Fiscal Transfers from the Union to States and Healthcare in India

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This study delves into the intricate relationship between fiscal transfers by the Union[1] to States and States' own revenue in shaping health spending by States in India. Focusing on the period beginning 2004-05 (when the National Rural Health Mission—NHM—was constituted), this study seeks answers to the following four key questions: (i) How have fiscal transfers from the Union government to States evolved over the last 20 years? (ii) How has health spending by States shaped in light of changes in their own revenue as well as fiscal transfers from the Union? (iii) Do States substitute their non-NHM health spending with NHM spending? (iv) To what extent inter-state or horizontal inequalities in healthcare spending have been addressed post-NRHM?

The study found that the share of States' own revenue in their total revenue receipts declined sharply from 2014-15, with a simultaneous rise in fiscal transfers from the Union government, primarily driven by conditional transfers, particularly those from Centrally Sponsored Schemes (CSSs). The share of tax devolutions increased initially immediately after the recommendations of the Fourteenth Finance Commission (FC-XIV), but declined by 2019-20.

Health spending increased post-NHM, driven mainly by States, yet remained broadly unchanged over a 30-year period. The central government has also expanded its footprints in healthcare post-NRHM, though the nature of its involvement has changed. In the first five years after the introduction of NRHM, its role in healthcare expanded through CSSs, but thereafter through central sector schemes.

The States' own revenue and unconditional transfers positively impacted health spending, though the impact of the latter was more significant than that of the former. However, the results varied when States were categorised into economically well-off states and economically weaker states. Economically well-off states tend to rely more on their own revenue than unconditional fiscal transfers from the Union government for their health spending. In contrast, economically weaker states depend solely on unconditional fiscal transfers for health spending, with their own revenues having no impact.

[1] The terms union, union government, and the central government have been used inter-changeably in this paper.

States, in general, substituted non-NHM health spending with NHM contributions. However, the extent of substitution was much more pronounced in the case of economically weaker states than economically well-off states. Post-NRHM, there was no evidence of States with initially low health spending catching up with those with high health spending levels. Horizontal inequalities in health spending widened somewhat in the post-NHM period for all States, as well as high focus states.

These findings have significant policy implications. The finding that unconditional transfers matter more for health spending by economically weaker states suggests that greater resource transfers from the Central government to states will spur health spending. The finding that health-specific transfers do not impact health spending, combined with the finding that States, especially economically weaker states, substitute health spending, suggests that the NHM has limitations in promoting health spending by States. This could be due to a lack of ownership of healthcare schemes sponsored by the Central Government. Therefore, there is a need for a more flexible approach for centrally sponsored schemes for States to innovate and adapt. The evidence of growing horizontal inequalities post-NHM suggests a need to rethink the NHM's strategy and focus in health spending. Prioritising unconditional transfers and designing a differentiated strategy for economically richer and economically weaker states could be expected to result in better healthcare outcomes in India.

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