

Financing Development: Some Issues

R Kavita Rao

National Institute of Public Finance and Policy

Describing state of development for Kerala

- Traditional thresholds don't apply – share of employment in agriculture is low – 20 percent versus 43 percent for all India – PLFS
- Share of regular wage or salary employment is higher in Kerala at 35 percent as compared to 21.7% all India; share of helper in household enterprise is significantly lower at 4% as compared to 19% all India.
- High density of population: 913 per sq km versus 415 all India
- Aging population: Median age of 35.1 years against 28 years all India
- Top scores in SDG, HDI
- Significant improvement in the ease of doing business – BRAP- top performer
 - Should help reduce gestation lag of projects – CMIE capex suggests an increase in gestation lag in last few years

Can we understand development goals as follows?

- Generating sustained economic activity, resulting in jobs and incomes in the state
- Investing in R&D for creation of niche markets for products generated in the state
 - New Zealand (Manuka Honey, Golden Kiwi)
- Creating and augmenting human capital for engaging with new age technologies

Financing development

- The resources side of the picture
 - Own tax revenue to GSDP of Kerala has declined over the years – even post covid – 2022-23 it was 6.92%, dropped to 6.13 percent by 2024-25 and forecast to drop below 6 percent in recent budget
 - Compared to other major states – somewhat lower – Chhattisgarh, Goa, Maharashtra, UP and Telangana report ratios > than 7 percent.
 - Own non-tax revenue – marginal moderation in ratio to GSDP – 1.3% IN 2024-25.
 - Better than other non-mineral rich states
- Improvements in GST revenue performance could be one element in the story – faceless adjudication, and amnesty for settling arrears

Finance Development

- The expenditure side of the picture: expenditure priorities could be broadly classified into three categories apart from basic public goods:
 - Supporting expansion in economic activity – infrastructure and other support
 - Augmenting human capital formation – education and health
 - Social welfare
- States: small open economies: expenditure side stimulus will leak out of the economy – multiplier cannot be localized
 - To maximize the local gains, the first category of expenditures might be critical – creates repeated cycles of employment and income generation in the local economy
- Finding a suitable balance between these three could be critical for sustainability of government finances in the medium term

Debt dynamics

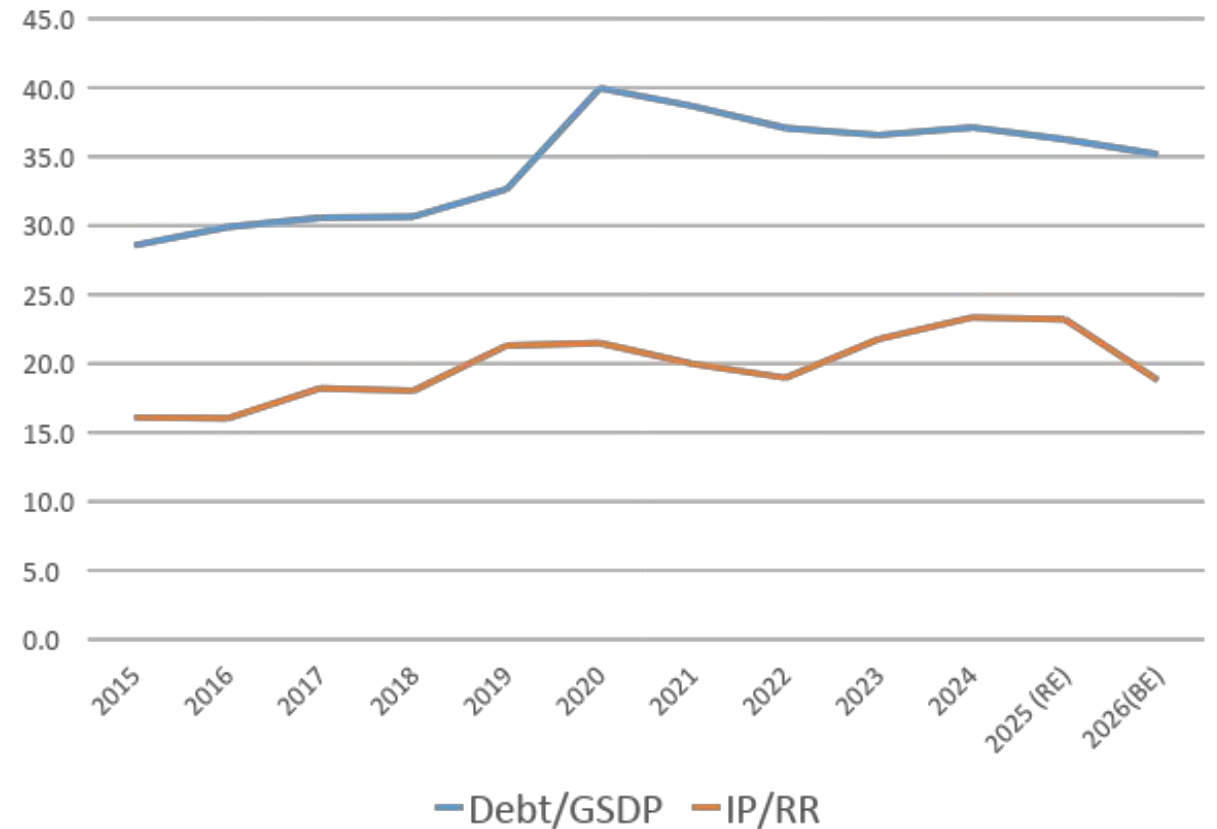
One way to think about debt dynamics:

$$D_t = D_{t-1} + FD_t$$
$$d_t = d_{t-1} * (1/(1+g)) + fd_t$$

- The average nominal growth of GSDP over the last decade has been marginally lower than 10%.
- If fiscal deficit is pegged at 3%, the debt to GSDP ratio would stabilize at 33 percent of GSDP
- Interest payment assuming nominal interest rate of 7 percent would amount to 2.31% of GSDP or 23 percent of revenue receipts

Kerala's debt and interest levels

- Interest payment is appropriating an increasing share of revenue receipts.
- Average interest rate on debt is around 7 percent – lower than growth in GSDP
- Should there be an effort to reduce debt to release resources for developmental spending in future?



Equity and Land Value Capture

- Improving the performance of PSUs: largest number of PSUs but a significant share of loss making PSUs
- Cochin Airport – interesting experiment of successful PPP involving stakeholders and state government – dividend payout as well.
- Given the scarcity of land in the state, there is scope to explore various methods of land value capture as well.
 - Equity for land parcels
 - Take Equity in Start-ups by providing seed capital (e.g. Finland, Sweden, Brazil, China)