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A Case Study on the Concept of Public Expenditure in India

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Abstract – *The coordination of the public fund strategies to enable the government to carry on a constructive position in the development of the economy poses a variety of concerns. Through that angle, this paper explores public spending in India. The following region is defined by a representation of the public fund and the amount and portion of the public budget. The funding of public expenditure by tax agreements is addressed. Stimulus of spending and failure to fund it through taxes have caused the government to resort to massive deficits and debt accumulation, with a threat to macroeconomic soundness. This has also led to the selection of a rule-based fiscal approach. These issues are discussed.*

Keywords – *Public Expenditure, Public Finance, Tax System*

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INTRODUCTION

In economics, the term 'expenditure' would not, in general, connote the coins & cash notes of a country, but rather the funds of an entity or a group of individuals allocated in respect of cash. Again, the term 'public' implies a heterogeneous group of individuals exchanging everything for all purposes and purpose; they will have a common connection connecting them for a cause for quite some time. Accordingly, public spending is described as spending in the public domain, where the relations are satisfactorily integrated for a typical purpose.

This section controls the adequacy of India's public accounts. The aims of public funds are to guarantee macro-economic stability, to attain the perfect condition of production, to give public forms of assistance to promote development and progression. Fiscal solution is both large-scale and micro-economic. Significant goals of public funds include the distribution of public administration properties and the promise of prosperity and development, the assurance of macro-economic stability and the accomplishment of the optimal flow of revenue.

OBJECTIVES OF THE STUDY

- To verify the relative impact of Public Expenditure on Economic Development.
- To study the impact of disinvestment policy of the Government of India on Public Expenditure.

- To assess the case studies in respect of Public Expenditure.

REVIEW OF LITERATURE

Mitchell (2005) claimed that an enormous and growing economy is not helping to boost fiscal performance; although Abu and Abdullah (2010) observed that government expenditure has remained on the rise owing to massive proceeds from unrefined oil output and exchange, which has raised demand in public goods such as highways, communications, police, instruction and so on. In addition, there is a increasing need to have both internal and external protection for individuals and the world. Open CBN quantifiable information indicates that all policy spending (capital and recurrence) remains on the increase during the evaluation era.

Schaltegger and Torgler (2006) have endeavored to understand the effects of public spending development in Switzerland over the period 1086-2001. The key aim of this study is to concentrate on the connection between financial development and public spending, utilizing a complete illustration of state and local governments within a wealthy country. The inquiry found that there is a clear negative correlation between the size of the government and financial performance. Be this as it might, the inquiry suggests this spending from capital financial plans will not have a major impact

on fiscal production, rather than on public spending from operational financial plans.

Okafor and Eiya (2011) examined the determinants of Government Expenditure growth in Nigeria. As such, the four factors related to real inflation, public debt, tax income and population were included in the inquiry to assess the rise in public spending. The information collected for these variables has been subjected to the usual least square relapse check. Results indicate that population, public debt and tax receipts have a big positive relationship with all government spending, although inflation has a negative relationship with all government spending. This indicates that these factors are the main determinants of growth in government expenditure. The report further suggests that the National Assembly's Bill on Fiscal Responsibility will periodically take a break in order to reduce spending gaps and public debt and their implications for the economy.

Mishra and Suresh (2005) considered the growth and determinants of public expenditure in all of the North-Eastern States and specifically in Nagaland. The inquiry uses details for thirty-eight years from 1963-64 to 2000-01 to explore the nature of the problem of public expenditure development in the north-eastern states and to assess if the political belief structure has taken on any role in defining and reshaping the trends and quantity of public spending in the state of Nagaland over an indefinite span of time. The inquiry found public spending to be a dependent variable, whilst the mixture of financial variables and policy variables on the region of parliament, the government section, the division of government, the sectoral revenues beginning with the horticultural sector and the rest of the segments were taken as free variables. The follow-up to the study suggests that both Congress and non-Congress structures have a detrimental effect on the development of non-formative spending in the state. Examining further the reasons that the ideological leanings of the gatherings in power or the difference in government from non-congress to congress do not appear to have any orderly effect on the assurance of public expenditure in the state of Nagaland.

Rahman (2008) inspected the advancement of public welfare expenditure in India. As such, the information board model is used to describe the key components that have an bearing on public health spending for the duration 1971 to 1991. The exact findings indicate that the main determinants in the definition of provincial health spending are the actual state per capita income and competence levels, whereas certain auxiliary priority variables, such as the size of the state population over 60 years of age, population per position of vital human services and population per expert, are measurably negligible.

TAX SYSTEM IN INDIA: TRENDS AND ISSUES

Tax policy is a significant mechanism by which funds are shifted from the corporate sector to the government to fund public administrations. Excluding the fact that taxes are imposed at every stage, twists become inescapable because they affect the impulses to conserve, participate and attempt hazards. A good tax system would collect the requisite taxes by reducing the expense of the variety, the expense of continuity and the cost of contortions. The best strategy when coping with tax reform is to offer an broad base, a medium rate, a high rate distinction and a clear and easy tax structure. Although taxes must be efficiently distributed, excessive focus on redistribution may be counter-productive. The focal point of the system will switch from a reduced deficit to a reduced need, and this is ideally done by public expenditure approaches.

Table 2: public expenditure in India

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16
I Non-Social Expenditures								
(1) Interest Payments	427	521	431	461	468	519	485	478
(2) Defence	263	211	208	209	203	201	201	192
(3) Other Admin. Services	384	404	348	349	388	406	418	371
Total I Non-Social Expenditures	1474	1837	1488	1619	1659	1826	1804	1841
II Social Expenditures								
(1) Education	111	239	447	618	717	817	938	1111
(2) Healthcare	129	111	171	148	119	117	141	141
(3) Total Social Services	529	459	618	806	836	934	1079	1252
(4) Total Economic Services	486	791	831	813	979	849	807	841
Total II Social Expenditures	1134	1379	1807	1975	1931	1934	2127	2344
Total Expenditures	2608	3216	3295	3594	3590	3760	3931	4185
Revenue Expenditures	114	111	111	111	111	111	111	111
Capital Expenditures	53	89	72	84	118	111	111	111
Total Central Government Expenditure	1441	1816	1812	1999	1961	2038	2011	1969
Total State Government Expenditures	1167	1400	1483	1595	1629	1722	1920	2216

Table 3: per-capita expenditure in large non-special category states 2014-15 (in rupees)

State	Per Capita Education Expenditure	Per Capita Health Expenditure	Per Capita Development Expenditure	Per Capita Total Expenditure	Per Capita GDP
Andhra Pradesh	1325	209	1258	2812	100152
Assam	1291	317	3579	5187	14954
Chhattisgarh	1319	883	13201	15403	87294
Gujarat	1801	1008	13886	16695	141455
Karnataka	2335	849	12379	20563	105720
Kerala	1866	481	7772	10119	60991
Madhya Pradesh	1899	521	18827	21247	144589
Odisha	1854	1244	13374	16472	105885
Rajasthan	2262	612	9584	12458	63321
Tamil Nadu	1999	783	13881	16663	103881
Uttarakhand	2340	732	18740	21812	71184
West Bengal	1811	811	9912	12514	129886
Chhattisgarh	2891	888	11255	15034	98237
Tamil Nadu	1131	887	12995	15013	149885
Telangana	1896	789	13609	16294	141979
Uttar Pradesh	776	382	4647	5805	58468
West Bengal	1905	754	8788	11447	94711

The tax framework in India, notwithstanding a few rounds of reforms, has not had the option to produce the necessary revenues. The tax-GDP ratio was 15.8 per penny in 1991-92 when financial reforms were started and the ratio of focal taxes to GDP was 10.2 per penny. Following a time of reforms, the tax-GDP ratio declined to 13.4 per penny in 2001-02 primarily because of the decrease in focal taxes by two percentage focuses to 8.2 per penny (Rao and Rao, 2006). The revenue from both import obligations and extract obligation declined separately by two and one percentage focuses and with revenue from income taxes expanding by one percentage point, the general decrease in the focal government's tax ratio was constrained to two percentage focuses. While the general experience

of advancement in creating nations is to recover the revenue misfortune from decreasing import obligations by presenting the worth included tax, such a choice couldn't be investigated in India as the ability to impose deals taxes rested with the states and state level reforms couldn't be composed with that of the Center (Rao and Rao, 2011).

Another round of tax reforms was started after 2004-05. The making of tax in-development network and extension of the base of administration tax at the Central level and re-position of the falling kind deals taxes with the worth included tax in 2005-06 by the States. Therefore the tax-GDP ratio expanded from 14.6 per penny in 2003-04 to 17.5 in 2007-08. A majority of this expansion, practically 2.6 percentage focuses was because of increment in income tax revenue comparative with GDP from 2.7 per penny in 2003-04 to 6.3 percent in 2007-08. Truth be told, revenue from income taxes enrolled a normal growth of more than 30 per penny during this period. At the state level, the substitution of falling kind deals taxes with numerous rates with a worth included tax with just two rates extensively improved the tax framework, diminished mutilations while expanding the revenue productivity. After 2007-08, be that as it may, the tax ratio declined to 15.5 per penny in 2009-10 mostly because of the improvement given as far as decrease in extract obligation and administration tax rates in the wake of global financial crisis. It step by step recouped to 17 per penny in 2016-17.

INDIAN PUBLIC FINANCE: DEFICITS AND DEBT

The continuation of massive fiscal deficits in India has contributed to a significant rise in debt. At more than 75 per cent of GDP, India's debt is significantly greater than that of nearly equivalent central-income countries (58 per cent). Although, broadly speaking, public expenditure funded by purchase is necessary, see that it stimulates extra monetary activity. There is an outstanding disagreement about the appealing efficiency of the funding of public spending from the funds gained. The Ricardian proportionality theorem claims that fiscal shortfalls will not impact interest levels and inflation on the grounds that the government's dissavings are arranged by the family's option to provide higher pension assets to cover extra tax liabilities later on. In fact, that's not possible, in any case. In order for the Ricardian identicalness theorem to hold, it is important to meet the strong suspicion that people in the economy have foresight, realize the discount rates proportional to the government's spending cap rate, and have extremely long timelines for assessing the current value of future tax installments (Rangarajan and Srivastava, 2011).

Consequently, there must be cut-off points for obtaining public expenditure as a source of funding.

In ordinary situations, the genius idea is that a single existing expenditure for the payment of wage rates, interest, funding for capital goods, allocations and other transactions could be funded by current profits by tax and non-tax revenues, and that capital spending should be funded from collection. This is just a broad guideline to ensure that the reserves acquired are used to finance expenditure that would accelerate the pace of growth of the economy at any rate that is the same as the interest rate on acquisition. Although it is beyond the scope of possibility to try to have a general roadmap on the optimal amount of scarcity and debt, transaction should be rendered to the point that it contributes to a net improvement in revenue and profits.

Unnecessary investments to fund public expenditure may have highly adverse implications. To begin with, as has now been described, the top proposal on financial reserve funds for the family sector will raise interest rates and pool out private projects. Second, high debt volumes give rise to high interest payments that seize public spending on productive exercises. Fourth, receiving now will be reimbursed at a later point by higher taxation and thus provides a weight for the community of citizens yet to arrive. Third, large shortfalls could contribute to parity of installment problems. For these factors, FICO score offices attach strong risk expectations of countries with large rates of deficits and debt resulting in higher foreign acquisitions. As a consequence, fiscal laws are applied in a variety of countries to control the degree of deficit and debt.

There have been long-standing concerns about shortages and debt in India, and the financial crisis of 1991 was largely due to retrenchment of fiscal policy. As Meager and Joshi (1994; p. 215) state, "... the recession of 1990/91 and 1991/92 is entirely inferable from the stagnant fiscal policy of the previous years. The accelerated growth of debt, ... along with the political steadfastness that postponed the persuasive answer of the growing storm, rendered it impossible to fund the equalization of the deficit of increments. The fiscal problem re-emerged in 2001-02 when the overall fiscal shortfall was 10.3 per cent of GDP, the basic deficit was similar to 3 per cent and the tax shortfall was about 7 per cent. With the government's unpaid obligations estimated at 72.5 per cent of GDP and the interest rate promising 35 per cent of the gross income, the debt sustainability inquiry was not repulsive. With a significant deficit of about 2-3 per cent of GDP, there were some years during this time where the debt-to-GDP level saw a clear growth (Buiter and Patel, 2006). This has led the central government to introduce the Fiscal Accountability of the Budget Control Act (FRBMA) in 2003 and this has been backed up by all States sanctioning the implementation of fiscal responsibility on the basis of the recommendation of the Twelfth Finance Commission. Clearly, the Twelfth Finance

Commission has provided noteworthy opportunities to the Member States by relating the discount and rescheduling of the focal government debt to the enforcement of the fiscal obligation and the elimination of the fiscal deficits for the term 2004-2009. The Commission has set goals to reduce tax shortfalls at both the central and state levels and to achieve a fiscal deficit of 3 per cent of GDP both at the central and state levels. The thirteenth Finance Commission has reset the fiscal deficit to 3 per cent for the focal government and 3 per cent for the GSDP for the States (2.4 per cent of GDP) to be achieved by 2014-2015.

The ensuing era, from 2004-2005 to 2007-08, saw substantial fiscal contraction at both rates of the C-State (Figure 1). At the state stage, so big a mix has been accomplished, despite the twelfth Finance Commissions' radical reward program to reduce part of the unpaid Central Loans on the ratification of the Tax Obligation Acts. As a result of a sharp acceleration in revenue growth, the Center's fiscal deficit to GDP ratio decreased from more than 6 per cent in 2001-02 to 3 per cent in 2007-08. As stated earlier, the introduction of the tax information network, along with a high pace of GDP growth over the decade, culminated in income tax revenue rising by two percentage points from 3.7 per cent of GDP in 2003-04 to 6.3 per cent of GDP in 2007-08. In comparison, income from administrative taxes rose by a percentage point for the most part. In any event, the Central Government has not been able to hold to its goal of fully reducing the tax deficit. On the other side, by 2007-08, the Member States together had the possibility of minimizing the tax deficit and thus reaching a significant portion of a penny of GDP. In fact, they were expected to low their fiscal deficit to 1.5 per cent in 2007-08. Subsequently, by 2007-08, when compared to GDP, the combined fiscal deficiency GDP was only about 4.5 per cent compared to the 6 per cent target, the revenue shortfall was only about a large portion per cent and there was a significant overflow of one per cent.

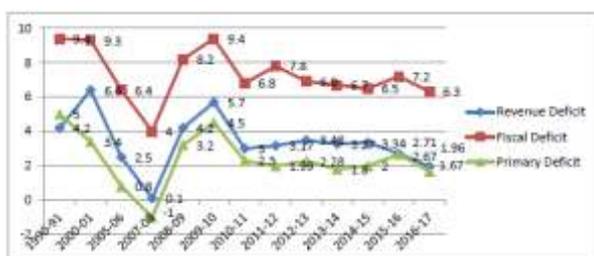


Figure 1: Fiscal Imbalances in India 1991-2017

Overall, the States had the ability to meet the targets, primarily because of the moderate debt reduction and the rescheduling focused on the recommendations of the Twelfth Finance Commission (which increased the Center's danger accordingly). Be it as it might, the fiscal situation of the focal government certainly shifted since 2008-09, mainly due to significant rises in sponsorships and

movements. The creation of rustic industry means the conspiracies of 200 areas around the country, the announcement of homestead loan waivers and the usage of pay commission proposals in the 2008-09 financial plan have raised the overall spending of the focal government. In addition, there has been a sharp increase in the international cost of crude oil, which has reached a record high of USD. 165/barrel in July 2008, and the government's inability to raise the rate of distillates, culminated in an extra dowry bill of around 2.5 per cent of GDP. As a result, the Center's sales deficit rose from 1.1 per penny in 2007-08 to 4.5 per penny in 2008-09, and its budgetary deficiency grew by more than five percentage points from 3.1 per penny to 8.2 per penny. The problem was further compounded by the fall in the tax-GDP target ratio by more than two percentage points to GDP from 11.8 per cent in 2007-08 to 9.6 per cent in 2010-11. As a result, the combined revenue and fiscal shortfall in 2008-09 increased to 4.4 per penny and 10.6 per penny individually. A surprising slippage has been rendered along these lines in obtaining a fiscal balance at the focal point.

Case study of Bangladesh: Public Expenditure on Education and Economic Growth

In Bangladesh, increased investments in education are associated with higher returns in the labor market and higher productivity in the agriculture sector. If education causes GDP to increase at a greater extent than the allocation to this sector should also be enhanced. Education is a long-term process and therefore it's necessary to establish long term relationship between these two variables. Though a number of researches on functional relationship between public spending on education and economic growth have been conducted in many countries but such type of study remains absent in Bangladesh. The objective of this study is to determine the long run relationship between public spending on education and economic growth in Bangladesh.

Numerous studies discussed about the relationship of the public expenditure on education and the economic growth. The size of government expenditures in social sector and its impact on economic growth has emerged as a major public choice issue facing economies in transition. Blankenau et al (2005) carried out an empirical study on expenditure-growth relationship in the context of an endogenous growth model. They found that the response of growth to public education expenditure may be non-monotonic over the relevant range. The relationship depends on the level of government spending, the tax structure and the parameters of production technologies. The literature has focused on the link between level of public expenditure on education and economic growth; majority of the studies deal with endogenously generated economic growth and

stress on the role of human capital accumulation in economic growth. An investment in education is very beneficial to the society, both at the micro level as well as macro level and affects the economic growth both directly and indirectly.

Education has high economic value. A considerable part of the community's wealth must be invested for the same. Investment in education leads to the formation of human capital, comparable to physical capital and social capital, and that makes a significant contribution to economic growth. The policymakers argued that expenditures in social sector plays an essential role in the economic development of a country by maintaining law and order, providing economic infrastructure, harmonizing conflicts between private and social interests, increasing labor productivity through education and health and enhancing export industries. Baum and Lin (1993) examined the impact of three different types of government expenditures on the growth rate of per capita GDP using cross-section data from both developed and developing countries for the period of 1975-85. This study determined that expenditures on defense, welfare and education have different impacts on economic growth. The growth rate of educational expenditures has a significant positive impact on economic growth in all cases. Kevin(2000) explores the transition mechanism that might link the income inequality and economic growth. He found that public education expenditures are positively associated with future economic growth, although the contemporaneous effect upon growth is negative. Barro et al (2001) examines a panel data of around 100 countries observed from 1965 to 1995 and finds that growth is positively related to the starting level of average years of school attainment of adult males at the secondary and higher levels Education as an investment secures returns in the form of skilled manpower that geared to the needs of development, both for accelerating economic development and for improving the quality of the society.

According to Chemingui (2005) an increase in government expenditure devoted to the three priority areas i.e. agriculture, education, and health will affect the economy through increase in sectoral or economy-wide total factor productivity (TFP). Kamara et al. (2007) indicate that public expenditure on education is positively correlated with economic growth in African countries. Nah (1997) studied the impact of various types of social expenditures on economic growth by using the 1992 data for 68 countries with the help of rank correlation and regression techniques. The conclusions through ranking reveal that the advanced countries spend relatively greater proportions of their public expenditure on health and social security but the developing countries allocate disproportionately larger amount for educational development. Ansari and Singh (1997) used annual time series data from 1951 to 1987 to study the relationship between

public spending on education and growth in India. They found that there is no long run relationship between the two. Afzal et al (2010) conducted a study to investigate short-run and long-run linkage between school education and economic growth in Pakistan and confirmed the existence of direct relationship between them. In another study Chandra (2010) made an attempt to explore the causal relationship between government spending on education and economic growth of India using 1950-2009 data. The study shows that the direction of causation is from education expenditure to economic growth is not immediate to take effect, rather it can be said that investment in education is expected to affect economic growth of a country after some period.

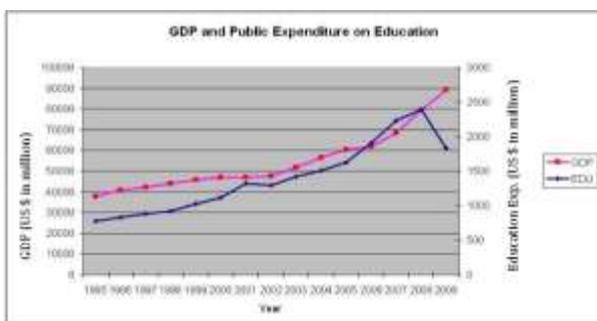
Education is an important determinant of economic growth for any country. On the other hand, Government budget policy affects the long-term growth rate through decisions on priority based public spending on different sectors. The study investigates the long-run relationship between public expenditure on education sector and economic growth in Bangladesh. An econometric model is applied to the analysis with time series data from 1995-2009. The result of the study shows that public spending in education has a positive and significant impact on economic growth in the long run. By employing Cointegration technique it is observed that a one percent increase in public expenditure in education contributes 0.34% increase in GDP per capita in the long run.

The study investigates the relationship between economic growth and public expenditure on education. The data set comprises of annual time series data for Bangladesh over the sample period of 1995-2009. The sources include World Development Indicators released by the World Bank and "Key Indicators of Asia and Pacific Countries" (Economics and Development resource Centre - Asian Development Bank). Economic growth is defined as the increase in a nation's ability to produce goods and services over time as is shown by increased production levels in the economy. There are numerous measures to depict economic growth and the study employed GDP per capita (US \$) as a proxy for economic growth. GDP per capita is measured as GDP divided by the total population of the country. The independent variable of the study is public expenditure on education (US \$). Public expenditure on education consists of current and capital public expenditure on education as such government spending on educational institutions (both public and private), education administration as well as subsidies for private entities (students/households and other privates entities). The descriptive statistics of the variables are shown in Table 6

Table 6: GDP per capita and expenditure on education as share of total budget and GDP

Year	GDP per capita (current US\$)	Public Expenditure in Education	
		(% of Total Budget)	(% of GDP)
1975	274.79	12.89	1.11
1980	324.68	6.15	0.94
1985	334.2	8.98	1.26
1991	387.26	10.33	1.80
1999	359.19	15.33	2.42
2000	363.64	14.99	2.38
2001	356.12	15.70	2.46
2002	354.30	15.76	2.32
2003	360.28	15.50	2.38
2004	407.99	14.83	2.25
2005	428.75	14.50	2.40
2006	434.64	14.24	2.46
2007	475.25	15.78	2.56
2008	546.85	13.99	2.39
2009	607.76	14.11	2.23

Figure 2 of the following page exhibits GDP (Current US \$ in million) and public expenditure on education (US \$ in million) of Bangladesh from the period of 1995-2009. The calculated average growth rate of GDP per capita (constant 2000 US \$) of Bangladesh is 3.91% which indicates that during the period of 1995 to 2009 GDP per capita has increased at an average rate of 3.91% per year. On the other hand, the acceleration rate of GDP per capita of Bangladesh is 0.16% which indicates that in future the growth rate of GDP per capita will be increasing at an average rate of 0.16% per year. Similarly, the calculated average growth rate of public expenditure on education of Bangladesh is 6.31% which indicates that during the period of 1995 to 2009 public expenditure on education has increased at an average rate of 6.31% per year.

**Figure 2: GDP and Public Expenditure on Education during 1995-2009**

CONCLUSION

This case study of functional relationship between public expenditure on education and economic growth of Bangladesh using data during the period of 1995-2009. The data is subject to unit root test to determine stationarity and also cointegration test. The study finds a positive and significant impact of public education expenditure on economic growth. The result shows that a 1% increase in education expenditure will increase GDP per capita by about 0.34% in the long run. The economy of Bangladesh can expect to grow by investing in education at a greater extent.

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