

Wagner's Hypothesis

Adolf Wagner, a noted German political economist (1835-1917) propounded an empirical law that analyses and explains the trend in the growth of public expenditure. Wagner argued that a functional, cause and effect relationship exists between the growth of an industrializing economy and the relative growth of its public sector.

According to Wagner, relative growth of the government sector is an inherent characteristic of industrializing economies. He illustrates this with the examples of Great Britain, U.S.A, France, Germany, and Japan. He came to the conclusion that as per capita income and output increases in industrializing nations; the public sectors of these nations necessarily grow as a proportion of total economic activity.

Wagner presented his law in the following words "Comprehensive comparisons of different countries and different times show that among progressive people, with which we alone are concerned an increase regularly takes place in the activity of both the central and the local governments. This increase is both extensive and intensive. The central and local governments constantly undertake new functions, while they perform both old and new functions more efficiently and completely."

According to Wagner's law, the expenditure of public authorities has a continuous increasing trend due to three reasons, they are:

- a. **Expansion of Traditional Functions:** Traditional functions mainly include defence, administration of justice, maintenance of law and order and provision of social overheads. The coverage and variety of such functions have gradually increased. Defence expenditure has expanded rapidly because of a change in military arts and sciences.

In modern times military activities has become sophisticated. From simple aggression, the modern warfare shifted to prevention of attack and use of sophisticated weapons. Defence outlays on men, materials and maintenance have been on a rising trend in modern times. Similar is the case with expenditure on internal protection and administration.

Increasing areas of administration and spread of government machinery with expertise have become more and more expensive.

- b. Coverage of New Functions:** Secondly the activities of the state were increasing in their coverage. Traditionally the state activities were limited to only defence, justice, law and order, maintenance of the states over heads etc. But with the growing awareness of its responsibilities to the society, the governments started expanding its activities in the field of various welfare measures to enrich the cultural life of the society.

Along with this new welfare programmes were designed to provide social security to the people. This required increasing government expenditure on education, public health, low-cost housing, subsidized provision of food, agricultural inputs, old age pension, sickness benefit etc.

- c. Expanding Sphere of Public Goods:** Almost all modern democratic governments have increasingly recognized the need to provide and expand the sphere of public goods. The need and necessity to provide social and merit goods through budgetary allocation was increasingly recognized by the modern state.

The state was trying to shift the composition of national product more in favor of public goods. As a result, state activities expanded to areas like irrigation and flood control projects, construction and maintenance of public parks, provision of education and health care facilities, creation of economic overhead capital etc., Provision of these public goods and merit goods means heavy investment in public enterprises.

Criticism of Wagner's Hypothesis:

Although the Wagner hypothesis has many attributes, it also has 'several defects. Wagner's law of increasing state activity was criticized by Allan.

T. Peacock and Jack Wiseman on the following grounds:

- i. Limited Applicability:
- ii. Normative Approach: Tells what ought to be
- iii. Neglects impact of war expenditure
- iv. Simplifies the role of the government

Peacock and Wiseman Hypothesis

Another hypothesis regarding the growth of public expenditure was put forth by Peacock and Wiseman, in their empirical study of public expenditure in U.K. for the period 1890-1955. Peacock and Wiseman emphasize the time pattern of public spending trends rather than striving for a genuine positive theory of public sector growth.

The main thesis of the authors is that public expenditure does not increase in a smooth and continuous manner, but in jumps and jerks or step like fashion. Their analysis involves three related elements. These are displacement, inspection and concentration effects.

Displacement Effect:

When a social disturbance occurs, the government raises taxes to increase revenue and increases public expenditure to meet the social disturbances. This creates a displacement effect by which low taxes and expenditures are replaced by higher tax and expenditure levels. The movement from the older level of expenditure and taxation to a new and higher level is the displacement effect.

However, after the disturbance ends, the people get used to the newly emerged level of **tax tolerance** and makes the people willing to support higher level of public expenditure. As a result, the new level of public expenditure and public revenue stabilise but are soon destabilised by another new disturbance which causes another displacement effect.

Inspection Effect:

The inadequacy of the revenue as compared with the required public expenditure creates an inspection effect. The government and the people review the revenue position and need to find a solution of the important problems that have come up and agree to the required adjustment to finance and thus increases expenditure.

They attain a new level of tax-tolerance. They are now ready to tolerate a greater burden of taxation and as result the general level of expenditure and

revenue goes up. In this way the public expenditure and revenue get stabilized at a new level till another disturbance occurs to cause a displacement effect.

Concentration Effect:

When an economy is experiencing economic growth there is a tendency of central government's economic activities and responsibilities to grow at a faster rate than that of state and local government's activities. This is known as concentration effect.

It is related to the political set up of the country. Thus, each major disturbance leads to the government assuming a larger proportion of the gross national activity. The concentration effect also refers to the apparent activity to grow faster than that of those state and local level governments.

Causes of Growth of Public Expenditure:

- 1. Expansion of traditional Functions**
- 2. Welfare state**
- 3. Rise in national income**
- 4. Growth of Population**
- 5. Urbanisation**
- 6. Inflation**
- 7. Specialization**
- 8. Servicing public debt**
- 9. Economic planning**
- 10. Democracy**