The Road Ahead

How to Balance Growth with Welfare

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Human society created governments to fulfill our collective needs. In a democratic society governments are elected by us, the people. There is always a temptation on the part of those who seek to be elected to please us temporarily at the cost of the purpose for which we created government. Poverty and inequality exist on a large scale in our society. But if governments focus only on short-term individual welfare to mitigate the pain of poverty temporarily and to please the voters, we pay a heavy price. If the collective needs of society are neglected, it is the poor who suffer the most. If the government fails in its main tasks, economy will not grow and poverty will continue. Rapid economic growth is the greatest anti-poverty measure. China has eliminated poverty by rapid economic growth for nearly four decades. Even a more modest growth of about 5% in India lifted hundreds of millions Indians out of poverty. Our great challenge for the next three decades is balancing long-term growth and collective needs with short-term welfare measures.

Economic growth needs high quality infrastructures, skills, healthcare, rule of law to settle disputes fairly and peacefully and to protect our rights, promotion of investment, incentives for employment generation and sensible tax policies. If all our resources go for day-to-day survival and short-term welfare, economy will stagnate and there will be no growth. Without growth, and with population increasing, we will become even poorer. With growth, government will have more tax revenues to spend more on welfare. It is clear that growth and welfare must go hand in hand.

In order to promote growth with welfare, two central questions need to be answered. First, how much can we spend on welfare; second, in what manner should welfare programmes be implemented to help the poor. Government money comes from three sources: first – tax revenues, cesses and fees government collects from people; second – any dividends and income from investments and sale of assets; third – borrowings. If we spend borrowed money, dividends and sale proceeds on day-to-day expenditure, then we will get into a debt trap and soon governments will go bankrupt and economy will collapse. Prudent families, companies and governments manage current expenditure from current earnings, and will save as much money as possible. But in government, borrowed money, instead of going for investments to create wealth, is going for consumption, increasing future debt burden without additional growth or income. This is a dangerous situation.

Can we reduce expenditure? In most states, salaries, pensions and interest payments already exceed states' own revenues. In addition, there is day-to-day administrative cost. All these expenditures are non-discretionary, and no government can reduce them instantly. Then we have large short-term welfare expenditure which needs to be brought under some control. But with lavish new welfare promises in each election cycle, rapid increase in salaries and wage indexation of unfunded pensions, revenue expenditure in most cases is way above revenues even after taking into account Union's transfers to states. In case of the Union too, after salaries, pensions, interests, all kinds of transfers to states and welfare programmes, there is a huge revenue deficit of Rs 11,10,546 crores in 2022-23 (RE), and Rs 8,69,855 crores in 2023-24 (BE). Our governments are living beyond the means. Unfunded, lavish pension scheme (OPS) and generous welfare programmes are bankrupting the nation. OPS burden will continue to increase steeply until about 2035-40 even where fully funded national pension system was embraced; in states where governments embraced OPS even for the future, a catastrophic collapse is inevitable after 2035.

Therefore, the simple rule should be that all current expenditure, including allocations for future pensions and welfare programmes, must come from current revenues, not borrowings and sale of capital assets. If welfare expenditure is incurred from current revenue and borrowed money goes for investments for the future, then future growth and current welfare can be balanced.

Then the second question: what kinds of programmes are desirable? Any welfare measure that enhances productivity and earning capacity is ideal. Skill promotion and incentives for employment–generation are good examples. Next best would be supplementing incomes of the poor. The truly counterproductive welfare measures give temporary benefit to individuals, but cause long-term damage to the economy and productivity. As a result, the cost society bears is far greater than the intended benefit to the poor.

For instance, loan waivers are a bad form of welfare. Only about 30-40% of farmers and micro-enterprises get loans from banks; others borrow from informal lenders at high interest rates. Therefore any waiver excludes the poorest 60% farmers and artisans. Those who repay honestly in time will be denied loan waiver benefit, and they feel cheated. Ultimately we are creating a culture of non-repayment of debt. Eventually all credit will dry up, and farmers and artisans will be worse off. No matter how many loan waivers are implemented at taxpayers' cost, the poor and marginalized remain trapped in poverty. Instead of loan waivers, timely and adequate credit availability, interest subsidies to those who repay on time, infusion of technology to enhance productivity and good marketing system to give better price will all enhance incomes and lift people out of poverty.

Unmetered free power to farmers, free rice and wheat distribution without nutritional balance and urea subsidy without plant nutrient balance are some of the examples of welfare measures which entail great costs on society and environment without real long-term impact on ending poverty.

Our policies and welfare measures should end poverty and bring all people into middle class fold, enhancing their productivity, giving them opportunity, and generating greater incomes. Instead, in most cases we are converting the people into mendicants, undermining their pride, dignity and self reliance and perpetuating poverty. Productivity, dignity and incomes are the keys to future prosperity. Will the parties learn?

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