Public Expenditure

Concept

In order to carry on their functions, Governments must obtain the services of labor and other factor units and (except in a completely socialist economy) acquire goods produced by private business firms. Public expenditure consists of expenditure by central Government, state Governments and local authorities (such as municipalities and public corporations), with central Government accounting for the major portion of such expenditure. Thus, the state is required to maintain good roads, bridges, defense activities, canals and harbors, to protect trade, to maintain the coinage and to provide social security, education and religious instruction.

Public expenditure refers to the expenditure incurred by the central, state or local Government of a country for its own administration, social welfare, economic development and for providing help to other countries. Public expenditure has a great impact on the economic development of a country and the public welfare in a country.

Need/Importance/ Significance of Public Expenditure

In modern economic activities public expenditure has to play an important role. It helps to accelerate economic growth and ensure economic stability. Public Expenditure can promote economic development as follows:

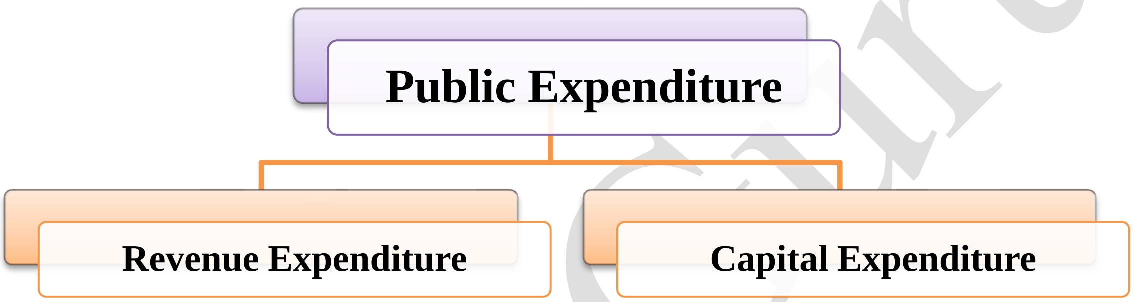
1. To promote rapid economic development.
2. To promote trade and commerce.
3. To promote rural development
4. To promote balanced regional growth
5. To develop agricultural and industrial sectors
6. To build socio-economic overheads e.g. roadways, railways, power etc.
7. To exploit and develop mineral resources like coal and oil.
8. To provide collective wants and maximize social welfare.

9. To promote full – employment and maintain price stability.

10. To ensure an equitable distribution of income.

Types of Public Expenditure

Public expenditure refers to estimated expenditure of the Government on its ‘development and non-development expenditure programmes’, or on its ‘pan and non-plan programmes’ during the fiscal year.



1. Revenue Expenditure

These are those expenditures which have the following characteristics:

a) **These expenditures do not create assets for the Government.** For example, expenditure by the Government on old-age pensions, salaries and scholarships are to be treated as revenue expenditure because these are just routine expenditures, not creating assets of any sort.

b) **These expenditures do not cause any reduction of liability of the Government.** Expenditure on the repayment of loans, for example, causes reduction of Government liability. Accordingly, this is not to be treated as revenue expenditure.

In short, revenue expenditure refers to estimated expenditure of the Government in a fiscal year which does not either create assets or cause a reduction in liabilities.

2. Capital Expenditure

Those expenditures of the Government are capital expenditures which:

a) **Create assets for the Government.** Equity (or shares) of the domestic or multinational corporations purchased by the Government may be cites as an example.

b) **Cause reduction in liabilities of the Government.** Repayment of loans certainly reduces liability of the Government. Accordingly, this is to be treated as capital expenditure.

In short, capital expenditure refers to the estimated expenditure of the Government in a fiscal year which either creates assets or causes a reduction in liabilities.

3. Other Types of Public Expenditure

Public expenditures are classified in many ways. However, principal types of public expenditure are as under:

1) **Development Expenditure:** Related to growth and development activities of the Government like expenditure on education, health, industry, agriculture, transport, roads, canals, rural development, water works and generation of power.

2) **Non-Development Expenditure:** Related to growth and non-development activities of the Government like expenditure on administration, police and military, law and order, collection of taxation, interest on loans, payment of old-age pensions, etc.

3) **Plan Expenditure:** Incurred by the Government for planned development programmes. This includes both consumption as well as investment expenditure by the Government or planning commission of the Government. For example, expenditure on agriculture, power, communication, industry, transport, public utilities, health and education.

4) **Non-Plan Expenditure:** Incurred beyond the purview of planned development programmes. This includes both consumption as well as investment expenditure by the Government. For example, expenditure on subsidies, defense, law and order as well as payment of interest on loans by the Government.

5) **Transfer Expenditure:** Not related to the production of goods and services or generation of income in the economy. These expenditures cause transfer of income from Government to the individuals and households. For example, scholarships and unemployment allowance by the Government.

6) **Non-Transfer Expenditure:** Result in the exchange of goods and services for money. These are real expenditures. These include payments made by the Government on the use of factor

services for production activities. For example, expenditure on weapons, education, post and telegraph, agricultural development and railways.

Effects of Public Expenditure

Public expenditure has a great bearing on economic development and social welfare of a country. Following observations may be noted in this regard:

1) On Production

According to **Dr. Dalton**, public expenditure tends to affect the level of production in the following manner:

a) **Effect on the Capacity to Work and Save:** As a result of public expenditure, capacity to work and save tends to rise. Government expenditure provides various kinds of social and economic facilities stimulating the capacity to work of the people. Increased capacity implies increased efficiency and greater employment. Level of income and saving tends to rise facilitating greater investment and adding to the pace of growth.

b) **Desire to Work and Save:** Expenditure incurred by the government includes the public's will to work and save. As a result, their income and standard of living tend to rise.

c) **Productive Utilization of Resources**: Public expenditure restores a balance in the economy by focusing on those areas of production which generate maximum linkages effect. Public expenditure acts as pump-priming, attracting idle resources to their productive utilization. Accordingly, production level tends to raise the resources from unproductive activities to productive ones. This results in increase in production.

2) On Distribution

Public expenditure has a salutary effect on distribution also. It affects distribution in the following possible ways:

a) **Regional Inequality:** In the capitalist economy, two methods can be adopted for removing the regional inequality by way of public expenditure: (i) The government expenditure should focus on development of backward areas, increasing the income of the people of those areas. Their standard of living will go up to get close to the living standards in developed areas. (ii) Public expenditure should render financial help to the small-scale and cottage industries. As a result of it, income of the people employed in these industries will increase. Besides, the government can increase the real wages of the people getting low salaries by giving them dearness allowance, travelling allowance, low-priced houses subsidized food and other facilities.

b) **Distribution of the Dividends of Industrial Development:** As a result of public expenditure, public sector industries in the country. The workers employed in these industries are paid higher wages. They get some facilities also better than others. Following the public sector industries, private-sector industries also provide higher wages and other facilities to the workers increase in the workers' wages will lead to the reduction in economic inequality.

c) **Benefit to the Weaker Section: P**ublic expenditure on social services like education, medical care, unemployment allowance, labor welfare, etc., made after collecting resources by way of taxes from the rich class, it will result in the increase in real income of the poor people, thus tilting the distribution further in favor of the latter.

d) **Increase in the Ability to work of The Poor:** Distribution of income can also be influences by increasing the ability to work of the poor with the help of public expenditure. This objective can be achieved in two ways: (i) **Direct Help:** The government can provide direct help to the poor people in the form of cash, commodities and service. (ii) **Indirect Help:** The government can provide loans to the poor at a low rate of interest. It can provide more social services to them. As a result of it, their efficiency will increase, and this will raise their income level and standard of living.