Research Paper *IJMSRR*
*Impact Factor :**3.029*** *E- ISSN - 2349-6746*
ISSN -2349-6738

GROWTH AND PUBLIC DEBT SCENARIO OF NORTH EASTERN STATES OF INDIA

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Abstract
The north eastern states are endowed with huge natural resources and they have been receiving special assistance from the center due to special category status. However it has been observed that the economic performance of these states is not satisfactory rather suffering from huge mounting public debt. In this context this paper has examined the sector wise growth and public debt scenario.

***Key Words: North Eastern States of India, Debt Scenario, State Domestic Period**.*

1. INTRODUCTION

There are 28 states and 7 union territories in India. Politically the country can be divided in to 6 regions such as Central India, East India, North India, South India, West India and North East India. The North East India[1] consists of eight states such as Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim[2] and Tripura. Excluding Sikkim, the other north eastern states are popularly known as 7 sister states. The north eastern states, as a region occupy 8% of India's geographical area and home to 4% of country's population. At the national level, these states stand way below in comparison with the rest of India. The annual per capita income of north east region is 6,625 INR against the rest of India average of 10,254 INR and nearly 34.28% of the population is below poverty line as compared to the national average of 26.1% but, the north east region is a highly literate region registering 64.8% of literacy rate except for Arunachal Pradesh (Census, 2001).

These states are unique in most respects and have similar economic and geographical characteristics. Endowed with huge natural resources in terms of forests, biological diversity and hydroelectricity but the region has remained largely underdeveloped. It is well accepted that as such these states are late starters of development and suffering from poor infrastructure and limited connectivity, both within the region as well as outside the region. The north east region is connected with the rest of India by a narrow stretch of land called the 'chicken's neck[3]'. In addition to their geographical bottlenecks, these states are witnessing a series of insurgencies and are alienated from the economic resurgence that the rest of the country is experiencing.

The above condition of these states merits special policy interventions since they need infrastructural support and ensure significant investments and developmental aids. Therefore, all north east states are officially declared as special category states[4] in the context of centre-state fiscal federalism setup of India. On the basis of special states provisions, they avail special grant provision in the context of revenue devolution from centre to states. Further in the recent days, important prescription for special category states is interest free loan with rationalization of public expenditure based on growth enhancing sectoral allocation of resources. However, today, the North East Region is in limelight and their issues has become more significant and serious particularly after the initiative of central government in terms of its India's look East Policy (LEP)[5] because it has been realized by Indian policy makers (especially after the inclusion of Myanmar into ASEAN as full member in 1997), that development of physical connectivity between North East Region and Southeast Asia is a prerequisite to utilize the opportunities provided by India's Look East Policy.

1.1. Objective and Research Methodology

In the above context, the basic objective of this paper is to observe the growth of state domestic product and debt scenario of north eastern states.

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[1] *Please visit https://en.wikipedia.org/wiki/Northeast_India for a brief idea about North East India.*

[2] *Sikkim was recognized as a part of North-East states in the 1990s and integrated as the eighth North Eastern Council state in 2002.*

[3] *It is formally the Siliguri Corridor, a narrow strip of Indian territory connecting the northeastern states to the rest of India.*

[4] *Other than the NE States, other special category states in India are Himachal Pradesh, Jammu Kashmir and Uttarakhand.*

[5] *In the year 1991-92, under the then Prime Minister, P.V. Narasimha Rao, India launched its "Look East" Policy (LEP), an active economic policy of engagement with Southeast Asia to be implemented as an official initiative in achieving two objectives: the encouragement of trade links with individual partners and to provide foreign employment for India's own expanding work force.*

IJMSRR
E- ISSN - 2349-6746
ISSN -2349-6738

The present study is essentially explorative in nature. It makes a statistical analysis of data on state finances in general and public debt in particular of north eastern states. Necessary comparisons have been made with 14 major states and all states of India.

All analysis of this study is based on secondary date which are collected from sources like "Hand Book of Statistics on State Government Finances", Published by Reserve Bank of India, "Handbook of statistics on Indian Economy", Published by Reserve Bank of India, "Reserve Bank of India occasional papers", Published by Reserve Bank of India, Different volumes of publication on state government budget and white Papers Published by the respective state governments, and data on different economic indicator compiled by www.indiastat.com.

Data collected from the above sources have been analyzed, tabulated and interpreted. Statistical tools like percentages, growth rates have been used. Whenever necessary, appropriate other statistical and econometrics techniques have been used for tabulation, presentation, and interpretation of data by estimating different relevant fiscal parameters.

1.3. Issue of Concern

When the development of north eastern states is a major concern, the unsatisfactory performance of these states in their economic growth and development and continuing fiscal imbalances in terms of mounting debt burden even after availing special central financial assistance is also a major concern in the recent days. It has drawn attention of people particularly in the context of role of central assistance and rate of development. The argument is, 'though the these states are getting special assistance from the centre because of their special state status still their development is not satisfactory rather they are suffering from fiscal imbalances and social conflict'. The states are suffering from high debt burden and not being able to finance the developmental expenditure in a satisfactory way. Whether they are debt sustainable or not and whether they are able increase the pace of development or not are big questions to address. In this context, the World Bank describes the economic condition of this region as a low-level equilibrium of poverty[6], non-development, civil conflict and lack of faith in political leadership.

1.4. Role of Central Assistance

Social scientist view that the grant given by the centre is not working for development rather it is helping for social conflict in terms of terrorism or insurgency. For example Rahman (2013)[7] explains "There is input of terrorism (commonly referred to euphemistically as 'insurgency') where there has been so little of industrial activity in the last 30 years, people have managed to turn terrorism into an industry. It got started as a cottage industry, but has now become a medium-scale industry of sorts. If we give it a few more years, we shall probably see terrorism turned into a heavy industry. This is what happens when the benevolent centre keeps on giving huge dollops of grants to states even when the States fail to show any performance or even to establish convincingly how and where the money was spent".

Further, it is also argued that there is no hard budget constraint for these states because the central transfer is high but the general category states suffer from hard budget constraint. Through the enactment of Fiscal Responsibility and Budget Management Act (FRBM), these states are also availing themselves of the benefit of debt swapping and debt relief schemes which facilitate reduction of the average annual rate of interest. There is a necessity of developing all these states at par with other states which can only be possible if all these states are guided by the norms of inter-state equity based on fiscal efficiency (Rana, 2012)[8].

In addition to the above issues, the fiscal-federalism set up has been questioned in different context relating to the provision of grant and loans for general/major category states and special category states.

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6 *Under certain conditions, an economy, region or household can find itself in a "poverty trap." This is a stable equilibrium but at a low level of wealth and output, and it cannot get out of this low-level equilibrium (sometimes called a "low-level attractor") without a potentially large injection of external assistance. Similarly, with a sufficiently large negative shock, the economy or individual might fall into this low-level equilibrium.*

7 *Please visit http://inpec.in/2013/05/14/the-north-east-in-indias-look-east-policy/ for a discussion on the issue.*

8 *Please visit for a discussion http://www.mightylaws.in/985/concept-special-category-states-india.*

IJMSRR
E- ISSN - 2349-6746
ISSN -2349-6738

To explain, according to the constitutional provision[9] there is clear cut division of power and responsibility between central and state governments. The justification behind such division of power and responsibility is that it will promote economic and political efficiency, regional balance and free flow of interstate trade (Lekhi 2007)[10]. Thirdly uniformity should be ensured in all areas of federation so that no preference is given to one state over the other with regards to payment of federal taxes (Mishra and Puri 2007)[11]. Therefore a well-developed mechanism of centre state fiscal relationship has been developed so as to have a micro economic efficiency and macroeconomic stability.

1.5. Role of Finance and Planning Commission

According to the provision, in the context of revenue transfer from centre to states, two important institutions participate namely; Finance Commission (FC)[12] and Planning Commission (PC) along with other grants and aid from the ministries and other sources. Further, to avoid vertical imbalances (between center and states) and horizontal imbalances (among different states), the constitution has also made provision of tax sharing between centre and state i.e proceeds of certain centrally levied taxes (e.g., non-corporate income tax, Article 270; and Union excise duty, Article 272) along with grants provision to the states from the Consolidated Fund of India (under Article 275).

So far as the FC's approach to federal transfers is concerned, it consists of (i) Assessing overall budgetary requirements of the center and states to determine the resources available for transfer from the center during the period of recommendation, (ii) Projecting states' own revenues and non-plan current expenditures, (iii) Determining the aggregate and individual states' share of the consolidated fund of the center, and (iv) Using grants to fill projected expenditure-revenue gaps remaining after tax devolution.

Grants recommended by the FCs are typically been based on projected gaps between non-plan current expenditures and post-tax devolution revenues. Although some commissions have attempted to enhance outlays on specified services in the states by making closed-ended specific purpose non-matching grants, generally these are unconditional. In either case, the incentive problems with this "gap-filling" approach are obvious. It is argued that the gap filling approach of the FC has been acting as pervasive incentive to go for none plan expenditure at the state level.

While the FC decides on tax shares and makes grants, the PC makes grants and loans on the basis of Gadgil formula[13] in the ratio 30:70 for general category states and 90:10 for special category states (NE states) for implementing development plans. This unequal provision of grants and loan is a major topic of discussion.

Further, as development planning gained emphasis; the PC became a major dispenser of such funds to the states. As there is no specific provision in the constitution for such plan transfers, the central government channeled them under the

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[9] *The Article-246 of the Indian constitution speaks about three lists such as Union List, State List and Concurrent list. The Union List is enumerated in List-I in the seventh schedule of the constitution which contains 97 items on which the parliament has exclusive powers to make laws. The second list contains 66 items on which the state legislature has the exclusive power to make laws and the third list contains 46 items on which both state legislature and the parliament has joint power to make laws.*

[10] *See for detail argument Lekhi R K (2007) Public Finance" pp 435-436.*

[11] *See for detail argument (Mishra and Puri , 2007) , pp.873-894.*

[12] *The Constitution of India envisages setting up of a Finance Commission every five years under Article 280 towards harmonizing the revenue and expenditure of the Union and State Governments in such a manner that the mismatch between powers to raise revenues and expenditure commitments to meet the functional responsibilities as envisaged under the subject lists i.e., the Union List, the State List and the Concurrent List is appropriately addressed and mitigated.*

[13] *The Gadgil formula was formulated with the formulation of the fourth five year plan for the distribution of plan transfers amongst the states. It was named after the then deputy chairman of the Planning Commission Dr. D R Gadgil. The central assistance provided for in the first three plans and annual plans of 1966-1969 lacked objectivity in its formulation and did not lead to equal and balanced growth in the states. The National development council (NDC) approved the following formula: 1. Special Category states like Assam, Jammu and Kashmir and Nagaland were given preference. Their needs should first be met out of the total pool of Central assistance. 2. The remaining balance of the Central assistance should be distributed among the remaining States on the basis of the following criteria: (i) 60 per cent on the basis of population; (ii) 10 per cent on the basis of tax effort, determined on the basis of individual State's per capita tax receipts as percentage of the State's per capita income; (iii) 10 per cent on the basis of per capita State income, assistance going only to States whose per capita incomes are below the national average; (iv) 10 per cent on the basis of spill-over into the Fourth Plan of major continuing irrigation and power projects; (v) 10 per cent for special problems of individual States.*

miscellaneous – and limited – provisions of Article 282. Before 1969, plan transfers were project-based. Since then, the distribution has been done on the basis of a consensus formula decided by the National Development Council (NDC)[14].

As with the FC formula, the PC tries to aggregate disparate objectives in its calculations, with the result that the overall impact is less than clear. One major contrast with the FC is the conditional nature of PC transfers. However, while the special category states (north eastern states) receive plan transfers based on projects that they formulate and submit, the general category states' plan transfers are not related to the required size or composition of plan investments.

Hence there is not even implicit matching of states' own resource commitments in this transfer channel, let alone an explicit matching formula. The process for determining plan transfers involves competing proposals from the PC and the states, with a certain amount of bargaining through the NDC, as well as in state-by-state discussions, to determine plan loans and grants. At the end of this process, the PC approves the state plans. At the margin, it is mainly the states' own resource position that determines their plan expenditures (Singh, 2006, pp 6).

Apart from resource transfer through FC and PC, resource transfer also happens thorough various ministries[15]. central ministries give grants to their counterparts in the states for specified projects, either wholly funded by the center (central sector projects) or requiring the states to share the cost (centrally sponsored schemes). Both these categories are reported together as central schemes.

The rationale for these programs is financing activities with a high degree of inter-state spillovers, or which are merit goods e.g., poverty alleviation and family planning but they are often driven by pork-barrel objectives[16].

These projects are supposed to be monitored by the PC, and coordinated with the overall state plans – which is why they are typically listed under Plan transfers, but both monitoring and coordination are relatively ineffective. There are over 100 schemes, and attempts to consolidate them into broad sectoral programs have been unsuccessful. These programs have provided the central government with an instrument to actively influence states' spending, replacing pre-1969 plan transfers in this role. The proliferation of schemes may also have increased the size

In addition to explicit transfers, intergovernmental loans to the extent that they are subsidized[17] or completely written off, also constitute implicit transfers to sub national governments.

Ideally, borrowing should be to finance investment, but state governments in general have increasingly used borrowing to meet current expenditure needs (now as much as 50 percent). State governments need central government approval to borrow from the market if they are indebted to the center, and this constraint binds for all the states. Central loans (including Planning Commission and ministry-based project loans) now constitute about 60 percent of the states' indebtedness, with another 22 percent being market borrowing, and the remainder made up of pension funds, shares of rural small savings, and required holdings of state government bonds by commercial banks (Rao and Singh, 2002; Srinivasan , 2002). While these captive sources of finance are limited, the states have been able to soften their budget constraints further by off-budget borrowing or nonpayment by their Public Sector Enterprises (PSEs). For example, the State Electricity Boards (SEBs) have

[14] *The NDC is chaired by the Prime Minister, and its members include all central cabinet ministers, Chief Ministers of the states, and members of the Planning Commission. Like the ISC, it serves as a bargaining and log-rolling body, though with a much narrower scope.*

[15] *'DONER' The Ministry of Development of North Eastern Region is responsible for the matters relating to the planning, execution and monitoring of development schemes and projects in the North Eastern Region. Its vision is to accelerate the pace of socio-economic development of the Region so that it may enjoy growth parity with the rest of the country.*

[16] *Pork barrel spending is a type of appropriated expenditure that is added into a non-related Congressional bill. The Oxford English dictionary differentiates pork barrel spending from normal appropriation spending as government funded projects "designed to please... and win votes" among congressional members. This is done so that the congressional bill that the pork barrel spending is attached to passes through the legislation process. While it may help some bills get passed through the legislative process, pork barrel spending is often considered a wasteful use of taxpayer funds because it benefits select constituents of Congressional members rather than the country as a whole.*

[17] *In some cases, central loans have been at higher than notional market rates, but it is not completely clear that those market rates would have been operative for sub national debt subject to risk without central guarantees.*

IJMSRR
E- ISSN - 2349-6746
ISSN -2349-6738

been tardy in paying the National Thermal Power Corporation (NTPC), a central PSE (Srinivasan, 2002). Other sources of softness in state government budget constraints include central government guarantees of loans made to state government PSEs by external agencies, and write-offs of past loans made to state governments. These write-offs have regularly been a part of Finance Commissions' recommendations as debt relief for the states.

It must be realized in the context of India that informal institutional norms and procedures, and formal legislative frameworks all play a role in determining fiscal behavior and outcomes at the state level. In particular, the system of intergovernmental relations, as it developed, combined poor explicit incentives for sub-national fiscal discipline with political and administrative controls to compensate. The current problems of state finances can be seen as the consequence of a relaxation of the latter controls, without complementary reforms in explicit incentives (Rao and Sing, 2005)

Taking above as the base, if we look in to the economic condition of north eastern states the economic performance of north eastern states is deteriorating. Comparing with the national average, the sector wise growth of GSDP of north eastern states is more than the national average, but the annual growth is deteriorating, simultaneously with a decreasing trend of public expenditure as a percentage of GSDP which is resulting in increasing debt.

Thus, to understand the economic condition of these states in general and fiscal condition in particular the following section is presenting about growth scenario of north eastern states.

2. DATA ANALYSIS AND INTERPRETATION

2.1. Growth of Sector wise State Domestic Product (SDP), Population and Per-capita SDP (PCSDP)

The State Domestic Product or SDP is the indicator of the performance of an economy. Table-1 presents the real growth rate of SDP, population and per-capita GSDP of north eastern states and India during 2004-05 to 2009-10. According to the table, the agriculture sector of all north eastern states has grown at a rate more than the national average. The real growth of industrial sector of all north eastern states is more than the growth rate of national average except two states such as Assam and Manipur. Similarly, the growth of service sector of north eastern states is observed to be more than the national average. Growth of population of north eastern states in average is almost equivalent to the population growth rate of India. In the case of two states such as Arunachal Pradesh and Mizoram the growth rate of population is more than the national average. The per-capita SDP (PCSDP) is another important indicator about productivity. The average PCSDP of north eastern states is observed to be more than the national average and also for individual states the PCSDP is more than the national average.

Table: 1 Sector Wise Growth Rate of State Domestic Product (SDP) 2004-05 to 2009-10

State	Agriculture	Industry	Service	Population	PCSDP
	2004-05 to 2009-10	**2004-05 To 2009-10**	**2004-05 to 2009-10**	**2004-05 To 2009-10**	**2004-05 to 2009-10**
Arunachal Pradesh	18.25	15.76	18.49	2.26	12.63
Assam	10.79	8.93	13.22	1.33	9.96
Manipur	11.33	6.66	12.42	1.95	7.73
Meghalaya	10.20	20.45	14.06	1.21	13.44
Mizoram	17.26	17.85	14.82	2.56	11.87
Nagaland	6.14	19.07	14.12	1.64	10.68
Sikkim	11.15	40.71	17.43	1.24	23.77
Tripura	5.01	14.16	12.14	1.21	10.03
Average of NE States	11.26	17.94	14.58	1.67	12.51
India	3.16	9.23	8.58	1.59	5.44

Source: Authors Own Calculation on the basis data collected from Data net India from: Central Statistical Organization, Indiastat.com

IJMSRR
E- ISSN - 2349-6746
ISSN -2349-6738

2.2. Annual Growth of GSDP

The annual percentage growth rate of GSDP of north eastern states and India at current prices has been presented in Table-2. It can be observed from Table-2 that states such as Assam and Manipur have experienced negative growth in most of the years during 2001-05 and even during 2005-06.There were less growth than the national average. Similarly, most of the north eastern states are registering annual growth of less than the national average. The north eastern states on average are having less growth of GSDP in comparison to the national average.

Table - 2 State-Wise Percentage Growth over Previous Year of Gross State Domestic Product (GSDP) At Current Prices Based on 1999-2000/2004-2005 Series In North-Eastern India (2000-2001 to 2011-2012-Upto 01.08.2012)

States	Based on 1999-2000 Series					Based on 2004-2005 Series						
	2000-2001	**2001-2002**	**2002-2003**	**2003-2004**	**2004-2005**	**2005-2006**	**2006-2007**	**2007-2008**	**2008-2009**	**2009-2010**	**2010-2011**	**2011-2012***
Arunachal Pradesh	10.86	17.74	-1.57	14.34	20.48	7.65	9.4	17.09	18.23	24.58	16.2	13.65
Assam	5.69	4.07	13.3	8.98	11.05	11.21	8.94	9.87	14.07	14.39	12.16	10.95
Manipur	-4.54	8.26	4.07	13.49	14.8	11.4	7.33	10.53	9.08	12.37	10.63	10.76
Meghalaya	10.7	13.05	6.36	10.85	9.94	10.76	18.72	12.87	19.33	9.4	10.83	12.84
Mizoram	12.06	12.09	11.25	7.34	5.59	10.78	10.74	15.99	19.94	14.92	15.17	NA
Nagaland	21.31	16.86	12.46	7.72	6.8	12.83	10.15	11.27	16.85	11.35	6.5	8.44
Sikkim	13.17	12.03	12.32	12.07	12.03	14.61	8.43	15.96	28.85	29.93	16.5	17.56
Tripura	12.99	15.84	5.7	12.15	9.88	10.35	11.07	8.09	15.05	13.08	13.29	13.48
Average of NE States	10.28	12.49	7.98	10.86	11.32	11.19	10.59	12.70	10.67	16.25	12.66	12.52
India	**7.75**	**8.97**	**7.8**	**12.24**	**13.38**	**14.1**	**16.6**	**15.91**	**15.75**	**14.86**	**17.5**	**15.02**
Note: Abbr. **: NA :** Not Available												
Source: Compiled by Datanet India from: Central Statistical Organization.												

2.3. Public Expenditure as a Percentage of GSDP

The expenditure of the states out of GSDP indicates the state's role for income generation. In this context literature suggest that the non-infrastructure category of the service sector contributes disproportionately to the growth of service sector particularly in the context of north eastern states[18]. The Table-3 reveals that the public expenditure as a percentage of GSDP on average for north eastern states has declined during the period 1991 to 2009. However, it is observed in Table -4 that on average the public debt as a percentage of GSDP has increased over the period.

[18] *See Nayak and Rath (2010)*

Table-3 Public Expenditure as a Percentage of GSDP

State	1991-95	1995-00	2000-05	2005-09
	Average	Average	Average	Average
Arunachal Pradesh	68.89	69.33	73.46	87.24
Assam	23.19	22.01	23.08	25.89
Manipur	55.70	53.65	55.61	52.44
Meghalaya	40.58	35.65	32.93	39.02
Mizoram	77.90	76.85	72.15	75.94
Nagaland	67.27	57.24	45.71	42.15
Sikkim	74.49	77.17	75.10	78.74
Tripura	44.93	40.86	37.41	36.83
NE States Average	37.15	36.60	33.45	36.48
14 Major States Average	18.38	17.35	20.33	19.74
Source: Author's Own Calculation using Data Collected form Hand Book of Statistics on State Government Finances,RBI,2010.				

2.4. Public Debt as a Percentage of GSDP

According to the 12th finance commission, the tolerable level of debt-GSDP is 28% and it has recommended that all states should reduce their respective ratios to 28% by 2009-10. In this context if we look at Table-4, except Assam, none of the NE states have a tolerable level of debt-GSDP ratio. On the other hand there are states like Mizoram, Sikkim, Arunachal Pradesh and Manipur have registered debt-GSDP ratio above 100%, above 70% and above 50% respectively.

Table- 4 Debt as a percentage of GSDP

State	1991-1995	1995-2000	2000-2005	2005-2009	2005-2006	2006-2007	2007-2008(RE)	2008-2009(BE)
	Average	Average	Average	Average	Total	Total	Total	Total
Arunachal Pradesh	40.5	38.2	52.7	71.1	72	68.9	73.6	69.8
Assam	33.8	27.6	29.4	29.5	32	30	27.8	28.2
Manipur	45.9	39.5	55.9	64.1	71.1	65	62.3	58.1
Meghalaya	23.4	28.2	36.7	41.1	40.3	40	42.2	42
Mizoram	57.6	60.6	95.8	115.3	115.3	111.5	119.3	115.2
Nagaland	43.8	39.7	48.6	42.8	43.5	41.9	42.6	43
Sikkim	60.9	50.3	77.1	72.8	71.5	69.1	74.2	76.5
Tripura	41.5	32.1	48.6	44.7	58.7	44.9	39.6	35.6
NE States Average	43.42	39.52	55.66	60.17	63.05	58.91	60.02	58.55
14 Major States Average	42.14	22.2	30.5	29.4	32	29.9	28.2	27.6
Note: (i) "+" indicated Deficit and"-" indicates **Surplus** (ii) 14 Major States includes Andhra Pradesh, Bihar,Gujrat,Haryana,Karnataka,Kerla,Madhyapradesh,Maharastra,Orissa,Panjab,rajasthan,Tamilnadu,uttarpradesh,and Westbengal								
Source: Author's Own Calculation using Data Collected form Hand Book of Statistics on State Government Finances,RBI,2010								

It is pertinent to note that the fiscal performance of north eastern states is not satisfactory even though the states have already received attention from the centre because of their special features. These states are receiving plan assistance from the centre where 90% is grant and 10% is loan. However, it has no impact in terms of reducing debt-GSDP ratio.

3. CONCLUSION AND SCOPE FOR FURTHER RESEARCH

From the above discussion it is clear that the current fiscal problem of north eastern states is increasing public debt in particular and unsatisfactory fiscal performance in general. In this context, there is scope for further research to study whether the north eastern states are debt sustainable or not. There is need to examine the fiscal problems, fiscal performance, role of central assistance and whether the public debt is sustainable for north eastern states or not in the context of north eastern states of India.

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