



# GUJARAT PUBLIC SECTOR RESOURCE MANAGEMENT

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**S. K. Shelat** has served as Chief Secretary to the Government of Gujarat State, India, since 1995. Prior appointments in his civil service career, which began in 1961, include three posts at the Principal Secretary rank: Finance (1993–1995), Agriculture and Rural Development Department (1993), and General Administration (Planning) (1992–1993). In addition, Mr. Shelat has held numerous other senior management positions, ranging from Secretary of Industries, Mines, and Energy to Commissioner of Training and Director, Sardar Patel Institute of Public Administration.

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**G**ujarat is one of the 26 States of India, occupying 196,024 sq. km. and having a population of 41.3 million.

Since its formation in 1960, Gujarat has achieved remarkable progress in economic development, and especially in industrialization. Following the economic liberalization policy initiated by the Government of India in 1991, Gujarat has been the number one State in attracting investment, and has projects worth US\$31 billion in the pipeline. However, despite all this, Gujarat's public sector is characterized by a structurally weak fiscal position, a large and inefficient State enterprise sector, and inadequate provision of basic infrastructure services such as ports, roads, and power.

The state's fiscal position weakened because of the lack of fiscal discipline and stagnation in tax revenues. State finances were also squeezed by slow growth in Central transfers, because of fiscal consolidation at the Central Government level, and restrictions on overdraft facility from the Central Bank, which forced the State to borrow increasingly at market-determined rates. Since 1991 the Government of Gujarat has adopted a cautious fiscal policy and was initially successful in curtailing the overall budget deficit from over 7 percent of the state's domestic product (SDP) in the early 1990s to 2.6 percent in 1993/94. But the Government was unable to sustain this fiscal adjustment, and the overall budget deficit rose again, reaching 4 percent of SDP in 1995/96. The reversal in fiscal consolidation in Gujarat is attributable to factors such as (i) stagnation in public revenues, (ii) inadequate control over public expenditures, and (iii) generally poor management of public resources.

The Government of Gujarat owns 54 State-owned Enterprises (SOEs), of which 37 are registered as companies and 17 as statutory corporations set up by State or Central legislation. SOEs are active in

most sectors of the economy, having a virtual monopoly in the mining, power, transport, and water sectors, and a dominant position in housing, finance, and social sectors. SOEs have been used to achieve a number of objectives, including employment creation, provision of subsidized services (such as power and transport), development of backward regions, and welfare of the weaker sections of the population. SOEs are vulnerable to political interference and suffer from the lack of commercial orientation, nonmerit-based managerial appointments, and inadequate reporting, accounting, and financial control systems.

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Infrastructure in Gujarat is overextended and cannot meet the growing demand of industrialization. The Government has estimated infrastructure investment requirements at over \$23 billion, which far exceeds the availability of public resources. The growing demand for infrastructure, the sharpening resource and implementation constraints, and the poor efficiency in delivery of services by the public sector have changed the Government's approach to infrastructure development. The Government has opened up all key infrastructure sectors to the private sector and is in the process of evolving an enabling policy environment that is transparent and provides adequate incentives to attract the required private investment.

### Public Sector Resource Management Program

The Gujarat Government set up a State Finance Commission in October 1992 to look at some of these issues, and the Commission submitted its report in May 1994. Also in 1994, the Asian Development Bank (ADB) initiated a process of dialogue with the Government of Gujarat which resulted in the approval of a loan of US\$250 million for the Gujarat

Public Sector Resource Management Program in 1996. The Government initiated a review of recommendations of the Finance Commission in 1994. Drawing on the recommendations of the Commission Report, the ADB simultaneously initiated a policy dialog in order to support implementation of the policy and institutional changes. Thus the Public Sector Resource Management Program is the continuation of a process of reform begun in 1994, in which the Gujarat Government and ADB have been partners from the very beginning.

The Resource Management Program is aimed at augmenting domestic resource mobilization, improving allocation and efficiency of the public sector, reducing the State's role in commercial activities, and promoting market-oriented policies to enhance private sector participation in the economy, particularly in the infrastructure sector. These objective are to be achieved by three initiatives:

- improving the management of the State's public finances;
- privatizing, divesting, or restructuring the SOEs; and
- strengthening the policy, regulatory, and institutional frameworks for the infrastructure sector.

1. Improving the Management of the State's Public Finances

The Program supports the formulation, adoption, and implementation of the Medium-term Fiscal Policy Framework for the period 1997/98 to 1999/2000, under which the overall fiscal deficit will be reduced from 4 per cent of SDP in 1996/97 to about 2 percent in 1999/2000. The reduction in the fiscal deficit will take place despite the substantive cost of structural reforms included in the Program, such as

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the rationalization of taxes and restructuring of SOEs. The key elements of tax reforms envisaged include the simplification and rationalization of the sales tax structure to improve its transparency and efficiency. The reforms of the sales tax have been designed to facilitate eventual introduction of a value added tax in line with the adoption of VAT by neighboring states. The Program supports rationalization of the rate structure of stamp duty, entertainment tax, and motor vehicle tax. An important element of the expenditure reform is the introduction of the Core Investment Program at aggregate and sector level.

## 2. Privatizing, Divesting or Restructuring the SOEs

The Program focuses on privatization, divestment and restructuring of 23 of the 54 SOEs. The subset of SOEs targeted under the Program includes a mix of strategic enterprises, key state financial intermediaries, and SOEs that perform overlapping developmental and social functions. The SOEs include a combination of both profit-making and loss-incurring enterprises.

The SOE reform program in Gujarat is the first comprehensive attempt towards privatization. In designing this Program appropriate institutional framework and policies have been put in place in advance to insulate the reforms from political disruption. The Government, for example, set up a high-level subcommittee headed by the Chief Minister to approve proposals of SOE reform. The technical work of privatization and restructuring is being handled by a Technical Secretariat and the Price Waterhouse International Group supported through a Bank technical assistance.

To facilitate privatization/restructuring, the Government set up a State Renewal Fund to finance the debt and labor liabilities of the SOEs.

### 3. Strengthening the Policy, Regulatory, and Institutional Frameworks for the Infrastructure Sector

The Program supports the creation of an enabling policy, regulatory, and institutional environment for private sector participation in the power, ports, and roads subsectors. The key objective of infrastructure reform is to evolve greater transparency and stability in the policy environment. This involves (i) introducing guidelines for transparent competitive bidding procedures and internationally accepted terms for financing of infrastructure projects, (ii) restructuring of public sector agencies that handle the infrastructure sector with a view to promoting commercial orientation and an effective partnership for public and private sector development, and (iii) a sound regulatory mechanism in the post-privatization era that serves both efficiency and equity goals.

The Program loan from the Bank will assist the Government in carrying out the structural reforms as it will enable the State to

- bear the cost of restructuring the Public Enterprise Sector which would involve the closure of nonviable units, such as the Gujarat State Textile Corporation, and the sale, merger, or downsizing of others;
- absorb the impact of the initial decline in Government revenues likely to result from the tax reforms and rationalization;
- protect a core investment program from ad hoc budget cuts; and
- enable the release of funds for social sectors by transferring some areas from public to private sector funding.

## Institutional Strengthening

As part of the Program, the Government will set up the Gujarat Infrastructure Development Body which will be responsible for the following functions:

- rationalization of sector development/master plans into a single intersectoral development plan;
- prioritization of specific projects within sectors and between sectors;
- assistance to private sector project proponents regarding project financial packaging; and
- administration of a project development assistance fund.

In this regard the Bank has provided a technical assistance to build capacity of the Gujarat Infrastructure Development Body to advise on policy, legal, and regulatory frameworks of key infrastructure sectors, as well as in the area of assessing, financing, and promoting infrastructure projects, including build-own-operate and build-own-transfer projects.

Additionally, institutional strengthening of the various Government departments for the effective implementation of reforms is planned under the Program. This includes the strengthening of the Finance Department, for which a Bank technical assistance will support the development of skills in

- budget policy formulation and projections,
- expenditure management and control,
- formulation of tax reforms, and
- treasury and debt management operations.

The Finance Department will be assisted by a State Public Finance Reform committee and working groups on tax reforms, expenditure management and control, and computerization and training. The

computerization of tax, expenditure, and debt records will upgrade the overall budgetary management and control systems. The Program will also support the reorganization, streamlining, and strengthening of the State tax administration with the establishment of a Directorate of Taxation.

Finally, the Bank is providing a technical assistance to train and advise policymakers and heads of SOEs in the modalities and techniques of privatization. To start off, some key officials closely involved in the process of privatization have attended courses on privatization and restructuring, and a workshop is scheduled to be held later in the year to provide greater exposure to officials on the privatization program and its techniques.

## Future Developments

Once the Program is completed, it is expected that Gujarat will be on the road to self-reliance in terms of resource mobilization, coupled with improvement in the quality of life resulting from the increased investment in social infrastructure.

In the Power sector, the most crucial for the State, the present capacity will be raised from 6000 MW to 15000 MW in five years, of which 8330 MW will be through private sector initiative. Also, for the first time, it is proposed to invite the private sector into power distribution. This initiative should instill further confidence among the independent power producers. Privatization of distribution should also help free the Government from the subsidy culture in the agriculture sector and reduce current excessive line losses.

In future, it is expected that private sector investment will grow not only in the ports, power, and roads sectors, but also in the social sectors. For instance, it is expected that secondary and tertiary

education, on which the State spends nearly US\$20 million per annum, could be gradually privatized by eliminating controls over fees. The public funds so released could then be used for the improvement of primary education. Similarly, in the health field it is proposed to involve private donors and institutions to supplement the infrastructure of Government Hospitals, thereby augmenting and improving the services for the poorest sections of the society. Also, private doctors will be allowed to use the facilities at Government Hospitals and Dispensaries, thus reducing their costs and fees.

A separate State Finance Commission for Local and Municipal Bodies has been set up and its report is expected by June 1997, covering a wide range of reforms and devolution of resources from the State to the local authorities, that will link reward to performance.

State Government would vacate areas that can be successfully operated by the private sector and would become more lean and clean, to perform its basic task of maintaining law and order and providing basic social services and thus making poverty alleviation easier.

To conclude, Gujarat is now on the threshold of both economic resurgence and social upliftment. In five years it will be able to compete with some of the Asian tigers, such as Indonesia; Malaysia; Singapore; and Taipei, China. In this transformation the Bank's assistance will have played a significant role.

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