REPORT OF THE KERALA PUBLIC EXPENDITURE REVIEW COMMITTEE

FIFTH COMMITTEE

[Appointed as per notification issued under G.O.(P) No. 1/2020 Dated 4.1.2020 and published as SRO No 6/2020 in the Kerala Gazette Extraordinary No.25 Dated 4.1.2020]

FIRST REPORT

2018-19

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Acknowledgments

This is the 1st report of the 5th Kerala Expenditure Review Committee (KPERC) (appointed as per notification issued under G.O(P) No. 1/2020 Dated 4.1.2020 and published as SRO No 6/2020 in the Kerala Gazette Extraordinary No.25 Dated 4.1.2020). This Report has examined Public Finance Management of the state for the financial year 2018-19 as mandated under Fiscal Responsibility Act (2003). The Committee acknowledges the support and co-operation rendered by Shri. Rajesh Kumar Singh IAS, Additional Chief Secretary and other officials of the Finance Department, Government of Kerala, which made possible the timely completion of this report.

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Glossary

ADB	Asian Development Bank
BCR	Balance from Current Revenue
BE	Budget Estimate
C&AG	Comptroller and Auditor General
CE	Capital Expenditure
CGST	Central Goods and Services Tax
CSS	Centrally Sponsored Scheme
DA	Dearness Allowance
DR	Dearness Relief
EAP	Externally Aided Project
FC	Finance Commission
FD	Fiscal Deficit
FRBMA	Fiscal Responsibility and Budget Management Act
GDP	Gross Domestic Product
GFD	Gross Fiscal Deficit
GRF	Guarantee Redemption Fund
GSDP	Gross State Domestic Product
GST	Goods and Services Tax
GSVA	Gross State Value Addition
IGST	Integrated Goods and Service Tax
IP	Interest Payments
KFR Act	Kerala Fiscal Responsibility Act
KIIFB	Kerala Infrastructure Investment Fund Board
KPERC	Kerala Public Expenditure Review Committee
KSEB Ltd	Kerala Electricity Board Ltd
KSRTC	Kerala State Road Transport Corporation
KWA	Kerala Water Authority
LGs	Local Governments
MoF	Ministry of Finance
MTFP	Medium Term Fiscal Policy
NSSF	National Small Savings Fund
OMB	Open Market Borrowing
PA	Pre Actuals
PD	Public Deposit
PF	Provident Fund
RBI	Reserve Bank of India
RD	Revenue Deficit
RE	Revised Estimate
SGST	State Goods and Services Tax
SIP	Salaries Interest and Pensions
SONTR	State's Own Non Tax Revenue
SOTR	State's Own Tax Revenue

TRR	Total Revenue Receipts
VAT	Value Added Tax

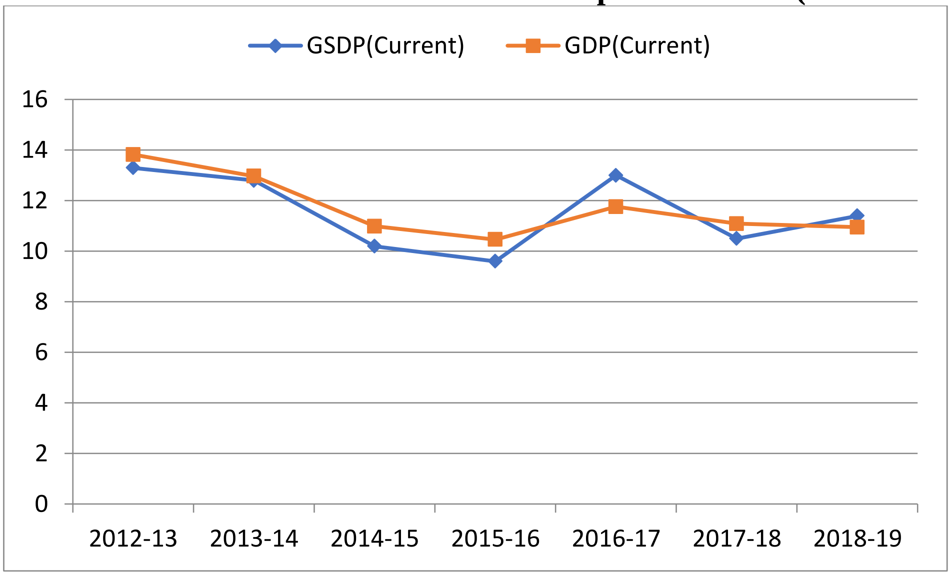
Chapter 1

Review of State Finances

1.1 State Economy

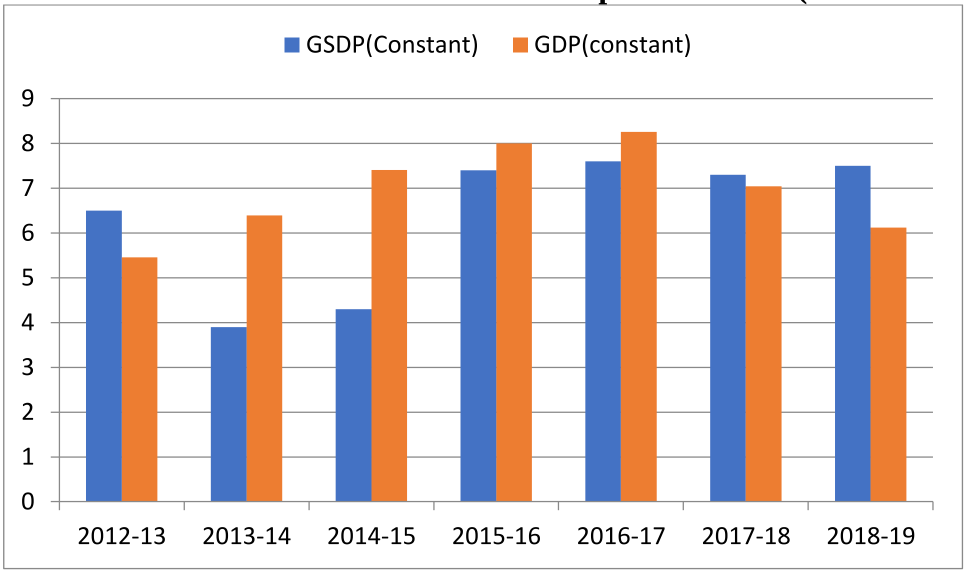
The rate of growth of Gross State Domestic Product (GSDP) of Kerala at current prices over 2011-12 to 2018-19 has broadly been in tune with the rate of growth of Gross Domestic Product (GDP) of the Nation (Figure 1). But the rate of growth of GSDP at constant prices has been showing a slightly different pattern. Except for the period from 2011-12 to 2012-13 and from 2017-18 to 2018-19, the rate of growth of GSDP (at constant prices) in Kerala has been lower compared to the national trend (Figure 2). A notable feature of the rate of growth of GSDP in Kerala has been that of maintaining a stable growth rate since 2016-17, when the rate of growth of GDP has steadily been falling. The year 2018-19, in particular, showed an increase in GSDP growth both in current and constant prices over GDP growth.

Figure 1: Rate of Growth of GSDP in Kerala Compared to GDP (at current prices)



Source: Budget in Brief, GoK and mospi.nic.in

Figure 2: Rate of Growth of GSDP in Kerala Compared to GDP (at constant prices)



Source: Budget in Brief, GoK and mospi.nic.in

The higher growth of GSDP in 2017-18 and2018-19 was in contrast to the expectation of a steep fall in GSDP due to the unprecedented flood and the loss of production and productivity across all the production sectors. A study conducted by the United Nations in association with state departments titled ‘Kerala Post Disaster Needs Assessment, Floods and Landslides August 2018’ estimated a total loss of Rs 26,720crore in the state excluding losses to private buildings other than residential buildings. The total recovery needs were assessed at Rs.31,000crore. The government acted with alacrity to cover the damage to the flood hit by its timely intervention in providing compensation to those who lost property, and life and livelihood support limiting the harm. While asset loss was high, timely action by the government did not lead to large losses in income and the GSDP growth turned out to be one of the highest in recent years.

An analysis of the sectoral growth rates of the economy showed the persistence of poor growth of the primary sector. Crops and Mining and quarrying took the hit respectively with negative growth rates of -5 per cent and -14.63 per cent respectively. The secondary sector grew at a healthy 11.41 per cent. All the sub sectors within secondary sector too registered positive growth. The tertiary sector also grew positively with a growth of 12.35 per cent[1]. Riding on the better performance of the secondary and tertiary sectors, the State

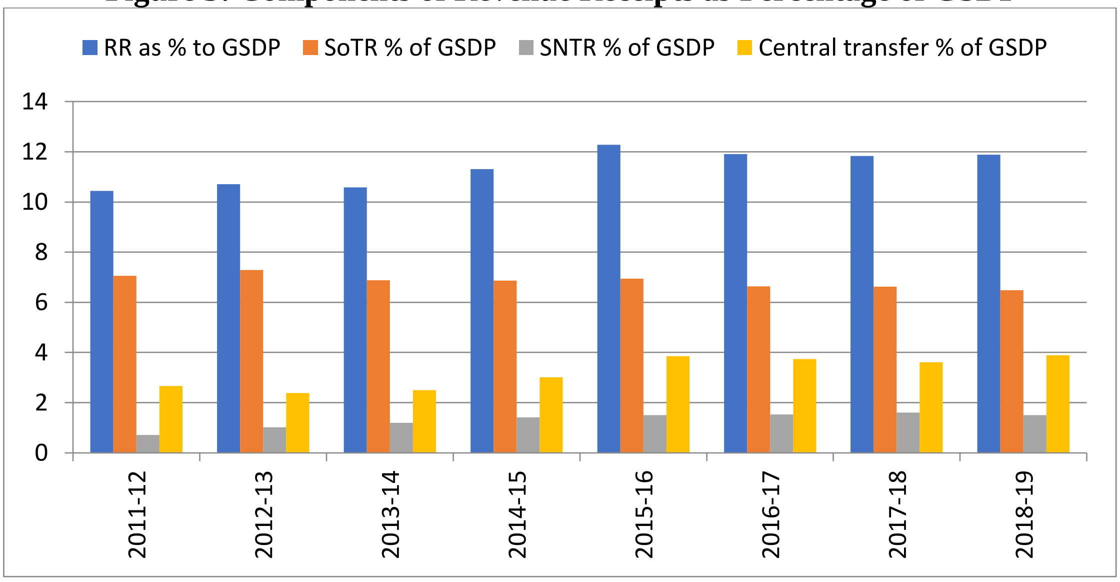
[1]All the above figures are in terms of GSVA.

economy grew at a healthy 11.41 per cent in current prices in 2018-19. The per capita GSDP growth too was higher (10.86 per cent) in 2018-19 compared to the previous year (9.96 per cent). Hence, it has to be inferred that notwithstanding the adverse impact of the devastating floods, the economy of Kerala recorded a healthy growth rate compared to GDP.

1.2 Overview of State Finances from 2011-12 to 2018-19

An overview of the State finances for the period from 2011-12 to 2018-19 has been presented in Figure 3 and Table 1. It may be seen that the Revenue Receipts (RR) as percentage of GSDP, which was 10.4 in 2011-12 took an upward turn to 12.3per cent in 2015-16 and remained around 12 per cent up to 2018-19. On a decomposition of RR some notable developments can be seen during this period. In 2012-13, while the RR as per cent of GSDP was 11, there was increase in the State's own tax revenue as percentage of GSDP to 7.29 from 7.06 during the preceding year. It has registered a marginal decline since then. The State non tax revenue as percentage of GSDP also increased to 1.02 in 2012-13from 0.71 per cent in 2011-12 and then to 1.51 during 2018-19. But the Central Transfers as per cent of GSDP came down to 2.39 in 2012-13 from 2.66 during 2011-12.

Figure 3: Components of Revenue Receipts as Percentage of GSDP



Source: Finance Accounts of C &AG of the respective years and Budget in Brief, GoK

Table 1: Trends in Major Indicators of State Finances, 2011-12 to 2018-19 (Rs crore*)

Items	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Revenue Receipts	38010	44137	49177	57950	69033	75612	83020	92854
State Tax Revenue	25719	30077	31995	35233	38995	42176	46460	50644
State Own Non-Tax Revenue	2592	4199	5575	7284	8425	9700	11200	11783
Net receipts of Lotteries in SONTR	381	591	593	960	1149	1291	1407	1445
Central Govt. Transfers	9700	9862	11607	15434	21612	23735	25361	30427
Share of Central Taxes	5990	6841	7469	7926	12691	15225	16833	19038
Grant in aid	3709	3022	4138	7508	8921	8510	8528	11389
Capital Receipts	12284	15685	17050	18719	17965	26763	27221	27242
% of GSDP	3.37	3.80	3.67	3.65	3.20	4.22	3.88	3.49
Total Receipts	50295	59823	66227	76670	86998	102374	110241	120096
% of GSDP	13.82	14.51	14.24	14.96	15.48	16.12	15.71	15.36
Total Expenditure	50896	59228	66244	76744	87032	102383	110238	120070
% of GSDP	13.98	14.36	14.24	14.97	15.49	16.13	15.71	15.36
Revenue Expenditure	46045	53489	60486	71746	78689	91096	99948	110316
% of GSDP	12.65	12.97	13.01	14.00	14.00	14.35	14.25	14.11
Expenditure on Lotteries in RE	902	2083	3203	4485	5123	5992	7628	7819
Capital Expenditure	3853	4603	4294	4255	7500	10126	8749	7431
% of GSDP	1.06	1.12	0.92	0.83	1.33	1.59	1.25	0.95

On Loan Disbursements	999	1136	1464	743	842	1160	1541	2323
% of GSDP	0.27	0.28	0.31	0.14	0.15	0.18	0.22	0.30
Revenue Deficit	8034	9351	11309	13796	9657	15485	16928	17462
% of GSDP	2.21	2.27	2.43	2.69	1.72	2.44	2.41	2.23
Fiscal Deficit	12815	15002	16944	18642	17818	26448	26837	26958
% of GSDP	3.52	3.64	3.64	3.64	3.17	4.17	3.83	3.45
Primary Deficit	6521	7798	8679	8872	6708	14332	11718	10210
IP/RR%	16.56	16.32	16.81	16.86	16.09	16.02	18.21	18.04
% of GSDP	1.79	1.89	1.87	1.73	1.19	2.26	1.67	1.31
GSDP (current prices)	364048	412313	465041	512564	561994	634886	701577	781653
Debt outstanding	89418	103561	119009	135440	157370	186454	210762	235631
% of GSDP	24.56	25.12	25.59	26.42	28.00	29.37	30.04	30.15

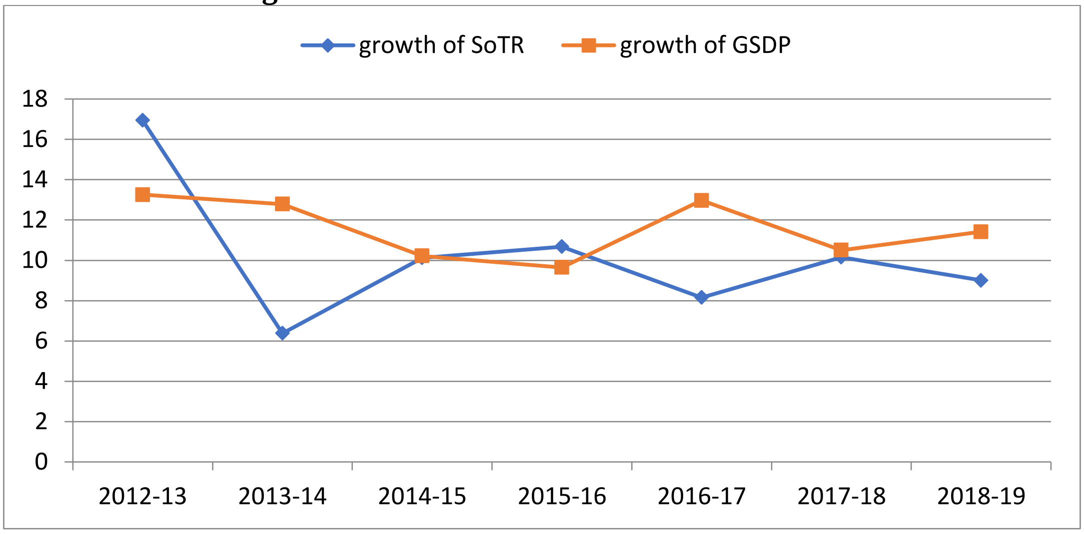
*Note: *indicated otherwise*
Source: Finance Accounts of C &AG of the respective years and Budget in Brief, GoK

It may be seen that in 2013-14 and 2014-15 the RR/GSDP remained at the same rate of 11 per cent as was recorded in 2012-13. It needs to be noted that in 2013-14, the SOTR/GSDP took a sudden dip to 6.88 per cent from the 7.29 per cent registered in 2012-13. This was balanced by the increase in SONTR/GSDP to 1.20 per cent and the Central Transfers / GSDP to 2.50 per cent. This compositional shift has been maintained since then. The declining trend in SOTR/GSDP can be adduced to the fall in revenue from VAT. From this period onwards VAT as a potential source of revenue came to occupy ashaky status. In the previous years, when the nominal GSDP growth rate was higher possibly because inflation played its role the tax buoyancy of VAT was higher than 'unity'. The GSDP fall as was noted earlier was very sharp in the years 2013-14 and 2014-15 in both current and constant prices and that probably had its effect on SOTR.

The GSDP growth rate recorded a revival and was almost the highest in constant and current prices in 2016-17, but a shift in the composition of revenue in favour of SOTR has not happened. The lower SOTR/GSDP that started in 2013-14 continued its decline with an exception of a slight increase in 2015-16 at 6.97 per cent. In the year 2018-19, the SOTR /GSDP were the lowest at 6.48 per cent. The Central Transfer as per cent to GSDP, meanwhile, recorded a consistent increase since 2013-14 up to 2018-19. The SONTR, however, has not recorded a decline as that of SOTR. A small increase can be seen up to 2017-18 and thereafter falling to 1.51 per cent in 2018-19. But, when compared to 2011-12, the ratio of State Non-tax Revenue to GSDP has almost doubled during 2018-19.

It may be inferred from the shift in composition of revenue receipts that the SOTR collection that has turned weak from 2013-14 is still locked in that trend. The SONTR has been increasing but has remained the least contributor. The Central Transfer registered continuous increase from 2012-13 up to 2015-16, then showed a slight decline during the next two years. But in 2018-19 it again increased and reached the highest level at 3.89 per cent of GSDP. The rate of growth of SoTR has not been in tune with the rate of growth of GSDP.

Figure 4: Rate of Growth of SoTR and GSDP



Source: Finance Accounts of C &AG of the respective years and Budget in Brief, GoK

Table 2: Rate of Growth of RR and its Components (%)

Year	Revenue Receipts	State Tax Revenue	State Own Non-Tax Revenue	Net receipts of Lotteries in SONTR	Central Govt. Transfers	Share of Central Taxes	Grant in aid
2012-13	16.12	16.94	62.00	55.12	1.67	14.21	-18.52
2013-14	11.42	6.38	32.77	0.34	17.69	9.18	36.93
2014-15	17.84	10.12	30.65	61.89	32.97	6.12	81.44
2015-16	19.13	10.68	15.66	19.69	40.03	60.12	18.82
2016-17	9.53	8.16	15.13	12.36	9.82	19.97	-4.61
2017-18	9.80	10.16	15.46	8.99	6.85	10.56	0.21
2018-19	11.85	9.01	5.21	2.70	19.98	13.10	33.55

Source: Computed from Finance Accounts of C &AG of the respective years

What stood the state in good stead during this period is the higher share of central transfers. Along with the growth in the share of Central taxes, growth in the grants from the Centre are also seen (Table 2). For 2012-13 it can be seen that the SOTR registered a growth of 16.94percent and the share of Central Taxes, a growth rate of 14.21per cent (Table 2). For the succeeding two years (2013-14 and 2014-15) it can be seen that growth of SOTR and share of Central Taxes ranged from 6.38 to 10.12 and 6.12percentrespectively. Meanwhile the grants from the Centre after coming down to a negative growth of 18.52percent in 2012-13 surged to show a growth of 36.93percent in2013-14. This can be attributed to the lower base in 2012-13 due to the negative growth recorded. Again in 2014-15 the Central grants recorded a high growth rate of 81.44 percent. This growth was not due to any policy change of the Centre to enhance grants to the State. It was in fact due to the decision of the Centre to release the grants under Centrally Sponsored Schemes (CSS) to the Consolidated Fund instead of the earlier practice of releasing funds to the implementing agencies and to incur expenditure from their own account. The change in the routing of the fund was the reason for the increase recorded in 2014-15.

In 2015-16, a phenomenal growth of 60 percent was recorded in the share of Central Taxes. In the case of grant in aid too, there was a significant growth of 19 percent but much lower compared to the previous two years. In 2015-16, the Centre accepted the recommendations of the 14^{th} Finance Commission (FC) and decided to make a vertical devolution of 42 percent of net taxes to the states and horizontal devolution of Kerala increased to 2.50 percent from the previous share of 2.32 percent during the 13^{th} FC period. Although the 60 per cent growth looks substantial, the Centre reduced plan grants. But the FC recommendation for a Revenue Deficit grant of Rs.4630crorefor the year more than compensated the loss under plan grants. These are the prime reasons for the compositional shift in the revenue receipts. During 2016-17 buoyant tax revenues at the Centre was recorded and correspondingly the growth was 20 per cent in the share of Central taxes. However, the grants recorded a negative growth of 5 per cent. This was because of the reduction in RD grant to only Rs.3500crore as against Rs.4630crore during the previous year as the grants would taper off by 2017-18 with a reduced allocation of Rs.1500 crore.

In 2018-19, there was not much change to the growth pattern in the SOTR growth stagnating at 10 per cent taking the long-term average to 9 per cent (Average for seven years from 2013-14 to 2018-19). Perhaps for the first time a long-term stagnation in growth was recorded. However, a healthy growth in the share of Central Taxes at 13 per cent and a surge in the growth of grants in aid at 34 per cent put the growth in RR at 12 per cent in 2018-19. This is an increase of 2 percentage points over 2017-18. The increase in share of Central taxes was more on account of the increase in the collection of direct taxes than the increase in indirect taxes. The increase of 34 per cent under grants in aid in 2018-19 was because of the GST compensation at higher levels as a result of a fall in collection under State GST below the 14 per cent threshold growth. It is likely that this compositional shift may remain during the entire period of the 14^{th} FC ending in 2019-2020 as the increased horizontal share in Central Taxes and GST compensation would remain constant because of the mandatory character of the grants.

Turning to the expenditure of the government, it can be seen that the period from 2012-13 to 2018-19 registered a growth rate of 13.81per cent under revenue expenditure. The major items constituting revenue expenditure are Salaries, Interest Payments and Pensions. Compensation and assignments to local Government, and grants in aid were expenditure items registering higher growth. Enhancement of welfare pensions also caused an increase in the expenditure under this item. The Revenue Expenditure showed increased growth in the years from 2012-13 to 2014-15 compared to the later period except in 2016-17. Increased growth in 2012-13 and 2013-14 were because of higher commitments under DA and DR instalments. In 2014-15, in addition to the higher expenditure under DA/DR, Plan expenditure in the case of some CSS also had to be shown under consolidated fund in respect of the release of grants through consolidated fund instead of through implementing agencies earlier. The RE normalized in 2015-16. But in 2016-17, it surged again on implementation of the recommendations of the 10th Pay Commission. Part of the pay revision commitments were staggered to 2017-18 as well. After pay out of the pay revision commitments the Revenue Expenditure normalized again in 2018-19. The cause for concern in respect of RE is growth on a higher base that had been reached in the state from the middle of 1980s and Pay/Pension revision commitments quinquennially. Growing commitments under Welfare Pensions are another unavoidable item of expenditure. With this almost all the Revenue Expenditure components have assumed the character of committed expenditure.

1.3 Capital Expenditure 2018 -19

The low growth of Capital Expenditure owing to a lower growth in RR or due to overrun in RE and at times a combination of both is an unhealthy trend of the State finance. The CE is constrained as a residuary item after meeting all the committed payments and repayment of loans. The period during which there was robust growth in RR or a reduced growth in RE thus came to show increased growth in Capital Expenditure. The CE as per cent of GSDP during 2011-12 to 2018-19 varied between 0.98 per cent in 2014-15 to 1.78 per cent in 2016-17. In absolute terms negative growth numbers were registered in 2014-15 and 2017-18 over the preceding years. The CE/GSDP ratio in 2018-19 is only 0.95per cent which is much lower than that of other states.

Turning to the Capital Receipts of the State, the non – debt capital receipts of the State could never register an increased growth from the traditionally low level. Poor servicing of the loans advanced to statutory corporations, PSUs, co-operatives and other institutions are the main reasons for the sluggish growth in non - debt capital receipts. Major portion of the Capital Receipts constituted the debt Capital receipts. The internal debt though constitutes a major sum, there were concerns about the rise in the Public Account liabilities, part of which carry higher interest liabilities than the borrowing from the internal market, especially through open market borrowings. The Central loan did not register sizeable increase and major chunk was that of loans from EAPs.

Against this backdrop, how the state stood in respect of achieving the major fiscal targets as against the MTFP targets in 2018-19 can been seen from Table 3.

Table 3: Targets in KFR Act and Actuals, 2018-19

Items	Target	Actual
RD/GSDP	0	2.23
FD/GSDP	3	3.45
Debt/GSDP	30.01	30.15
IP/RR	14.37	18.04

Source: Kerala Fiscal Responsibility (Amendment) Act 2018

The RD which was Rs.16,928 crore in 2017-18 went up to Rs. 17,462crore in 2018-19registering a lower growth of 3 per cent compared to the growth of 6 per cent in 2017-18. The FD too surpassed the statutory limit of 3 per cent of GSDP. The Debt/GSDP ratio which was required to be brought down to 30.01per cent in 2018-19 went up to 30.15 per cent. The IP/RR ratio which was 18.04 per cent had to be at13.78 per cent to comply with the statutory limit. The state was not able to achieve the fiscal consolidation targets. The task of achieving the fiscal targets has been turning very difficult year after year. Growth in the economy has been very slow. Tax buoyancy remained subdued. While the growth in SOTR was stagnant RE was steadily rising. While the share of Central Taxes was showing a low growth, the grants were rising. The RD grant and GST compensation are not dependable resources to be relied upon continuously for long term. The growth in the liabilities under the Public Account needs to be targeted for reduction in debt in order to achieve the targets of Debt/GSDP and IP/RR.

1.4 Revenue Receipts 2018-19

The total Revenue Receipts of the state registered a growth of 9.80(Table 2) per cent in 2017-18 that increased to 11.84(Table 2) per cent in 2018-19. The growth in SOTR was only 9.01per cent against 10.16per cent growth recorded in 2017-18.

Table 4: Trends in Own Tax Revenue, 2011-12 to 2018-19 (Rs crore)

Item	**2010-11**	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017- 18**	**2018- 19**
GST								12007.69	21014.71
Share%								25.85	41.49
GrowthRate%									75.01
Sales Tax/VAT	15833	18939	22511	24885	27908	30737	33453	24577.81	19225.75
Share%	72.9	73.6	74.8	77.8	79.2	78.8	79.3	52.9	38.0
GrowthRate%		19.6	18.9	10.5	12.1	10.1	8.8	-26.5	-21.8
Excise Duty	1700	1883	2314	1942	1777	1964	2019	2240.42	2521.4
Share%	7.83	7.32	7.69	6.07	5.04	5.04	4.79	4.82	4.98
GrowthRate%		10.76	22.89	-16.08	-8.50	10.52	2.80	10.97	12.54
Motor Vehicle Tax	1331	1587	1925	2161	2365	2814	3107	3662.85	3708.61
Share%	6.13	6.17	6.40	6.75	6.71	7.22	7.37	7.88	7.32
GrowthRate%		19.23	21.30	12.26	9.44	18.99	10.41	17.89	1.25
Stamp duty and Registration	2552	2987	2938	2593	2659	2878	3007	3452.56	3693.17
Share%	11.75	11.61	9.77	8.10	7.55	7.38	7.13	7.43	7.29
Growth Rate%		17.05	-1.64	-11.74	2.55	8.24	4.48	14.82	6.97
Others	306	323	389	414	523	602	590	518.28	480.46
Share%	1.41	1.26	1.29	1.29	1.48	1.54	1.40	1.12	0.95
Growth Rate%		5.56	20.43	6.43	26.33	15.11	-1.99	-12.16	-7.30
States Own Tax Revenue	21722	25719	30077	31995	35232	38995	42176	46459.61	50644.1

Source: Finance Accounts of C &AG of the respective years and Budget in Brief, GoK

The decomposition of SOTR shows that there was a growth of 75.01 per cent under GST in 2018-19. This growth is not comparable for the reason that GST was introduced in 2017-18 only for part of the year and this happened to register a lower number in 2017-18 and growth cannot be compared with the figures in 2018-19. In this context, a comparison with the Budget Estimate in 2018-19 shows that as against the BE of Rs.27000crore in 2018-19, the collection was only Rs.21015crore. The achievement was 75 per cent only. This shows that GST has not achieved the status of buoyant revenue source even in 2018-19. As already explained in the previous reports, GST regime still suffers from infirmities. The system requires further tuning. In this respect details of monthly collection, compensation and *adhoc* payment may be seen in the Table 5.

Table 5: GST Collection (Rs crore)

Month	SGST	IGST	*Adhoc* Settlement	Compensation	Total
2017-2018					
Aug.17	716.47	451.74		810	1978.21
Sept.17	807.05	763.46			1570.51
Octo.17	740.47	822.65		395	1958.12
Nov.17	610.3	801.36			1411.66
Dec.17	600.51	795.95			1396.46
Jan.18	700.39	826.9			1527.29
Feb.18	619.68	808.82	736	567	2731.5
Mar.18	604.24	794.12			1398.36
Total	**5399.1**	**6065**	**736**	**1772**	**13972.11**
2018-2019					
April.18	693.64	802.07			1495.71
May.18	661.8	785.97		330	1777.77
June.18	682.47	879.89	1052		2614.36
July.18	658.46	848.44		67	1573.9
Aug.18	527.51	746.21	252		1525.72
Sept.18	525.3	651.9		780	1957.2
Octo.18	793.5	1068.4	631.04		2492.97
Nov.18	676.02	1014.3		1033	2723.36
Dec.18	719.81	816.86	378.63		1915.3
Jan.19	816.5	862.29		195	1873.79
Feb.19	723.5	845.72			1569.22
Mar.19	791.41	792.83		899.7	2483.94
Total	**5573.6**	**6798.6**	**1261.67**	**2907.7**	**16541.5**

Source: Data from SGST department

The GST regime in 2018-19 in its second year has not matured into an effective and efficient system of taxation. This can be seen from the monthly collection. GST collection at the national level was hampered with shortcomings in respect of uncertainties in the rates, difficulties in filing returns, non-compliance in respect of way bills and such other issues cropping up from time to time. Even in 2018-19, the GST regime were saddled with the same issues. From August 2018 collections dipped heavily in respect of SGST and in September 2018 both the SGST and IGST went down sharply over the collection in September 2017. The dip in August and September to some extent can be attributed to the unprecedented floods that devastated Kerala. However, from October 2018 things were looking up but a consistent and firm growth trend was not visible like that of VAT when it was introduced.

The next biggest source of tax resource was Sales Tax / VAT. The tax on petroleum products and foreign liquor were not subsumed under GST. These are the only two items on which states still have the freedom to decide rates on the levy of taxes. But as is well known, revenue from the sale of liquor is stagnating even after the tax rates have been raised. This phenomenon was visible from 2016-17. This points to the fact that the demand for foreign liquor in Kerala is stagnating. Sales tax revenue from the sale of foreign liquor was Rs.8870 crore in 2017-18 and this went up to Rs9616 crore in 2018-19, a rate of increase of only8.41 per cent. In respect of ST on petroleum products also the growth in collection is low. As against the collection of Rs7443crore in 2017-18, the collection registered in 2018-19 was only Rs 8000 crore, a growth of only 7.48 per cent.

The other major items of State Taxes are Stamps and Registration fees, State Excise and Vehicle Tax. The growth under State Excise was 12.54 per cent compared to the year 2017-18. The growth in the Tax on Motor Vehicles has come down in 2018-19. Compared to the growth of 17.89 per cent in 2017-18, the increase is only 1.25 per cent in 2018-19. This is reflective of the national trend of reduced sales volume in motor vehicles. The Stamps and Registration Fees too registered a growth of only 6.97 per cent in 2018-19 compared to the growth of 14.82 per cent in 2017-18. The stagnation in the real estate market was the prime reason for the subdued growth. The share of State Excise, Taxes on Vehicle and Stamps and Registration together was 19.59 per cent in 2018-19 compared to 20.14 per cent in 2017-18. The trend of growth in respect of other smaller items of tax are negative since 2016-17. In 2018-19, it continued with a negative growth rate of -7.30 per cent with a share of 0.95 per cent.

The tax buoyancy of the State from the year 2012-13 to2018-19 is given in Table 6.

Table 6: SOTR - Growth Rates and Buoyancy, 2011-12 to 2018-19 (Rs crore)

Year	SOTR	Growth rate %	GSDP(current prices)	Growth rate %	Buoyancy
2011-12	25719		364048		
2012-13	30077	16.9	412313	13.3	1.3
2013-14	31995	6.4	465041	12.8	0.5
2014-15	35232	10.1	512564	10.2	1.0
2015-16	38995	10.7	561994	9.6	1.1
2016-17	42176	8.2	634886	13.0	0.6
2017-18	46460	10.2	701577	10.5	1.0
2018-19	50644	9.0	781653	11.4	0.8

Source: Finance Accounts of C &AG of the respective years and Budget in Brief, GoK

The stagnant buoyancy of revenue receipts for more than 7 years in a row needs to be looked into by the departments concerned so as to adopt measures to increase revenues and enhance the fiscal health of the state. Better tax effort is required in the state for achieving fiscal consolidation targets. Some of the measures suggested by the committees set up recently in connection with the COVID19 pandemic are worth mentioning in this context

The revenue expenditure needs to be reduced along with better tax effort for achieving fiscal consolidation in the state so that the capital expenditure is augmented for economic growth, increase in output, employment and income. Some of the measures recommended /suggested by various committees for revenue augmentation through direct and indirect measures are highlighted in this context.

Some of the suggestions in the fourth report of the fourth KPERC 2017-18 (April2019) are listed below.

- The taxes and duties on electricity is a state tax levied by the state and collected by the KSEB Ltd. As per G.O.(Ms) No 42/2011/PD dt 3/11/2011, government has allowed the KSEB Ltd to retain this amount for 10years with the objective of creating a pension fund by the KSEB Ltd. The committee feels that being a state tax this shall be accounted as revenue receipts of the state and whatever amount government gives as support to the KSEB Ltd shall be shown as budgetary support of the state in order to ensure transparency and also to ensure that the amount of assistance is utilised for the intended purpose. This will reflect the Revenue Receipts of the state correctly and under - reporting can be avoided and proper accounting can also improve the IP/RR ratio, one of the fiscal indicators to be achieved by the state as per KFR Act 2003.

- As regards some of the non - tax revenue items that registered negative growth, revision of rates can be considered by the government if found necessary.
- The institutions receiving grant in aid like Universities, KWA and LGs shall take measures to harness their own resources in order to relieve burden on the state exchequer.
- The property tax levied by the LGs shall be revised in time. The taxation shall be equitable.
- All other tax and non-tax resources of LGs shall also be revised in time.
- Water charges levied by the KWA shall be revised in order to recover the cost of providing services.

Some important measures suggested by the Expert Committee constituted for assessing the impact of COVID 19 are:

- A scheme of additional tax revenue from petrol and diesel.
- A calibrated increase in the fair value of land accompanied by reduction in stamp duty in order to earn additional revenue from Stamp Duty and Registration fees.
- A 50% hike in the present rates of Excise duty and ST on liquor.
- Additional non-tax revenue from the sale of high value monthly lottery creating an attractive price structure.
- A 5% annual increase on non-tax revenue items other than lottery.
- To collect lease rent arrears along with re-assessment and resumption of land not being used as per lease terms.

The proposals listed above are worth considering for implementation by the Government with a view to improve revenue collection and strengthening the revenue base of state level institutions.

1.5 Revenue Expenditure 2018-19

The average growth in the RE for the period from 2012-13 to 2018-19, a period spanning 7 years was 13.34 per cent. The expansion in the RE is without giving due regard to the growth in the revenue receipts. Because during the same period the growth in the RR was only 10per cent. The widening gap is giving rise to massive imbalance in the revenue account. This high trend growth in RE is the most significant reason for fiscal imbalances and for non-achievement of fiscal consolidation in the state. Growth of RE beyond the RR needs to be contained in order to attain fiscal consolidation gradually in the state. Major component-wise, the annual average growth in salaries was 10.24 per cent. Payment of interest grew by 15.10per cent annually. The growth in pension was 12.30 per cent. The average growth rate for devolution to Local governments was 17.32 per cent.

Table 7: Trends in Salary, Interest, Pension, 2011-12 to 2018-19 (Rs crore)

Year	Salary	Interest	Pension	Revenue Expenditure	Revenue Receipt
2011-12	16029	6294	8700	46045	38010
2012-13	17257	7205	8867	53489	44137
2013-14	19280	8265	9971	60486	49177
2014-15	21334	9770	11253	71746	57950
2015-16	23450	11111	13063	78690	69033
2016-17	27954	12117	15277	91096	75612
2017-18	31802	15120	19938	99948	83020
2018-19	31406	16748	19012	110316	92854
Shares of Salary, Interest and Pensions to Revenue Expenditure					**Revenue Receipt**
2011-12	34.81	13.67	18.89	67.38	81.62
2012-13	32.26	13.47	16.58	62.31	75.51
2013-14	31.88	13.66	16.48	62.02	76.29
2014-15	29.74	13.62	15.68	59.04	73.09
2015-16	29.80	14.12	16.60	60.52	68.99
2016-17	30.69	13.30	16.77	60.76	73.20
2017-18	31.82	15.13	19.95	66.89	80.54
2018-19	28.47	15.18	17.23	60.88	72.33
Average	31.18	14.02	17.27	62.48	75.20

Source: Finance Accounts of C &AG of the respective years

For 2018-19 there occurred a growth of 10.37 per cent in RE. This is against a growth of 9.71per cent in 2017-18.For the year 2018-19, salaries registered a negative growth of -1.25 per cent over the growth of 13.77 per cent in 2017-18. The growth of interest payment also fell below the average of 15.10per cent. The growth in respect of Pension too was negative at -4.65 per cent as compared to30.51 per cent in 2017-18. The negative growth of salary and pension was owing to the staggering of the pay commission awards the previous two years. The growth under Local governments also was lower at 21.35per cent over the growth of 39.79 per cent in 2017-18. But under ‘others’ a higher growth was registered in 2018-19 than was in the year 2017-18. One of the major items under others is lotteries that registered only 2.55 per cent growth in 2018-19.

Payment of salaries, interest and pension constitute the major share of RE. The average of these payments as a per cent of total RE for the period from 2011-12 to 2018-19 was 62.48 per cent. For the year 2018-19 the share was only 60.88 per cent. Compared to the average the growth was less in 2018-19. The years in which pay/pension revisions are implemented would see the expenditure flare up under salaries and pensions. High level of debt and interest payment thereon is also a reason for the share remaining high. The SIP as a proportion of RR shows an average of 75.20 per cent for the same period. This too is a reason for worry. Because, the share of SOTR in the total RR has been coming down. The share of Central transfers in the recent years has gone up. If this share also reduces, the financial stringency in the state can aggravate.

1.6 Local Government

The Local Governments in the state play a vital role in the developmental effort of the state by virtue of the transfer of functions, functionaries and funds to them from a very early stage after the 73rd and 74th Constitution amendment. General purpose funds are ensured for any gap in discharging their traditional functions. Maintenance funds are provided for the purpose of the maintenance of the assets transferred to them and also for the assets created by them. Development funds are devolved for the purpose of local government plan. It can be seen that the average of the total devolution to Local Governments for the period from 2012-13 to 2018-19 surpassed the average growth of the Revenue Expenditure. The commitment of the State government to ensure unfettered fund flow to the local governments are evident from this.

It may be seen that only in 2015-16 a negative growth was recorded in the devolution to Local Government institutions. This was because from 2015-16 the practice of transferring development fund and maintenance funds in instalments to the PD accounts of the Local Governments were stopped. In lieu of the earlier practice, the LGs also were made to incur expenditure by presenting bills against the allotment provided to them like the state departments. Only General-Purpose Funds are transferred to their Spl TSB accounts from which expenditure can be met. If any balance is left in the allotment from Development Fund and Maintenance Funds that would be resumed at the end of the year. The resumed funds will be treated as eligible entitlements to the LGs in the next year. This transition in the system caused only the actual incurred expenditure to be shown as expenditure both in the accounts of State government and LGs. The transition has caused only a temporary reduction in the growth in 2015-16 and from 2016-17 the growth in expenditure has been at higher levels. For the year 2018-19 the growth in expenditure was 21.35 per cent on a higher base of 39.77 per cent growth in 2017-18.

The developmental partnership of state government and the LGs are very significant in combating the calamities striking the state. This was seen first during 2018-19 while fighting the flood impact and later in 2019-2020 and in 2020-2021 in the fight of the state against COVID 19.

1.7 Subsidies

As regards the payment of subsidies, it may be noted that, after registering a peak of Rs1730.68 crore in 2016-17, it came down to Rs 1583.84 crore in 2017-18. For the year 2018-19 it increased to Rs 1663.01 crore but was below the peak recorded in the year 2016-17. The containment of subsidy payment is a welcome development. The subsidy payment from2012-13 may be seen in Table 8.

Table 8: Trends in Subsidy, 2011-12 to 2018-19 (Rs crore)

Year	Total Subsidy	Food	Others	GSDP	Subsidy as a proportion of GSDP(%)	Food subsidy as a proportion of Total subsidy (%)
2011-12	1011.43	699.57	311.86	364048	0.28	0.19
2012-13	1267.18	894.96	372.22	412313	0.31	0.22
2013-14	1278.98	903	375.98	465041	0.28	0.19
2014-15	1252.51	1026.57	225.94	512564	0.24	0.20
2015-16	1372.39	1106.35	266.04	561993	0.24	0.20
2016-17	1730.67	1492.15	238.52	634886	0.27	0.24
2017-18	1583.84	1309.53	274.31	701577	0.23	0.19
2018-19	1663.01	1346.69	316.32	781653	0.21	0.17

Source: Finance Accounts of C &AG of the respective years

Subsidy as a proportion of GSDP has also not grown after 2016-17. Major item of payment under subsidy is the 'Reimbursement of price difference of ration rice and wheat to the Food Corporation of India.' This item of payment after dipping to Rs 784.38 crore in 2017-18 rose to Rs934.01crore in 2018-19. The next biggest item of Subsidy payment is on account of 'Paddy procurement through Kerala Civil Supplies Corporation and other agencies'. The payment on this item came down to Rs 325.14 crore in 2017-18 from Rs486.51 crore in2016-17. In 2018-19, the payment came down to Rs 285.47 crore. Altogether subsidy payment in the state is only for essential interventions and the payment has not grown exorbitantly.

Major items of payments including lotteries has acquired the character of committed expenditure. Policy measures are needed to limit expenditure both on the major items as well as a large number of smaller items to contain further growth in the Revenue Expenditure.

In this context the Committee would like to highlight some of the expenditure reduction measures put forward by various Committees set up by the Government in the wake of the COVID 19 pandemic.

Some important measures suggested by The Expert Committee constituted for assessing the impact of COVID 19 to reduce expenditure are;

- Comprehensive functional review should be undertaken for identification of objectives, functions and structure so as to consider manpower movement to local level considering the success of decentralized governance in the state.
- To introduce a scheme of re-employment at the option of employee so that pension age is enhanced to 60 years from 56 years.
- Setting up a High Level Expert Group to submit a report as to the financing of aided educational institutions, the burden on the finance of the state and the benefit the society is getting out of it and framing of new legislations and administrative framework.
- Seeking concessional repayment facilities by way of write offs/moratoriums/ Debt swap accommodation/ Debt consolidation and relief activities.
- Arrange a switch/conversion programme of State Development Loan with RBI in the manner that is available to GoI so as to reduce interest payment commitment.

Some proposals put forward by the Expenditure Reduction Committee under the broad categorisations of; i.) Employment and Recruitment related ii.) Expenditure related iii.) Rationalisation of office space and iv.) Others: are;

Employment and Recruitment related proposals:

- Even after decentralization of functions to LGs more staff has been recruited in the Secretariat and line departments. This must be reviewed/undone.

- After implementation of e-office, posts have been identified as excess in several departments. Redeployment of excess posts should be done after conducting a similar exercise in all the departments. The post of typist shall be abolished.
- Increasing the retirement age by two years.
- Posts in various Government departments which have become redundant and not filled up for a period of more than one year shall be abolished.
- No new posts should be created in Government/Aided Organizations for the next two years.
- All offices should be subjected to a proper work study for identification and deployment of excess staff.
- Clerical scrutiny of technical proposals shall be ended. Such proposals shall be scrutinised by Executive Engineer Grade officers as in GoI.
- Incentivise Government Employees for innovation.
- Employees may be allowed to accumulate earned leave up to 300 days only. Enhancement shall be allowed only at the time of retirement.
- Rationalization and integration exercise have to be done in all the Government funded agencies like boards, authorities, societies, commissions, universities to avoid different organizations for similar areas of activities.
- Temporary posts need not be created and all the existing temporary posts should be subjected to a study to see whether they are required and whether existing permanent staff can do it.

Expenditure related proposals

- All the separate Fund Board legislations shall be repealed by a common Act to ensure economy in avoidable executive positions and to prevent duplication and ineligible beneficiaries.
- A system of appointment of personnel in non-statutory commissions, limiting the time of functioning of the Judicial Commissions, digital payment in all departments, integration of PSUs of similar nature and a host of other proposals are also made under expenditure related category.

Rationalisation of office space

- An inventory of built-up space under various Government departments and Organizations shall be maintained to use space optimally instead of taking office space on lease. Construction of new office buildings shall be frozen for two years.
- Facilities like office cars, hospital equipment and construction machinery shall be availed on a rental basis to avoid dysfunctional machineries due to lack of funds for repairs and maintenance.

Others

- Reforms in the Aided educational sector
- Re-organization of KSRTC

The proposals listed above and those in the previous KPERC reports are worth consideration for implementation by the Government with a view to improve revenue collection and reduce expenditure.

1.8 Capital Expenditure 2011-12 to 2018-19

Table 9: Trends of Capital Expenditure, 2011-12 to 2018-19 (Rs crore)

Items	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Capital Outlay	3853	4603	4294	4255	7500	10126	8749	7431
Loan Disbursement	999	1136	1464	743	842	1160	1541	2323
Capital expenditure	4851	5739	5759	4998	8342	11286	10289	9753
GSDP	364048	412313	465041	512564	561994	634886	701577.4	781653
CE as % to GSDP	1.33	1.39	1.24	0.98	1.48	1.78	1.47	1.25

Source: Finance Accounts of C &AG of the respective years

With the Revenue Account not being balanced as targeted in the KFR Act2003, debt contracted by the state is used for filling this imbalance resulting in the Capital Expenditure being a residuary item after meeting all other payments. This is the reason for the low and highly erratic trend in growth of Capital Expenditure. Table 9 shows the CE as per cent of GSDP. Over a time span of 8 years this ranged between 0.98to 1.78 per cent. Consistency in the ratio has been lost. Either RR has to increase or RE has to be reduced to beat the inconsistent trend. One among the prime objectives of the FRBM Act is to achieve the golden rule of eliminating RD and to spruce up capital expenditure to augment economic growth. CE of the state is perched on a lower trajectory because of rising RD. Almost all the RE have attained the character of committed expenditure in the state and suggestions for reducing the RE has been made in the foregoing paragraphs. Both 2017-18 and 2018-19 have registered reduction of CE in absolute terms.

The situation needs a reversal in the immediate future. Reduced CE can drag development down in the state and needs urgent attention by the government. One bold initiative of the Government to ramp up Capital spending is the projects initiated under KIIFB. While some social sector projects with revenue expenditure characterisation are included in the current projects due to its strong orientation towards positive externalities, in the future it is hoped that projects will be overwhelmingly revenue generating.

1.9 Debt and Liabilities 2018-19

The debt and liabilities of the state are grouped under the major categories of internal debt, loans from the Centre and PF and small savings within the public account. According to the KFR Act 2003 total net debt shall not exceed 3 per cent of GSDP. Consent under Article 293(3) of Constitution is required for the borrowings under internal debt and central loans. In respect of liabilities under Public Account including PF and small savings, no consent is required from the Centre. In fact, in respect of the liabilities accruing under Public Account, the role of the State Government is that of a banker. Some of the liabilities under Public Account are to be met by the Government at call and some are term liabilities and some others are liabilities created for convenience of administration. For example, creation of Personal Deposit Accounts under which funds is transferred from Consolidated Fund for some specific purposes. These accounts, according to The Kerala Financial Code shall be closed by the administrators of this PD Account at the end of the financial year and credit the balance back to the Consolidated Fund.

Table 10: Debt Profile of the State, 2011-12 to 2018-19 (Rs crore)

Item	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Internal Debt	48528	55397	65628	76804	89068	102496	118268	135500	150991
Share of Total Debt%	61.68	61.95	63.37	64.54	65.76	65.13	63.43	64.29	64.08
Growth Rate %		14.15	18.47	17.03	15.97	15.08	15.39	14.57	11.43
of which Market Borrowings	30744	38239	48810	60183	71960	84846	99532	115735	129719
Share of Total Debt%	39.08	42.76	47.13	50.57	53.13	53.91	53.38	54.91	55.05
Growth Rate		24.38	27.64	23.30	19.57	17.91	17.31	16.28	12.08
of which NSSF	11781	11290	11323	11281	11806	12537	13509	14557	15608
Share of Total Debt%	14.97	12.63	10.93	9.48	8.72	7.97	7.25	6.91	6.62
Growth Rate %		-4.17	0.29	-0.37	4.65	6.19	7.75	7.76	7.22
Loans from the Centre	6359	6396	6622	6662	7065	7235	7614	7484	7244
Share of Total Debt%	8.08	7.15	6.39	5.60	5.22	4.60	4.08	3.55	3.07
Growth Rate		0.58	3.53	0.60	6.05	2.41	5.24	-1.71	-3.21
PF Small savings	23786	27625	31311	35543	39307	47639	60571	67777	77397
Share of Total Debt%	30.23	30.89	30.23	29.87	29.02	30.27	32.49	32.16	32.85
Growth Rate %		16.1397	13.3430	13.5160	10.5900	21.1972	27.1458	11.8968	14.1936
Total Debt	78673	89418	103561	119009	135440	157370	186453	210761	235632
Growth Rate %		13.66	15.82	14.92	13.81	16.19	18.48	13.04	11.80

Source: Finance Accounts of C &AG of the respective years

Within this broad categorisation, total borrowings have to be limited at 3 per cent of GSDP. This is where the success of debt management of Government depends. Even if the RBI acts as the debt manager of the Government, it is very often limited to the borrowings from the OMB. The borrowings from financial institutions, from NSSF, loans from the Centre and the creation of liabilities under the Public Account on the other hand are determined mostly by the Government. The OMB constitute about 55 per cent of the total debt and of the remaining borrowing sources, 32 per cent is from PF and small savings. The share of the rest constitutes only 17 per cent. The RBI even if it acts as debt manager in respect of OMB, it is ultimately the Government which decides the share from each source at the time of making its budget. Thus, a proper mix has to be decided by the Finance Department. Since the size of Government debt has grown to about Rs 2.50 lakh crore and in addition, incremental borrowings have to be made year after year, debt management of the Government requires a lot of professional planning.

Analysis of debt dynamics during the period 2011-12 to 2018-19 shows that average growth in debt during this period is 14.5 per cent. High growth rate has been recorded in some years. The growth ranges from a low of 10.59 per cent in 2014-15 to a high of 27.14 per cent in 2016-17. For the year 2018-19, the growth was 14.19 per cent. This is against a growth rate of 11.90 per cent in 2017-18. During all these years, the growth of debt (as also FD) exceeded the ceiling of 3per cent of GSDP. Along with growth in debt, expenditure in respect of payment of interest also has increased. This has prevented the State Finance from achieving the IP/RR ratio. Likewise, the debt/GSDP ratio also has been increasing because of debt exceeding beyond the mandatory limit of 3 per cent of GSDP each year.

Debt servicing is done from the consolidated fund of the state. Receipt into the consolidated fund comprises all Revenue Receipts and Capital receipts. When growth of Revenue Receipts shrinks, it is from Capital receipts that debt servicing has to be done. When the RR shrinks continuously for a long period, this will create a vicious circle in which debt servicing will be not only from RR but also from Capital Receipts. Year after year more amounts will have to be appropriated from Capital Receipts for debt servicing unless amortisation arrangement of debt is there in the system.

In the state there is a Consolidated Sinking Fund for amortisation of debt. Contribution to the sinking fund has to be made annually at the minimum rate of 0.5 per cent of the outstanding debt at the beginning of the year. The interest accrued to the fund only can be used for meeting the debt obligations of the state. Contribution to the fund was made only from the year 2006-07 to 2010-11. Thereafter no contribution was made to the fund. The accruals in the fund including interest was Rs 2018.54 crore as on March 31 2019. As against this, the debt obligation of internal debt and loans from the Centre outstanding as on March 31^{st} 2019 was Rs 1,58,235crore. The sinking fund constitutes only 1.28 per cent of the debt.

The Consolidated Sinking Fund is invested in the GoI securities. There is no surplus in the revenue accounts. In this context, borrowed funds only can be invested in the CSF. For raising debt through the OMB, State Government securities have to be issued. Interests on these securities normally are higher than the GoI securities. Thus, if provisions are to be made for the CSF, the State Government will end up investing funds borrowed at higher interest rates in GoI securities yielding lower returns. This will result in negative carry. The state is not making provision for CSF on this plea. In this context, the need to bring down growth of debt to the mandatory level and also to increase State's Own Tax and Non Tax Revenues targeting a reduction in RD and ultimately eliminating it are an imperative.

Another cause of concern in the debt and liabilities front is the increasing liabilities under the Public Account. The Public Account liabilities outstanding as on March 31^{st} 2019 was Rs 77,397 crore. The repayment obligations are to be met either from the incremental receipts into the Public Account or from the Consolidated Fund of the State. But when the net under Public Account is negative, repayment is made from the Consolidated Fund. Fiscal space for both revenue spending of inevitable nature and capital spending will come down causing negative externalities. This situation will repeat to the detriment of the State economy as well. All these call for prudential debt and liability management by the state.

The Finance Department at present manages raising of debt and repayment in respect of loans from the financial institutions and discharge of Public Account liabilities. As the total debt assumes larger dimensions, the present tools of debt management will become inadequate and without modern tools, debt management can impair total financial planning. The rates of interest, tenure, switching or swapping options and such other facilities have to be decided by a team in the Finance Department. The Finance Department shall plan a training programme for a selected few in modern debt management.

1.10 Government Guarantees - Contingent Liability

Section 3 of 'Kerala Ceiling on Government Guarantees Act 2003' amended in Kerala Finance(No.2) Act 2018, provides that total outstanding Government Guarantees should be within the limit of 5% of GSDP of the state as calculated by Economics and Statistics Department for the respective year. This act came in to force with effect from 1.04.2018. The outstanding Guarantee at the end of the 2018-2019 is Rs.26834.65 crore. This is within the limit of 5% of projected estimate of GSDP for the year 2018-19. The act stipulated that a minimum of 0.75% of the Government Guarantee outstanding against the entity should be charged by the Government each year as Guarantee Commission which could not be waived under any circumstances. Guarantee commission of Rs 124.50 crore was received during 2018-19. Guarantee commission outstanding as on 31st march 2019 is Rs 228.38 crore. Guarantees are invoked if the debtor fails to repay the amount. Effective steps are to be taken for monitoring Guarantee and Guarantee commission.

In terms of the Kerala Ceiling on Government Guarantees Act, 2003 the guarantee commission received annually are to be transferred to the Public Account and these contributions shall form the corpus of the Guarantee Redemption Fund (GRF) under Public Account of the State. The State government has not constituted GRF as per para 6 of the Kerala Ceiling on Government Guarantees Act, 2003 and RBI guidelines, and the guarantee commission of Rs124.50 crore collected during 2018-19, was not transferred to the Guarantee Redemption Fund under Public Account. If the loan amount against the guarantee is not discharged in time, the guarantee becomes contingent liabilities of the state. Hence the Govt. shall seriously consider setting up of the GRF as per the provisions of the Act. In this regard the observations of the C&AG at page 64 of Finance Accounts 2018-19 Vol 1 is reproduced below

(b) Guarantee Redemption Fund: As per the recommendations of the Twelfth Finance Commission, State Governments are required to constitute a Guarantee Redemption Fund to be utilized for meeting the payment of obligations arising out of the guarantees issued by the Government. The Fund is operated outside the State Government account and administered by the Reserve Bank of India. Under the guidelines, the State Government is required to make minimum annual contribution of 0.5 per cent of outstanding guarantee at the beginning of the year. The proceeds of the Fund are invested in Government of India securities and this does not form a part of the State Government Cash balance. In terms of the Kerala Ceiling on Government Guarantees Act, 2003 the guarantee commission received annually are to be transferred to the Public Account and these contributions shall form the corpus of the Guarantee Redemption Fund (GRF) under Public Account of the State. As the State government has not constituted GRF as per para 6 of the Kerala Ceiling on Government

Guarantees Act, 2003 and RBI guidelines, guarantee commission of `124.50 crore collected during 2018-19, was not transferred to the Guarantee Redemption Fund under Public Account, leading to understatement of revenue expenditure to this extent. Guarantee commission `1,099.79 crore collected during 2003-04 to 2018-19 had not been credited to the Fund but treated as non-tax revenue and used for meeting the revenue expenditure of Government.

Chapter 2

A Medium - Term Fiscal Path for Kerala Post COVID 19

2.1 Introduction

History is replete with visitations of pandemics in India. The 'Black Death' plague of 1346-1353, Spanish flu pandemic during 1918-20, several bubonic plague pandemics during 1855-1960, the spread of small pox in 1974 are some of the major examples. Each pandemic was associated with large human cost and economic distress. All pandemic episodes 'were associated with a contraction/deceleration in GDP, with the 1918 flu registering the sharpest downturn of about 13 per cent' (RBI, 2020, p.39). The recovery pattern is also observed to be quite similar – 'a sharp rebound in the immediate subsequent year because of favourable base effects, followed by contraction again, with the GDP growth rate finally subsiding back to pre-pandemic years in about 3-4 years'(ibid.). It was also observed that generally the recovery was swift except in the case of the 1918 flu, largely because it was superimposed on a pre-existing slowdown in the economy.

Policy responses post pandemics have essentially focused on the provision of medical and public health services, measures offsetting the pernicious impact of pandemics on the livelihoods and large - scale fiscal stimuli to resuscitate the economy. How quick is the recovery, has depended on the size and scope of fiscal response. COVID 19 has many similarities with the 1918 flu as the GDP contraction has occurred at the back of an already decelerating economy since 2016-17. The states have a huge responsibility as they are closer to the people. In this context a report of the Committee at this juncture, although for the year 2018-19, needs necessarily visualize a fiscal path for the medium term to aid quick and stable recovery.

2.2 The Path of Deficits in Kerala

Kerala had been facing severe fiscal stress in the 1990s and early 2000s. GFD running at more than 3.5 per cent of GSDP in the early 1990s rose steadily and crossed 5 per cent in 1998-99 and reached close to 7 per cent in 1999-00. Although it came down by about one percentage point in the next year was hovering between 5 and 6 per cent till the FRA was implemented in 2004-05. Since then, a concerted effort has been made to bring down the FD to meet the specified targets.

Table 11: RD and FD Trends, Kerala, 1990-91 to 2007-08

Year	Three Year Average	
	GFD	RD
1991 - 92	3.93	1.93
1994 - 95	3.5	1.23
1997 – 98	4.58	2.44
2000 - 01	5.38	4.32
2003 – 04	5.22	3.98
2006 - 07	3.36	2.29

Source; GoK, Budget in Brief, Various Years

In conventional fiscal practice, a fiscal deficit is run to meet higher capital expenditures. But the Kerala experience has been different. Capital expenditure that was 1.6 per cent of GSDP in 1991-92 and was maintained at around 1.4 per cent till 1997 – 98 fell sharply to 0.7 per cent by 2000-01. The bulk of FD has gone to meet the burgeoning RD since the mid-1990s (Table 11). While RD accounted for about 40 per cent of FD in the early 1990s, it steadily rose to 80 per cent by the end of 1990s and continued at that level till the mid-2000s. Thus, high and rising current expenditure was behind the rising RD and FD till the FRBM Acts were introduced.

The factors accounting for the high RD are the rising shares of salary and pension in TRR. The share of salary was more than 40 per cent of TRR in the early 1990s and towards the end of the decade had crossed 50 per cent in a few years. The share of pension rose steadily from around 10 per cent in the early 1990s to over 20 per cent by the end of the decade. Along with these two the rising debt caused interest payments too to rise from less than 15 per cent in 1990-91 to over 25 per cent in 2000-01. The three components – SIP- together accounted for two – thirds of TRR in the early part of the decade and were larger than the TRR in 1999-00. Generally, the Revenue Expenditure bears a ratio of over 1.50 to the SIP total and its difference from TRR is the RD.

FRA 2003 and Kerala Fiscal Responsibility Rules 2005 brought about a change in the overall fiscal situation in the state. SIP as a proportion of TRR was brought down from more than 80 per cent in 2003-04 to around 60 per cent by 2009-10. Total Revenue Expenditure that was ranging between 16 and 18 per cent of GSDP throughout the 1990s into the early 2000s was brought down by 3 percentage points to less than 14 per cent by 2005-06 and to below 13 per cent by 2009-10. Total Expenditure too was brought down by a small percentage point initially by maintaining Capital Expenditure at around 1.4 per cent of GSDP till 1998-99 and by reducing it since then.

The initial period of FRBM, 2004-05 to 2010-11, saw the Total Expenditure maintained below 15 per cent of GSDP and Revenue Expenditure below 14 per cent. During this period, Capital Expenditure witnessed mild increase but remained less than 1 per cent of GSDP. GFD was brought down from close to 6 per cent in 2002-03 and 2003-04 to below 3 per cent by 2006-07 and RD from close to 4 per cent to below 2 per cent. While many Indian states succeeded in achieving surplus in the Revenue Account during this period, Kerala was only able to reduce it below 2 per cent of GSDP. Fiscal 2010-11 showed the best performance by achieving RD of 1.13 per cent and FD of 2.38 per cent. The factor contributing to the rising RD was the growing Revenue Expenditure on the back of high SIP and growing ratio of RE/SIP. This period, 2004-05 to 2010-11, saw the ratio maintained around 1.5 and mostly below it.

The decade of 2010s did not begin well for Kerala. RD doubled to 2.21 per cent in 2011-12 and FD rose by over 1 percentage point. The average RD for the next five years continued to remain high at 2.26 per cent and FD at 3.52 per cent. The declining trends observed during the preceding five years were reversed. Along with the rising deficit the debt too began to rise. The initial period has seen debt come down steadily from 39 per cent of GSDP in 2004-05 to 24.24 per cent in 2010-11, the lowest point of the period since 1990-91. Debt climbed by 0.75 percentage points every year during 2011-12 to 2015-16 to hit a high of 28 per cent of GSDP in 2015-16. The period also saw considerable relaxation of the ratio of RE to SIP that had been kept below 1.5 per cent, rising steadily and reaching 1.69 in 2014-15 and 1.65 in 2015-16. The next year, 2016-17, weighed by the stress of demonetization saw RD go up by 0.79 percentage points, FD by 1.12 percentage points and debt by 2.25 percentage points. Increase in TRR at an average rate of 17.43 per cent annually had fallen by half to 9.5 per cent in 2016-17.

The low growth of TRR that began with demonetization continued during the period 2016-17 to 2019-20 (Pre-Actuals) the average for the period being 6.4 per cent. But a concerted effort was taken to reverse the worsening fiscal situation. While the annual average of RD for the period 2016-17 to 2019-20 remained high at 2.19 per cent, the trend was a steady decline from 2.5 per cent in 2016-17 to 1.67 per cent in 2019-20. GFD too showed a similar reversal with the average remaining at 3.54 per cent and the terminal year FD falling by 1.6 percentage point to 2.59 per cent in 2019-20. Thus, despite the falling GDP growth rate and falling revenues the deficits were contained and the path set for fiscal consolidation was strengthened. This was achieved by keeping a tight leash on Revenue Expenditure other than SIP. The ratio of RE to SIP that had steadily gone up from 1.5 during the initial FRBM years to over 1.6 during 2011-12 to 2015-16 was brought down to an average of 1.57 during 2016-17 to 2019-20. In fact, in 2019-20, the ratio was only 1.47.

2.3 Fiscal 2019-20

The fiscal achievement of year 2019-20 calls for a special mention. The year reported one of the worst growth performances by India. The GDP growth rate that had fallen from 8 per cent in 2016-17 to 6.1 per cent in 2018-19 fell further to 4.2 per cent in 2019-20. Especially sharp was the fall in manufacturing, construction, trade, hotels and transport, and finance and real estate. The drastic fall in the key sectors and the resultant fall in consumption led to severe shortfall in tax revenue collection. The Central government could collect only Rs 13.55 lakh crore in 2019-20 compared to Rs 13.17 lakh crore in 2018-19 (2.94 per cent growth). The drastic reduction in central taxes resulted in severe shortfall in the receipt of assigned taxes by the states. The shortfall in the case of Kerala was 18 per cent from the budgeted figures (Table 12).

Table 12: Revenue Shortfall in Kerala, 2019-20

Revenue Receipts	Budget Estimates (Rs crore)	Pre-Actuals (Rs crore)	% Shortfall
1.Tax Revenue	88582.21	66530.68	24.89
GST	37616.34	24309.58	35.37
Stamps and Registration	4486.95	3614.05	19.45
Land Revenue	221.29	332.42	----
Taxes on Sales, Trade etc.,	23948.17	20316.67	15.16
Excise Duty	2983.74	2255.26	24.41
States Share of Union Taxes	14191.89	11668.53	17.78
Other taxes and duties	5133.83	4034.17	11.49
2.Non-Tax Revenue	15070.07	11750.37	22.03
3.Grant-in-Aid and contributions	11702.43	9415.50	19.54
Total Revenue Receipts	**115354.71**	**87696.55**	**23.98**

Source: https://cag.gov.in/en/state-accounts-report?defuat_state_id=77

The tax revenue shortfall is much larger than the fall in GDP growth rate. Obviously, the compositional effect and the large fall in consumption has hit the tax receipts hard. At the state level, the shortfall in GST was a whopping 35 per cent. Even after the addition of the compensation received from the Centre (shown under Grants in aid and Contributions) the shortfall is about 23 per cent. The shortfall in various other taxes varied between 15 to 24 per cent (Table 12). Fiscal management under such circumstances required a discipline of very high order.

Table 13: Expenditure Compression in 2019-20

Expenditure	**Budget Estimates (Rs crore)**	**Pre-Actuals (Rs crore)**	**% Difference**
Revenue Expenditure (a+b+c+d+e)	131087.20	102275.02	-21.98
a. Expenditure on Revenue Account (excluding (b),(c),(d)&(e)	57513.73	32726.40	-43.10
b. Expenditure on Interest Payment	18995.63	16175.57	-14.85
c. Expenditure on salaries and wages	33602.29	32930.75	- 2.00
d. Expenditure on Pension	18911.84	19064.27	0.81
e. Expenditure on Subsidy	2063.71	1378.03	- 33.23
Capital Expenditure	17179.26	8007.47	- 53.39

Source: https://cag.gov.in/en/state-accounts-report?defuat_state_id=77

The response to a large revenue shortfall is often a contraction in capital expenditure. Kerala too resorted to this practice by reducing capital spending by 53 per cent. But capital expenditure accounts for less than 12 per cent of the total expenditure and hence a large reduction in it is not adequate to restore fiscal health. Expenditure had to be cut on revenue account and there is limited scope for contraction in SIP component of revenue expenditure. But all the three of them were maintained at the level of budget estimates, not allowing any overshoot. The only item that could be compressed was revenue expenditure excluding SIP. It was brought down by 43 per cent. Such a compression brought the ratio of total revenue expenditure to SIP to 1.50 from 1.64 the previous year. Borrowing too was brought down consequent to reduction in Revenue Deficit and Fiscal Deficit to 1.67 and 2.59 per cent respectively. The fiscal consolidation path was adhered to despite the adverse circumstances.

2.4 Medium - Term Fiscal Path post COVID 19

The deceleration in GDP and the fall in revenue could be managed by a tight leash on revenue spending other than SIP and contraction of capital expenses. But these options get closed in a pandemic situation where non - SIP expenses have to expand to meet medical and public health needs and livelihood support, and capital spending for sustained recovery. Thus, in the current year (2020-21) both RD and FD are expected to shoot up and the path for bringing these down post COVID 19 has to be visualized.

Working out the medium - term fiscal path post COVID 19 involves four distinct steps. The first step is to make projections of the GSDP for 2020-21 and the subsequent three years. The second step is to project the revenue stream for the relevant years. The third step is to project the revenue expenditure for the period under consideration. The fourth is to make definite assumptions about capital spending so as to make projections of the Total Expenditure. With these steps it is possible to arrive at the RD and FD for the medium term and also derive modified paths altering various assumptions.

GSDP at current prices in 2019-20 is taken as Rs 871534 crore (quoted in the Budget 2020-21). For India, Asian Development Bank has projected GDP contraction of 8 per cent in real terms and the latest RBI projection was a contraction of 7.5 per cent. For Kerala we have taken the Indian growth numbers. We have taken 8 per cent contraction in real terms and inflation projection of 5.8 per cent of ADB as the RBI's projection of 4 per cent is an underestimate. The two together will give a growth of GSDP at current prices of -2.2% = -8 + 5.8. The estimate of GSDP for 2020-21 would then be Rs 8,52,361 crore. Historical experience suggests that the recovery in the immediately succeeding year of a pandemic would be large. Accordingly, we take the generally talked about 11 per cent (Fitch Ratings) real growth and an inflation of 5 per cent. The 16 per cent increase in GSDP will generate Rs 988739 crore for 2021-22. Going by the historical experience, a sharp recovery is followed by a fall in growth rate. Taking 6 per cent growth in real terms and inflation of 4 per cent, the GSDP for 2022-23 would be RS 10,87,613 crore and taking the same trend for the next year would give Rs 11,96,374 crore for the next year (2023-24).

Total Revenue Receipts (TRR) for 2020-21 is taken as Rs 87697 crore arrived at by projecting the monthly trends till October 2020 (CAG website- State Accounts Report). The projections for the subsequent years have taken the GSDP growth rate in current prices assuming a tax buoyancy of 1 as seen in the previous chapter. The projections are shown in Table 4. Salary (S), Interest Payments (I) and Pension (P) have been projected taking the growth rates for the period 2011-12 to 2019-20 (S – 10.4%, I – 13.8%, and P – 12.6%) and 2019-20 as the base. Revenue Expenditure for 2020-21 has been worked out taking the ratio of RE to SIP till October 2020, that is 1.7. For the next three years, the ratio is taken as 1.5 achieved in 2019-20. Capital Expenditure is projected at Rs 9210 crore for the year 2020-21 taking the trend till October 2020. For the next three years Capital Expenditure is assumed to grow at the rate of GSDP growth rate to maintain the CE/GSDP rate achieved in 2020-21, that is 1.08. The projections are presented in Table 14.

It is evident from the RD and FD figures in Table 4 that the year 2020-21has completely scuttled the fiscal consolidation efforts of the previous four years by taking the RD and FD to levels seen only in the 1990s. And as long as the SIP grows at the rate at which they have been growing the last ten years, even when the RE to SIP ratio is maintained at a low level of 1.5 and capital expenditure is not above 1 per cent of GSDP, RD and FD may not be coming down (Table 14).

Table 14: Projections of Revenue, Expenditure and Deficits, 2020-21 to 2023-24 (Rs crore)

Description	**2020-21**	**2021-22**	**2022-23**	**2023-24**
GSDP at current prices	852361	988739	1087613	1196374
Total Revenue Receipts (TRR)	87697	101729	111901	123092
Interest Payments (I)	18408	20949	23840	27129
Salary (S)	36356	40137	44311	48919
Pension (P)	21466	24171	27216	30646
Revenue Expenditure	129591	127884	143050	160042
Capital Expenditure	9210	10684	11752	12927
Total Expenditure	138801	138568	154802	172969
Revenue Deficit (RD)	4.92	2.65	2.86	3.09
Fiscal Deficit (FD)	6.00	3.73	3.95	4.17

Note: RD and FD are per cent of GSDP.

It is important for the state to visualize a fiscal consolidation path after the very high RD and FD suffered in the COVID 19 year of 2020-21. A few scenarios have been worked out here. Scenario I keeps the expenditure trends as in Base Scenario, that is salary and pension grow at historical trends, capital expenditure is maintained at 1% of GSDP, and Revenue Expenditure bears a ratio of 1.5 to SIP. Total Revenue Receipts is projected to grow at 20 per cent. In such a scenario, FD will continue to remain above 3 per cent and RD above 2 per cent even three years after the COVID 19 year (Table 15). If Total revenue is projected to grow at 25 per cent per year beyond the COVID 19 year, other things remaining as in Scenario I, RD will come down to below 1 per cent in 2023-24 and FD below 2 per cent. It is difficult to think of achieving 20 or 25 per cent annual growth of revenue as the experience of the last ten years suggest otherwise. Especially so, as the award of the 14^{th} FC was bountiful to Kerala and we do not visualize such a situation with regard to the 15^{th} FC.

Table 15: Four Different Fiscal Consolidation Paths post COVID 19

Description	2020-21	2021-22	2022-23	2023-24
Base Scenario (Copied from Table 14)				
Revenue Deficit (RD)	4.92	2.65	2.86	3.09
Fiscal Deficit (FD)	6.00	3.73	3.95	4.17
Scenario I: Salary and Pension growing at historical high levels, capital expenditure growing at GSDP rate, Revenue receipts growing at 20%				
Revenue Deficit (RD)	4.92	4.02	3.30	2.49
Fiscal Deficit (FD)	6.00	5.10	4.38	3.57
Scenario II: Salary and Pension growing at historical high levels, capital expenditure growing at GSDP rate, Revenue receipts growing at 25%				
Revenue Deficit (RD)	4.92	3.57	2.31	0.84
Fiscal Deficit (FD)	6.00	4.65	3.39	1.92
Scenario III: Salary and Pension growing at 5%, Capital Expenditure growing at GSDP rate, Revenue receipts growing at Base Scenario				
Revenue Deficit (RD)	4.16	1.50	1.21	0.95
Fiscal Deficit (FD)	5.24	2.58	2.29	2.04
Scenario IV: Salary and Pension growing at 5%, Capital Expenditure kept at 2020-21 level, Revenue receipts growing at Base Scenario				
Revenue Deficit (RD)	4.16	1.50	1.21	0.95
Fiscal Deficit (FD)	5.24	2.43	2.06	1.72
Scenario V: Salary and Pension growing at 9%, Revenue receipts growing at 16% in 2021-22, 10% in 2022-23 and 12% in 2023-24				
Revenue Deficit (RD)	4.92	1.60	1.62	1.42
Fiscal Deficit (FD)	6.00	3.00	3.00	3.00

One of the ways to bring down RD and FD is to reduce the rate of increase of Salary and Pension. The ratio of RE to SIP cannot be brought down below 1.5 and the rate of increase of Interest Payments are not available for intervention. Instead of the over 10 per cent increase of Salary and Pension if they were reduced to 5 per cent then the RD comes down rapidly (Scenario III). If a milder fall in RD is desired, then Salary and Pension increase can rise above 5 per cent. The FD would also come down. By keeping capital expenditure at a low-level RD cannot be brought down (Scenario IV). In fact, Scenario III and IV suggest that capital expenditure can be increased to maintain the FD at the level of 3 per cent.

Scenario V has been worked out by keeping FD at 3 per cent (Table 15). As Scenarios I - II and III – IV take extreme values for the growth of Revenue Receipts and Salary and Pension, a more pragmatic set of growth rates has been taken. Salary and Pension are taken to grow at slightly lower than (9%) the long term trend values and the ratio of Revenue Expenditure to SIP is taken at 1.4. Revenue Receipts are taken to grow at 16 per cent in 2021-22, 10 per cent in 2022-23 and 12 per cent in 2023-24. In Scenario V, RD will come down to

1.6 per cent in 2021-22, 1.62 per cent in 2022-23 and 1.42 per cent in 2023-24. As the FD is kept at 3 per cent, Capital Expenditure would rise to 1.40 per cent in 2021-22, 1.38 per cent in 2022-23 and 1.58 per cent in 2023-24. That would mark a fiscal consolidation path again with a rising Capital Expenditure.

2.5 Conclusion

This chapter has brought out the significance of visualizing a fiscal consolidation path post COVID 19. Without the projections made based on the analysis of trends in salary, pension, interest payments it would have been difficult to see what time period is required to bring RD down to 1 per cent or zero. The options before the government are: either to raise the rate of growth of revenue, or to lower the rate of increase of salary and pension, or a combination of the two.

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