National Pension System (NPS)	Funded	1.36%	

Even the most developed countries with much higher tax-GDP ratios than India have adopted the system of funded pensions.

1. The annual contributions are taken from the period between June 30, 2022 and June 30, 2023.
2. The Accumulated Reserves or Assets Under Management are as of June 30, 2023.

Most Public Expenditure is at the State level

Year	Level of Government	Expenditure		
		Amount (₹ Crore)	As a share of GDP (%)	As a share of General Government Expenditure (%)
2015-16	General Government	3,760,611	27.31	
	<i>State Government</i>	2,360,229	17.14	62.76
	<i>Union Government</i>	1,400,382	10.17	37.24
2016-17	General Government	4,265,969	27.72	
	<i>State Government</i>	2,708,215	17.60	63.48
	<i>Union Government</i>	1,557,754	10.12	36.52
2017-18	General Government	4,515,946	26.42	
	<i>State Government</i>	2,924,599	17.11	64.76
	<i>Union Government</i>	1,591,347	9.31	35.24
2018-19	General Government	5,040,747	26.67	
	<i>State Government</i>	3,337,713	17.66	66.21
	<i>Union Government</i>	1,703,034	9.01	33.79
2019-20	General Government	5,410,887	26.92	
	<i>State Government</i>	3,495,003	17.38	64.59
	<i>Union Government</i>	1,915,884	9.53	35.41

- India's **general government expenditure** in the pre-pandemic years was around **27% of the GDP**
- The **expenditure pattern, as seen in the Table, indicates that States are playing a vital role** in delivering services to the citizens.

Source: Economic Survey 2022-23, Statistical Appendix – Table 2.6

“I contend that for a nation to try to tax itself into prosperity is like a man standing in a bucket and trying to lift himself up by the handle.”

Winston S. Churchill

“There is no worse tyranny than to force a man to pay for what he does not want merely because you think it would be good for him.”

Robert A. Heinlein