Changing the state-economy relationship: some unreasonable thoughts

Abhijit V. Banerjee
The state is everywhere

• Quite literally
  – Education
  – Healthcare
  – Public health
  – Banking/Finance
  – Infrastructure
  – Industry
  – Agriculture
  – Labor markets
  – Land markets
  – Media
  – Environment
  – Army/poilce
  – Private lives
  – Etc.

• As a owner, operator, financier, buyer, seller, regulator, taxman, redistributor, protector, moral guide..
We run all of this with

- Less than 5000 IAS
- Similar numbers of IPS and other elite civil services—railways, revenue service, audit and accounts.
- Elite public sector corps—banking, ONGC etc.
- May be 50,000 really empowered people
We run it very badly

- Kenya has higher “ASER” scores than we have—even though they have many more language issues
- Our PISA scores (from Tamil Nadu) are the second worst in the world
- 80 percent of all healthcare visits are to non-government facilities
  - 80 percent of those practicing medicine in those facilities are not qualified to do so
- Bangladesh does better on infant mortality
  - Many countries in SSA do better on immunization.
- We have many of the most polluted cities in the world but relatively little manufacturing
- Our police registers less than 50% of cases that people try to register and 1 in 10 property crimes are reported
- We have (of honestly reported) perhaps 20% NPA in public sector banks
- Our infrastructure is an embarrassment
- And so on..
We need a bigger government

• That does a lot less
• What should we cut?
• Are we worse as owner/operators or as regulators?

As owners
  – Labor is overpaid and underworked
  – Lots of wage compression—talent is not necessarily rewarded
  – Subject to populist pressures—free power and water, loan write offs

As regulators
  – Subject huge hold up problems—badly designed contracts
  – Corruption/capture/indifference/incompetence
A little bit of indirect evidence

• Two experiments in Gujarat by Duflo, Greenstone, Pande

1. Who pays the (environmental) auditor?
   – Standard model—firms pay
   – Alternative—paid from a central pool
   – Makes a huge difference—the state as regulator of auditors fails completely

2. Intensity of (environmental) inspections by the government inspectors
   • Had almost no effect on pollution—because the worst polluters were being inspected and punished already
   • State as an implementer was reasonably effective
   • Not clear how general this is.
What would an “economist” say?

• Let the market do the things where the market can in principle work
  – Education, healthcare, food, fertilizer
  – Provide effective certification of outcomes
• And where it just needs price-quality regulation—do just that
  – Distribution of water and power, sewer removal services
• Make (rather than buy) where the possibility of hold up is huge
  – Infrastructure, hospitals, educational institutions
  – But if you buy, go for the final product and a uniform price for all sellers
• Try to cut loose the financial sector
  – Never really works
  – So let them at least buy competence
• Focus on things where the market price is wrong
  – Environment, public health, policing, land
Why is this wrong?

• Redistribution away from the poor?
• Credit constraints—say for investing in education
• Merit goods—we don’t want no one to die because of they are poor. Or to not have water
• Behavioral issues—savings, health etc.
• Unconventional externalities:
  – Antibiotic resistance
  – Clean cook-stoves
Taking these into account: An unreasonable (but mostly standard) proposal

- Large universal cash transfers—age, disability and gender based
  - Require going and claiming it every week to discourage the non-poor
- Subsidize savings—pay high interest on the first X thousand in savings
  - Security against risk and old age
- Shut down the government school system (give out vouchers?)
  - Increase in the supply of private schools--prices down and quality up
- Introduce generous scholarships based on “merit”
- Shut down sub-centers and PHCs
  - Transfer the resources to many more public hospitals in central locations, ambulances and cheap life-saving drugs
  - And in giving incentives for peri-natal/health checks, immunization
  - (Don’t pin your hopes on health insurance)
- Some drinking water given free--then charge the usual cost-plus price.
And then

• Focus on things where the market price is wrong
  – Environment, public health, policing, land

• Don’t be shy of using incentives and subsidies widely
  – Give out clean cook-stoves (make them work first), clean fuels (if you cut kerosene subsidy, do you get more coal burnt?)

• Very difficult to judge success
  – limited market metrics of success
  – Requires careful evaluations
The objections

• How could you....?
  – The poor are much more practical about these things than their defenders
  – Some entitlements (like free rural power and water) will be hard to take away
• The government
  – Massive shrinkage in opportunities for rent-seeking
  – Inflation tax finances the government—inconsistent with protecting savings
  – Raise taxation (wealth taxes, estate taxes)
• The teachers and the health workers will have a fit
  – Important to fight this fight—distorts the entire labor market.
• Corruption: we are staking a lot on one transfer—we need some backup protection.