KERALA ECONOMY
2023, VOL. 4, NO.4. pp 01-10.
ISSN : 2583-4436

Rebuilding a sustainable Kerala economy: Raising two issues

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Broadly speaking an economy is a social arrangement for meeting the material needs of its people and therefore is socially embedded. I would say, Kerala a sub-national state economy linked to the Indian economy via its federal constitutional setup found a 'local habitation and a name' from April 5, 1957, when the first Communist Party of India (CPI) rode to power via the ballot box. That event was the triumph of public reason over superstition, a saga of public action over class-caste iniquities. The state had several splendid social attainments since then which made Robin Jeffery, a co-panelist today to call it "an object of fascination of scholars and policy makers" around the world.[Jeffrey (1992) p.xi]. While Kerala continues to hold its head high it has to be eternally vigilant to keep it on an even keel. Five years ago after the devastating flood of 2018 Chief Minister Pinarayi Vijayan wanted the people to encounter it as "a challenge and an opportunity to rebuild the state to ensure better standards of living to all sections of the society". With AI ChatGPT capabilities, large language model (LLM) and the like knocking at our doors a nonagenarian like me is excited to participate on this occasion. I would like to take only two issues, which I consider basic to building *Navakeralam* and its economic foundation.

(i) Environmental Issue

Walled off by the Western Ghats and watered by the Arabian Sea, replete with 44 rivers, backwaters, rich coastal areas wetlands and forests Kerala one of the beauty spots of this planet faces an ecological crisis that demands strategic intervention to build 'a green economy' as the PDNA (Post-Disaster Needs Assessments) report suggests. That paddy lands once a main stay of Kerala's food economy declined from 35 per cent of the total cropped area at the time of the formation of the state to below 7 per cent now is an irreparable loss for everyone who loves the state and its beauty. The rice cultivation in Kerala unlike in other parts of India is done on a watershed basis which commands the highest environmental value per hectare in the world [Costanza R etal (1957)]. Reports say that almost 97 per cent of paddy lands in Wayanad got reclaimed for non-agricultural purposes, not to speak of the damage done to Kuttanad, Kole and other wet lands. The water scarcity that Kerala faces today is largely linked to this reclamation. The Kerala Conservation of Paddy Land and Wetland Act 2008, passed much late in the day only ratifies illegal transgressions. We cannot also forget the story of the fast shrinking backwaters, the identification of the Cochin-Kalamassery industrial belt as one of the 'toxic hotspots' of the world, devastation of the state's vast coastal natural eco-system without attempting an integrated approach to its environment, and many such lapses. Ignoring this is a disaster which affects the sustainability of Kerala economy and much more the rebuilding of the Navakeralam project.

That quarrying, metal crushing and sand-mining controlled by vested interests endanger our ecosystem is a fact to be reckoned with but quietly ignored. Instructively most reports of the Legislative Environment Committees regarding the working of the quarries did not approach the problem directly. Although the 2019 report pointed out that illegal quarries were ten times more than the legal ones, more quarrying and crushing units were sanctioned, and that too notwithstanding the 2018 and 2019 floods and landslides. Even though the state itself is an environmentally fragile entity our Legislative Assembly in their wisdom unanimously rejected the Madhav Gadgil Committee Report (2013) which made very valid recommendations to rebuild the future of this land which we proudly call God's own country. In this context Kerala cannot forget, Gadgil's comment on the Pettimuddi landslide that killed 70 persons in the night of August 6, 2020:

> "The government, it seemed, stood with the mining mafia and not with the environment or the people even after the devastating landslides at Puthimala, Kavalappara and Pettimudy"[*The Hindu,* Trivandrum edition, August 12, 2020].

Indeed this government responded to the flood disasters remarkably well and even mobilised $370 million from the World Bank which brought on board three other partners and prepared "the course for centering resilience-related policies and institutional reforms in key cross-cutting areas and sectors of the economy to enhance resilience to enable holistic river basin management, sustainable sand climate-resilient agriculture, risk-informed land-use planning and multi-year capital planning, disaster management plans at all levels" [GoK(2022):p.6]. But why then until August 31, 2022, Kerala has requested funds for only US$ 23.20 or just

6.2 per cent and utilised only around 3 per cent of the total promised fund? This is a baffling question when we think of Kerala's future.

(ii) Fiscal Sustainability Issues

How and why Kerala which has been admirably implementing the directive principles of state policy in education, health, social security and so on, besides implementing Articles 243G, 243W and 243ZD creditably is projected as fiscally unsustainable needs scrutiny. A study on human development index spanning a period of 28 years from 1991 finds Kerala invariably on top of the major Indian states. This study also shows a reduction in interstate disparities (5 year convergence) of HDI with the rate of convergence decelerating after 2004-05 with the implementation of FRBM Act by the states [Oommen and Chakravartti (2023)]. However Kerala looks like a sinner on the cross as exemplified in the Chart 4 of RBI (2022:p.119) which shows the state-wise five year average of revenue expenditure (2017-18 – 2021-22) as percentage of total expenditure. Although Kerala finance managers are not saints in keeping prudential norms I would hypothesis that the revenue classification and the FRBM Act may have to accept a big share of the blame, for everything is hooked around the debt-deficit ratio targets as the measuring rod of fiscal success.

To be sure, it is the Finance Minister who has to face the quotidian reality of fiscal crisis. In an earlier regime a Chief Minister was reportedly denied the Air ticket to Delhi for want of money. Today we have no such catastrophe. But if this contrast is by postponing pending payments (in the cash based accounting system of today it is difficult to get a full picture and for best results, there is no alternative to accrual-based accounting system) we are only postponing an impending economic crisis. Evidence shows that vital payments to mid-day meal scheme, supply co., contractors, hospital consumables etc., are held up via treasury control. It is not a liquidity crisis, but a revenue crunch to meet expenditure which is a serious issue. Kerala economy is indeed robust and kicking as the concept note underscores. It appears Kerala state is like a beggar sitting on a bench of gold. If so where should one seek the way out? For this, one should figure out the magnitude, however rough it could be.

Staying within the debt-deficit ratio framework a study by two scholars of GIFT, arrive at a sustainable threshold level debt-GSDP ratio of 27.8 per cent (one can have different levels depending on the assumptions)[Renjith and Joseph (2023)]. If one accepts this as a benchmark the state is in the financial doldrums. For one thing, the FRBM limit is 29.67 per cent (including off-budget borrowings). Or look at the CAG's overall debt –GSDP ratio of 42.8 per cent for the year ending 31st March 2021 [see GoK (2022), p.70]. To draw attention to the magnitude, assuming that the threshold figure has some relevance and using the Budget-in-Brief numbers for 2023-24, the debt-GSDP ratio works out to 36 per cent gives a margin of about 8 per cent which in figures is Rs.90675 crore. Although I do not want to hold any brief for the government, it is incorrect to ignore the historically accumulated burden of the social sector expenditure on the state that needs to be maintained, leave alone improved. The unfolding fiscal situation has to be taken seriously. Although Kerala can satisfy the Domar conditions because of low real interest rates, several other norms like annual debt rate increase outdistancing economic growth rate for several years continuously and so on, leave many things to be desired. But the crucial test of sustainability is the capability to increasingly plough back the growing GSDP share into capital outlay. Table 1 showing the capital outlay/GSDP ratio for 11 years does not tell a consistent or sanguine story. Till 2016-17, there was steady improvement. The situation reversed from 2020-21.

Table 1: Share of Kerala's Capital outlay to GSDP (2012-13 to 2022-23)

Year	Capital Outlay (In Crore)	GSDP (In Crore)	Capital Outlay/GSDP
2012-13	3465.66	379417	0.91%
2013-14	3497.62	462916	0.76%
2014-15	3880.54	526002	0.74%
2015-16	6518.48	557947	1.17%
2016-17	8945.65	616357	1.45%
2017-18	8748.87	701577.4	1.25%
2018-19	7430.54	790302.3	0.94%
2019-20	8454.8	824374.2	1.03%
2020-21	11935.76	771008.7	1.55%
2021-22	13207.68	906920.9	1.46%
2022-23 (Revised Estimate)	14079.47	1017873	1.38%

Source: Budget in Brief, Govt of Kerala, Various Years

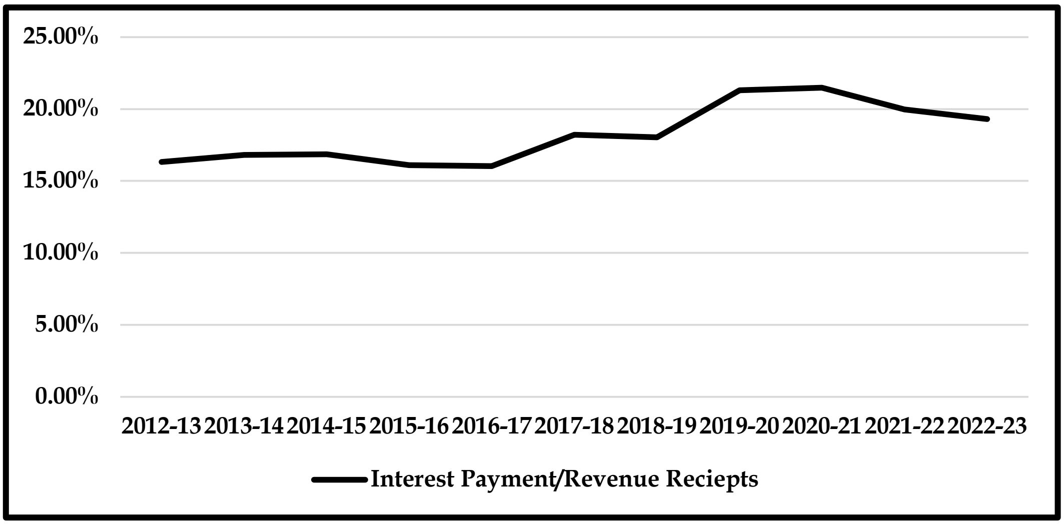
The interest payments and revenue receipts ratio given in table 2 and the graphical account given in Figure 1 show that there was consistency up to 2017and worsened since then with pick up in 2019-20 and 2020-21.

Table 2: Interest Payments And Revenue Receipts Ratio (2012-13 to 2022-23)

Year	Interest Payment	Revenue Receipts	Interest Payment/ Revenue Receipts
2012-13	7204.81	44137.3	16.32%
2013-14	8265.38	49176.9	16.81%
2014-15	9769.59	57950.5	16.86%
2015-16	11110.6	69032.7	16.09%
2016-17	12116.5	75611.7	16.02%
2017-18	15119.9	83020.1	18.21%
2018-19	16747.9	92854.5	18.04%
2019-20	19214.7	90224.7	21.30%
2020-21	20975.4	97616.8	21.49%
2021-22	23302.8	116640	19.98%
2022-23 (Revised Estimate)	24960.4	129268	19.31%

Source: Budget in Brief, Govt of Kerala, Various Years

Figure 1: Interest Payments and Revenue Receipts Ratio (2012-13 to 2022-23)



Source: As above

The Masala Bond bearing 9.723 per cent interest (due from 2018-19), taking loans from the auction window of Reserve Bank of India with interest above 8 per cent and so on might have also altered the situation.

To be forewarned is to be forearmed. It is important to launch short-term, medium term and long-term correctives. This involves fiscal, economic and political strategies. I take up only a few medium-term economic measures which have to be simultaneously taken up to obtain sustainable results.

One, the State needs a compensative vision, Kerala economy is a service-led growth episode, which may be called 'precocious servicification' to borrow a phrase from Lamba and Subramanian (2020). Admittedly Kerala's growth is not manufacturing-induced as is the usual growth pattern in other countries. This highly consumerist-state economy has a huge trade deficit, with other states buying more than it exports which in 2019-20 was to the tune of one trillion rupees as Sushil Khanna has well documented [Khanna (2020)]. Barring large exports from the public sector unit like the Cochin refinery and traditional cash crops and marine products Kerala does not have a strong export market. Why a high consumeristic economy failed to stimulate production in the state is a bigger issue to be investigated. For example the state has failed to capitalise on the tremendous demand from the schools, colleges, and hospitals of the state. Even writing pencils and pen are not made in Kerala, not to speak of hospital equipments. Can the digital economy which is well-rooted take us into sustained take-off? Admittedly it was not the lack of money that was the bottleneck. Then what is a larger question to be addressed. As Gulf-money flow tapers, the large exodus of youth continues with permanent exit options and the demographic transition slipping into a geriatric home wanting more care industries it is high time we seriously sit back and think about our future.

Two, Kerala has 163 public sector enterprises, the largest compared to other states with a total investment of Rs.62262 crore or 6.7 per cent of the GSDP in 2021-22. Although the average investment per employee increased from Rs.41.13 lakh in 2020-21 to Rs.48.87 lakh in 2021-22, the average profitability per employee registered a loss of Rs.1.35 lakh. All units both profitmaking as well as loss making are entitled to bonuses. The negative net worth loss also is staggering. If we take the net worth loss of KSEB and KSRTC alone, it is a huge sum of Rs.30503.57 crore. No Finance Minister can swim crises with weighty stones around his/her neck. Some rationalisation is inevitable before it is too late.

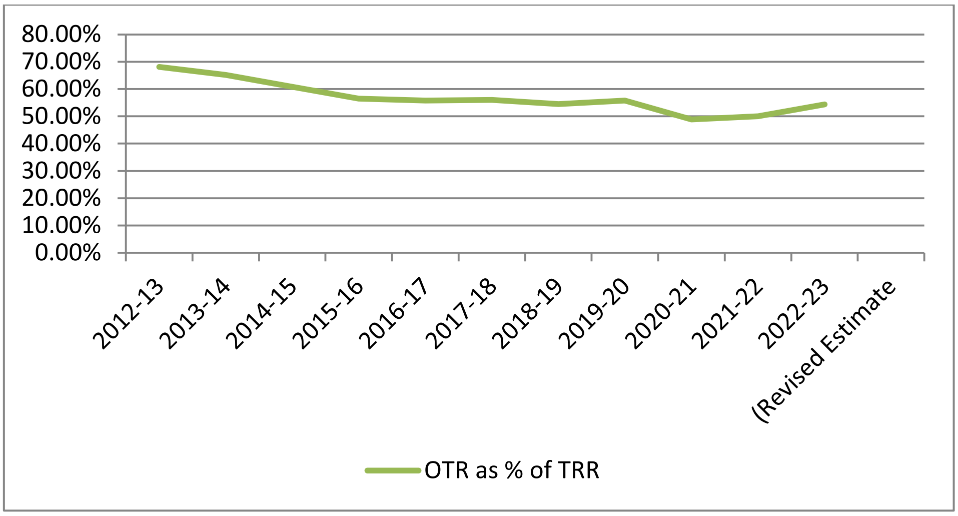
Three, while most countries and now India follow the pay-as-you-go pension system Kerala has to make strong decisions on this issue. In the current budget pension accounts for 21 per cent of total revenue and 32 per cent of own tax revenue, (highest among the non-special category states). There is a valid case for rectification because own tax revenue even a little over a decade before in 2012-13 was as high as 68. 1 per cent and it steadily declined and reached 48.8 per cent in 2020-21 and only marginally picked up. (see Table 3and fig.2). Fiscal space for development expenditure is getting severely constrained as own tax revenue support weakened. Paying pension to a person of two years of service till eternity,(provided to the staff of Ministers) however meritorious his/her service be, is a totally unjustifiable case of unfunded liabilities. Expansion of unfunded liabilities such as the compulsion to pay the repayment obligations of loans taken by public sector undertaking cannot continue for long. It is difficult to finance unfunded liabilities unless you have an Aladdin's wonder lamp.

Table 3: Own Tax Revenue (OTR) as percentage of Total Revenue Receipts (TTR) (2012-13 – 2022-23)

Year	Own Tax Revenue	Total Revenue Receipts	OTR/TRR
2012-13	30076.6	44137.3	68.10%
2013-14	31995	49176.9	65.10%
2014-15	35232.5	57950.5	60.80%
2015-16	38995.2	69032.7	56.50%
2016-17	42176.4	75611.7	55.80%
2017-18	46459.6	83020.1	56.00%
2018-19	50644.1	92854.5	54.50%
2019-20	50323.1	90224.7	55.80%
2020-21	47660.8	97616.8	48.80%
2021-22	58340.5	116640	50.00%
2022-23 (Revised Estimate)	70188.5	129268	54.30%

Source: Budget in Brief, Govt. of Kerala, Various Years

Figure 2: Own Tax Revenue (OTR) as percentage of Total Revenue Receipts (TRR)



Source: As above

Four, the cooperative sector has been for long a great support to the Kerala economy. The primary credit corporative societies with less than 2 per cent of the total number in India accounted for nearly 70 per cent of India's deposits. This is proof of the dynamism of the sector. That the Kerala government created the primary cooperatives consortium for security pensions and borrowed funds from it is because it was a viable source. Today several cooperative banks could not repay their depositors and there is a loss of public trust. Redeeming this trust is crucial to the stability of the Kerala economy because the cooperative sector once served the poor of the state in their need.

Although this is not the occasion to consider the larger issue of union-state relations, reconsidering the FRBM regime is pertinent. The relevance of the debt-deficit ratios need be theoretically rationalised and be managed by a federal agency with adequate representation from the states. Further, the context of division of powers made under Article 246 and the Seventh Schedule has radically changed. The shift to a market-mediated paradigm of governance, the ascendancy of state level political parties, technological advancement, changes in demographic structure, centre legislating on subjects in the state and concurrent list and imposing burden on the states and so on demand a revisit of the seventh schedule. The addition of eleventh and twelfth schedules which list the functional responsibilities of panchayats and municipalities which was simply lifting items from state and concurrent lists have added tremendous confusion in assigning functions to the three tiers of panchayats and the nagar panchayats, municipalities and corporations. It is high time the Indian federation asks the question *denovo* who should do what on the basis of the subsidiarity principle viz., what can be done best at a particular level should be done at that level and not at a higher level. The Constituent Assembly failed to raise the question by borrowing heavily from the Government of India Act, 1935.

To conclude, several other issues stare us in the face. Building a sustainable Kerala economy with a comprehensive vision is a multi-faceted challenging project. At this momentous occasion of 'Keraleeyam', Can Kerala make a resolve to eradicate corruption and walk the talk letting words flow from the depth of truth and promote viable investments for the youth and future generations. Indeed, we have also to restore Kerala's beauty and make it as poet Keats said 'a joy forever'.

[An expanded version of the talk delivered at the *Kerala Economy* seminar of Keralyeeam, on November 3, 2023 at the Sankara Narayanan Thambi Hall, Kerala Legislative Assembly]

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