Policy for Regional Development

V. J. Ravishankar
Indian Institute of Public Administration
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Why is regional equity an issue?

“Large regional disparities represent serious threats as the inability of the state to deal with such inequities creates potential for disunity and, in extreme cases, for disintegration”

Table 1: Regional Disparities in Selected Countries, 1997

<table>
<thead>
<tr>
<th>Country</th>
<th>Max / Min</th>
<th>Simple C.V</th>
<th>Wt. Gini Index</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States</td>
<td>1.927</td>
<td>0.162</td>
<td>0.039</td>
</tr>
<tr>
<td>Canada</td>
<td>1.838</td>
<td>0.201</td>
<td>0.067</td>
</tr>
<tr>
<td>India</td>
<td>3.811</td>
<td>0.387</td>
<td>0.227</td>
</tr>
<tr>
<td>China</td>
<td>11.625</td>
<td>0.692</td>
<td>0.250</td>
</tr>
<tr>
<td>Russia</td>
<td>21.307</td>
<td>0.625</td>
<td>0.280</td>
</tr>
<tr>
<td>Brazil</td>
<td>7.567</td>
<td>0.563</td>
<td>0.267</td>
</tr>
<tr>
<td>Mexico</td>
<td>5.793</td>
<td>0.473</td>
<td>0.301</td>
</tr>
</tbody>
</table>
Trends in Disparities -- Highlights

- US has seen declining regional inequality during 1990-94
- Canada’s inequality more or less constant during 1994-98
- India saw rise in inequality during 1980-96, with dramatic increase in 1992 post liberalization
- Russia saw dramatic rise in inequality during 1994-97
- Brazil saw rising inequality in 1980s, slight fall in early 1990s and a slight rise during 1995-97
- Mexico’s regional inequality has remained at around 5 times that of the United States
Divergence among Indian States

Researchers have found a persistent divergence in per-capita income growth rates among two subsets or clubs of Indian states over the 1965-1997 period -- one at roughly 50% and the other at 125% of the national average.

Can India achieve its development goals if the lagging states are left behind?
Nirvikar Singh and T. N. Srinivasan (2002) conclude: “The differences in infrastructure and institutions that seem to explain interstate differences have been persistent … and neither Finance Commission transfers, Planning Commission transfers, nor centrally sponsored schemes have made a substantial dent in regional inequalities in India.”
Types of Regional Dev Policies

- Central intervention for regional balance
- Common market (economic union)
- Fiscal equalization

“Regional development policies have failed in almost all countries … to reduce regional inequalities” – Raja Shankar & Anwar Shah (2003)
What is to be equalized?

- Outcomes? They will never be equal
- Opportunity? Yes, a level playing field
- Capacity? This is the aim of fiscal equalization
Paradigm Shift in India

Old paradigm relied heavily on direct central intervention in the name of equal outcomes, curbing opportunities in the process.

New paradigm is to foster a common market by reducing barriers to inter-state trade and investment flows, along with more effective fiscal capacity equalization.
“Most developing countries adopted Comparative Advantage Defying (CAD) strategies, which caused distortions and did not bring about convergence … replacing the old CAD strategy with a new Comparative Advantage Following (CAF) strategy is essential”

New Environment for Indian States

Two phases of significant change:

- over the 1970s and 1980s – growth of regional political parties
- since 1991 – liberalization of external trade and investment policy by the Government of India

*States now have a larger role in determining their development paths*
Poorer states attracted less Investment in the 1990s

**Poor and less developed states lagging behind:**
Bihar, Jharkhand, Madhya Pradesh, Chhattisgarh, Orissa, Rajasthan, Uttar Pradesh (UP)

- account for 50% of India’s poor; 23% of investment in 2003; 13% of FDI during the 1990s; 25% of All-India GDP & per capita income; 54% of the average per capita income of other major states.

**More developed states racing ahead:**
Andhra Pradesh, Gujarat, Karnataka, Maharashtra, Punjab, Tamil Nadu

- attracted over 66% of the total investment in 2003; 72% of FDI during the 1990s
State fiscal management and governance do make a difference

Through a 3-sector growth model of the Uttar Pradesh economy, Buffie (1998) concluded that state-financed infrastructure in power, roads and irrigation can have a very important locking-in or “crowding-in” effect on private investment in agriculture, industry and services.
State Ranking by Infrastructure

- **High**: Goa, Maharashtra, Punjab
- **High middle**: Gujarat, Haryana, Kerala, Tamil Nadu
- **Middle**: Andhra Pradesh, Karnataka
- **Lower middle**: Himachal Pradesh, Madhya Pradesh, Orissa, Uttar Pradesh, Uttaranchal, West Bengal
- **Low**: Arunachal Pradesh, Manipur, Meghalaya, Jharkhand, Mizoram, Nagaland, Assam, Chhattisgarh, Sikkim, Tripura, J&K, Bihar, Rajasthan

Differences in Business Climate

- Time to start a business is longer in poorer states – 79 days in Orissa compared to 57 in Karnataka and Punjab
- Time and cost to register a property are much higher in India’s poorer states
- It takes longer to enforce a contract – 1165 days in Uttar Pradesh versus 425 in Maharashtra
- It takes 15 years to close a business in Uttar Pradesh; it takes 8 years in Karnataka

(Doing Business – India Regional Profile, World Bank, 2004)
Laggards need to leap forward

“While all Indian states need to focus on improving their investment climate, efforts in the lagging states will need to be twice as intensive as the better states”

# Infant Mortality Rates, 1980-2000

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<tbody>
<tr>
<td>Kerala</td>
<td>37</td>
<td>17</td>
<td>14</td>
<td>6</td>
</tr>
<tr>
<td>West Bengal</td>
<td>91</td>
<td>63</td>
<td>51</td>
<td>21</td>
</tr>
<tr>
<td>Karnataka</td>
<td>69</td>
<td>70</td>
<td>57</td>
<td>23</td>
</tr>
<tr>
<td>Bihar</td>
<td>118</td>
<td>75</td>
<td>62</td>
<td>25</td>
</tr>
<tr>
<td>Rajasthan</td>
<td>108</td>
<td>85</td>
<td>79</td>
<td>28</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>150</td>
<td>99</td>
<td>83</td>
<td>33</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>142</td>
<td>111</td>
<td>88</td>
<td>37</td>
</tr>
<tr>
<td>Orissa</td>
<td>135</td>
<td>122</td>
<td>96</td>
<td>41</td>
</tr>
<tr>
<td>All India</td>
<td>110</td>
<td>80</td>
<td>68</td>
<td>27</td>
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</tbody>
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**Sources:** 1980 and 1990 Sample Registration System; 2000 National Family Health Survey
## Developmental Role of State Governments

<table>
<thead>
<tr>
<th>Instrument</th>
<th>Outcome</th>
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<tbody>
<tr>
<td>Fiscal Policy, Public Sector Mgt &amp; Service Delivery</td>
<td>Public Investment in Quality Infrastructure &amp; Human Capital</td>
</tr>
<tr>
<td>Investment Policy &amp; Regulatory Regime</td>
<td>Private Capital Investment &amp; Employment Growth</td>
</tr>
<tr>
<td>Mechanisms for civil society interface &amp; oversight</td>
<td>Accountable Government &amp; Empowered Citizens</td>
</tr>
</tbody>
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Role of Central Policy

- Fiscal Capacity Equalization (Twelfth Finance Commission)
- Fostering a common Indian market
- Addressing particular disadvantages (Finance Commission, Planning Commission, Line Ministries, External Donors)
Partial Fiscal Equalization

Per capita revenues (normalized to Punjab=1), 2000/01
Further Steps to Level the Field

- Phase out Central Sales Tax
- Rationalize and restructure public food procurement
- Improve rural credit access
To sum up … lesson for Government of India

“Countries experiencing convergence have had a hands-off approach to regional development policies and instead focused on policies to promote a common economic union … and ensuring minimum standards of basic services across the country”

To sum up … lessons for State Governments

- Need to evolve a state specific development strategy based on one’s comparative advantages and specific binding constraints – *not* the old planning paradigm of spreading resources too thinly

- All states need to strengthen
  - Fiscal policy, public administration and service delivery
  - Investment policy & regulatory regime
  - Role of civil society

- Laggards need a great leap forward