

**GOVERNMENT FINANCE :
PUBLIC DEBT OF KERALA
1974-75 TO 1996-97**



*Thesis submitted to the
Cochin University of Science and Technology
for the award of the Degree of
DOCTOR OF PHILOSOPHY
under the Faculty of Social Sciences*

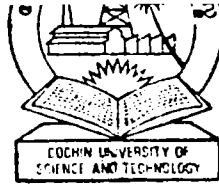
by

RAJAN VARUGHESE
Reg. No. 1406

under the supervision of
Dr. K. K. GEORGE
Professor and Director
School of Management Studies
Cochin University of Science and Technology

**DEPARTMENT OF APPLIED ECONOMICS
COCHIN UNIVERSITY OF SCIENCE AND TECHNOLOGY
COCHIN - 22, KERALA.**

AUGUST - 1999



SCHOOL OF MANAGEMENT STUDIES

COCHIN UNIVERSITY OF SCIENCE
AND TECHNOLOGY

Prof. (Dr.) K. K. GEORGE

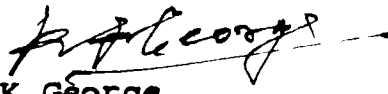
DIRECTOR

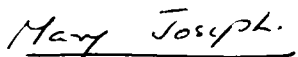
No: SMS.....

Date... **20 August 1999**

CERTIFICATE

Certified that the thesis "Government Finance - Public Debt of Kerala: 1974-75 to 1996-97" is the record of bona fide research carried out by Mr. Rajan Varughese under my guidance. The thesis is worth submitting for the Degree of Doctor of Philosophy in Social Sciences.


K.K. George
(Supervising Guide)


Dr. Mary Joseph
(Member, Doctoral Committee)

LIST OF TABLES

Table No.	Title	Page No.
3.1	India's Public Debt as Percentage of GDP	68
3.2	Growth of India's Public Debt :- 1950-51 to 1996-97	69
3.3	Total Interest Payments/GDP Ratio (1950-51 to 1996-97)	72
3.4	Interest Payment/Revenue Expenditure Ratio	73
3.5	Combined Repayments/Capital Disbursement Ratio of Centre and State Governments. (1950-51 to 1996-97)	74
3.6	Combined Debt Servicing (Centre and States)/ Total (Revenue + Capital) Disbursement Ratio of Centre and States: (1950-51 to 1996-97)	75
3.7	Ratio of Interest Payments to Total Debt Servicing (1950-51 to 1996-97)	77
3.8	Ratio of Debt Servicing to Gross Loans (1950-51 to 1996-97)	78
3.9	Domestic Debt and Liabilities of the Central Government as Percentage of GDP at Factor Cost	79
3.10	Domestic Debt and Liabilities of the Central Government (Annual Average Growth Rates): (1950-51 to 1996-97)	80
3.11	Share of Internal Debt/External Debt to Total Debt of Central Government	81
3.12	Interest Payments of Central Government - 1950-51 to 1996-97	83
3.13	Interest Payments of the Central Government (Percentage to Total Interest Payments)	85
3.14	Interest Payments of the Central Government (Percentage to Total Revenue Expenditure)	86
3.15	Interest Payments of the Central Government/GDP Ratio	87
3.16	Share of Central Government Interest Payment in Total Interest Payments (Centre & State)	87
3.17	Repayment/ Capital Disbursement (%) of Central Government	88
3.18	Share of Central Government Repayments in Total Repayment (Centre & States)	89
3.19	Total Debt Servicing/Total Disbursements (Revenue + Capital) of Centre	90
3.20	Ratio of Interest Payments to Total Debt Servicing of Central Government	91
3.21	Ratio of Debt Servicing to the Gross Loans of Central Government	92

Table No.	Title	Page No.
4.1	Public Debt of State Governments (Annual Average Growth Rates)	96
4.2	Outstanding Debt of State Governments /GDP Ratio (1950-51 to 1996-97)	97
4.3	Outstanding Public Debt of State Governments in India (1950-51 to 1996-97)	99
4.4	Category Wise Interest Payment of State Governments (Percentage of Total Interest Payments)	100
4.5	Category Wise Interest Payment of State Governments (to Total Revenue Expenditure)	103
4.6	Total Interest Payment (State Governments)/GDP ratio	104
4.7	Repayment-Capital Disbursement Ratio of State Governments (1950-51 to 1996-97)	106
4.8	Debt Servicing/Total (Revenue + Capital) Disbursement Ratio of State Governments 1950-51 to 1996-97	107
4.9	Ratio of Interest Payment to Total Debt Servicing of State Governments (1950-51 to 1996-97)	108
4.10	Ratio of Debt Servicing to Gross Loans of the State Governments	110
4.11	Relative Importance of Central Loans in Total Transfer of Resources from Centre to States	116
4.12	Ratio of Debt Servicing Payments to Gross Loans from the Centre, 1974-75 to 1996-97	118
4.13	Debt Servicing Payments on Central Loans and Inflow of Central Funds, 1979 to 1997	121
4.14	Ratio of Debt Servicing Payments of Central Loans to Total Disbursements (Capital and Revenue) 1974-75 to 96-97.	123
4.15	Ratio of Loan Repayments (Central Loans) to Non-plan Capital Disbursement 1974-75 to 1996-97	124
4.16	Ratio of Debt Servicing (Central Loans) to States' Own Resources (Revenue and Capital) 1974-75 to 1996-97	126
4.17	Outstanding Aggregate Debt of States 1978-79 to 1996-97	128
4.18	Rate of Interest on Central Loans (Other than Small Saving Loans) Plan and Non-plan	129
4.19	Rate of Interest on Small Saving Loans to States	132
4.20	Plan Outlay and Market Borrowings, V th to VIII th FYP	135
4.21	Maturity and Rate of Interest of Central and State Governments Borrowings (1974-75 to 1996-97)	138

Table No.	Title	Page No.
5.1	Composition of the Outstanding Debt of the Government of Kerala, 1975-75 to 1996-1997	144
5.2	Per capita Outstanding Debt of the Government of Kerala 1975-75 to 1996-1997	145
5.3	Outstanding Debt/SDP Ratio (Kerala) 1975-75 to 1996-1997	147
5.4	Ratio of Revenue Surplus/Deficits to Revenue Expenditure of Kerala and All States, 1974-75 to 1996-1997	149
5.5	Revenue Deficits /SDP Ratio (Kerala)	150
5.6	Ratio of Revenue Surplus/Deficits to Total Capital Receipts and Receipts in Public Accounts of Kerala and All States 1974-75 to 1996-1997	152
5.7	Gross Fiscal Deficit Movement over Years (Kerala and All States)	154
5.8	Uses of Gross Fiscal Deficits (Kerala and All States)	155
5.9	Share of Revenue Expenditure in Total Expenditure	157
5.10	Pattern of Plan Financing of Kerala VI th to VIII th FYP (1980-1997)	159
5.11	Growth and Composition of the Debt Receipts of the Government of Kerala, 1974-75 to 1996-97.	161
5.12	Per capita Debt Receipts of Kerala , 1974-75 to 1996-97	162
5.13	Growth of State Provident Funds and Small Savings - Kerala and All States: 1974-75 to 1996-97	167
5.14	Total Transfer of Resources from Centre to Kerala and the Relative Importance of Central Loans 1974-75 to 1996-97	171
5.15	Central Loans to Kerala and All States: 1974-75 to 1996-97	173
5.16	Composition of Central Loans to Kerala 1974-75 to 1996-97	177
5.17	Plan Outlay and Market Borrowings of Kerala 1974-75 to 1996-97	179
5.18	Percentage Share of Kerala in All States Market Borrowing 1974-75 to 1996-1997	180
5.19	Open Market Borrowing of Kerala: Period of Maturity and Redemption Yield; 1974-75 to 1996-1997	182
5.20	Negotiated Loan Receipts of Kerala 1974-75 to 1996-1997	186
6.1	Growth & Composition of the Total Disbursements	191
6.2	Ratio of Expenditure to State Domestic Product (Kerala)	193
6.3	Components of Final Outlay of Kerala 1975-76 to 1990-91.	195
6.4	Sources of Capital Receipts 1974-75 to 1996-97	196
6.5	Financing of Capital Disbursements by Public Debt in Kerala: 1974-75 to 1996-97.	198

Table No.	Title	Page No.
6.6	Arrears in Recovery of Amounts Overdue at the End of March 1997	200
6.7	Growth and Composition of the Capital Disbursements of Kerala - 1974-75 to 1996-97.	203
6.8	Debt as Percentage of Capital Outlay and Loans & Advances Made by the Government of Kerala 1974-75 to 1996-97.	210
6.9	Developmental Capital Outlay and Developmental Loans as Percentage of Total Capital Disbursement of Kerala 1974-75 to 1996-97.	212
6.10	Outstanding Public Debt of Kerala as Percentage of Progressive Capital Outlay: 1974-75 to 1996-97.	214
6.11	Sectorwise Classification of Capital Outlay of Kerala.	216
6.12	Sectorwise Classification of Loans and Advances 1974-75 to 1996-97.	224
7.1	Growth and Composition of Interest Payments 1974-75 to 1996-97.	234
7.2	Gross and Net Interest Payments 1974-75 to 1996-97.	237
7.3	Ratio of Interest Receipts to Outstanding Loans of the Government of Kerala, 1974-75 to 1996-97.	239
7.4	Growth and Composition of Repayments	242
7.5	Gross and Net Repayment of Debt by Government of Kerala 1974-75 to 1996-97	244
7.6	Debt Servicing/SDP Ratio of Government of Kerala 1974-75 to 1996-97	248
7.7	Debt Servicing/Expenditure Ratio of the Government of Kerala 1974-75 to 1996-97.	251
7.8	Per capita Debt Servicing.	253
7.9	Gross and Net Transfer (Loans) from the Centre to the Government of Kerala: 1974-75 to 1996-97.	255
7.10	Aggregate Debt Relief Recommended by the VI th Finance Commission 1974 to 1979	262
7.11	Debt Relief Recommended by the VII th Finance Commission 1978-84	263
7.12	Debt Relief Recommended by the VIII th Finance Commission, 1984-89	266
7.13	Outstanding Central Loans and Debt Relief as per VI, VII, VIII Finance Commission Recommendations	268
7.14	Debt Relief Recommended by the Ninth (1990-95) & Tenth Finance Commissions (1990-2000)	270

LIST OF APPENDICES

Appendix	Title	Page No.
3.1	Growth and Composition of Domestic Debt and Liabilities of the Union Government: 1950-51 to 1996-97	285-86
4.1	Outstanding Public Debt of State Governments in India (1950-51 to 1996-97)	287
4.2	Interest Payment of State Governments 1950-51 to 1996-97	288
4.3	Outstanding Aggregate Debt of States 1978-79 to 1996-97	289
5.1	Comparative Position of Budgetary Surplus/ Deficits of Kerala and All States 1974-75 to 1996-1997	290
6.1	Sector Wise Classification of Capital Outlay of Kerala	291
7.1	Growth and Composition of Interest Payments of the Government of Kerala 1985-86 to 1996-97	292
7.2	Details of Interest Receipts of Kerala - 1985-86 to 1996-97	293
7.3	Outstanding Central Loans (1988-89 to 1996-97)	294

CONTENTS

**CERTIFICATE
DECLARATION
ACKNOWLEDGMENT
LIST OF TABLES
LIST OF APPENDICES
CONTENTS**

		Page No.
CHAPTER		
1	INTRODUCTION	.. 1 - 9
2	THEORETICAL ISSUES IN PUBLIC DEBT AND REVIEW OF EMPIRICAL LITERATURE	.. 10 - 59
3	PUBLIC DEBT OF INDIA	.. 60 - 93
4	PUBLIC DEBT OF STATE GOVERNMENTS IN INDIA	.. 94 -142
5	PUBLIC DEBT OF KERALA (1974-75 TO 1996-97)	..143-188
6	GROWTH AND COMPOSITION OF CAPITAL DISBURSEMENTS AND DEBT RECEIPTS UTILIZATION OF GOVERNMENT OF KERALA 1974-75 TO 1996-97.	..189-230
7	DEBT SERVICING BURDEN AND DEBT RELIEF	..231-276
8	CONCLUSIONS AND RECOMMENDATIONS	..277-284
	APPENDICES	..285-294
	SELECT BIBLIOGRAPHY	..295-307

CHAPTER 1

INTRODUCTION

1.1 Introduction

Growth of public debt has been a widely discussed topic of Public Finance especially since the 1980's. The mismatch between government expenditure and revenue has resulted in a persistent and seemingly unsustainable gap in resources. The consequent fiscal stress has made financial management an increasingly difficult task. Several research projects have examined the origin, implications and options in respect of the resource gap of the governments. However, it was the Central Government finances, that have been the focus of research in India. The resource gap of State Governments, manifested in the form of growing public debt of these governments, has not received adequate attention. In the present situation of large fiscal imbalance, there is need to measure and analyse the public debt of State Governments in a comprehensive and systematic manner.

1.2 Borrowing Powers of the Central and the State Governments under the Indian Constitution

The Constitution of India confers the power of borrowing on both the Centre and the States though the two are not placed on equal footing. The Central Government has unrestricted powers of borrowing in India and from abroad subject only to such limits as may be fixed by the Parliament by law (Article 292). On the contrary, the borrowing powers of the States are both territorially and otherwise limited (Article 293). They have no power to raise loans outside India. Within India, a State may raise loans from the Government of India or float public loans. However, a State cannot raise a public loan without the consent of the Government of India if there is still outstanding any part of a loan which has been advanced to it by the Government of India or in respect of which a guarantee has been given by the Government of India. The borrowing powers to the States had also been defined in the Government of India Act 1919 and Government of India Act, 1935.

Borrowing powers, in fact, have been one of the most contentious issues between the States and the Centre in the Indian federation. The States have no independent borrowing powers and as such depend on Central Government permission with many conditions laid down in the process to borrow either

from the public or from financial institutions or from the Centre. On the other hand, the Central Government has unlimited borrowing powers. An asymmetry has developed in that while there is no control over the Centre because it can run up deficits by borrowing from the Reserve bank of India (RBI), the States have to stick to the overdraft limit laid down by the RBI. Moreover, the external credits sanctioned for State projects are not entirely allocated to the States on the same terms and conditions.

1.2.1 Public Debt of State Governments

In India, public borrowing has been a significant element of the financing of government expenditure at the Central and State levels. Consequently, public debt has increased considerably in recent years. Considering the magnitude of the problem, it is not surprising that the issues surrounding public debt in India have received considerable attention. However, public debt of the Central Government has been the focal point in all these discussions, even though more than one third of the currently outstanding combined public debt is owed by the State Governments in India.

In the context of huge expenditure responsibilities, revenues of the State Governments consisting of non-debt Central transfers and States' own

resources have become increasingly insufficient and the resultant resource gap of a State is met through borrowing. Public borrowing has become the mechanism often resorted to cover the gap between the expenditure needs and available resources of State Governments. The growth of States' public debt and servicing of these debts pose serious strain on the State's budget. In this analysis, the problem of States' indebtedness and its implications are examined, with special reference to the public debt of Kerala.

1.2.2 Burden of Debt

Public borrowing may at times be preferred to tax financing to meet governmental expenditure. Apart from the adverse political fallout, heavy taxation adversely affects the incentive to work and invest. Public borrowing, given its voluntary character, is free from these limitations. But unlike tax revenue, funds raised through borrowing have to be repaid along with interest. This is referred to as the burden of public debt. The problem of debt servicing becomes a serious issue when the ratio of interest payment to revenue expenditure rises continuously leading to diversion of resources on account of interest payment. This will set limits on the governments' ability to incur their expenditure. This hampers economic growth and in turn adversely affects the growth of government revenue mobilization. So a sort of vicious

circle develops, whereby the ratio of the interest payments to revenue receipts becomes larger. Governments are thus compelled to borrow more just to meet their debt servicing obligations. Nowadays, this is manifested in the form of revenue account deficits of State and Central Governments, which are financed by borrowings. Debt servicing capacity can improve only if the amount borrowed by a government is used for investment purposes which yield returns high enough to meet the interest and repayment obligations. A detailed discussion of theoretical issues in public debt, is attempted in the second chapter.

In a country like India, the quantum of resource of State Governments are influenced by federal fiscal transfers from the Centre to the States. Even when States' own revenue resources expand sufficiently; but the share of non-debt resource transfer from the Centre declines, the growth in the total revenue receipts of the State Governments may be far less than desired. Similarly, increase in the share of Loans and Advances from the Central Government (LACG) in total transfers, leads to growing debt servicing burden on the States. The revenue and capital resource mobilization of State Governments in India are not totally within States' own control. So the public debt situation of a State can be meaningfully analysed only in the backdrop fiscal transfers to the State and its composition.

The burden of debt in terms of gross interest payments overstate the burden of debt. The net interest burden which takes into account the interest receipts on debt financed investment provides a better measure of the burden of debt. Debt relief recommended by the various Finance Commissions also influences the debt position of State Governments in India.

1.2.3 Public Debt of Kerala

In this study, the various aspects of the public debt of Kerala are examined in detail. An attempt is made to trace the genesis of Kerala's fiscal crisis and the debt problem. Though all State Governments in India are experiencing the budgetary problem of revenue account deficit, Kerala's fiscal problems are unique for more than one reason. The frequency and magnitude of the crisis are much more for Kerala than for other States. The fiscal crisis of Kerala surfaced in the Seventies itself, much ahead of other States. For long by keeping total capital disbursements at a low level, surpluses in the capital account were generated by Kerala to finance revenue deficits. All other States, on the other hand, had been utilizing their revenue surpluses to meet capital deficits till recently. Thus Kerala's mounting and recurrent revenue deficits have become a charge on the State's capital receipts including loans from the Centre, market borrowings and negotiated loans. The public

debt problem of Kerala and the fiscal crisis of the State are closely linked. So in the present context of large fiscal imbalance, there is need to measure and analyse the public debt of Kerala State in a comprehensive and systematic manner.

1.3 Objectives of the Study

The following are the broad objectives of the study:

1. To analyse the growth and composition of the public debt of Kerala, in the context of the growing debt burden of the Central and State Governments in India.
2. To examine the growth and composition of the debt receipts and their utilization by the Government of Kerala.
3. To study the problem of servicing of the public debt of Kerala.
4. To study debt relief recommended by various Finance Commissions to Kerala.

1.4 Methodology

The present study is essentially explorative and makes a statistical analysis of data on the public debt of Kerala. Necessary comparisons have

been made with All States' and Central Government's public debt. The secondary data are collected from sources like the Reserve Bank of India Bulletins, RBI Report on Currency & Finance, Finance Commission Reports, Five Year Plan documents of the Central and State Governments, Economic Reviews published by the Government of Kerala, Finance Accounts of Kerala published by the Comptroller and Auditor General of India, Papers of the Kerala State Planning Board and Budget documents of the Government of Kerala. Data collected from the above sources have been tabulated and interpreted in accordance with the chapter scheme.

1.5 Limitation

The study is explorative in nature and no hypothesis has been used in the analysis of the public debt of Kerala. The study covers only the period between 1974-75 to 1996-97. State finances data are not comparable with those published prior to 1974-75, due to changes in budgetary classification. However, to provide the public debt scenario of the country, data from 1950-51 onwards have been used in the presentation of Indian public debt and public debt of the State Governments in India.

1.6 Chapter Scheme

There are eight chapters in the study. They are:

Chapter - I Introduction

Chapter - II Theoretical Issues in Public Debt and Review of Empirical Literature

Chapter-III Public Debt of India

Chapter-IV Public Debt of State Governments in India

Chapter- V Public Debt of Kerala. (1974-75 to 1996-97).

Chapter-VI Growth and Composition of the Capital Disbursement and Debt Receipts Utilization of the Government of Kerala. (1974-75 to 1996-97).

Chapter-VII Debt Servicing Burden and Debt Relief

Chapter-VIII Conclusions and recommendations.

CHAPTER 2

THEORETICAL ISSUES IN PUBLIC DEBT AND REVIEW OF EMPIRICAL LITERATURE

2.1 Introduction

In this chapter, an attempt is made to discuss the various theoretical issues surrounding public debt. The issues discussed include, burden of debt as viewed by the classical, Keynesian and modern economists, the sustainability of domestic debt, debt and inflation and the 'crowding' out debate. The macro economic implications of domestic debt accumulation and policy options are also discussed. A survey of empirical literature on the problem of public debt of the Central and State Governments in India is included as the last section of the chapter.

2.2 Classical views on Public Debt

The views of classical economists on public debt depended on their faith in the role of the government in the economic life of a

country. J.B. Say observes that, “there is a grand distinction between an individual borrower and a borrowing government, that, in general, the former borrows capital for the purpose of beneficial employment, the latter for the purpose of barren consumption and expenditure.”¹ He believed that the burden of the debt could be shifted over a great number of successive years.

Adam Smith was of the view that the State was wasteful; it took borrowed funds for unproductive purposes from private capitalists and deprived them of capital which was badly needed for promoting production and trade. To quote him, ...“a certain portion of the annual produce turned away from serving in the function of a capital to serve in that of a revenue; from maintaining productive labourers to maintaining unproductive ones, and to be spent and wasted, generally in the course of the year, without even the hope of any future reproduction.”²

Ricardo too was convinced of the wastefulness of public expenditure. He admitted that debt service involves transfer payments within the community, but did not know whether the recipients of such income would “employ it productively” or “squander it unproductively.” Ricardo was greatly concerned with the effects of

public debt. "National Debt was an evil which almost any sacrifice would not be too great to get rid of. It destroyed the equilibrium of prices."³ On the question of shifting the burden of the debt to the future generations, Ricardo was explicit:.. "the argument of charging posterity with the interest of our debt, or of relieving them from a portion of such interest is often used by otherwise well informed people, but we confess, we see no weight in it."⁴

According to Malthus, the existence of the national debt by maintaining a body of "unproductive consumers" contributed "powerfully to distribution and demand."⁵ He argued that public debt contributed among other things to the evils resulting from changes in the value of money and expressed the desirability of containing the growth of public debt. J.S. Mill argued that "government borrowing was harmful because it destroys capital which could otherwise be used for productive employment."⁶ According to Mill, it is expedient to pay off a debt as early as possible either through immediate payment by a general contribution or by gradual payment from the surplus revenue.

Adam Smith, Say, and Ricardo disapproved of public debt because they thought it interfered with the natural order which was

conducive to the creation of wealth and increase in the material welfare of the nation.

The classical formulation of public debt found its best expression only in the last two decades of the 19th century in the works of H.C.Adams, C.F.Bastable and P.Leroy-Beaulieu. They made a distinction between the creation of public debt per se and the effects of public expenditure.

Adams held that “ a loan calls for no immediate payment from the people— the lenders are satisfied, since they have secured a good investment.”⁷ He refuted the argument that the burden of the expenditure cannot be shifted forward in time.

Bastable stated that public credit is only one form of credit in general and is governed by the same principles which control private credit. Making a distinction between loan and tax finance, he wrote “A loan is voluntary and supplied by willing givers, taxation is levied on the willing and unwilling alike. To make things smooth for the present at the cost of the future is not the duty of the wise and farseeing Statesman.”⁸ He felt that it was only partly true that loans are made out of capital and taxes are paid out of new income. Public

debt affects income as well as capital and taxation affects capital as well as income.

Paul Leroy - Beaulieu made one of the clearer expositions of the classical position on public debt. He remarked that a public debt is, in and of itself, neither a good nor an evil. He criticised the classicists for their failure to see that public expenditure can be productive. As he puts it, "a loan will be useful or harmful to the society in general depending on whether the State preserves and usefully employs the proceeds or wastes or destroys the capital which the rentiers have given up." ⁹

The following set of propositions summarize the dominant views of the classical school on public debt:

- a) Government loan finance withdraws funds from productive private employment.
- b) Deficits are less painful than current taxes; unbalanced budgets therefore expand governmental activity and invite irresponsible governmental action.

- c) Government borrowing makes future financing more difficult by increasing the proportion of the budget which must go for fixed charges and by increasing the amount of taxes which must be paid to finance the interest on the debt.
- d) Loan finance is costly; public outlays financed in this way must be paid for twice- once in meeting the interest charges and once in amortising the debt.
- e) Public debt leads to currency depreciation¹⁰.

2.3 Keynesian Theory of Public Debt.

The economics of public debt in modern public finance was powerfully influenced by the Keynesian Revolution which produced theoretical results entirely different from the body of economic thought existing at the time of its development. The scientific basis for the modern theory of public debt was provided by the 'General Theory of Employment, Interest and Money' in 1936. The new theory in its purest form finds expression in Functional Finance which holds that "the absolute size of the national debt does not matter at all, and that, however large the interest payments that have to be made, these do not constitute any burden upon society as a whole."¹¹

The proponents of the 'no burden' doctrine treats the economy as a unit, and accordingly hold... " that private debt differs from national debt in being external. It is owed by one person to others. That is what makes it burdensome. Because it is interpersonal, the proper analogy is not to national debt but to international debt. A nation owing money to other nations is impoverished or burdened in the same kind of way as a man who owes money to other men. But this does not hold for national debt which is owed by the nation to citizens of the same nation. There is then no external creditor. We owe it to ourselves."¹² The society in this analysis, is regarded as being analogous to a family. It also ignores the distinction between economic order based on private enterprise and a command economy.

The 'no burden' thesis also relies on certain advantages of public borrowing. Through debt creation, the government can tap savings streams, put the resources thus raised to productive use and bring about an increase in national income. The increased flow of income facilitates the payment of taxes to service the debt. At the time of unemployment, increase in public debt contributes to current capital formation. It promotes the development of more and more institutionalised sources of savings like banks, stock markets and insurance companies. It helps curb consumption, encourages savings

and promotes capital formation and makes it possible for the people of a country to improve their standard of living.

2.4 Post Keynesian Theories of Public Debt

2.4.1 Buchanan Thesis

J.M.Buchanan calls the currently dominant theory of public debt the 'New Orthodoxy' which according to him is based on three basic propositions:

- (a) The creation of public debt does not involve any transfer of the primary real burden to future generation.
- (b) The analogy between individual or private debt and public debt is fallacious.
- (c) There is a sharp and important distinction between an internal debt and an external debt.

Since the publication of Buchanan's *Public Principles of Public Debt* (1958), "the time honoured controversy over the burden of the National Debt has flared up once more. The view that the National Debt is no burden on the economy and that the real cost of government

expenditure, no matter how financed cannot be shifted to future generations has been on the retreat under a powerful attack by the contributions of J.M. Buchanan, J.E. Meade and R.A. Musgrave.”¹³

Buchanan has tried to prove that in the most general case,

- (a) the primary real burden of a public debt is shifted to future generations.
- (b) the analogy between public debt and private debt is fundamentally correct.
- (c) the external debt and the internal debt are fundamentally equivalent.

Buchanan asserted that payment of taxes is per se a burden. Since debt finance postpones the levy of taxes, it obviously shifts burden to future generations. Justification for this is that taxes are compulsory and involuntary. In contrast, market transactions, including the purchase of public debt are voluntary agreements. Buchanan's view implies that democratic societies “burden” themselves, whenever they agree to a social compact binding on their

members. On the other hand, agreements which do not involve governmental coercion evidently burden none of the participants.

2.4.2 Bowen-Davis-Kopf on Burden of Debt

Bowen-Davis-Kopf (1960)¹⁴ (BDK) in a joint article supported James Buchanan, but pointed out that Buchanan

- (a) did not define real burden in a satisfactory manner.
- (b) defined “generations” in such a manner that the same person could be considered a member of many different generations.

The authors tried to rectify these deficiencies and argued that if the real burden of the debt is defined as the total amount of private consumption goods given up by the community at the moment of time the borrowed funds are spent, then the cost of the public project simply must be borne by the generation alive at the time the borrowing occurs. It is the existence of marketable bonds that transfer the real burden of debt-financed government expenditure to future generations.

Vickery (1961)¹⁵ supported the BDK analysis and showed the effects of debt finance on the future level of real income for the

society as a whole. Scitovsky (1961) argued that “the burden of Public debt can be shifted if by burden is meant what individuals consider a burden: the balance of private costs and private benefits, corrected for changes in disposable income occasioned by the public debt.”¹⁶

Musgrave (1959) held the view that it will be equally advantageous for the government to use tax or loan finance. “If the taxpayer wishes to spread his burden, he may secure a tax or consumer loan and thus obtain command over resources that otherwise would have gone into capital formation. The outcome will be similar to that of public loan finance, the only difference being that private rather than public debt is issued ... public loan finance may then be thought of as a means of enabling individual taxpayer to secure tax credit at equal term. By placing payment on a pay-as-you-go basis, loan finance remains a significant instrument of policy even though it does not increase the total availability of resources.”¹⁷

2.4.3 Modigliani Burden Thesis

Another significant Post-Keynesian public debt theory is Modigliani’s Burden Thesis (1961)¹⁸. He adopted the aggregate

investment approach with a view to isolate the economic effects of the national debt. His conclusions include :

- (a) Given the government purchase of goods and services, an increase of the (real) national debt whether internal or external is generally advantageous to those present at the time of increase.
- (b) An increased national debt will generally place a gross burden on those living beyond that time through a reduction in the aggregate stock of private capital.
- (c) If the rate of interest at which the government borrows can be taken as a good approximation to the marginal productivity of capital, then the gross burden(gain) to future generation can be measured by the interest charges on the national debt.
- (d) Gross burden of the national debt may be off-set or even reduced in so far as the increase in the debt is accompanied by rising public expenditure which contributes to the real income of future generations i.e., productive public capital formation.

Modigliani pointed out that the method of financing government expenditure does not alter the size of the draft on current resources. But it may alter the nature of the private uses of resources which are displaced. He argues that debt finance will displace mainly investment, and tax finance mainly consumption.

The socialist objection to the creation of a large public debt arises due to its aggravating influence on the inherent tendency for income and wealth to be distributed inequitably in a free enterprise economy and even in a mixed economy. Creation of a large public debt, it is argued, develops a rentier class which receives interest on government bonds. With the growth of the rentier class, the gulf between the haves and have-nots widens giving rise to greater inequality in the society. A rapid growth of public debt is likely to intensify inequality in wealth distribution.

2.5 Macro economic Implications of Domestic Debt

Macro economic implications of domestic debt have been a subject of long standing controversy and two distinct phases can be identified. In the old tradition, domestic debts are created during wars or national emergencies and retired during peace time. In the recent

past, many industrial countries have experienced a substantial peace time accumulation of domestic debt. So there is a growing realisation that domestic debt accumulation is not necessarily transitory.

2.5.1 Traditional controversies

2.5.1.1 Ricardian Equivalence Theorem

Way back in 1817, Ricardo enunciated a theorem which has been called the *Ricardian Equivalence Theorem*. The theorem puts forth a proposition that domestic debt and a lump sum tax of equivalent amount exert identical effects on the individual. The theorem was derived under the conditions of

- (a) perfect capital markets with no-borrowing constraints
- (b) non distortionary taxes
- (c) perfect certainty about future taxes and
- (d) equal planning horizon for private and public sectors.

With these restrictive premises, the contention of the theorem is that for the individual, each of the two alternatives (ie, taxation and domestic debt) impose, a burden that in a present value sense is substantially the same. Buchanan (1968) clarified that “this Ricardian

equivalence does not suggest, however, that the objective pattern of cost payments remains the same over the two alternatives. Taxation and debt issue remain different, not similar, financing institutions - - for the simple reason that taxes require a transfer of resource services from the individual to the fisc during the initial period, whereas debt issue postpones such transfer until later periods.”¹⁹

Leiderman and Blejer (1988)²⁰ provided a simple model to show the implications of relaxing some of the assumptions of Ricardian equivalence. In practice, existing taxes tend to be distortionary. These taxes can affect the private sector and economy wide allocations because of their induced wealth, redistribution and inter temporal substitution effects. The level and type of taxation have distribution effects that reflect differential incidence across individuals.

The nature, amount and timing of future increases in taxes are assumed to be known with certainty. This, however, does not happen in practice since the incidence of taxes across individuals is uncertain and so are the future increases in taxes. This can cause deviations from equivalence.

The assumption that, individuals act as if they will live forever (or that households and Government have the same planning horizons) is a necessary condition for this equivalence. But since there is an uncertainty amongst individuals about their life time, thus assuring no bequest motive, a tax cut will lead to a rise in perceived wealth and consumption of currently alive individuals. Thus with a tax cut, future tax liabilities can be shifted to later generations without affecting the welfare of the current generation. This leads to a violation of the equivalence theorem.

The traditional approach for testing this hypothesis with time series data was to regress private consumption on government budget as well as other relevant variables. The empirical evidence on this issue is inconclusive because of differences in sample periods, econometric techniques and methods of empirically measuring the different variables. Leiderman and Blejer have attempted to overcome these shortcomings by directly deriving the estimated relations from explicit intertemporal optimisation frameworks. From a number of studies, they found that if the assumptions of the Ricardian equivalence are violated, then there would exist deviations from this proposition and hence fiscal policies can have an impact on private consumption and aggregate demand.

In their attempt to revive the Ricardian Equivalence Theorem, Rational Expectation theorists have contended that domestic debt does not have any adverse wealth effect on private savings. They argued that when government accumulates large domestic debt in relation to GDP, 'rational' households anticipate higher taxes in the future. Because of this expectation, their 'permanent' income is reduced. So the impact of accumulated domestic debt falls on consumption rather than on savings, avoiding the dampening effect on the saving rate.

2.5.1.2 "We owe it to ourselves" proposition

The essence of this argument is that the interest payments arising out of domestic debt represent nothing more than transfer from tax-payers to bond holders and so long as both groups are members of the same polity, no macro economic cost is involved. On the basis of this proposition, domestic debt is often dismissed as of no macro economic consequence.

Buchanan (1968) exposed the fallacious nature of this proposition, when he observed. "This conception of national debt contains a fundamental flaw in its failure to translate opportunity cost

or burden from aggregate components into something that is meaningful to individual members.”²¹ According to him, “The core of the fallacy lies in the equating of the community as unit in some aggregated national accounting sense, with the individuals in the community in some political sense as participants, direct or indirect in collective decision making.”²² So the belief that domestic debt is of no macro economic consequence is illusory.

2.5.2 Recent Trends in the Study of Domestic Debt

2.5.2.1 Sustainability of Public Debt

The “sustainability” aspect of domestic debt is an important area of discussion. It is actually related to economic 'stability' rather than 'sustainability'. This is evident from the fact that debt- financing of government deficits is deemed to be 'sustainable', when the resultant debt-GDP ratio is low and is considered explosive otherwise.

Domar (1944)²³ pointed out, that if the rate of interest is higher than the growth rate of the economy , any primary deficit will lead eventually to an explosive rise in the debt –GDP ratio. Bispham (1987)²⁴ and Mason (1987)²⁵ derived similar results, based on inter temporal budget constraints. The budget constraint states that the

present value of debt service must equal the value of debt outstanding. The inter temporal budget constraint gives the link between the current stock of public debt and the future requirements of debt service. It provides an analytical framework for projections of the debt-GDP ratio for an economy.

Dornbusch, et. al. (1985)²⁶ pointed out two major kinds of disturbances that can lead to fiscal instability. The first is the emergence of a large, persistent deficit due to wars, populism etc. The second is a change in economic structure which changes the relative magnitudes of growth and real interest rate. The most relevant case is the one where the real interest rate rises and the trend output growth rate declines. Dornbusch, et. al. have analysed the data on Europe for 1984 and 1985. A rising real interest rate and a declining growth rate of output have been observed in most European countries, opening the prospect of fiscal trouble.

The question of the government budget constraint and government solvency has been considered by Buiters (1986)²⁷. In his paper he points out that during peace-time conditions, no government would resort to “wholesale repudiation of domestically-held public debt”. However, such repudiation has not been uncommon after a war

or a major political change. It happened in France in 1770 and Germany in 1923 and 1948 when capital levies were introduced in these countries. For Italy, such a levy was recommended by Basevi and Giavazzi in 1983.

Thus for most of the European countries of today, there does not seem to be any reason to suppose that the inter temporal budget constraint would not be met and that the budget deficits would become unsustainable.

2.5.3. Debt and Inflation

A theory of the relationship between debt and inflation arises from the work of the Minnesota School, especially Sargent and Wallace. Their argument rests on the ultimately inflationary effect of a shift from money to debt finance of a given deficit.

According to Buiter (1986)²⁸ there are two distinct views of the debt-deficit-inflation nexus. According to the first view, there is an incentive for the government to decrease the real value of its outstanding stock of interest-bearing, nominally denominated debt through an unexpected burst of inflation. The second view is the one

stated by Sargent and Wallace which emphasizes the long run inflationary consequences of a short or medium term switch from money or tax finance to debt financing of a given public spending programme.

The scope for deficit financing is constrained by medium and long term inflation dangers. A country can avoid these dangers if it incurs a balance of payment deficit on current account but this will cause an external imbalance and a withdrawal of external finance, which could further result in accelerating inflation. So when the government runs excessive budget deficit, the choice is between inflation and a payment deficit.

Tanzi, et. al. (1987)²⁹ in their paper showed the link between inflation and fiscal deficits. As the rate of inflation rises, the conventional definition measure of fiscal deficit may magnify the size of the fiscal adjustment that a country needs. So all inflation induced interest payments must be subtracted from the conventional deficit to get an operational measure of fiscal deficit. Both these measures have their shortcomings but together they provide more information.

2.5.4 The 'Crowding out' Debate

There are several levels, according to Blinder and Slow (1973)³⁰, at which crowding out has been alleged to occur. The first and most obvious one is the view that when the government engages in productive activities which could be provided by the private sector, then public spending would simply supplant private investment.

The second level of crowding out is an integral part of the Keynesian tradition. This states that when the government indulges in deficit financing, not by issuing money but by floating debt issues, then these compete with private debt instruments in financial markets. There is an upward pressure on the rates of interest which will reduce any private expenditures which are interest -elastic.

Buiter (1986) made a distinction between 'Keynesian crowding out' and 'Classical crowding out' and also between 'short run' and 'long run' crowding out. In the 'short run,' it is assumed that changes in outstanding stocks of domestic capital, government debt, high powered money etc. brought about by the flows (investment, government borrowing etc.) over the period under consideration are

very small relative to the stocks and can be ignored . Expectations (of future interest rates, exchange rates etc.) are also taken as given .

In Keynesian ‘crowding out’, we consider the horizontal shift of the aggregate demand schedule and the composition of that change in terms of changes in investment, consumption or the current account balance. A tax cut boosts private consumption and crowds out the current account surplus through an appreciation of the nominal and real exchange rate.

According to the classical economists, all modes of financing Government budget namely, taxation, debt financing and money creation crowds out an equal amount of resources available to the private sector, under conditions of full employment. According to this view, crowding out effect is not exclusively associated with debt financing.

2.5.5 Policy Options

The option of reducing the real value of debt and debt service by inflation has to be examined. This option has been exercised by governments to meet their inter temporal budget constraint. According

to Dornbusch, et. al. (1988), the Keynes-Clark model of debt liquidation assumes that a deliberate inflation policy can succeed in reducing the real value of public debt. If the government can in one go increase price level in the economy, then as long as debt is denominated in nominal terms, this will reduce the real value of the debt as well as the interest payments on the debt. However, it is not possible to have an unanticipated overnight increase in the rate of inflation. Bond holders may demand an inflation premium to compensate for higher expected inflation.

Dornbusch, et. al. after analysing empirical data for the US concluded that in that country, there has been a marked switch from long term debt to short maturity debt. This shift has also occurred in Europe. In both France and Germany, major debt build - ups had ended in inflation. However, the reduction in debt in the UK at the end of the Napoleonic wars was accomplished not by inflation but by taxes.

Buiter (1986) says that there are four ways through which Governments can reduce the real value of their debt.

- (a) At a given general price level and a given nominal price of bonds, they can run a budget surplus;
- (b) They can attempt to reduce the real value of the outstanding stock of debt, at a given price level, by pursuing or announcing policies that cause a drop in bond prices;
- (c) Even with a balanced budget and given nominal bond prices, an inflationary policy can reduce the real value of the stock of debt that exists;
- (d) A Government can formally repudiate past all of its past debt.

Buiter advanced distributional and efficiency reasons for reducing the real value of government debt. Those who hold the debt and those who pay the taxes to service the debt are not the same people. According to the efficiency argument, public debt crowds out private saving and capital formation.

2.5.6 Empirical evidence on the issue of Public Debt.

Some of the empirical literature on the issue of public debt is presented in this section. The American debt situation can be briefly examined with the help of two papers by Phelps (1987)³¹ and Penner

(1987)³². It has been pointed out that in the 1980's, there was considerable reduction in the US public savings leading to a huge increase in public debt. There was no offsetting increase in private savings. This situation offered some real benefits to the US, such as

- (a) a reduction in price level;
- (b) (Income) Tax cut increases the supply of labour;
- (c) A tax cut by reducing the tax rate on interest income helps to hold up the after tax interest rate. This avoids the problems of inflation and disinflation to a certain extent;
- (d) Tax incentives in 1981 played a major role in dampening the recession.

There are certain adverse effects also. One is the loss of potential national income resulting from the budgetary deficit. The other is the worth or shadow cost, of the customers lost to American firms in foreign markets resulting from the fiscal stimulus and the appreciation of the dollar. Phelps showed that the benefits outweighed the costs in the early 1980's, but warned that costs intensify and

benefits erode; so a gradual phasing out of the fiscal stance is indicated.

Penner (1987) in his paper has analysed the impact of rising US federal deficit on capital formation. With the steadily rising deficit in 1981 and 1982, many American economists concluded that this would result in high real interest rates and low investment. Though high real interest rates emerged, this has also attracted massive inflows of international capital to the US. This has stopped the rise in interest rates. So the argument that rising US budget deficits crowded out US capital formation was proved wrong. However as the dollar appreciated with capital inflows, the export and import-competing sectors of the economy were depressed. Crowding out occurred but it afflicted the trading sectors of the economy rather than capital formation.

Another important strand in recent fiscal literature relates to the impact of domestic debt on private savings. Boskin (1987)³³ and others provide detailed analysis of the issue in the context of the US economy, where the saving rate has declined substantially in the recent years. Of the four avenues by which national fiscal policies can affect private savings, Boskin finds that the growth of implicit and explicit

domestic debt may be the major cause of the decline in the US saving rate.

Besides the potential impact of domestic debt on the saving rate several specific issues are also being addressed. In the Italian context, impact of domestic debt on financial markets has been explored by Pagano (1988)³⁴ and the impact on households demand for monetary assets has been analysed by Bollino and Rossi (1988)³⁵. The relationship between debt accumulation and capital controls has been investigated by Giovannini (1988)³⁶.

Modigliani and Jappelli (1987)³⁷ studied the determinants of consumption and saving and their effects on fiscal policy using Italian data for more than a century. This study indicated that the long swings in the saving ratio reflect primarily two forces - fiscal policies via expenditure and deficits and variations in the growth rate of economy, which manifest themselves in variations of the wealth to income ratio. The authors found that contrary to popular belief, the major cause of the decline in saving ratio was not the large and highly visible deficit. The decline in savings is related to the sharp drop in the growth of the economy.

Indian

2.6 Review of ~~Indian~~ Literature on Public Debt

In India, literature on public debt mainly focuses on the problems of mounting public debt of the Central Government. The indebtedness of the State Governments was treated mostly as part of the analysis of Centre - State financial relations.

One of the earliest studies of Indian public debt by Sreekantaradhya (1972)³⁸ examined the historical reasons for the growth of public debt in India. A similar study of N.R.Rao (1972)³⁹ during the same period analysed the constitutional arrangements of public borrowing in federal States and constitutional evaluation of public borrowings in India. A more rigorous study of the problem of public debt by Ghuge (1977)⁴⁰ had shown that national debt in India had grown enormously since 1956, and became a major factor influencing monetary and fiscal policy in the country.

Kiran Barman (1978)⁴¹ analysed the growing problem of public debt both at the Central and State levels since independence. But the most important work analysing financial management at all levels of government was done by Thavaraj (1978)⁴². He outlined the fiscal operations of governments in a federation like India. Mishra (1985)⁴³

dealt in detail with the phenomenal growth of Indian public debt and highlighted the virtues of debt as an instrument of resource mobilization for planned development. He argued that prudent management of debt can minimize the cost of debt-servicing. By mid-eighties, literature on public debt expressed serious concern about the growing volume of debt and debt servicing in India.

Seshan (1987)⁴⁴ was the first to draw pointed attention to the possibility of domestic debt in India reaching an unacceptable high level in the none too distant future. Subsequently, the Report of the Comptroller General of India (1988)⁴⁵ also warned against the alarming growth in domestic debt. Based on simple trend analysis Rakshit (1989)⁴⁶ questioned the methodological premises of these predictions.

Ghosh (1988)⁴⁷ argued that rapid increase in public debt and the burden of interest charges have become, a major hindrance in the process of orderly implementation of development planning not only in the public sector but also in the private sector.

The study by Rangarajan, et. al. (1989)⁴⁸ can be described as the most serious study of Indian public debt in recent times. It developed

a sound analytical framework to explore the dynamic nexus between government deficits and different modes of financing them. It examined the macro economic implications of domestic debt accumulation and the danger of resorting to RBI financing leading to a vicious circle of deficit and inflation.

Lakdawala (1990)⁴⁹ analysed the various aspects of Indian Public debt. He pointed out the dangers arising from the large size of public debt in India. He warned that the present debt situation, if allowed to persist, will throw a grave burden on the treasury and an intolerable monetary deficit.

Chelliah (1993)⁵⁰ explained the strength and limitations of the fiscal deficit concept of debt in the context of macro-economic stabilization in India. His analysis of the growth of public debt made illustrative projections of the public debt profile of India upto 2003 AD. Gulati (1993)⁵¹ while commenting on the sustainability of public debt argued for better allocation of governmental expenditures to facilitate the growth of national income.

As indicated earlier, the resource gap of the State Governments in India, measured in terms of their public debt, has not received

adequate attention in the discussion of fiscal federalism in India. Venkataraman (1968)⁵² who presented a detailed analysis of the fiscal operations of the Union and State Governments in India, noticed that during the first three five year plans, the volume of debt of the State Governments had increased enormously and servicing of it had become a matter of great concern.

Kher (1967)⁵³ presented an analysis of the finances of the Mysore State in which he pointed out the resource gap experienced by the State leading to increased public debt, on the eve of the Third Five Year Plan. In his analysis of Orissa State finance, Patnaik (1970)⁵⁴ warned that the rapid growth of State public debt imposed a heavy strain on the revenue position for meeting the interest and repayment liabilities.

Porwal (1971)⁵⁵ in his study of Rajasthan State finance showed that the increase in annual income of the State could not cope with the increase in public debt and interest charges. He analysed the debt position of the State from 1949-50 to 1968-69. During the same period Nanjundappa (1974)⁵⁶ analysed the impact of Central loans on State government finance which formed 74.1 per cent of the States' total debt. In his opinion, if debt is accompanied by a rise in the States'

income and if the debt-revenue and debt-service ratios are within manageable limits, it need not cause anxiety.

Bhargava (1969)⁵⁷ in his analysis of Uttar Pradesh State finances noted that public debt of the State increased by more than twenty-one times during the twenty year period between 1947-48 and 1967-68. The percentage share of Central loans in the total debt of the State came up to 79.9 percent at the end of 1967-68. This was at the expense of permanent debt and unfunded debt components of the State debt. He suggested that the loan operations of the Union and State Governments should be centralized to eliminate the disadvantages of small scale borrowings. Bajaj and Aggarwal (1992)⁵⁸ also examined the financial position of Uttar Pradesh during the period between 1965 and 1990. An examination of the various aspects of the State's budgetary operations revealed that the public debt of the State has remained low. This is attributed to the low per capita plan assistance and lack of access to market borrowing of the State government.

Thimmaiah (1977)⁵⁹ pointed out that the Central loans to the States have given rise to a sort of financial imperialism of the Central Government in India. The market borrowings of State Governments have not been distributed or allocated consistently on any objective

principle. He suggested that solutions to the mounting burden of Union loans on the States should aim at reducing both financial and economic burden of Union loans.

The study by the Birla Institute of Scientific Research (1979)⁶⁰ points to a kind of vicious circle that has developed in which the problem of growing State indebtedness to the Centre is feeding upon itself. The study points out that the debt liabilities of the States are not supported by corresponding income-yielding assets. Similarly Central transfers to the States are inadequate and the loan-grant composition of Central loans faulty.

In the 1980's, there was renewed interest in the study of State finances in India. It was during this period that several noteworthy studies of multilevel finances came up. Some of them were case studies of Indian States. OmPrakash (1983)⁶¹ analysed the finances of Punjab State and pointed out that the indebtedness of the State was within manageable limits compared to its income level.

Christine Wallich (1982)⁶² in a study of State finances in India for the World Bank, detailed the mechanism of transfer of funds from the Centre to the States under the auspices of the Planning Commission

and the Finance Commission, in general, and the impact of World Bank lending in particular. Bhuyan (1984)⁶³ made an analysis of Assam State finances. He showed that the State had been using its debt raised resources on less productive areas. He pointed out that public debt policy must be accompanied by a suitable monetary policy. State Governments have very little to contribute on their own in this respect.

Although State governments in India are increasingly getting into debt traps, the problem is much more acute for Kerala. George (1993)⁶⁴ observed that debt servicing payments which take away nearly two-thirds of the fresh Central loans in the case of All States, take away as much as 87 percent of fresh loans in the case of Kerala. The outstanding debt of Kerala in relation to its capacity to service the debt as indicated by the State domestic product has been one of the highest among States in India. By 1987-88 the debt-SDP ratio of Kerala reached 37.7 percent. It appears that the State of Kerala is caught in a vicious circle of deficits, debt servicing payments and still more deficits.

George (1988)⁶⁵ while studying the effects of federal transfers in India examined the indebtedness of the State Governments to show that the mounting debt servicing payments have progressively reduced

the net Central loans to the States into a trickle. In the analysis of Central loans, between Second and Seventh FYP periods, he noted that most of the States in India have fallen to 'debt traps', a situation wherein fresh loans are necessary to service old loans. During the three decades studied, debt servicing accounted for about 11 per cent of the States' combined revenue and capital expenditure. He pointed out that high interest rates and short maturity of Central loans have contributed to the growing debt burden of State Governments. The Centre was borrowing long from the market and lending short to the States. The study also highlights the need for debt relief to the States.

Govinda Rao (1992)⁶⁶ emphasised the urgent need for State level budgetary reforms. He traced the major issue at the State level as continuous outpacing of the growth of revenue expenditures over that of revenue, and the growth of outstanding debt of State Governments. S.Guhan (1992)⁶⁷ reviewed Tamilnadu State finances during the period 1960-90 with particular emphasis on developments in the 1980's. It highlighted the problem of access of Central transfers of a middle income State like Tamilnadu. In his opinion, Tamilnadu is one of the relatively less indebted States due to the availability of current account surpluses and the lack of major capital projects.

Nizar Jetha (1992)⁶⁸ reviewed the structure and trends of Gujarat's finances during the period between 1973 and 1987. The study pointed out that the emergence of current account deficit in the State was caused by the rapid growth of expenditure. He suggested that beneficiary targeting and greater cost effectiveness are required to sustain the high and growing level of State expenditure. Pattnaik, et. al. (1994)⁶⁹ designed a new measure of State public debt in terms of Basic Resource Gap. The study revealed that the fiscal dependency and stress of the States during the 80's and 90's did not show any perceptible decline. It suggested the need for budgetary reforms by the State Governments in India.

The problem of States' indebtedness with particular reference to the debt servicing problem of Central loans was examined by almost all Finance Commissions. The Second Finance Commission (Report 1956) was the first to be asked to look into the problem of State debt, in view of the rising Central loans to the States. The Commission attempted to rationalise the interest rate structure of Central loans as it was opposed to the policy of giving loans interest free. The Third Finance Commission (Report 1961) observed that interest liabilities on Central loans take away a substantial portion of the States' revenue. The Fourth Finance Commission (Report 1965) recommended an

assessment of the system of intergovernmental debt operation in India for taking measures to lessen the problem of State debt. The problem of unauthorised overdraft of the States from the RBI was referred to the Fifth Finance Commission. The Sixth, Seventh and Eighth Finance Commissions went in for massive debt rescheduling as the States were facing huge non-plan capital gaps during this period. Even after debt relief, all the deficit States continued to be deficit States

The Ninth Finance Commission reviewed the debt position of the States and strongly opposed the use of borrowed funds for revenue expenditure. The Tenth Finance Commission suggested two methods to reduce the burden of State debt. The first one was the disinvestment of the State public sector units to repay Central loans. Secondly, they suggested that the Centre rewards those States which take steps to improve their revenue account.

2.7 Studies on Kerala Finances

Absence of analytically sound quantitative studies on States' budgetary behaviour and the effects of different types of intergovernmental transfers are an important shortcomings of the literature on Indian fiscal federalism. The study on the various aspects of the fiscal crisis of Kerala by George (1993)⁷⁰ is a serious attempt in

this direction. The study covers the 16 year period ended in 1989-90. The study traces the origin of Kerala's fiscal crisis and assesses its dimensions. The resource mobilization efforts of Kerala, in the context of the constraints posed by the Kerala model of development are discussed. Federal fiscal transfers of all types are examined to see the roots of the State's budgetary crisis. The level and pattern of Kerala's public expenditure and its implications for the State's fiscal positions are analysed in detail. The study reveals that the debt servicing payments of Kerala have steadily increased compared to All States. This high share of debt servicing reduced the capital available for investment and increased the revenue expenditure of the State government.

Aiyer and Kurup (1992)⁷¹ in their analysis of Kerala State Finances noted that the State's capacity to generate budgetary resources for economic development has been adversely affected by the pattern of expenditure growth in the State. Non-developmental expenditure has increased faster than in other States. By 1991-92, interest charges accounted for 13.6 percent of total revenue expenditure of Kerala. The share of debt servicing in non plan expenditure rose to 26.6 percent during the Seventh Plan period. The repayment obligation during the same period constituted as much as 95 percent of its non- plan capital

outlay. The major share of liabilities has been the loans from Central Government. The total outstanding debt of Kerala at the end of 1989-90 represented 3.3 percent of State domestic product. They noted that the Kerala's situation of having to borrow in order to square its revenue account is not unique.

Lizy (1989)⁷² made a study on Kerala finances. It was a trend and evaluative type study. Broadly, it studied the State's economic development vis-à-vis other States, its resources and expenditure, level of Central transfers and State's debt position. The study noticed that the debt burden of States has been increasing and Central loans formed about 77 percent of total indebtedness of State government. It also revealed that the relative importance of Central loans decreased over the plan period.

Sen and Rao (1970)⁷³ as members of the Resource Commission appointed by the Government of Kerala to study certain aspects of State finances pointed out that the fiscal problem of Kerala has been aggravated by certain peculiar factors. The study revealed that a large proportion of borrowed funds is used up in financing current expenditure leaving little for physical capital formation. In their opinion, the increasing interest burden and successively larger plan outlay on social services have resulted in high current expenditure.

References:

1. J.B.Say, *A Treatise on Political Economy* (Augustus M Kelly, New York 1964), P.477..
2. Adam Smith, *The Wealth of Nations*, Vol.2, Book V, Chapter 3, (J.M.Dent and Sons, London 1954) P.407.
3. Edwin Cannan, *Ricardo in Parliament*, *The Economic Journal*, Vol. IV 1894, P.421.
4. David Ricardo, *Funding System*, in *Works and Correspondence of David Ricardo*, Vol. IV (upc) 1951, P.187.
5. T.R.Mathus, *Principles of political Economy* (William Pickering, London 1836) PP 411-412.
6. J.S.Mill, *Principles of political Economy*, (Longmans, Green and Co, London 1929) P. 76.
7. H.C.Adms. *Public Debts 1833*: Quoted in J.M.Buchanan, *Public Principles of Public Debt*, (Richard d Irwin-Illinois, 1958) P.106.
8. G.F.Bastable, *Public Finance*, (Macmillon, London 1903) P.674-75.

9. Paul Leroy-Beaulieu, *Traite' dela Science de finances*, Paris 1883, cited in J.M.Buchanan, *Public Principles of Public Debt*, P.111.
- 10.J.Burkhead, *The balanced Budget*, in *Readings in Fiscal Policy*, The AER (George Allen and Unwin, London 1995) PP. 14-17.
- 11.A. P. Lerner, *Functional Finance and the Federal Debt Social Research*, Feb, 1943 reprinted in *Readings in Fiscal Policy*, (George Allen and Unwin, London,1955) P. 475.
- 12.A.P.Lerner, *The Burden of the National Debt*_ in Llyod.A.Metzler and others (ed.) reprinted in James.M.Ferguson, *Public Debt and Future Generations*, (The University of North Carolina Press, 1964) P. 17.
- 13.Franco Modigliani, *Long Run Implications of Alternative Fiscal Policies and The Burden of the National Debt*, *Economic Journal* LXXI, Dec, 1961, P.730, reprinted in J. M. Ferguson (ed.) op, cit, P. 31.
- 14.William, G. Bowen, Richard G. Davis and David H. Kopf, *Public Debt; A Burden on Future Generation? The AER*, Vol, Sept, 1960, PP 701, reprinted in J. M. Ferguson (ed) op. Cit., PP 67- 74.

15. William Vickery, *The Burden of the Public Debt*; The AER, Vol LI, March, 1961, P. 132, reprinted in J. M. Ferguson (ed) op. Cit, P. 75.
16. Tibor Scitovsky, *The Burden of the Public Debt: a comment*, The AER, Vol.L1, March 1961, P.137 reprinted in J.M.Ferguson, (ed.) opitic, P.82.
17. Richard.A.Musgrave, *The Theory of Public Finance*, 1959, (McGraw-Hill Book Company, New),P. 559 .
18. Franco Modigliani, *Long Run Implications of Alternative Fiscal policies and the Burden of the National Debt*, Economic Journal, Vol LXXI, Dec., 1961, P.730 reprinted in Jame M.Furguson (ed.) op, cit., P.108.
19. Buchanan.J.M. *Public Debt* in International Encyclopedia of Social Sciences. (1968). (The Macmillan company and The Free Press)P.32.
20. Leiderman.L and Blejer,M.T. “*Modelling and Testing Ricardian Equivalence*” IMF staff Papers. 1988.
21. Buchanan.J.M. (1968) *Public Debt* in International Encyclopedia of the Social Sciences, (The Macmillan Co and Free Press) P.4.
22. Ibid. P-63.

23. Evsey.D.Domar. *The Burden of the Debt and the National Income*.
The AFR Dec.1944, Vol XXXIV reprinted in Readings in Fiscal
policy, op.cit., P480.
24. Bispham.A.J. *Rising Public sector Indebtedness: Some more
unpleasant Arithmetic*, Private Savings and Public Debt (ed.) by
Boskin Flemming et. al., USA (1987)
25. Mason,P.R. (1987) *The sustainability of Fiscal Deficits*. IMF Staff
Papers, Vol. 32, No. 4 Dec.
26. Olivier Blanchard, Rudiger Dorubusch and Williem Buitter (1985)
Public Debt and Fiscal Responsibility, Paper prepared for the
Centre for European Policy studies (Brussels, Belgium)
27. Buitter,W. H. *A Guide to Public Sector Debt and Deficits*, Yale
University Discussion Paper 1986.
28. Ibid P-17.
29. Tanzi, Vito, Blejer, Mario I, and Teijeiro, Mario. O. *Inflation and
Measurement of Fiscal Deficits IMF Staff Papers*. Dec. 1987.

0. Blinder, A. S. and R. M. Solow (1973) "*Does Fiscal Policy Matter?*" *Journal of Public Economics*. Vol. 4 (November) P 319-37.
1. Phelps E. S. (1987) "*Appraising the American Fiscal Stance*" in Boskin et. al. 1987.
2. Peneer R. G., (1987) "*Government Deficits: The Case of the United States*" in Boskin et al. (1987).
3. Boskin, M. J., Flemming, J. S. and Gorini, S (1987) (eds) *Private Savings and Public Debt*, Basil Blackwall, USA).
4. Pagano, M. (1988) *The Management of Public Debt and Financial Markets- In High Public Debt, The Italian Experience* (ed) by Giavazzi and Spaventa (CUP).
5. Bollino, A and Rossi, N (1988) *Public Debt and Household's Demand for Monetary Assets in Italy: 1970-1985 in High Public Debt the Italian Experience* ed. by Giavazzi and Spaventa (CUP).
6. Giovanni A. (1988) *Capital Controls and Public Finance, The Experience in Italy in High Public Debt The Italian Experience* (ed.) by Giavazzi and Spaventa (CUP).

37. Modigliani, F. and T. Jappelli (1987) *"Fiscal Policy and Saving in Italy since 1860"* in Boskin et al 1987. (Basil Blackwell USA).
38. Sreekantaradhya B. S. (1972) *Public Debt and Economic Development in India*, Sterling Publishers, Delhi.
39. Rao N. R. (1972), *Union State Financial Resources in India*, Karnataka University, Dharwad (1972).
40. Ghuge V. B. (1977) *Burden and Benefits of India's National Debt*. Himalaya Publishing House, Bombay.
41. Kiran Barman (1978) *India's Public Debt and Policy since Independence*, Chugh Publications, Allahabad.
42. Thavaraj M. J. K. (1978) *Financial Administration in India*, Sultan Chand and Sons, Delhi.
43. Mishra D. K. (1984) *Public Debt and Economic Development in India*, Lucknow: Print House.
44. Seshan. A. (1987) *The Burden of Domestic Public Debt in India*, RBI Occasional Papers. Vol. 8. No.1 June.
45. Report of the comptroller and Auditor General of India (1988) No. 10 Government of India.

46. Rakshit M. (1989) *Internal Debt Trap, the Shadow and the substance*, delivered as S. N. Sen Memorial Lecturer, Calcutta.
47. Ghosh Arun (1988) *India's Public Debt: A Partial Analysis*, Economic and Political Weekly October 29, 1988 P. 2253.
48. Rangarajan C, Anupam Basu and Narendra Jadhav (1989) *Dynamics of Interaction between Government Deficits and Domestic Debt in India*, Reserve Bank of India, Occasional Papers, vol. 10, No. 3 Sept.
49. Lakadawala, D.T. (1990) *Indian Public Debt*, Gokhale Institute of Politics and Economics-Pune-4, April 1990 (Text of R.R.Kale memorial lecture).
50. Chelliah, R.J. (1993) *An Essay on Fiscal Deficit*, Gokhal Institute of Politics and Economics-Pune 14 August 1993_(Text of R.R.Kale memorial lecture).
51. Gualati, I.S. (1993) *Tackling the Growing Burden of Public Debt*, Economic and Political weekly XXIX 1297-1298.
52. Venkataraman, K (1968) *States Finances in India*; George Allen and Unwin, London.

53. Kher, S.P. (1967) *The Finances of the Mysore State* (1956-97 to 1965-66), Popular Prakashan, Bombay.
54. Patnaik, Srish Chandra (1970) *Orissa Finances in Perspective*, Peoples Publishing House, New Delhi.
55. Porwal, L.S. (1971) *State Finances in India-A case Study of Rajasthan*, Sultan Chand and Sons, Delhi.
56. Nanjundappa, D.M. (1974) *Intergovernmental Fiscal Relations in India*, Sterling Publications, New Delhi.
57. Bhargava, P.K. (1969) *Uttar Pradesh Finance Since Independence*, Vora and Co, Publishers Pvt Ltd, Bombay.
58. Baja, J.L. and Aggarwal, O.P. (1992) *State Finances in Uttar Pradesh 1965-90*, in *State Finance in India* (ed.) by Bagchi & Bajaj, J.L. (NIPFP) Vikas, New Delhi.
59. Birla Institute of Scientific Research Byrd, W. Economic Research Division (1979) *Centre-State Financial Relations in India*. Abhinav Publications, New Delhi.
60. Om Prakash (1983) *The Finances of Punjab State*, Guru Nanak Dev University, Amritsar.

61. Christine Wallich (1982) *State Finances of in India, Vol. I, Revenue Sharing*, World Bank working paper No. 523.
62. Bhuyan.P.K. (1984) *The Regional Fiscal Economics of Assam.*, Chung Publishers, Allhabad
63. Geroge,K.K.(1993) *Limits to Kerala Model of Development*, Monograph series, Centre for Development Studies, Trivandrum.
64. Thimmaiah,G. (1977) *Burden of Union Loans on the States*, Sterling Publication, New Delhi.
65. George,K.K. (1988) *Centre-State Financial Flows and Inter-State Disputes*. Creterion Books, Delhi.
66. Govinda Rao,M. (1992) *A proposal for State Level Budgetary Reforms*, Economic and Political Weekly, Feb 1, 1992.
67. S.Guhan (1992) *State Finance in Tamilnadu 1960-90*, in *State Finance in India*, (ed.) by Bagchi & Bajaj.J.L. (NIPFP) Vikas, New Delhi.
68. Nizas Jetha (1992) *Gujrat State Finances*, in *State Finance in India* (ed.) by Bagchi & Bajaj.J.L. (NIPFP) Vikas, New Delhi.

69. Pattnaik, R.K., Banger, R.D., Pillai, S.M. and Rekha Sharma (1994) *Resource Gap of the State Governments: Measurmental and Analysis*, RBI occasional papers, Vol. 15 No. 4, Dec. 1994.
70. Geroge, K.K. (1993) *Limits to Kerala Model of Development*, Monograph series, CDS Trivandrum.
71. R. Ramalingam Aiyer and K.N. Kurup (1992) *State Finance in Kerala*, in *State Finance in India* (ed.) by Bagchi & Bajaj. J.L. (NIPFP) Vikas, New Delhi.
72. Lizy, M.A. (1989) *Centre-State Financial Relations in India*; Ashish Publishing House, New Delhi.
73. Tapas. K. Sen and Govind Rao, M. (1993) *State Finance in Kerala*, National Institute of Public Finance and Policy, New Delhi.

CHAPTER 3

PUBLIC DEBT OF INDIA

.1 Introduction

Before analysing the problem of public debt of State Governments in India, it may be necessary to have an idea of the total public debt scenario in India. Public debt of India consists of the internal and external debt of the Central Government and the public debt of all the State Governments in India. But loans and advances from the Central Government to State Governments are excluded in the calculation of total public debt of India to avoid double counting. Part I of this chapter presents the growth and composition of the total public debt of India. Public debt of the Central Government comprising of internal and external governmental liabilities of the Government of India is shown in part II. Debt servicing payments of India and the Central Government are analysed in relation to revenue and capital disbursements as also the GDP.

3.2 Analytical Concepts of Public Debt in India

Fiscal imbalance in any economy is measured by the government deficit. Conceptually, government deficit is simply the difference between aggregate disbursements and aggregate receipts. In practice, different measures of government deficit are possible depending upon what items are deemed to comprise aggregate disbursements and aggregate receipts.

3.2.1 Government Deficits

A wide spectrum of concepts of government deficit has been developed depending on the purpose of analysis. Here it is necessary to choose the concept which can fully capture the impact of fiscal operations on the indebtedness of the government.

The total resource gap arising out of government transactions i.e. the difference between aggregate disbursements (revenue expenditure, capital expenditure, and net domestic lendings) and own revenue receipts must necessarily be matched by the sum total of all other financing items. The financing items include grants, foreign borrowing, domestic borrowing (net RBI credit to government, current market loan and other liabilities such as small savings, provident funds etc.) and change in cash balances.

3.2.2 Budget Deficit

In India, aggregate disbursements cover revenue expenditure, capital disbursements and net domestic lendings. Receipts are not confined to revenue receipts alone. Grants, foreign borrowings and domestic borrowing (excluding 91- days treasury bills) are also included in aggregate receipts.

Budget Deficit = (revenue expenditure + capital disbursements + net domestic lendings) – (revenue receipts + grants + foreign borrowings + domestic borrowings).

The traditional budget deficit depicts only a part of the resource gap in current fiscal operations that is expected to be financed by

(a) issuing 91- day Treasury Bills and

(b) running down on the government's cash balances with treasuries and RBI .

This concept of government deficit is narrow. Current fiscal operations lead to increase in several other liabilities of the government. For example, besides foreign borrowings, there are internal debt liabilities like current market loans, special securities issued to the RBI and other liabilities such as small savings, provident funds etc, which in recent years have been filling significant portions of resource gap in the government operations. In the budget documents, these are treated in the same way as

other receipts and hence the traditional budget deficit does not reflect the full magnitude of resource gap and relevant borrowing requirements.

3.2.3 Monetary Concept of Government Deficit

The Chakravarty Committee Report (1985)¹ observed that the traditional measure of budget deficit does not reveal the full extent of the government's reliance on Reserve Bank credit. A part of new issues of the government securities is taken up by the Reserve Bank when the response from the public and financial institutions is inadequate. These securities contribute to an increase in reserve money much the same way as new issues of treasury bills taken over by the Reserve Bank. The exclusions of this severely understate the monetary impact of fiscal operations. So the broader concept of monetary deficit is used.

$$\begin{aligned} \text{Monetary deficit} &= (\text{Revenue receipts} + \text{capital receipts}) \\ &\quad - (\text{Revenue expenditure} + \text{capital disbursements}). \end{aligned}$$

The stock of deficit defined above is nothing but the stock of treasury bills. So the public debt corresponding to the monetary deficit concept is the stock of treasury bills.

3.2.4 Fiscal Deficit Concept of Public Debt

The total resource gap or the overall financing requirement in government's fiscal operations is given by the excess of revenue

expenditure, capital disbursements and net domestic lending over revenue receipts. When grants are deducted from the overall financing requirement, the residual which represents the overall borrowing requirement may be called the gross fiscal deficit.

$$\text{Gross fiscal deficit} = (\text{revenue expenditure} + \text{Capital disbursements} + \text{net domestic lending}) - (\text{revenue receipts} + \text{grants})$$

The gross fiscal deficit captures the entire shortfall in government's fiscal operations that is expected to be covered by borrowing operations and/or running down its cash holdings, while the traditional measure is confined besides the depletion of liquidity holdings, to one particular form of domestic borrowing i.e. 91-day treasury bills, thus ignoring other domestic borrowings such as current market loans, small savings, provident funds etc as well as foreign borrowings. Since the excess of expenditure over revenues would have to be covered by borrowing, the fiscal deficit can be said to be the same as net borrowing by the government. If this is positive, there will be an equivalent addition to public debt. So,

$$\text{Fiscal deficit} = \text{net borrowing by the government} = \text{net addition to public Debt.}$$

3.2.5 Measurement of Domestic Debt

In the Indian budgetary practice, there are two sets of liabilities which comprise domestic debt.

- A. *Internal Debt* which consists of current market loans, treasury bills, special securities issued to RBI and the like and *Special floating and other loans*. The last mentioned are the non-negotiable, non interest bearing securities issued to international financial institutions like World Bank and International Monetary Fund.
- B. *Other liabilities* which consists of small savings, provident funds etc. These liabilities are also classified as the debt because they involve servicing through interest payments and redemption. Other liabilities include *Reserve funds* comprise of depreciation and reserve funds of Railways, Posts and Telecommunications Departments etc. The *Reserve funds*, of the State Governments are another important item in this category. '*Deposits*' comprise of dozens of diverse items such as civil deposits, judicial deposits, deposits of local funds etc.

Part I

3.3 Growth and Composition of Public Debt of India (1950-51 to 1996-97)

Indian public debt consists of the public debt and other liabilities of Central and State governments. It includes both internal debt and liabilities and external debt of the Central government and public debt of State government excluding Central loans.

The components of internal debt of the Central Government are

- (1) Market loans and Bonds
- (2) Treasury Bills
- (3) Special floating and other loans

The other liabilities include

- (1) Small savings collections
- (2) Provident Funds
- (3) Other unfunded debt and Reserve Funds and Deposits.

Other unfunded debt consists of Postal Insurance and Life Annuity Fund, Hindu Family Annuity Fund and from 1966 Compulsory Deposits and Income Tax Annuity Deposits.

The State Governments debt consists of

- (1) Internal Debt
- (2) Loans and advances from Central Government
- (3) Provident Fund , Small Savings, Trusts and Endowments, and Insurance and Pension funds

The components of Internal Debt of the State Government are

- (1) Market loans and bonds
- (2) Ways and means advances from the RBI
- (3) Negotiated loans from banks and other Institutions

Tables 3.1-3.2 indicate the size and growth of the Indian public debt. These Tables indicate the following

The aggregate liabilities of the Centre and State Governments excluding Central loans to States increased from Rs. 3059 crores in 1950-51 to Rs. 763721 crores in 1996-97. Expressed as a percentage of GDP at factor cost, it increased from 33.9 to 65.6 during the same period. This shows that India's public debt as a percentage of GDP nearly doubled within a period of 45 years. In 1993-94, the debt/GDP ratio reached the peak 74.1 per cent. Thereafter it, showed a decline during the next three years.

The outstanding liabilities of the Central Government constitute the major component of Indian public debt. The domestic debt and liabilities of the Central Government increased from Rs.2812 crore in 1950-51 to Rs.615199 crore in 1996-97. As a percentage of GDP, it increased from 31.3 to 52.8 during the same period. The external debt of Government of India is a small proportion of GDP throughout the period of study. It was only less than one per cent of GDP in 1950-51. But in 1970-71, it reached the level of 16 per cent and came down to less than 5 per cent in 1996-97. In absolute terms, it increased from Rs. 32 crores in 1950-51 to Rs. 53620 crores in 1996-97.

TABLE 3.1: INDIA'S PUBLIC DEBT* AS PERCENTAGE OF GDP

(in percentage)

	1950-51	1960-61	1970-71	1980-81	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
1 PUBLIC DEBT & OTHER LIABILITIES OF CENTRE	31.3	40.1	33.7	39.6	50.8	57.0	57.1	59.6	57.1	50.3	52.8
2 PUBLIC DEBT OF STATES EXCLUDING CENTRAL LOANS	2.2	4.7	6.0	5.6	7.2	8.2	7.9	8.0	7.9	7.3	8.0
3 TOTAL DOMESTIC DEBT (CENTRE & STATES) (1+2)	33.5	44.9	39.7	45.2	57.9	65.2	64.9	67.6	65.0	57.6	60.8
4 EXTERNAL DEBT*	0.4	6.6	16.3	9.2	6.6	6.6	6.4	6.5	5.9	4.9	4.7
5 AGGREGATE DEBT (3+4)	33.9	51.4	56.0	54.5	64.6	71.8	71.4	74.1	71.0	62.50	65.6

Note: *Include only India's external governmental liabilities.

Source: Report on Currency and Finance (RBI), various issue

TABLE 3. 2: GROWTH OF INDIA'S PUBLIC DEBT -1950-51 TO 1996-97

YEAR	CENTRE			PUBLIC DEBT OF STATES EXCLUDING CENTRAL LOANS	PERCENTAGE INCREASE (OVER THE DECADE/ YEAR)	TOTAL PUBLIC DEBT	PERCENTAGE INCREASE (OVER THE DECADE/ YEAR)
	DOMESTIC DEBT AND LIABILITIES	EXTERNAL DEBT	PERCENTAGE INCREASE (OVER THE DECADE/ YEAR)				
1950-51	2812	-	32	215	-	3059	-
1960-61	6121	54.1	1001	722	3028.1	7844	156.4
1970-71	13379	118.6	6485	2379	547.9	22243	183.6
1980-81	48451	262.1	11298	6979	74.2	66728	200.0
1990-91	242434	400.3	31525	36172	179.0	310131	364.8
1991-92	314806	29.8	35501	42847	12.6	393154	26.8
1992-93	359634	14.2	42629	49766	20.1	452029	15.0
1993-94	430623	19.7	47345	58131	11.1	527734	16.7
1994-95	487682	13.2	50928	67822	17.5	606432	14.9
1995-96	554983	13.8	51249	80726	0.6	686958	13.3
1996-97	615199	10.8	53620	94902	4.6	763721	11.2

Note:

- Total Public Debt of India include (a) Domestic debt and liabilities of the Central Government
(b) External liabilities of the Governments of India
(c) Public Debt of State Governments in India excluding Central loans given to the States
- External Debt includes only official Government of India liabilities taken from the Budget document.

Source: RBI Report on Currency and Finance, various issues

The public debt of State Governments in India excluding Central loans to States, though small compared to the liabilities of the Central Government is steadily rising. It increased from Rs. 215 crores in 1950-51 to Rs. 94902 crores in 1996-97. Expressed as a proportion of GDP, it increased from 2.2 in 1950-51 to 8 per cent in 1996-97.

The public debt of India, more than doubled in the first two decades i.e. between 1950-51 and 1970-71. Between 1970-71 and 1980-81, the increase was two fold. This signaled a still faster growth in the next decade. By 1990-91, the public debt of India registered a more than three fold increase within a ten years period. The period between 1980-81 and 1990-91 can be regarded as the high growth period of Indian public debt. This was mainly attributed to the growth in internal debt. But during the decade ended in 1990-91 external governmental liabilities recorded high growth rate. During the same period, the public debt of State Government recorded relatively higher growth rate than that of the Central Government. The decline in the growth of debt of the Central Government in the nineties should be viewed in the context of a general contraction in government activities. The slow pace of budgetary reforms of the State level during this period, is reflected in the comparatively high growth rate of State public debt.

3.4 Debt Servicing Payments of India (Centre and State Governments Combined, 1950-51 to 1996-97)

A nation's debt bearing capacity can be assessed by

- (i) interest payment/GDP ratio
- (ii) Interest payment/ Revenue expenditure ratio
- (iii) Repayment/ Capital disbursement ratio
- (iv) Debt Servicing/ Total disbursement ratio
- (v) Interest payment/ Debt servicing ratio

and

- (vi) Debt servicing/ Gross loans ratio.

3.4.1 Interest Payment/GDP Ratio

The total interest payments consist of interest payments of Central Government on its internal and external liabilities and interest payments of all State Governments in India. But the interest paid on Central loans by the States are excluded. The total interest payments increased from Rs.39 crores in 1950-51, to Rs. 71709 crores in 1996-97 (Table 3.3). Expressed as a percentage of GDP, it increased from 0.4 per cent to 6.2 per cent during the same period. It remained less than 2 per cent till 1970-71. Thereafter, it steadily increased to reach 2.5 per cent in 1980-81 and further to 5.2 per cent in 1990-91. In the 1990's interest payments of the Centre and State Governments exceeded 5 percentage of the GDP. In 1996-97, the combined interest payments formed 6.2 per cent of the GDP.

TABLE 3.3: TOTAL INTEREST PAYMENTS/GDP RATIO (1950-51 TO 1996-97)

YEAR	TOTAL INTEREST PAYMENT (CENTRAL + STATE GOVTS EXCLUDING INTEREST ON LACG) Rs. Crore	% TO GDP
1950-51	39	0.4
1960-61	217	1.4
1970-71	745	1.9
1980-81	3042	2.5
1990-91	25055	5.2
1991-92	31118	5.6
1992-93	36457	5.8
1993-94	43047	6.0
1994-95	51824	6.1
1995-96	62698	5.7
1996-97	71709	6.2

Note: Total interest payments = Interest payments by the Central Government plus interest payments by all State Governments. Interest payments by the State Governments on Central loans and advances (LACG) are excluded

Source: RBI, Report on Currency and Finance, various issue

3.4.2 Interest payment/ Revenue expenditure ratio

Another measure of the growing burden of debt is the amount of revenue expenditure devoted towards interest payments by the Centre and the States. The proportion of interest payments to revenue expenditure was only 5.9 per cent in 1950-51 (Table 3.4). By 1960-61, it increased to 12 per cent and declined in the next two decades to 11.2 and 10.5 per cents. In 1990-91 it reached 16.9 per cent and increased in all the years of the nineties. In 1996-97 interest payment/revenue expenditure ratio

reached 21.9 per cent. This shows that nearly one-fifth of the revenue expenditure of the Central and State Governments in India goes for interest payments alone. This is a clear indication of the growing burden of Indian public debt.

TABLE 3.4: INTEREST PAYMENT/REVENUE EXPENDITURE RATIO
(1950-51 to 1996-97)

YEAR	INTEREST PAYMENT (Rs. Crore) (Centre + States)	REVENUE EXPENDITURE (Rs. Crores) (Centre + States)	INTEREST PAYMENT/ REVENUE EXPENDITURE RATIO (%)
1950-51	39	660	5.9
1960-61	217	1813	12.0
1970-71	745	6666	11.2
1980-81	3042	28972	10.5
1990-91	25055	147988	16.9
1991-92	31118	174002	17.9
1992-93	36457	188907	19.3
1993-94	43047	221742	19.4
1994-95	51824	255018	20.3
1995-96	62698	293016	21.4
1996-97	71709	326958	21.9

Source: RBI, Report on Currency and Finance, various issues

3.4.3 Repayments/Capital Disbursement Ratio

The repayment of the Centre and State Governments consists of repayment of internal and external debt of the Central Government and discharge of internal debt by States. The repayment of Central loans by the states are excluded. The combined repayments of the Centre and States increased from Rs. 47 crores in 1950-51 to Rs. 10052 crores in 1996-97

(Table 3.5). The repayment/ capital disbursement ratio declined from 12.6 per cent in 1950-51 to 8.7 per cent in 1960-61. But by 1970-71, this ratio increased to 11.5 per cent. The lowest ratio of 5.4 was in 1980-81. It was still lower at 6.8 per cent in 1990-91. But from 1991-92 onwards, this ratio increased considerably and in 1996-97, it reached 12.8 per cent. This indicates that, of late, repayment of debt by the Central and State Governments together is taking away increasing amounts from the government's capital budget which in normal case is meant for investment.

TABLE 3.5: COMBINED REPAYMENTS/CAPITAL DISBURSEMENTS RATIO OF CENTRE AND STATE GOVERNMENTS. (1950-51 to 1996-97)

YEAR	REPAYMENTS BY CENTRE + STATES (Rs. Crore)	TOTAL CAPITAL DISBURSEMENTS OF THE CENTRE + STATES (Rs. Crores)	REPAYMENTS/ CAPITAL DISBURSEMENTS RATIO (%)
1950-51	47	372	12.6
1960-61	145	1662	8.7
1970-71	553	4796	11.5
1980-81	839	15641	5.4
1990-91	3482	51094	6.8
1991-92	6939	50865	13.6
1992-93	7349	53045	13.9
1993-94	7616	58956	12.9
1994-95	8278	71741	11.5
1995-96	9210	72078	12.8
1996-97	10052	78506	12.8

Note: Repayments by States include repayment of internal debt only. Repayment of Central loans are excluded. Repayments of the Centre consist of repayment of internal and external debt.

Source: RBI, Report on Currency and Finance, various issues.

3.4.4 Debt Servicing/ Total Disbursement Ratio

Debt servicing here refers to repayment and interest payment by the Central and State Governments on its internal and external liabilities (Debt servicing on Central loans to States is excluded) (Table 3.6). The debt

TABLE 3.6: COMBINED DEBT SERVICING/ TOTAL (REVENUE+CAPITAL) DISBURSEMENT RATIO (1950-51 TO 1996-97)

YEAR	DEBT SERVICING OF THE CENTRE + STATE GOVTS. (Rs. Crores)	TOTAL REVENUE + CAPITAL DISBURSEMENT OF THE CENTRE + STATE GOVTS. (Rs. Crores)	DEBT SERVICING/ TOTAL REVENUE + CAPITAL DISBURSEMENT OF THE CENTRE + STATE GOVTS. (%)
1950-51	86	998	8.6
1960-61	362	3476	10.4
1970-71	1298	11033	11.8
1980-81	3881	45285	8.6
1990-91	28537	199082	14.3
1991-92	38057	224866	16.9
1992-93	43806	250983	17.5
1993-94	50663	280699	18.1
1994-95	60102	326759	18.4
1995-96	71908	332388	21.6
1996-97	81761	417011	19.6

Note: Debt Servicing = Debt servicing of the Central Government includes repayments and interest payments by the Centre on its internal and external debt plus repayments and interest payments by the State Governments on their internal debt. Debt servicing on Central loans to State Governments is excluded.

Source: RBI, Report on Currency and Finance, various issues

servicing/ total disbursement ratio increased from 8.6 per cent in 1950-51 to 10.4 and 11.8 per cent in 1960-61 and 1970-71. But by the end of

1980-81, it declined to 8.6 per cent, that is to a level that prevailed in 1950-51. In 1990-91, it increased to 14.3 per cent and thereafter, it increased every year during the nineties. In 1996-97, it reached 19.6 per cent indicating that the public debt of India has reached a level at which nearly one fifth of the revenue and capital disbursements are going to service the liabilities of the Central and State Governments.

3.4.5 Interest Payment/ Debt Servicing Ratio

The interest payment/debt servicing ratio of the Centre and State Governments was steadily rising during the period of study. The ratio increased from 45.4 per cent in 1950-51 to 87.7 per cent in 1996-97 (Table 3.7). This is indicative of two vital aspects of public debt. A high interest payment/debt servicing ratio indicates an increase in interest rates. Secondly, it points to the term structure and mix of debt indicating the presence of loans with long maturity period. This increasing ratio suggests the necessity to deploy a larger share of current revenue for debt servicing. The analysis also reveals that the burden of debt servicing especially in recent periods comes more from interest payments than from repayment obligations. It makes the revenue account more vulnerable than the capital account of Centre and State Governments.

**TABLE 3.7: RATIO OF INTEREST PAYMENTS TO TOTAL DEBT SERVICING
(1950-51 TO 1996-97)**

YEAR	TOTAL INTEREST PAYMENTS (CENTRE+STATE) (Rs. Crores)	TOTAL DEBT SERVICING (CENTRE + STATE) (Rs. Crores)	INTEREST PAYMENT / DEBT SERVICING (CENTRE+ STATE) (%)
1950-51	39	86	45.4
1960-61	217	362	55.9
1970-71	745	1298	57.4
1980-81	3042	3881	78.4
1990-91	25055	28537	87.8
1991-92	31118	38057	81.8
1992-93	36457	43806	83.2
1993-94	43047	50663	85.0
1994-95	51824	60102	86.2
1995-96	62698	71908	87.2
1996-97	71709	81761	87.7

Source: RBI Report on Currency and Finance, various issue

3.4.6 The Ratio of Debt Servicing to Gross Loans of the Centre and States

The gross loans of the Centre consists of internal and external debt and liabilities of the Central Government. Gross loans of the States take into account the loans raised by the State Governments as Internal debt. Central loans to States are excluded. Gross loans of the Centre and State Governments so defined, increased from Rs.3059 crore in 1950-51 to Rs.763721 crores in 1996-97 (Table 3.8). The ratio of debt servicing to gross loans increased steadily during this period. It ranged between 2.8 and 5.8 per cent between 1950-51 and 1980-81. By 1990-91, it increased to 9.2 per cent. In all the subsequent years of the nineties, the debt servicing/gross loan ratio registered marginal rise. In 1996-97, it came up

to 10.7 per cent. The debt servicing payments of the Centre and State Governments have progressively reduced the net loan availability. This can adversely affect the capital disbursements of Governments for productive purposes at both levels of the federation.

TABLE 3.8: RATIO OF DEBT SERVICING TO GROSS LOANS (1950-51 TO 1996-97)

YEAR	DEBT SERVICING (CENTRE + STATE GOVTS.) (Rs. Crore)	GROSS LOANS (CENTRE + STATE GOVTS.) (Rs. Crore)	DEBT SERVICING / GROSS LOANS (CENTRE + STATE GOVTS.) (%)
1950-51	86	3059	2.8
1960-61	362	7844	4.6
1970-71	1298	22243	5.8
1980-81	3881	66728	5.8
1990-91	28537	310131	9.2
1991-92	38057	393154	9.7
1992-93	43806	452029	9.7
1993-94	50663	527734	9.6
1994-95	60102	606432	9.9
1995-96	71908	686958	10.5
1996-97	81761	763721	10.7

Note: Central loans to States are excluded from the gross loans of the States.

Source: RBI, Report on Currency and Finance, various issues

Part II

3.5 Public Debt of the Central Government (1950-51 to 1996-97)

3.5.1 Growth and Composition of Domestic Debt and other liabilities of the Central Government

The internal debt and other liabilities of the Central Government as a percentage of GDP at factor cost increased from 31 per cent in 1950-51 to 53 per cent in 1996-97 (Table 3.9). The relative share of internal debt in

TABLE 3.9: DOMESTIC DEBT AND LIABILITIES OF THE CENTRAL GOVERNMENT AS PERCENTAGE OF GDP AT FACTOR COST

YEAR	MARK- ET LOANS AND BONDS	TREASURY BILLS	SPECIAL FLOATING LOANS	TOTAL INTERN- AL DEBT	SMALL SAVINGS	PROVI- DENT FUNDS	OTHER UNFUNDED DEBT	RESERVE FUNDS & DEPOSITS	TOTAL OF OTHER LIABILITIES	TOTAL OF DOMESTIC PUBLIC DEBT & OTHER LIABILITIES 11=5+10
1	2	3	4	5=2+3	6	7	8	9	10=6+7+8+9	11=5+10
1950-51	16.0	4.1	2.9	22.5	3.7	1.1	2.2	3.1	3.9	31.3
1960-61	17.0	7.3	1.9	26.1	6.4	1.9	1.7	4.1	14.1	40.1
1970-71	14.4	8.2	2.3	24.9	7.2	2.7	3.0	5.7	18.5	40.5
1980-81	13.0	10.5	1.7	25.2	6.5	2.0	2.9	3.0	14.4	39.6
1990-91	15.2	15.3	1.6	32.2	10.5	1.2	9.5	4.6	27.1	59.3
1991-92	14.4	14.7	1.7	30.8	10.1	1.3	9.4	4.3	26.3	57.0
1992-93	13.2	4.7	13.8	31.6	9.5	1.3	9.5	3.8	25.5	57.1
1993-94	15.5	5.7	12.8	34.0	9.3	1.4	10.0	3.4	25.6	59.6
1994-95	15.8	4.7	10.8	31.2	9.6	1.4	10.0	3.4	25.9	57.1
1995-96	14.8	4.3	8.6	27.6	8.4	1.3	8.7	2.9	22.7	50.3
1996-97	16.2	4.8	7.9	28.8	9.0	1.4	9.1	3.1	24.1	52.8

Source: RBI Report on Currency and Finance, various issue

GDP is higher than the corresponding percentage share of other liability. This is mainly on account of the high and steady growth of market loans and bonds in internal debt. The rate of growth of internal debt and other liabilities during 1980's and 1990's is 19.5 per cent and 17 per cent respectively, which represent near doubling of the corresponding growth rate of 9.8 per cent in the 1950's (Table 3.10). The growth rates of other liabilities during 1980's and 1990's exceeded the corresponding growth rates of internal debt. A table detailing the growth and composition of domestic debt and liabilities of the Central Government is given in Appendix 3.1.

TABLE 3.10: DOMESTIC DEBT AND LIABILITIES OF THE CENTRAL GOVERNMENT (ANNUAL AVERAGE GROWTH RATES): (1950-51 TO 1996-97)

(In percentage)

	1950-51 to 1959-60	1960-61 to 1969-70	1970-71 to 1979-80	1980-81 to 1989-90	1990-91 to 1996-97
MARKET LOANS AND BONDS	7.0	5.3	12.3	16.8	17.8
TREASURY BILLS	23.8	9.1	15.8	27.6	43.7
SPECIAL FLOATING LOANS	1.3	16.1	6.9	52.7	3.8
TOTAL INTERNAL DEBT	18.5	7.3	13.2	17.8	14
SMALL SAVINGS	11.1	8.7	12.9	20.3	13.2
PROVIDENT FUNDS	11.4	11	12.1	21.7	22.1
OTHER UNFUNDED DEBT	-	14	21.9	29.4	15.2
RESERVE FUNDS & DEPOSITS	2.4	8.4	7.7	21.8	8.6
TOTAL OF OTHER LIABILITIES	8.1	9.7	12.3	22.2	22.4
TOTAL OF DOMESTIC PUBLIC DEBT & OTHER LIABILITIES	9.8	8.2	12.9	19.5	17

Note Annual average growth rate is calculated by taking the average of the yearly growth rates.

Source: RBI, Report on Currency and Finance, various issue.

The external debt as a percentage of total debt has been steadily falling since 1970-71 (Table 3.11). In 1950-51, it was only 1.2 per cent of the total debt. After reaching a share of 32.7 per cent in 1970-71, it came down gradually to 8 per cent in 1996-97. This can be attributed to the general contraction of governmental activities under the new economic policy initiated in 1991.

TABLE 3.11: SHARE OF INTERNAL DEBT/ EXTERNAL DEBT TO TOTAL DEBT OF CENTRAL GOVERNMENT

YEAR	SHARE OF INTERNAL DEBT & LIABILITIES TO TOTAL DEBT (%)	SHARE OF EXTERNAL DEBT TO TOTAL DEBT (%)
1950-51	98.8	1.2
1960-61	85.9	14.1
1970-71	67.3	32.7
1980-81	81.1	18.9
1990-91	88.5	11.5
1991-92	89.9	10.1
1992-93	89.4	10.6
1993-94	90.1	9.9
1994-95	90.5	9.5
1995-96	91.5	8.5
1996-97	92.0	8.0

Note: *External Debt here includes only Government of India liabilities shown in the Budget document (Receipt Budget). This is different from the external debt shown in BOP statements which shows all the non-government liabilities including NRI deposits, Trade credit, commercial borrowing and short term debt.

Source: RBI, Report on Currency and Finance, various issue.

3.5.2 Money Burden

The burden of public debt are of two types: one is the money burden and the other is the real burden.

In the broad sense, the money burden of the debt is the repayment of the principal (amortisation of the debt) and payment of interest. However conceptually, the repayment is not considered as a burden as the government is just distributing the capital after use to the original owners. Further more, repayment may be effected through perpetual borrowings without increasing the stock of debt. But payment of interest is a true money burden which is to be met from the current revenues.

It is seen that the interest burden of public debt has been increasing overtime for three reasons;

- (i) the size of government aggregate liabilities is rising
- (ii) the interest rate over time has been rising and
- (iii) in the total liabilities, the proportion of other liabilities for which the interest rates are relatively high has been increasing.

3.5.3 Interest Payments of Central Government

The annual average growth rate of interest payment of the Central government during the period 1974-75 to 1996-97 at 20.7 per cent exceeded the corresponding growth rate of the revenue expenditure of the Central government at 16.5 per cent (Table 3.12). If the growth of interest

TABLE 3.12: INTEREST PAYMENTS OF CENTRAL GOVERNMENT - 1950-51 TO 1996-97

YEAR	TOTAL INTEREST PAYMENTS	INTEREST ON INTERNAL DEBT	INTEREST ON MARKET LOANS	INTEREST ON EXTERNAL DEBT	INTEREST ON OTHER LIABILITIES	REVENUE EXPENDITURE OF CENTRAL GOVERNMENT
1	2	3	4	5	6	7
1950-51	33	10	-	16	7	351
1960-61	188	118	-	25	46	826
1970-71	606	418	-	171	17	3130
1974-75	1000.8	530	292	160	311	5714
1975-76	1228.2	601	339	190	438	7188
1976-77	1374.4	643	377	208	524	8320
1977-78	1521.4	692	442	209	621	9162
1978-79	1829.4	887	556	226	716	10711
1979-80	2209.9	1672	671	235	983	11755
1980-81	2604.4	1370	808	231	1005	14836
1981-82	3194.7	1635	1016	258	1302	15433
1982-83	3937.6	2020	1194	304	1613	18761
1983-84	4795.5	2499	1567	356	1940	22115
1984-85	5974.5	3101	1999	460	2419	27047
1985-86	7511.9	3919	2465	538	3055	35066
1986-87	9245.9	4763	3099	766	3717	40726
1987-88	11251.4	5514	3681	977	4761	46167
1988-89	14278.5	6913	4506	1243	6124	54107
1989-90	17757	8273	5768	1494	7990	64011
1990-91	21498.3	9814	6366	1834	9351	76212
1991-92	26595.6	11317	7355	2784	12575	87195
1992-93	31075	13542	8147	3529	14004	92702
1993-94	36741	15587	9258	3724	17430	112366
1994-95	44060	19108	13205	4026	20866	126578
1995-96	52000	22267	15770	4899	24834	144644
1996-97	58500	27310	19134	4550	26640	164914
Annual average growth rate(%)	20.7	20.8	22.1	15.9	22	16.5

Source: RBI Report on Currency and Finance, RBI Bulletin various issues.

payments exceeded the growth of revenue expenditure or GDP, it is often referred to as an explosive situation. The annual rate of growth of GDP from 1950-51 to 1994-95 was only 11.2 per cent.² The situation shown in Table 3.12 is also indicative of high interest rates at which funds are borrowed by the Government of India. The growth rate of interest payment on market loans and other liabilities (22 per cent) exceeded the average growth rate of interest payment as a whole.

The percentage share of interest on other liabilities steadily increased from 31 per cent in 1974-75 to 45.5 per cent in 1996-97 (Table 3.13). Between 1991-92 and 1995-96, the percentage share of interest on other liabilities clearly exceeded the percentage share of interest on internal debt. This implies that interest rates are relatively high for these liabilities and their share in total liabilities is on the rise in the post-liberalization period.

The aggregate interest payment of the Central Government on its domestic liabilities and external debt constituted 17.5 per cent of the revenue expenditure in 1974-75. This percentage rose to 35.5 per cent in 1996-97, nearly doubling within 23 years (Table 3.14). Interest on external debt, however, formed only 2.8 per cent of the Central revenue expenditure in 1974-75 and declined till 1990-91. It exceeded 3 per cent thereafter. In 1996-97 it remained at 2.8 per cent of revenue expenditure.

TABLE 3.13: INTEREST PAYMENTS OF THE CENTRAL GOVERNMENT
(Percentage to total interest payments)

YEAR (1)	INTEREST ON INTERNAL DEBT (2)	INTEREST ON MARKET LOANS (3)	INTEREST ON EXTERNAL DEBT (4)	INTEREST ON OTHER LIABILITIES (5)
1950-51	30.0	-	48.0	22.0
1960-61	63.0	-	13.0	24.0
1970-71	68.0	-	29.2	3.0
1974-75	52.9	29.2	16.0	31.0
1975-76	48.9	27.6	15.5	35.6
1976-77	46.8	27.4	15.1	38.1
1977-78	45.5	29.1	13.7	40.8
1978-79	48.5	30.4	12.4	39.2
1979-80	75.6	30.4	10.6	44.5
1980-81	52.6	31.0	8.9	38.6
1981-82	51.2	31.8	8.1	40.8
1982-83	51.3	30.3	7.7	41.0
1983-84	52.1	32.7	7.4	40.5
1984-85	51.9	33.5	7.7	40.5
1985-86	52.2	32.8	7.2	40.7
1986-87	51.5	33.5	8.3	40.2
1987-88	49.0	32.7	8.7	42.3
1988-89	48.4	31.6	8.7	42.9
1989-90	46.6	32.5	8.4	45.0
1990-91	45.7	29.6	8.5	43.5
1991-92	42.4	27.6	10.4	47.1
1992-93	43.6	26.2	11.4	45.1
1993-94	42.5	25.2	10.1	47.4
1994-95	43.4	30.0	9.1	47.4
1995-96	42.8	30.3	9.4	47.8
1996-97	46.7	32.7	7.8	45.5

Note: Column 2 inclusive of Column 3.

Source: RBI Report on Currency and Finance, various issues.
RBI Bulletins, various issues

TABLE 3.14: INTEREST PAYMENTS OF THE CENTRAL GOVERNMENT
(Percentage to total revenue expenditure)

YEAR	INTEREST ON INTERNAL DEBT	INTEREST ON MARKET LOANS	INTEREST ON EXTERNAL DEBT	INTEREST ON OTHER LIABILITIES	TOTAL INTEREST PAYMENTS
1	2	3	4	5	6
1950-51	2.8	-	4.5	2.0	9.4
1960-61	14.2	-	3.0	5.6	22.8
1970-71	12.8	-	5.4	0.5	18.8
1974-75	9.3	5.1	2.8	5.4	17.5
1975-76	8.4	4.7	2.7	6.0	17.1
1976-77	7.7	4.5	2.5	6.3	16.5
1977-78	7.5	4.8	2.3	6.8	16.6
1978-79	8.3	5.2	2.1	6.7	17.1
1979-80	14.2	5.7	2.0	8.4	18.8
1980-81	9.2	5.4	1.6	6.8	17.6
1981-82	10.6	6.6	1.7	8.4	20.7
1982-83	10.8	6.4	1.6	8.6	21.0
1983-84	11.3	7.1	1.6	8.8	21.7
1984-85	11.5	7.4	1.7	8.9	22.1
1985-86	11.2	7.0	1.5	8.7	21.4
1986-87	11.7	7.6	1.9	9.1	22.7
1987-88	11.9	8.0	2.1	10.3	24.4
1988-89	12.8	8.3	2.3	11.3	26.4
1989-90	12.9	9.0	2.3	12.5	27.8
1990-91	12.9	8.4	2.4	12.3	28.2
1991-92	13.0	8.4	3.2	14.4	30.6
1992-93	14.6	8.8	3.8	15.1	33.5
1993-94	13.9	8.2	3.3	15.5	32.7
1994-95	15.1	10.4	3.2	16.5	34.8
1995-96	15.4	10.9	3.4	17.2	36.0
1996-97	16.6	11.2	2.8	16.2	35.5

Source: RBI Report on Currency and Finance, various issues.
RBI Bulletins, various issues.

In 1950-51, interest payment of the Central government was less than one per cent (0.4 per cent) of the GDP, and it exceeded 2 per cent in 1980-81. By 1990-91, it rose to 4.5 per cent and in 1996-97 it reached 5 per cent of GDP (Table 3.15).

TABLE 3.15: INTEREST PAYMENTS OF THE CENTRAL GOVERNMENT/GDP RATIO

YEAR	INTEREST PAYMENT OF CENTRAL GOVT. (Rs. Crore)	INTEREST PAYMENT OF CENTRAL GOVT. /GDP RATIO(%)
1950-51	33	0.4
1960-61	188	1.2
1970-71	589	1.5
1980-81	2604	2.1
1990-91	21498	4.5
1991-92	26596	4.8
1992-93	31075	4.9
1993-94	36741	5.1
1994-95	44060	5.2
1995-96	52000	4.7
1996-97	58500	5.0

Source: RBI Report on Currency and Finance, various issues.

TABLE 3.16: SHARE OF CENTRAL GOVERNMENT INTEREST PAYMENT IN TOTAL INTEREST PAYMENTS(CENTRE & STATE)

YEAR	TOTAL INTEREST PAYMENTS (CENTRE + STATES) EXCLUDING INTEREST ON LACG (Rs. Crore)	INTEREST PAYMENT BY CENTRAL GOVT. (Rs. Crore)	SHARE OF INTEREST PAYMENT OF CENTRE IN TOTAL INTEREST PAYMENTS (%)
1950-51	39	33	84.6
1960-61	217	188	86.6
1970-71	745	606	81.3
1980-81	3042	2604	85.6
1990-91	25055	21498	85.8
1991-92	31118	26596	85.5
1992-93	36457	31075	85.2
1993-94	43047	36741	85.4
1994-95	51824	44060	85.0
1995-96	62698	52000	82.9
1996-97	71709	58500	81.6

Note: LACG -- Loans and Advances from the Central Government

Source: RBI Report on Currency and Finance, various issue.

The share of Central Government in total interest payments (of the Centre and States), excluding interest on Central loans to States, was high (Table 3.16). It was as high as 84.6 per cent. The situation remained unchanged till 1994-95. But in 1995-96 and 1996-97, the share of Central

Government interest payments marginally declined to 82.9 and 81.6 percents respectively.

3.5.4 Repayment/Capital Disbursement Ratio: Central Government

From Tables 3.17, it can be seen that in 1950-51, repayment by Centre constituted nearly 25 per cent of its capital disbursement. But this ratio has been steadily declining, In 1990-91, it reached 10 per cent. After that it again started rising. By 1996-97, nearly 20 per cent of the capital disbursement of Centre has been used for repayment of its domestic and external debt. This increase in the ratio points to the decline in the quantum of capital available for investment.

TABLE 3.17: RATIO OF REPAYMENT TO CAPITAL DISBURSEMENT OF CENTRAL GOVERNMENT

YEAR	REPAYMENTS (Rs. Crores)	TOTAL CAPITAL DISBURSEMENTS (Rs. Crores)	REPAYMENT/ CAPITAL DISBURSEMENT RATIO (%)
1950-51	46	183	25.1
1960-61	127	1029	12.3
1970-71	487	2972	16.4
1980-81	661	8358	7.9
1990-91	3145	31782	9.9
1991-92	4269	29122	14.7
1992-93	5451	29916	18.2
1993-94	6098	33684	18.1
1994-95	6423	38627	16.6
1995-96	8150	39482	20.6
1996-97	8422	42840	19.7

Note: Repayment of the Centre consists of repayment of Internal Debt and External Debt.

Source: RBI Report on Currency and Finance, various issues.

The share of Central Government in total repayment of Centre and States was 79 per cent in 1950-51 (Table 3.18). It steadily declined and reached 29 per cent in 1980-81. By 1990-91, it again rose to 42 per cent. The 1990's witnessed continuous rise in the share of Central government repayment. In 1995-96 and 1996-97, it reached 60 and 53.7 percent respectively. It points to the increased public borrowings of the Central Government than the States. Consequently, the debt servicing burden of the Central Government in terms of interest payments and repayments remains high.

TABLE 3.18: SHARE OF CENTRAL GOVERNMENT REPAYMENTS IN TOTAL REPAYMENT (CENTRE & STATES)

YEAR	TOTAL REPAYMENTS (CENTRE + STATES) (Rs. Crore)	REPAYMENT BY CENTRE (Rs. Crore)	REPAYMENT BY CENTRE / TOTAL REPAYMENT (%)
1950-51	58	46	79.3
1960-61	259	127	49.0
1970-71	1187	487	41.0
1980-81	2297	661	28.8
1990-91	7479	3145	42.1
1991-92	10634	4269	40.1
1992-93	11527	5451	47.3
1993-94	12493	6098	48.8
1994-95	12770	6423	50.3
1995-96	13598	8150	59.9
1996-97	15698	8422	53.7

Source: RBI Report on Currency and Finance, various issues.

3.5.5 Debt servicing/ Total Disbursement Ratio.

In 1950-51, the ratio of debt servicing to total disbursement (Revenue and Capital) was only 15.6 per cent (Table 3.19). It steadily increased, except in the years 1980-81, when it actually declined to 14.1 per cent. By 1990-91, it reached 22.8 per cent. In 1995-96 nearly one third of the total disbursements of the Central Government was used to service its internal and external debt. This trend persisted in 1996-97 also. This is indicative of the gradually mounting burden of Central Government debt.

TABLE 3.19: TOTAL DEBT SERVICING/TOTAL DISBURSEMENTS (REVENUE+CAPITAL) OF CENTRE

YEAR	DEBT SERVICING (Rs. Crore)	TOTAL (REVENUE + CAPITAL) DISBURSEMENTS (Rs. Crore)	DEBT SERVICING/ TOTAL DISBURSEMENT (REVENUE + CAPITAL) (%)
1950-51	79	500	15.6
1960-61	315	1856	17.0
1970-71	1093	5673	19.3
1980-81	3265	23194	14.1
1990-91	24643	107994	22.8
1991-92	30865	116317	26.5
1992-93	36526	122618	29.8
1993-94	42839	146050	29.3
1994-95	50483	165205	30.6
1995-96	60150	184126	32.7
1996-97	66922	207754	32.2

Source: RBI Report on Currency and Finance, various issues.

3.5.6 Interest payment/Debt servicing Ratio.

The interest payment/debt servicing ratio of Central Government has

been steadily rising (Table 3.20). In 1950-51, it was only 42.3 per cent. By 1960-61, interest payments constituted nearly 60 per cent of the debt burden of the Central Government. In 1980-81, and 1990-91, it reached 80 and 87.2 per cent respectively. This high proportion of interest payments in debt servicing of the Centre remained in all the years of 1990's. This points to the rising rate of interest at which funds are borrowed.

TABLE 3.20: RATIO OF INTEREST PAYMENTS TO TOTAL DEBT SERVICING OF CENTRAL GOVERNMENT

YEAR	INTEREST PAYMENTS (Rs. Crore)	TOTAL DEBT SERVICING (Rs. Crore)	INTEREST PAYMENT / DEBT SERVICING (%)
1950-51	33	79	42.3
1960-61	188	315	59.7
1970-71	589	1093	55.4
1980-81	2604	3265	79.8
1990-91	21498	24643	87.2
1991-92	26596	30865	86.2
1992-93	31075	36526	85.1
1993-94	36741	42839	85.8
1994-95	44060	50483	87.3
1995-96	52000	60150	86.5
1996-97	58500	66922	87.4

Source: RBI Report on Currency and Finance, various issues.

3.5.7 Debt servicing/ Gross Loans Ratio.

The ratio of debt servicing to gross loans of Central government however remained low (Table 3.21). This was only 2.8 per cent in 1950-51. By 1970-71, it nearly doubled to 5.5 per cent and remained constant in

TABLE 3.21: RATIO OF DEBT SERVICING TO THE GROSS LOANS OF CENTRAL GOVERNMENT

YEAR	DEBT SERVICING (Rs. Crore)	GROSS LOANS (Rs. Crore)	DEBT SERVICING / GROSS LOANS (%)
1950-51	79	2844	2.8
1960-61	315	7122	4.4
1970-71	1093	19864	5.5
1980-81	3265	59749	5.5
1990-91	24643	273959	9.0
1991-92	30865	350307	8.8
1992-93	36526	402263	9.1
1993-94	42839	477968	9.0
1994-95	50483	538610	9.4
1995-96	60150	606232	9.9
1996-97	66922	668819	10.0

Source: RBI Report on Currency and Finance, various issues.

1980-81. But by 1990-91, it reached 9 per cent. In 1996-97, nearly 10 per cent of the fresh loans raised by the Central government from internal and external sources were used to service its old debts.

3.6 Conclusion

The aggregate liabilities of the Central and States Government excluding Central loans to States, as a percentage of GDP nearly doubled during the period of study. The outstanding liabilities of the Central Government constitute the major component of Indian public debt. Public debt of State Governments though small is steadily rising. The share of internal debt of Central Government is higher on account of the growth of market loans and bonds. The external Governmental liabilities is only a

small portion of the total debt. The burden of debt servicing of the Centre is gradually increasing. One-third of the total disbursement of the Central Government is now used to service its internal and external debt. The high proportion of interest payments in debt servicing is indicative of the term structure and mix of debt instruments. It points to high rate of interest of borrowings and the presence of long-maturity loans in total debt. Rising repayment burden reduces the net loan available for capital outlay. The high growth of interest payments and low growth of output poses the problem of sustainability of India's public debt.

Reference

1. Chakraborty Committee Report. (1985) P153.
2. India's National Income Statistics, Centre for Monitoring Indian Economy (CMIE), October, 1996.

CHAPTER 4

PUBLIC DEBT OF STATE GOVERNMENTS IN INDIA

4.1 Introduction

In India, public debt has been growing in magnitude at the national level, as seen in the previous chapter. Problems arising from the growth of public debt of State Governments in India, however, have not been systematically examined so far. This chapter is devoted to the study of public debt of State Governments between the period 1950-51 to 1996-97. It examines the various aspects of States' public debt, such as, growth and composition of debt and the debt servicing problem of State Governments. The burden of Central loans to States is analysed in detail, since Central loans constitute the single largest component of State debt in India.

4.2 Structure of the State Government Debt

Public debt of State Governments in India consists of

- (i) Internal Debt.
- (ii) Loans and Advances from Central Government.

- (iii) State Provident Funds, Small Savings, Trusts and Endowments, Insurance and Pension funds.

The components of internal debt of the State Governments are Market Loans and Bonds, Ways and Means advances from the RBI and negotiated loans from banks and other institutions such as

- (1) National Agricultural Credit Fund of RBI.
- (2) National Co-operative Development Corporation.
- (3) Khadi and Village Industries Commission.
- (4) Central Warehousing Corporation.

Loans and advances from the Centre are given for plan and non-plan purposes. Under the Plan, funds are given for State plan schemes including plan assistance for natural calamities, Central plan schemes and Centrally sponsored schemes. The non-plan loans include share of small savings, loans for non-plan Central Government Schemes, Ways and Means Advances etc.

4.2.1 Growth of Public Debt of State Governments 1950-51 to 1996-97

The outstanding public debt of State Governments consisting of internal debt, loans and advances from the Centre and provident

funds and small savings, increased from Rs. 454 crore in 1950-51 to Rs. 245470 crore in 1996-97, (Appendix 4.1). The annual average growth rate of State debt was 24.1 per cent during the period 1950-51 to 1959-60. This growth rate came down to 10.2 per cent between 1970-71 and 1979-80. But the eighties and first half of the nineties witnessed an annual average growth rate of 14.7 and 14.2 per cent respectively (Table 4.1).

TABLE 4.1: PUBLIC DEBT OF STATE GOVERNMENTS (ANNUAL AVERAGE GROWTH RATES)

(In percentage)

YEAR	MARKET LOANS AND BONDS	WAYS AND MEANS ADVANCES FROM RBI	LOANS FROM BANKS AND OTHER INSTITUTIONS	TOTAL INTERNAL DEBT	LOANS AND ADVANCES FROM CENTRAL GOVERNMENT	PROVIDENT FUND & SMALL SAVINGS ETC.	TOTAL PUBLIC DEBT
1	2	3	4	5	6	7	8
1950-51 to 1959-60	15	4.5	-	14.9	29.8	10.0	24.1
1960-61 to 1969-70	9.6	8.5	18.1	11.2	13.3	13.9	12.9
1970-71 to 1979-80	10.3	-6.9	14.2	8.7	10.0	16.4	10.2
1980-81 to 1989-90	17.5	52.6	12.9	15.6	16.5	20	14.7
1990-91 to 1996-97	17.1	-40.3	28.1	17.5	12.6	16.6	14.2

Note: Annual average growth rates are calculated by taking the average of yearly growth rates
Source: RBI Report on Currency and Finance; Various issues

Expressed as a percentage of GDP, the outstanding debt of the State Governments was only 4.7 per cent in 1950-51. In 1970-71 it increased to the all time high of 28.4 per cent. Thereafter it

declined to 19.8 per cent in 1980-81 to rise again to 22.8 per cent in 1990-91. It decreased to 21 per cent in 1996-97. During the same period, the total internal and external liabilities of the Central Government increased from 31.7 in 1950-51 to 58.2 per cent of GDP in 1996-97. The growth in State Government debt-GDP ratio is lower when compared with that of the Central Government debt (see, Appendix 4.1). An increasing debt- GDP ratio both at the Central and State levels leads to 'crowding out' of private investment in the Indian economy. This also poses the question of sustainability of debt.

**TABLE 4.2: OUTSTANDING DEBT OF STATE GOVERNMENTS /GDP RATIO
(1950-51 TO 1996-97)**

(Percentage)							
YEAR	MARKET LOANS AND BONDS	WAYS AND MEANS ADVA- NCES FROM RBI	LOANS FROM BANKS AND OTHER INSTIT- UTIONS	TOTAL INTERN- AL DEBT	LOANS AND ADVANCES FROM CENTRAL GOVERNM- ENT	PROVI- DENT FUNDS AND SMALL SAVINGS ETC.	TOTAL PUBLIC DEBT
1	2	3	4	5	6	7	8
1950-51	1.4	0.2	-	1.6	2.5	0.6	4.7
1960-61	3.2	0.3	0.3	3.9	13.2	0.8	18.0
1970-71	4.0	1.2	0.7	6.0	20.7	1.8	28.4
1980-81	2.5	0.4	0.8	3.6	14.2	2.0	19.8
1990-91	3.3	0.1	0.5	3.9	15.5	3.3	22.8
1991-92	2.8	0.2	1.1	4.9	15.9	3.4	22.5
1992-93	3.6	0.1	0.5	4.2	14.7	3.7	22.6
1993-94	3.6	0.1	0.5	4.2	14.1	3.9	22.1
1994-95	3.5	-0.1	0.7	4.1	13.7	3.8	21.6
1995-96	3.2	-0.1	0.8	3.9	12.1	3.4	19.4
1996-97	3.5	-0.1	1.0	4.3	13.0	3.7	21.0

Source: GDP -figures are taken from CSO Data
 1996-97 figures are provisional
 RBI Report on Currency and Finance; Various issues

4.2.2 Composition of Public Debt of State Governments

The Loans and advances from the Central Government (LACG) is the single most important component of States' debt in India (Table 4.3). As a proportion of States' total debt, its share which was only 52.6 per cent in 1950-51, rose to 73.6 per cent by the end of March 1961. This high proportion of Central loans in States' debt remained unchanged till 1980-81. But by march 1991, it came down to 67.2 per cent, and gradually declined in the nineties. In March 1997, Central loans constituted only 61.3 per cent of States' outstanding debt. In 1950's, Central loans to State Governments increased at an annual average growth rate of 29.8 per cent. But during 1960's and 1970's it came down to 13.3 and 10 per cent respectively. In the 1980's, it slightly improved to 16.5 per cent, but in the 1990's, it recorded a growth rate of only 12.6 per cent, the lowest rate of growth for any item in the States' debt (Table 4.1). The share of market loans and bonds which was 29.5 per cent in 1950-51, declined to 18.0 and 14.1 per cent by the end of March 1961 and 1971 (Table 4.4). In 1980-81, it was only 12.7 per cent of the States' total debt. The share of market loans slightly improved in the 1990's, and it came up to 17.3 per cent in 1996-97.



R
 2000 (100)
 1999

**TABLE 4.3: OUTSTANDING PUBLIC DEBT OF STATE GOVERNMENTS IN INDIA
 (1950-51 TO 1996-97)**

(In percentage)

YEAR AS AT THE END OF MARCH	MARKET LOANS AND BONDS	WAYS AND MEANS ADVAN- CES FROM RBI	LOANS FROM BANKS AND OTHER INSTITU- TIONS	TOTAL INTERN AL DEBT	LOANS AND ADVANCES FROM CENTRAL GOVERN- MENT	PROVI- DENT FUND & SMALL SAVINGS ETC.	TOTAL PUBLIC DEBT
1	2	3	4	5	6	8	9
1950-51	29.5	3.5	-	34.8	52.6	12.6	100
1960-61	18.0	1.5	1.9	21.4	73.6	4.9	100
1970-71	14.1	4.3	2.7	21.1	72.8	6.1	100
1980-81	12.7	2.0	3.8	18.5	70.9	10.7	100
1990-91	14.2	0.6	2.6	17.4	67.2	15.4	100
1991-92	15.0	0.7	2.5	18.2	66.1	15.7	100
1992-93	15.8	0.5	2.2	18.5	65.0	16.5	100
1993-94	16.3	0.5	2.2	18.9	63.7	17.4	100
1994-95	16.3	-0.7	3.4	19.1	63.2	17.7	100
1995-96	17.0	-0.01	3.4	20.4	62.0	17.7	100
1996-97	17.3	-0.2	3.7	20.8	61.3	17.8	100

Source: RBI Report on Currency and Finance: Various issues

The share of provident funds, and small savings has increased considerably and exceeded the share of market loans in States' total debt during the period of study. The share of provident funds, small savings etc. declined between the period 1950-51 and 1980-81 from 12.5 per cent to 7.8 per cent. But by 1990-91, it reached 15.4 per cent of States' total debt. It increased during all the years of the 1990's and it reached 17.8 per cent in 1996-97. The debt item PF and Small Savings recorded 20 per cent annual average growth rates during 1980's and in the first half of the 1990's, the growth

TABLE 4.4: CATEGORY WISE INTEREST PAYMENT OF STATE GOVERNMENTS
(PERCENTAGE OF TOTAL INTEREST PAYMENTS)

YEAR	(In percentage)					
	INTEREST ON LOANS FROM CENTRE 2	INTEREST ON INTERNAL DEBT 3	INTEREST ON MARKET LOANS 4	INTEREST ON OTHER INTERNAL DEBT 5	INTEREST ON SMALL SAVING PF etc. 6	INTEREST ON OTHER LIABILITIES 7
1950-51	36.7	63.3*	-	-	-	-
1960-61	66.2	33.8*	-	-	-	-
1970-71	65.1	34.9*	-	-	-	-
1974-75	64.9	23.3	17.1	6.2	10.0	1.9
1975-76	64.8	24.1	16.6	7.6	9.4	1.7
1976-77	64.1	24.0	16.6	7.3	10.2	1.7
1977-78	62.0	25.1	16.1	9.0	11.4	1.5
1978-79	58.9	25.0	16.9	8.1	14.5	1.6
1979-80	61.5	22.5	15.7	6.8	13.8	2.3
1980-81	64.2	20.7	13.2	7.6	13.1	2.0
1981-82	60.8	23.7	13.0	10.7	13.3	2.2
1982-83	59.4	24.3	11.7	12.6	14.0	2.3
1983-84	60.9	22.1	12.4	8.6	14.9	2.2
1984-85	63.6	23.4	12.0	11.4	11.2	1.8
1985-86	58.1	20.9	11.7	9.2	12.2	8.8
1986-87	65.3	18.8	12.7	4.2	14.4	1.5
1987-88	64.2	18.3	15.0	3.4	15.6	1.9
1988-89	62.3	17.6	14.9	2.7	17.8	2.3
1989-90	61.1	18.7	16.0	2.7	17.7	2.6
1990-91	59.3	18.0	15.4	2.6	20.4	2.4
1991-92	59.1	19.6	15.3	4.4	19.2	2.1
1992-93	59.3	18.7	15.9	2.8	18.7	3.3
1993-94	60.1	17.6	14.9	2.6	19.5	2.8
1994-95	59.0	20.1	17.1	2.9	18.3	2.7
1995-96	50.8	14.9	14.8	0.7	16.6	17.7
1996-97	49.8	17.5	15.3	2.1	15.5	17.3

* Include interest payments of all items other than Central loans

Source: RBI Bulletin, various issues

rate was 16.6 per cent. The Ways and Means Advances (WMA) from the Reserve Bank of India (RBI), to the State Governments showed a marked decline in the 1990's after reaching all time high growth rate during the period 1980-81 to 1989-90. This was mainly due to the Centre's decision to convert these advances into medium term loans, and strict implementation of the Overdraft Regulation Scheme.

On the recommendation of the Sarkaria Commission and keeping in view the pressures on the finances of State Governments, with effect from November 1, 1993, normal Ways and Means Advances and Special Ways and Means Advances have been fixed at 84 times and 32 times, respectively of the minimum balance kept with RBI. Overdraft Regulation Scheme, 1985 and its modification with effect from November 1, 1993 require the RBI to stop payments of State Governments which run an overdraft for more than ten consecutive working days.

4.2.3 Interest Payments of State Governments

As seen earlier, payment of interest is a true money burden which is to be met from the current revenues. The total interest payment of the State Governments was just Rs.9 crore in 1950-51

(Appendix 4.2). But by 1970-71, it increased to Rs. 398 crores. In 1996-97, it reached Rs. 26298 crore. Between 1974-75 and 1996-97, it registered an annual average growth rate of 20 per cent. This growth rate of interest payments exceeded the growth rate of revenue expenditure of State Government (16.6 per cent) during the same period. This growth trend is clearly in line with the growth trend of Central Government interest payments and revenue expenditure. This raises doubts about the sustainability aspect of debt. It is also indicative of high cost of borrowing.

4.2.4 Interest Payments and Revenue Expenditure

The total interest payments of State Governments on various debt items as a proportion of States' revenue expenditure increased from 9.6 per cent in 1974-75 to 16.2 per cent in 1996-97 (Table 4.5). The corresponding figures for Central Government interest payment were 17.5 and 35.5 per cents. Interest payments on Central loans to State Governments accounted for nearly 8.1 per cent of the revenue expenditure of States in 1996-97. The growing interest burden has inflicted severe pressure on the revenue account of the States' budget. This in turn reduces the funds available for developmental expenditure of States.

**TABLE 4.5: CATEGORY WISE INTEREST PAYMENT OF STATE GOVERNMENTS
(TO TOTAL REVENUE EXPENDITURE)**

(In percentage)

YEAR	INTER- EST ON LOANS FROM CENTR E	INTER- EST ON INTER- NAL DEBT	INTER- EST ON MARKET LOANS	INTER- EST ON OTHER INTER- NAL DEBT	INTER- EST ON SMALL SAVING PF etc.	INTER- EST ON OTHER LIABI- LITIES	TOTAL INTER- EST PAYME- NTS
1	2	3	4	5	6	7	8
1950-51	1.1	1.8	-	-	-	-	2.9
1960-61	5.8	3.0	-	-	-	-	8.8
1970-71	7.3	3.9	-	-	-	-	11.3
1974-75	6.2	2.2	1.6	0.6	0.963	0.18	9.6
1975-76	6.8	2.5	1.7	0.8	0.99	0.18	10.5
1976-77	6.4	2.4	1.7	0.7	1.023	0.17	10.0
1977-78	6.1	2.5	1.6	0.9	1.122	0.14	9.8
1978-79	5.3	2.2	1.5	0.7	1.297	0.14	8.9
1979-80	5.0	1.8	1.3	0.6	1.125	0.18	8.2
1980-81	5.6	1.8	1.1	0.7	1.137	0.17	8.7
1981-82	5.4	2.1	1.2	1.0	1.179	0.2	8.9
1982-83	5.2	2.1	1.0	1.1	1.229	0.2	8.8
1983-84	5.3	1.9	1.1	0.8	1.289	0.19	8.7
1984-85	5.8	2.1	1.1	1.0	1.016	0.16	9.1
1985-86	5.2	1.9	1.1	0.8	1.096	0.79	9.0
1986-87	7.2	2.1	1.4	0.5	1.579	0.17	11.0
1987-88	7.0	2.0	1.6	0.4	1.692	0.21	10.9
1988-89	7.1	2.0	1.7	0.3	2.026	0.26	11.4
1989-90	7.3	2.2	1.9	0.3	2.109	0.31	11.9
1990-91	7.2	2.2	1.9	0.3	2.485	0.29	12.2
1991-92	7.5	2.5	1.9	0.6	2.438	0.27	12.7
1992-93	8.1	2.6	2.2	0.4	2.571	0.46	13.7
1993-94	8.7	2.5	2.1	0.4	2.822	0.4	14.5
1994-95	8.7	3.0	2.5	0.4	2.698	0.39	14.7
1995-96	7.5	2.2	2.2	0.1	2.432	2.6	14.7
1996-97	8.1	2.8	2.5	0.4	2.513	2.8	16.2

Source: RBI Bulletin, various issues

4.2.5 Interest Payments of State Governments to GDP ratio

Total interest payments of State Governments in India, expressed as a proportion of GDP, increased steadily from just 0.1

per cent in 1950-51 to 2.3 per cent in 1996-97 (Table 4.6). The Central Government's interest payments in 1996-97 came upto 5 per cent of GDP. This shows that interest burden of the State Governments are low in relation to GDP and Central Government's interest payment burden.

TABLE 4.6: TOTAL INTEREST PAYMENT (STATE GOVERNMENTS)/GDP RATIO

YEAR 1	INTEREST PAYMENT OF STATE GOVERNMENT (Rs. Crores) 2	INTEREST PAYMENT/ GDP RATIO (%) 3
1950-51	9.0	0.1
1960-61	87.0	0.6
1970-71	398.0	1.0
1980-81	1225.5	1.0
1990-91	8734.8	1.8
1991-92	11048.4	2.0
1992-93	13210.1	2.1
1993-94	15820.4	2.2
1994-95	18922.1	2.2
1995-96	21753.3	2.0
1996-97	26298.5	2.3

Source: RBI Report on Currency and Finance, Various issues

4.2.6 Composition of Interest Payment

Interest payment on Central loans formed the largest item in the total interest payment of State Governments in India (Table 4.4). In 1950-51, it was only 36.7 per cent of the total interest payments of State Governments. During 1960-61 and 1970-71, it formed 66.2 and 65.1 per cent of States' interest payments.

Thereafter it recorded marginal decline. In 1990-91, it came down to 59.3 per cent and by the end of 1996-97, it declined to 49.8 per cent. This is mainly on account of the rise in the interest payment on State provident funds and small savings items of State Government debt. This can be attributed to the increase in the share of provident funds and savings deposits in state debt and the rise in the interest rate on these items. The proportion of interest paid on internal debt declined considerably from 23.4 in 1974-75 to 17.5 per cent in 1996-97. This is partly due to the fall in interest payment on the other components of internal debt namely negotiated loans from banks and other financial institutions. The proportion of interest paid on market loans declined marginally from 17.1 to 15.3 per cent in 1996-97.

4.2.7 Repayment/ Capital Disbursement Ratio.

Repayment of debt here refers to the repayment of internal debt and Central loans by the State Governments. (Table 4.7). Repayments of State Governments increased from Rs. 12 crore in 1950-51 to Rs. 7276 crore in 1996-97. During the same period, the capital disbursements of State Governments increased from Rs. 189 crore to Rs. 35666 crores. The repayment-capital disbursement ratio

was only 6.3 per cent in 1950-51. In the period between 1960-61 and 1970-71, the ratio fluctuated between 20.9 and 38.4 per cent. This ratio came down to 22.6 and 24.4 per cents in 1980-81 and 1990-91. It again declined in the subsequent years and in 1996-97, it was only 20.4 per cent. The ratio is slightly higher than that of Central Government during the same period.

TABLE 4.7: REPAYMENT-CAPITAL DISBURSEMENT RATIO OF STATE GOVERNMENTS (1950-51 to 1996-97)

YEAR 1	REPAYMENT (Rs. Crores) 2	TOTAL CAPITAL DISBURSEMENT (Rs. Crores) 3	REPAYMENT/ CAPITAL DISBURSEMENT RATIO (%) 4
1950-51	12	189	6.3
1960-61	132	633	20.9
1970-71	700	1824	38.4
1980-81	1636	7283	22.6
1990-91	4334	19312	22.4
1991-92	5183	21743	23.8
1992-93	5429	23129	23.5
1993-94	6070	25272	24.0
1994-95	6347	33114	19.2
1995-96	5448	32596	16.7
1996-97	7276	35666	20.4

Source: RBI Report on Currency and Finance: Various issues

4.2.8 Debt Servicing / Total Disbursement (Revenue + Capital) Ratio.

Debt servicing by the State Governments consists of both interest payments and repayments of debt. This is reflected both in the revenue and capital disbursements of State Governments, as interest payments form part of revenue expenditure, and repayment

comes under capital disbursements. The mounting debt servicing problem can be gauged by the high proportion of both revenue and capital resources required to service the debt of State Governments. The debt servicing- total disbursement ratio was only 4.2 per cent in 1950-51 (Table 4.8). But by 1970-71, it increased to 20.5 per cent implying that one-fifth of resources under revenue and capital accounts were used to pay for the debt of the State Governments in India. In 1980-81, the ratio declined to 13.7 per cent. By 1990-91, it again started rising and reached 15.3 per cent. This trend continued till 1995-96, when it reached 18.5 per cent. In 1996-97, the ratio stood at 16.2 per cent.

TABLE 4.8: DEBT SERVICING/TOTAL (REVENUE+CAPITAL) DISBURSEMENT RATIO OF STATE GOVERNMENTS 1950-51 to 1996-97

YEAR	DEBT SERVICING (Rs. Crores)	TOTAL (REVENUE + CAPITAL) DISBURSEMENT (Rs. Crores)	DEBT SERVICING/ TOTAL (REVENUE + CAPITAL) DISBURSEMENT (%)
1	2	3	4
1950-51	21	498	4.2
1960-61	219	1620	13.5
1970-71	1098	5360	20.5
1980-81	3034	22091	13.7
1990-91	13559	91088	14.9
1991-92	16662	108549	15.3
1992-93	19294	128335	15.0
1993-94	22615	134649	16.8
1994-95	26683	161554	16.5
1995-96	37380	148262	18.5
1996-97	33839	209257	16.2

Source: RBI, Report on Currency and Finance; Various issues

4.2.9 Ratio of Interest Payments to Total Debt Servicing

The interest payments / debt servicing ratio is very high in the case of State Governments (Table 4.9). In 1950-51, it was 42.9 per cent and in the subsequent decades it declined marginally. By 1990-91, it reached 64.4 per cent and in all the years of the 1990's, it showed clear indication of growth. In 1996-97, the interest payment/debt servicing ratio reached 77.7 per cent. This clearly

TABLE 4.9: RATIO OF INTEREST PAYMENT TO TOTAL DEBT SERVICING OF STATE GOVERNMENTS (1950-51 to 1996-97)

YEAR 1	INTEREST PAYMENT (Rs. Crores) 2	TOTAL DEBT SERVICING (Rs. Crores)	INTEREST PAYMENT / DEBT SERVICING (%) 4
1950-51	9	21	42.9
1960-61	87	219	39.7
1970-71	398	1098	36.2
1980-81	1226	3034	40.4
1990-91	8735	13559	64.4
1991-92	11048	16662	66.3
1992-93	13210	19294	68.5
1993-94	15820	22615	70.0
1994-95	18922	26683	70.9
1995-96	21753	37380	79.4
1996-97	26299	33839	77.7

Source: RBI, Report on Currency and Finance: Various issues

indicates that for the State Governments, the burden of debt is falling more on the revenue budget than on the capital budget. As pointed out earlier, this shows the high rate of interest at which funds are borrowed by State Governments in India. This can lead to fiscal instability. The pressure experienced by the State

Governments on their revenue account can be partly traced to this high interest payment component in total debt servicing.

4.2.10 Ratio of Debt Servicing to Gross Loans.

The increasing debt servicing payments of the State Governments have reduced the net loans available to them. The debt servicing payments on internal debt and Central loans increased from Rs. 21 crore in 1950-51 to Rs. 33839 crore in 1996-97 (Table 4.10). During the same period, gross loans of the State Governments increased from Rs. 175 crores to Rs. 40886 crores. This shows that the debt servicing – gross loans ratio has increased considerably. In 1980-81, the ratio was 76.8 per cent. But loan availability to States improved, when the ratio dipped to 66.8 per cent in 1990-91. Thereafter, the ratio increased steadily and in 1995-96, debt servicing exceeded the gross loans of the State Governments. In 1996-97, it remained at 82.8 per cent. A steady rise in this ratio indicates that the net loans available to the State Governments are falling with the passage of time. It is the State Governments in India, which have to contend with a low net loan availability than the Central Government. This is due to the

limitations imposed on State Governments in raising loans and the high debt servicing payments by the State Governments.

TABLE 4.10: RATIO OF DEBT SERVICING TO GROSS LOANS OF THE STATE GOVERNMENTS

YEAR 1	DEBT SERVICING (Rs. Crores) 2	GROSS LOANS (Rs. Crores) 3	DEBT SERVICING / GROSS LOANS (%) 4
1950-51	21	175*	12.0
1960-61	219	420*	52.0
1970-71	1098	1142*	96.1
1980-81	3034	3953	76.8
1990-91	13559	20308	66.8
1991-92	16662	21020	79.3
1992-93	19294	21453	89.9
1993-94	22615	23929	94.5
1994-95	26683	32772	81.4
1995-96	37380	32349	115.5
1996-97	33839	40886	82.8

Note: Gross loans of the State Government consist of Annual Internal Debt receipts, LACG and PF and Small savings receipts
Gross loans of these three years include only Central loan receipts and market borrowings of States.

Source: RBI, Report on Currency and Finance; Various issues

4.2.11 The Relative Importance of Central Loans in Total

Transfer of Resources from the Centre to States.

A separate detailed discussion on Central loans to States in India can be justified for more than one reason. The share of Central loans in the States' total outstanding debt is very high (61.3 per cent in 1996-97). The interest payments on these loans

registered a growth rate of 18.5 per cent between 1974-75 and 1996-97, and form nearly half of the total interest payments of States. This is 8.1 per cent of the revenue expenditure of State Governments. So the growth of Central loans and the extent of the financial burden they impose in the form of repayment and interest have financial implications for the States.

In all countries, federal or unitary, there are questions of inter governmental fiscal relations that arise from imbalances of expenditure responsibilities and revenue sources among the levels of governments (Graham John, 1982). In India, inter governmental fiscal problems are of two types. One, vertical fiscal imbalance and two, horizontal fiscal imbalance. The former relates to the fiscal imbalance between the Centre and the states and the latter among the states themselves. In all the federations, the constitution and conventions provide for devices to set right the above mentioned imbalances, involving transfer of financial resources from the Central Government to the State Governments in the form of Tax sharing, Grants-in-Aid and Loan assistance.

Federal fiscal transfers from the Centre to the States in India take the following forms.

- (i) shared taxes
- (ii) grants
- (iii) loans.

The constitution of India empowers the Central Government under provision (2) of Article 293 to give loans to States and/or guarantee loans raised by the State Governments within the country. Under this constitutional provision, the Central Government has been providing short-term loans in the form of ways and means advances. Medium and long-term loans have also been advanced mainly from the Consolidated Fund of India though some loans have been advanced from the Special Development Funds built with the funds received in the form of foreign aid.

In India, these fiscal transfers are channelled through three different agencies namely, Finance Commission, Planning Commission and Central Ministries. Devolution of funds to the States, on the basis of the recommendations of the Finance Commission consists of tax revenue shares and grants. Loan assistance predominates fiscal transfers under the aegis of the

Planning Commission and discretionary transfers made by the Union Ministries. The Central Government, on the advice of the Planning Commission, provides plan assistance to the States which consists of grants and loans. The grants-loan component of the plan assistance was not properly defined, in the early years of planning. It was only after 1969 (Fourth Five Year Plan onwards), that the Gadgil Formula of plan assistance was evolved. Under this formula, the grant loan component was fixed as 30:70 (30% grants and 70% loans) on a uniform basis for all States except Assam, Arunachal Pradesh, Himachal Pradesh, Jammu and Kashmir, Meghalaya, Nagaland, Sikkim and Tripura. Even after modification and revision of this formula, the grant-loan component is the same. Fiscal assistance provided at the discretion of the Union Ministries, to States comprises of both grants and loans. At times, loan assistance is given for non-plan revenue expenditure and in recent years for clearing unauthorized overdrafts of the States with the Reserve Bank of India.

4.2.12 Growth of Central Loans to States in India

Central loans to State Government in India are thus advanced as plan and non-plan assistance for both development and non-

development programmes. Loans from the Centre supplement the capital outlay of States but a loan dominated fiscal transfers from Centre to States result in States' rising indebtedness to the Centre. This creates the problem of debt servicing leading to a reduction in net loan availability to the States. This in turn leads to more dependency of the States on the Centre in the mobilization of debt receipts. This situation is analysed, with the help of Table 4.11, which shows the composition of total fiscal transfers made by the Centre to the States in India during the period 1974-75 to 1996-97.

The Table shows that

- (i) Loans from the Centre constitute a major component of these transfers. In 1974-75, total fiscal transfers from the Centre to States in India accounted to Rs. 3320 crores of which loans to states constituted 32.4% (i.e. Rs 1020 crores).
- (ii) By the end of 1978-79, loans from Centre to state as a percentage of total transfers have shown an increasing trend and in 1978-79, loans to the state formed nearly 40.6 per cent of total resources transfers.
- (iii) Between 1978-79 and 1984-85 the volume of Central loans to States increased but as share of total transfers, they had declined

from the high of 40.6 per cent in 1978-79 to an average of 33 per cent.

(iv) During 1985-86 and 1989-90, the same trend prevailed and the percentage share of Central loans marginally declined.

(v) But the nineties witnessed a steady decline in the percentage share of Central loans in total transfer of resources. In 1993-94 it came below the 25% mark. In 1996-97, it has been 29.42 per cent.

(vi) For the entire period of study (1974-75 to 1996-97) the States received total transfer of Rs.648090 crores of which aggregate loans were Rs.197793 crores forming 30.5 per cent of total transfers. Shared taxes constituted nearly 38% of total transfer and grant-in-aid formed 31.47 per cent of total transfer.

(vii) Over the 23 years period of study, loans from the Centre had steadily declined as a proportion of total transfer of resources from the Centre to States in India. During the nineties, the decline was more pronounced compared to the earlier years.

TABLE 4.11: RELATIVE IMPORTANCE OF CENTRAL LOANS IN TOTAL TRANSFER OF RESOURCES FROM CENTRE TO STATES

(Rs crores)

YEAR 1	SHARED TAXES 2	CENTRAL GRANTS 3	CENTRAL LOANS 4	TOTAL TRANSFERS 5	LOANS AS % OF TOTAL TRANSFERS 6
1974-75	1224	1020	1076	3320	32.4
1975-76	1599	1219	1274	4092	31.1
1976-77	1690	1549	1460	4699	31.1
1977-78	1799	1948	1972	5719	34.5
1978-79	2025	2399	3028	7452	40.6
1979-80	3408	2083	2669	8160	32.7
1980-81	3789	2623	3022	9434	32.0
1981-82	4260	2727	3372	10359	32.6
1982-83	4633	3382	4165	12180	34.2
1983-84	5215	4247	5030	14492	34.7
1984-85	5856	4761	5909	16526	35.8
1985-86	7260	6323	8368	21951	38.1
1986-87	8384	6985	7703	23072	33.4
1987-88	9660	8275	9034	26969	33.5
1988-89	10705	9962	10039	30706	32.7
1989-90	12196	10316	10853	33365	32.5
1990-91	14241	12643	13974	40859	34.2
1991-92	16847	15225	13069	45142	29.0
1992-93	20580	17758	13099	51438	25.5
1993-94	22394	21176	14409	57980	24.9
1994-95	24884	20004	19252	64141	30.0
1995-96	29047	29938	19599	69640	28.1
1996-97	34626	36350	25417	86394	29.4
Total	246322	222913	197793	648090	30.5

- Note: 1. Shared Taxes = Income Tax, Union Excise duty, Estate duty
 2. Central Plan Grants (a) State plan schemes, (b) Central plan schemes, (c) Centrally sponsored schemes, (d) Special plan schemes
 Non-Plan Grants= (a) Statutory grants, (b) Grants for natural calamity, (c) Non-plan non-statutory grants.
 3. Central Loans = (a) plan loans, (b) non-plan loans.

Source: RBI Bulletins; various issues.

The decline in the share of Central loans and the increase in the share of tax devolution to States are to be welcomed. Firstly, the burden of Central loans is lessened. Secondly the increase in

the flow of non-debt transfers through the Finance Commission conforms to the spirit of the constitutional provisions.

4.3.1 Debt Servicing Payments and Central Loans to State Government.

As noted earlier, Loans and Advances from the Central Government (LACG) constitute the single most important component of State's debt in India. As a proportion of total debt, it increased from 52.6 per cent in 1950-51 to 61.3 per cent in 1996-97. So it is necessary to examine the various aspects of Central loans to State Governments in the context of rising debt servicing burden of State Governments. The debt servicing burden of Central loans to different categories of States are examined in relation to the overall transfer of resources from the Centre to the States and State's own resources.

4.3.2 Ratio of Debt servicing Payments to the Gross Loans from the Centre: 1974-75 to 1996-97

The increasing debt servicing payments have progressively reduced the net loans given to the States by the Centre (Table 4.12). Many States in India have fallen into 'debt traps', a situation wherein fresh loans are necessary to service old loans. During the Fifth Five Year Plan period (1974-79), the ratio of net loans to

gross loans was only 33 per cent. The situation appeared to be improving during the Annual Plan period (1979-80) as the ratio increased to 48 per cent. But after that, from Sixth Five Year Plan to Eighth Five Year Plan the situation steadily worsened. The ratio of net loans to gross loans came down to 16 per cent in the last year (1996-97) of the Eight plan (35%-Sixth Five Year Plan, 33%-Seventh Five Year Plan, 28% Annual Plan).

TABLE 4.12: RATIO OF DEBT SERVICING PAYMENTS TO GROSS LOANS FROM THE CENTRE, 1974-75 TO 1996-97 (in percentage)

PLAN PERIOD STATES	V (74-79)	AP (79-80)	VI (80-85)	VII (85-90)	AP (90-92)	VIII (92-97)
Punjab	76	75	69	30	31	91
Haryana	87	51	71	117	81	80
Maharashtra	80	34	46	62	72	103
Gujarat	79	28	46	165	74	107
West Bengal	62	75	69	91	78	80
Karnataka	76	63	74	81	86	82
Tamil Nadu	57	58	61	91	65	70
Kerala	77	56	87	92	81	79
Andhra Pradesh	68	47	68	76	67	72
Rajasthan	100	83	84	75	102	83
Orissa	77	47	70	78	86	88
Uttar Pradesh	50	50	65	65	62	74
Madhya Pradesh	58	52	51	72	95	103
Bihar	66	40	60	76	62	94
Assam	64	34	62	64	56	34
Himachal Pradesh	147	47	96	54	82	105
Jammu & Kashmir	50	13	48	46	169	215
Tripura	188	22	104	54	92	128
Manipur	95	88	115	130	128	121
Nagaland	61	77	144	89	89	264
Meghalaya	84	26	92	67	89	96
Sikkim	14	8	39	38	101	94
Arunachal Pradesh	-	-	-	108	40	31
Mizoram	-	-	-	65	321	80
Goa	-	-	-	32	77	124
All States	67	52	65	67	72	84

Source: RBI Bulletin, various issues "Finances of State Governments' 1974-to 1996-97.

The phenomenon of negative loan 'assistance' was faced by States like Tripura and Himachal Pradesh, during the Fifth Five Year Plan period itself. More States joined this rank during the Sixth Five Year Plan period (e.g. Manipur and Nagaland). Four States, Haryana, Gujarat, Manipur, Arunachal Pradesh, faced this problem during the Seventh Five Year Plan period. During the Annual plan period (1990-92) five States- Rajasthan, J&K, Manipur, Sikkim and Mizoram had to contend with a situation of negative loan assistance from Centre. The Eighth Five Year Plan period witnessed a record number of 9 States experiencing this problem. (Maharashtra, Gujarat, M.P., Himachal Pradesh, J & K, Tripura, Manipur, Nagaland, Mizoram).

In the case of other States too, the percentage of debt servicing payments to gross loans was steadily going up. All categories of States experienced this problem of increasing debt servicing payments in relation to gross Central loans. This trend would have been much worse but for the debt rescheduling made by the Sixth, Seventh, Eighth and Ninth Finance Commissions. During the Annual Plan (1990-92) period, the problem was acute for special category States and low income States. But in the Eight Five Year Plan period almost all categories of States stood exposed

to the problem of mounting debt servicing and negative loan assistance.

4.3.3 Debt servicing Payments on Central Loans and inflow of Central Funds to States.

Debt servicing payments of Central Loans formed 20.8 per cent of the aggregate budgetary transfers from the Centre to the States between March 1979 and March 1997 (Table 4.13). This indicates that State Governments in India use around one-fifth of the total resources from Centre just to service their loans from the Central Government. This proportion is still higher for States like Punjab, Haryana, Maharashtra, Gujarat, West Bengal, Karnataka, Kerala, Andhra Pradesh, Rajasthan and Bihar.

Debt Servicing payments formed 52 per cent of statutory transfers of all State Governments in India between March 1979 and March 1997. These payments exceeded statutory transfers in the case of Punjab, Haryana, and Bihar. Other States with higher proportions of debt servicing payments to statutory flows were Maharashtra, Gujarat, West Bengal, Karnataka, Kerala, Rajasthan, Bihar and Assam.

TABLE 4.13: DEBT SERVICING PAYMENTS ON CENTRAL LOANS AND INFLOW OF CENTRAL FUNDS, 1979 TO 1997 (Rs. Crores)

STATES	DEBT SERVICING 1	STATUTORY TRANSFERS 2	PLAN TRANSFERS 3	DISCRETIONARY TRANSFERS 4	TOTAL TRANSFERS 5 (2+3+4)	NET INFLOW 6 (5-1)	PERCENTAGE OF COLUMN 1 TO 5				
							2	3	4	5	
Punjab	533	305	343	921	1569	1036	174.75	155.39	57.87	33.97	
Haryana	349	314	322	420	1056	707	111.15	108.39	83.10	33.05	
Maharashtra	226	369	269	362	1000	774	61.25	84.01	62.43	22.60	
Gujarat	239	363	261	410	1034	795	65.84	91.57	58.29	23.11	
West Bengal	311	467	213	382	1062	751	66.60	146.01	81.41	29.28	
Karnataka	261	390	211	314	915	654	66.92	123.70	83.12	28.52	
Tamil Nadu	176	454	263	208	925	749	38.77	66.92	84.62	19.03	
Kerala	293	444	312	266	1022	729	65.99	93.91	110.15	28.67	
Andhra Pradesh	248	449	271	225	945	697	55.23	91.51	110.22	26.24	
Rajasthan	324	415	274	386	1075	751	78.07	118.25	83.94	30.14	
Orissa	237	544	385	349	1278	1041	43.57	61.56	67.91	18.54	
Uttar Pradesh	185	407	207	248	862	677	45.46	89.37	74.60	21.46	
Madhya Pradesh	161	441	284	202	927	766	36.51	56.69	79.71	17.37	
Bihar	197	116	280	227	623	426	169.83	70.36	86.78	31.62	
Assam	416	688	709	467	1864	1448	60.47	58.67	89.08	22.32	
Himachal Pradesh	343	1293	1463	659	3415	3072	26.53	23.45	52.05	10.04	
Jammu & Kashmir	697	1350	1618	1035	4003	3306	51.63	43.08	67.34	17.41	
Tripura	240	1753	1769	476	3998	3758	13.69	13.57	50.42	6.00	
Manipur	700	1567	2183	1743	5493	4793	44.67	32.07	40.16	12.74	
Nagaland	1069	4690	3940	1326	9956	8887	22.79	27.13	80.62	10.74	
Meghalaya	276	1785	2188	512	4485	4209	15.46	12.61	53.91	6.15	
Sikkim	329	1615	5720	2054	9389	9060	20.37	5.75	16.02	3.50	
Arunachal Pradesh	151	1904	2869	106	4879	4728	7.93	5.26	142.45	3.10	
Mizoram	387	2279	2122	154	4555	4168	16.98	18.24	251.30	8.50	
Goa	464	720	538	220	1478	1014	64.44	86.25	210.91	31.39	
All States	241	463	372	323	1158	917	52.05	64.79	74.61	20.81	

Note : Debt Servicing of Central loans means Repayment of loans to Centre and interest payment on Central loans

Source: RBI Bulletin, various issues, "Finance of State Governments' 1974-to 1996-97.

During the same period, debt servicing on Central loans formed 64.8 per cent of plan assistance to State Governments. In the case of States like Punjab, Haryana, West Bengal, Karnataka and Rajasthan, debt servicing of Central loans exceeded the plan assistance. Other States with high proportion of debt servicing to plan assistance were Maharashtra, Gujarat, Kerala, Andhra Pradesh, UttarPradesh and Bihar.

Further, debt servicing payments formed three- fourth of discretionary transfers for all states. These payments were more than the total discretionary transfers in the case of States like Kerala, Andhra Pradesh and Arunachal Pradesh.

4.3.4 Ratio of Debt Servicing Payments to Total Disbursements; State Wise Analysis: 1974 -75 To 1996 -97.

The burden of Central loans to State Governments can also be gauged in terms of the debt servicing/total disbursement ratio. This clearly shows the financial stress of the States' revenue and capital accounts. During the 23 year period of the study, debt servicing of Central loans accounted for 8-10 per cent of States' combined revenue and capital disbursements (Table 4.14).

TABLE 4.14: RATIO OF DEBT SERVICING PAYMENTS OF CENTRAL LOANS TO TOTAL DISBURSEMENTS(CAPITAL AND REVENUE) 1974-75 TO 96-97.
(in percentage)

PLAN PERIOD STATES	V (74-79)	AP (79-80)	VI (80-85)	VII (85-90)	AP (90-92)	VIII (92-97)
Punjab	13	10	15	10	8	18
Haryana	10	6	10	18	9	7
Maharashtra	7	4	6	8	9	9
Gujarat	9	3	7	10	10	12
West Bengal	13	16	14	16	13	14
Karnataka	9	8	7	9	8	8
Tamil Nadu	7	7	6	9	7	8
Kerala	10	6	10	13	11	8
Andhra Pradesh	9	8	7	8	8	9
Rajasthan	13	16	14	12	12	8
Orissa	17	9	11	15	13	11
Uttar Pradesh	10	9	9	10	10	10
Madhya Pradesh	8	6	6	9	9	8
Bihar	17	9	11	13	12	13
Assam	13	22	17	17	12	17
Himachal Pradesh	10	3	8	6	9	10
Jammu & Kashmir	14	4	13	13	14	15
Tripura	6	1	6	4	7	6
Manipur	10	12	14	8	6	7
Nagaland	7	6	8	5	9	3
Meghalaya	3	1	6	5	5	7
Sikkim	-	1	3	3	6	3
Arunachal Pradesh	-	-	-	5	3	2
Mizoram	-	-	-	9	18	3
Goa	-	-	-	11	11	11
All States	10	8	9	10	10	10

Source: RBI Bulletin various issues "finance of state governments' 1974-to 1996-97.

The burden of debt indicated by this ratio is not being felt uniformly by all States. The burden was the highest for Assam followed by West Bengal, Rajasthan, Orissa, Bihar and Punjab. Among the non-special category States, it was the lowest for Maharashtra, Tamilnadu and Madhya Pradesh.

4.3.5 Ratio of Central Loan Payments to Non- Plan Capital Disbursement: 1974-75 to 1996-97.

The intensity of the debt service burden of State Governments is felt on the non-plan capital account. The ratio of Central loan repayment installments to non-plan capital disbursements shows that during the Fifth Five Year Plan period 97.5 per cent of States' non-plan capital disbursements were used for repayment obligations of Central loans (Table 4.15). This provides the rationale for debt

TABLE 4.15: RATIO OF LOAN REPAYMENTS (CENTRAL LOANS) TO NON-PLAN CAPITAL DISBURSEMENT 1974-75 TO 1996-97

STATES	1974-79*	1980-85*	1985-90*	1990-92	1992-97
Punjab	98.1	93.7	94.0	103	115
Haryana	98.3	90.3	93.6	89	62
Maharashtra	99.2	89.3	94.1	69	54
Gujarat	98.2	67.0	85.2	48	46
West Bengal	89.2	85.2	97.3	106	96
Karnataka	99.1	74.5	92.4	51	40
Tamil Nadu	97.8	72.9	93.4	43	34
Kerala	99.0	85.2	94.1	78	63
Andhra Pradesh	99.2	86.6	93.6	59	54
Rajasthan	98.8	90.1	95.6	76	62
Orissa	98.9	89.5	93.2	82	64
Uttar Pradesh	93.8	99.7	95.8	49	40
Madhya Pradesh	99.4	79.3	95.7	75	77
Bihar	97.4	89.2	98.0	79	72
Assam	99.8	87.9	97.1	85	77
Himachal Pradesh	99.0	89.4	92.0	89	70
Jammu & Kashmir	99.4	96.4	97.8	61	86
Tripura	98.3	99.4	91.0	152	82
Manipur	99.5	87.1	96.3	132	48
Nagaland	99.5	93.1	90.6	82	221
Meghalaya	99.1	92.3	87.7	36	43
Sikkim	-	73.2	97.0	130	44
Arumachal Pradesh	-	-	-	0	31
Mizoram	-	-	-	67	34
Goa	-	-	-	99	164
All States	97.5	86.8	94.9	60	55

Note: * These are estimates of Finance commissions

Source: RBI Bulletin, various issues "Finance of State Governments' 1974-to 1996-97.

rescheduling recommended by the Sixth, Seventh and Eighth Finance Commissions. The ratio was 86.6 and 94.9 per cents during the Sixth and Seventh Five Year Plan periods, covered by the Seventh and Eighth Finance Commissions' recommendations. This ratio declined during the Annual plan period (1990-92) and the Eighth plan period coinciding with the debt relief recommended by the Ninth and the Tenth Finance Commissions.

4.3.6 Ratio of Debt Servicing To States' Own Resources.

Another indicator of debt servicing burden of Central loans, is the ratio of debt servicing payments to States' own capital and revenue resources (Table 4.16). The ratio of the debt servicing to States' own resources is a measure of the ability of State Governments to service the debts out of their own resources and not out of Central funds. From 18 per cent in the Fifth plan, this ratio declined to 16 per cent in the Eighth Plan period. The burden was the highest for Special Category States like Nagaland, Manipur, Jammu and Kashmir, Assam and Tripura. For States like Manipur, Nagaland and Mizoram, debt servicing exceeded their own resources, during several plan periods indicating their insolvency position. To them, debt servicing payments could be met only out of additional Central loans or Central transfers like tax sharing and

TABLE 4.16: RATIO OF DEBT SERVICING (CENTRAL LOANS) TO STATES' OWN RESOURCES (REVENUE AND CAPITAL) 1974-75 TO 1996-97

(In percentage)

PLAN PERIOD STATES	V (74-79)	AP (79-80)	VI (80-85)	VII (85-90)	AP (90-92)	VIII (92-97)
Punjab	19	10	29	22	15	28
Haryana	15	9	15	28	11	7
Maharashtra	9	5	9	11	12	12
Gujarat	13	5	10	14	13	16
West Bengal	25	35	30	32	24	26
Karnataka	13	13	13	14	10	11
Tamil Nadu	11	13	10	13	10	11
Kerala	18	9	18	21	18	12
Andhra Pradesh	16	15	12	13	13	16
Rajasthan	26	35	28	23	22	20
Orissa	28	27	29	25	30	23
Uttar Pradesh	19	20	21	23	22	19
Madhya Pradesh	12	11	10	17	16	14
Bihar	41	24	27	27	22	32
Assam	37	24	56	62	37	41
Himachal Pradesh	33	12	24	22	17	26
Jammu & Kashmir	49	13	46	85	98	100
Tripura	44	4	32	18	47	70
Manipur	172	78	138	62	37	32
Nagaland	62	181	53	39	77	170
Meghalaya	24	5	36	29	26	33
Sikkim	4	3	16	11	22	8
Arunachal Pradesh	-	-	-	87	19	21
Mizoram	-	-	-	279	85	18
Goa	-	-	-	21	20	14
All States	18	15	18	17	17	16

Note : 1. Debt Servicing of Central loans means Repayment of loans to Centre and interest payment on Central loans

2. States' own Resources include States' own Revenue and Capital Resources
States own Revenue = Total Revenue minus the sum of share in Central Taxes and grants from Centre.

3. States' own Capital Resources = Total Capital receipts minus loans and advances from Centre.

Source: RBI Bulletin, various issues "Finances of State Governments' 1974-to 1996-97.

grants. The Sixth Finance Commission found it irrational to assess the debt servicing capacity of States by relating the debt burden to actual own revenues of State Governments, as it puts to disadvantage those States which exploited their revenue potential more fully. So they related the burden of debt to per capita income.

4.3.7 Outstanding Debt / State Domestic Product Ratio-Inter State Variations

The ratio of outstanding debt to State Domestic Product increased considerably during this period. At the end of March 1979 and 1984, outstanding debt of All States accounted for more than a quarter of the State Domestic Product. This ratio increased to 45 per cent at the end of March 1989 and 1994. The estimates for March 1997 shows that outstanding debt constitutes more than half (55 per cent) of the State's Domestic Product. This ratio shows considerable inter-state variations. The outstanding debt of Jammu and Kashmir exceeded the State Domestic Product in March 1979. Manipur and Orissa had high ratio of outstanding debt to SDP during this period. The outstanding debt of Arunachal Pradesh exceeded its SDP by the end of March 1989. For States like J&K and Nagaland, debt nearly equaled the SDP in March 1994 (Table 4.17).

TABLE 4.17: OUTSTANDING AGGREGATE DEBT OF STATES 1978-79 TO 1996-97

STATES	AT THE END OF 96-97		AT THE END OF 93-94		AT THE END OF 88-89		AT THE END OF 83-84		AT THE END OF 78-79	
	PERCAPITA	% SDP	PERCAPITA	% SDP	PERCAPITA	% SDP	PERCAPITA	% SDP	PERCAPITA	% SDP
Punjab	6739	48.3	5059	39.2	2472	38.4	692	17.7	447	16.2
Haryana	3636	27.1	2550	24.0	1401	24.3	753	22.5	516	22.5
Maharashtra	2517	16.6	2455	21.5	1209	22.3	565	17.7	329	15.5
Gujarat	2804	26.0	2245	25.6	1456	31.3	603	20.4	318	17.0
West Bengal	2469	32.1	1865	28.7	1032	27.7	645	27.4	370	24.3
Karnataka	2272	26.1	1835	25.6	929	25.3	434	20.8	335	24.5
Tamil Nadu	2447	25.3	2012	25.8	821	22.5	396	20.9	282	23.1
Kerala	3754	47.0	2589	41.3	1170	35.9	566	30.7	376	29.1
Andhra Pradesh	2373	27.8	1790	25.6	962	27.4	481	23.2	320	25.2
Rajasthan	2825	42.0	2173	41.4	1331	42.8	782	38.7	491	34.8
Orissa	3154	52.1	2338	50.2	1193	42.6	642	46.6	429	42.7
Uttar Pradesh	2214	38.7	2039	42.4	975	35.6	450	26.7	282	25.5
Madhya Pradesh	1904	29.7	1337	24.2	913	29.7	481	28.0	273	25.7
Bihar	1989	47.6	1598	43.5	875	38.4	468	37.0	211	29.1
Assam	2324	37.7	2051	39.0	149	47.8	752	39.2	479	37.7
Himachal Pradesh	5897	72.2	3570	54.5	10151	42.8	787	33.4	571	37.7
Jammu & Kashmir	5644	146.2	4129	96.7	3363	93.1	1816	93.8	1516	102.7
Tripura	2931	74.5	2639	71.1	1185	39.2	648	54.2	395	31.2
Manipur	2995	63.6	3556	66.0	1715	48.4	1273	70.7	702	22.1
Nagaland	7231	101.6	5277	91.5	3112	86.1	1628	115.4	1360	80.9
Meghalaya	2261	35.1	1957	32.6	927	29.8	632	39.7	412	32.9
Sikkim	6530	129.0	4682	74.9	1897	44.3	529	37.2	304	N.A.
Arunachal Pradesh	6781	67.4	3120	39.4	4595	108.4	-	-	-	-
Mizoram	6083	90.9	5243	77.6	2984	73.5	-	-	-	-
Goa	9184	70.0	5689	38.3	5487	79.4	-	-	-	-
All States	2613	55.0	2080	45.6	1118	45.5	554	26.6	347	25.2

Note : Aggregate debt includes IDEBT, LACG and PF etc.

SDP figure are (CSO) taken from Report on Currency and Finance (RBI)

4.3.8 Rates of Interest on Central Loans: Plan and Non- Plan.

Loans advanced by the Centre by way of assistance to finance State plans constitute the bulk of Central loans to States. The burden of debt servicing of States on this account has gone up with the progressive increase in plan outlays and the rise in interest rates. This is shown in Table 4.18. The rate of interest increased

**TABLE 4.18: RATE OF INTEREST ON PLAN AND NON-PLAN CENTRAL LOANS
(OTHER THAN SMALL SAVING LOANS)**

STATE PLAN LOANS		INTEREST RATE (per cent per annum)
i	Pre-1979 Consolidated State plan loans	4.75
ii	Loans advanced during 1979-84 consolidated for terms ranging from 15 to 30 years	6-6.75
iii	As per Ninth FC recommendations State plan Loans advanced during 1984-89 and outstanding at the end of 1989-90.	9.00
OTHER PLAN AND NON-PLAN LOANS GIVEN TO STATES FROM		
i	1.6.84 to 31.5.85	7.50
ii	1.6.85 to 31.5.86	8.00
iii	1.6.86 to 31.5.87	8.75
iv	1.6.87 to 31.5.88	9.25
v	1.6.88 to 31.5.90	9.75
Vi	1.6.90 to 31.5.91	10.25
Vii	1.6.91 to 31.5.92	10.75
Viii	1.6.92 to 31.5.93	11.75
ix	1.6.93 to date	12.00

Source: Tenth Finance Commission Report (1995).

from 4.75 per cent on pre-1979 consolidated State plan loans to 9 per cent on loans outstanding as at the end of 1989-90. But the rate of interest on other plan and non-plan loans increased steadily

from 7.5 per cent to 12 per cent during June 1984 and May 1995. This coupled with the increase in the interest rate on Small Savings loans to States contributed to the burden of debt servicing of States.

The other aspects of Central loans to States in India are

- (i) The terms of repayments are uniform for all states irrespective of their different stages of development or nature of investment.
- (ii) Loans for relief of distress caused by natural calamities are repayable in 10 years. It would be highly unrealistic to assume that they would generate enough revenues to meet both interest and repayment schedules in 10 years.
- (iii) Loans are granted not only for building of physical assets, but also for meeting the revenue component of the State plan outlay.

The above discussion of the various aspects of Central loans to State Governments shows that the financial relation between the Central Government and the State Governments in India, has become partly a creditor-debtor relationship with unduly heavy burden of loans on the states. The Central Government in India, unlike the ordinary creditors, partakes in the profits generated besides getting back the principal and interest, because the

economic development financed by loans also adds to the buoyancy of Centre's revenues (George 1988)².

4.3.9 Rates of Interest on Small Savings Loans to States.

The present arrangements entitle States to a 75 per cent share of net collections under various small savings schemes to be given to them by the Central Government as a loan for development purposes. The repayment period is 25 years. The rate of interest on these loans to the States has been increasing steadily over time. It increased from 6.25 per cent in July 1974 to 14.5 per cent in May 1997 (Table 4.19). The rates are rising steadily reflecting the deregulation of interest rates in an era of financial reforms. The entitlement to a loan against small savings is worked out on the basis of net collections of State Governments. The repayments insisted on by the Central Governments is open to criticism by the States. It is argued that the small savings actually belongs to States and the role of the Centre is only to ensure economies of scale through Central management. So the State Governments argue that these loans should be treated as loans in perpetuity. Since States get only a share of net collection of fund, there is no justification for insisting on repayment and high interest charges on these loans.

TABLE 4.19: RATE OF INTEREST ON SMAL SAVING LOANS TO STATES

DATE OF LOAN		INTEREST RATE (per cent per annum)
1	1.8.74 to 31.5.81	6.25
2	1.6.81 to 31.5.82	7.25
3	1.6.82 to 31.5.83	7.75
4	1.6.83 to 31.5.84	8.75
5	1.6.84 to 31.5.85	9.75
6	1.6.85 to 31.5.86	10.25
7	1.6.86 to 31.5.89	12.0
8	1.6.89 to 31.5.91	13.0
9	1.6.88 to 31.5.90	13.5
10	1.6.91 to 31.5.92	14.5
11	1.6.92 to 31.5.93	15.0
12	1.6.93 to date	14.5

Source: Tenth Finance Commission Report (1995).

4.3.10 Growth of Market Borrowings and Share of State Governments

Sharing of funds raised through market borrowings between the Centre and States is worked out by the Planning Commission in consultation with the Ministry of Finance and the Reserve Bank of India. In this decision making process, States are not adequately consulted (G.Thimmaiah, 1985)¹. Moreover, distribution of resources, raised through market borrowings between the Centre and States is not based on any definite criterion. The share of State Governments in total market borrowing has remained stagnant and low. But total market borrowings are increasing in size and nearly three fourth of it is used by the Centre to finance its plan outlay. Market borrowings by State Governments are governed by a simple

critterion. From 1975-76, the net market borrowings of each State was allowed to increase by 10 per cent annually. But during the Sixth Plan period, States were allowed to increase the amount of market borrowings by 20 per cent from the amount in 1982-83.

In India, the Reserve Bank of India keeps Central and State Government funds and co-ordinates their borrowings. It floats all State Government loans. The Central Government in consultation with the Planning Commission finalises the size of the market borrowing of the State governments. The Central Government in India controls the market borrowings of State governments. This is due a to variety of reasons:

- (i) All the State Governments are always indebted to the Central Government. So they are required to obtain prior permission of the Central Government before embarking on any market borrowing
- (ii) The Governments in India borrow from a captive market owned and controlled by Central Government whose constituents are statutorily required to invest in government securities.

The major constituent of the captive markets are (1) the commercial banks (2) the Reserve Bank of India (3) Insurance Corporations (4) the various Public Funds. Almost all these institutional investors are owned or controlled by the Central Government. Therefore it can be stated that market borrowing by States is controlled by the Central Government and guided by the Reserve Bank of India.

4.3.11 Market Borrowing and Total Plan Outlay (Centre and State).

Table 4.20 shows the increase in the market borrowings of the Centre and State governments from the Fifth to the Eighth FYP period. In the Fifth Plan period (1974-79) market borrowing financed only 16.5 per cent of the total plan outlay. But this went up during the Annual plan (1979-80) and Sixth Plan period (1980-85), and reached 20 per cent by the end of 1984-85. It declined marginally during the Seventh plan period to 17 per cent. During the two annual plans, it was around 19 per cent. But in the Eighth plan period, market borrowing as a percentage of total plan outlay came down to 10 per cent.

TABLE 4.20: PLAN OUTLAY AND MARKET BORROWINGS, VTH TO VIIITH FYP

Plan Period		V th PLAN 1974-79	A.P. 1979-80	VI th PLAN 1980-85	VII th PLAN 1985-90	A.P. 1990-91	A.P. 1991-92	VII th PLAN 1992-97
Total	Plan outlay	39303	12601	110827	180000	59548	62588	434100
	Market Borrowing	6507	2371	22120	30562	11307	11691	42916*
	% to Plan outlay	16.56	18.60	20.0	17.00	19.00	18.67	9.9*
Centre	Plan outlay	20586	6639	60684	99302	36008	37641	249708
	Market Borrowing	3751	1850	17401	15000	8989	8919	18270*
	% to Plan outlay	18.22	27.87	28.67	30.67	25.44	23.70	34.50
States	% to total Market Borrowing	57.6	78.03	78.67	76.92	79.50	76.29	42.58
	Plan outlay	18717	5962	50138	80698	22361	24947	184392
	Market Borrowing	2756	521	4719	9942	2569	3364	24646*
	% to Plan outlay	14.7	8.74	9.41	12.32	11.49	13.48	10.49
	% to total Market Borrowing	42.4	21.97	21.33	32.53	20.5	23.71	57.42

Note: * Provisional

Source: RBI Report on Currency and Finance, 1974-75 to 1996-97.

4.3.12 Market Borrowing and Central Plan Outlay

Market borrowings were increasingly used to finance Central plan outlay, from the Annual plan period of 1979-80 onwards. In the Fifth Five year Plan period, (1974-79) only 18.2 per cent of Central plan outlay was financed through market borrowings, which constituted 57.6 per cent of the total market borrowings envisaged during that plan period. But with the Annual Plan of 1979-80, the proportion of market borrowings used to finance plan outlay of the Centre gradually increased. Nearly 78 per cent of the total market borrowing went to finance 25 to 30 per cent of the central plan outlay between 1979-80 and 1991-92. But during the Eighth Plan period (1992-97), the situation changed considerably. During the period, 34.5 per cent of Central plan outlay was financed by market borrowing. But this constituted only 42.6 per cent of the total market borrowings.

4.3.13 Market Borrowing and States' Plan Outlay

The share of market borrowing in States' plan outlay remained low. In the Fifth FYP period, it was 14.7 per cent. But

this declined in subsequent FYPS. It was only 8.7 and 9.4 in the Annual plan (1979-80) and Sixth FYP periods. In the Seventh FYP, it was 12.3 per cent and this proportion remained more or less the same in the next two Annual plans (1990-92). In the Eighth FYP period, it was only 10.5 per cent. Thus the States' share in total market borrowing declined from the Fifth FYP onwards.

4.3.14 Average Maturity Period and Rate of Interest of Market Borrowings of Central and State Governments in India.

The maturity periods of States' loans from the Centre were shorter than that of Central Government's own loans. In fact, the Centre was borrowing long from the market and lending short to the States. The average period of maturity of Central Government market borrowing was 18 ½ years in 1975-76 (Table 4.21). It remained high till 1985-86 when it reached 20 years and 2 months, All State Government securities had a maturity of only 10 years till 1979-80. Between 1980-82, it came to 12 years and in 1984-85 it was 15 years. The rate of interest on Central Government market borrowing was only 5.7 per cent in 1974-75 and it gradually increased to 10.5 per cent in 1985-86. The rate of interest on the market borrowings of State Government was higher at 6.14 per cent in 1974-75 and increased in line with the interest rate increase of

Central Government securities. It came up to 9.75 per cent in 1985-

86.

TABLE 4.21: MATURITY AND RATE OF INTEREST OF CENTRAL AND STATE GOVERNMENTS BORROWINGS. (1974-75 TO 1996-97)

YEAR	CENTRAL GOVERNMENT			STATE GOVERNMENT		
	Period of maturity No. of Years & month	Rate of interest (%)	Gross borrowings (Rs. crores)	Period of maturity No. of Years & month	Rate of interest (%)	Gross borrowings (Rs. Crores)
1974-75	12-3	5.7	697	10	6.1	311
1975-76	18-6	5.6	661	10	6.1	275
1976-77	21-6	6.3	1124	10	6.1	283
1977-78	20-4	6.2	1312	10	6.1	284
1978-79	19-7	6.4	1834	10	6.3	283
1979-80	18-6	6.5	2259	10	6.5	306
1980-81	16-4	6.8	2871	12	6.8	400
1981-82	17-8	7.2	3191	12	7.0	507
1982-83	17-6	7.8	4166	15	7.5	557
1983-84	18	8.8	4129	14.8	8.6	829
1984-85	18-3	9.3	4591	15	9.0	1301
1985-86	20-2	10.5	5767	13	9.8	1414
1986-87	13-2	10.9	6351	15	11.0	1446
1987-88	13-4	10.9	7821	15	11.0	1789
1988-89	14-6	11.0	7725	20	11.5	2285
1989-90	13-6	11.0	8044	20	11.5	2555
1990-91	7-25	11.0	8989	20	11.5	2561
1991-92	12-7	11.3	8919	20	11.8	3364
1992-93	7.2	12.5	4821	15	13.0	3805
1993-94	6-1	12.9	49012	10	13.5	4145
1994-95	6-3	11.9	38068	10	12.5	5123
1995-96	6-11	17.1	40509	10	14.0	6274
1996-97	6-11	12.2	29616	10	13.9	6536

Source: RBI, Report on Currency and Finance, various issues.

From 1986-87, there was some definite change both in the maturity pattern and interest rate of Central and State Government market borrowings. The maturity period of Central Government securities declined from 20 years and 2 months in 1985-86 to 6

years 11 months in 1996-97. But the maturity period of State Government securities increased to 20 years during 1988-89 and 1991-92. Between 1993 and 1997 it came down to 10 years. In other words, from the mid 1980's onwards, State Government securities had a higher maturity period compared to the Central Government securities. But the average rate of interest on State Government market borrowings increased and remained marginally higher than that of the Central Government securities between 1986-87 and 1994-95.

The captive market for government securities would shrink further in the wake of reduction in the Statutory Liquidity Ratio (SLR), which is an integral part of the financial sector reforms. In response to SLR reductions, the Central Government have moved over to an auction system by offering market related interest rates on securities. But the State Governments are still continuing with the existing arrangements of market borrowings at a pre-determined coupon rate, amount and fixed maturity. This distorts the term structure of interest rates and could create problems for the State Governments. Therefore, alternative methods to raise borrowings from the market need to be devised, with the State Governments moving over to a system of market determined interest rate based on

auctions. The cost effectiveness of multiple price auction over the uniform price auction should be weighed in terms of revenue maximization on the one hand and development of broad based market for State Government bonds on the other. The existing system of market borrowing for States has led to segmentation of the Government security market, with one part operating under price regulation. But with fixed prices for bond, some degree of quantity rationing and intervention become inevitable. Similarly, financially better managed States lack the scope and incentive for tapping funds from the market at competitive rates of interest. The success of the auction system for market borrowing of State Government hinges on the quality of fiscal management at the State level. The creditworthiness of a State will be assessed by the market on the basis of its financial performance. Since the borrowing powers of State Governments are limited unlike the Central Government, their bonds may not be perceived by the market as sovereign issues. In order to strengthen confidence of the investors in the financial credibility of the State Governments need to restore to certain institutional arrangements such as Sinking Fund to ensure orderly repayment and servicing of bonds.

4.4 Conclusion

The public debt of State Governments in India increased both in absolute terms and in relation to GDP during the period of study. The composition of State debt shows the preponderance of Central loans in total debt. Its share, no doubt, is coming down. The share of market loans and bonds are falling while that of provident fund and small savings are raising. So the change in the composition of debt shows the shift from low cost to high interest bearing items of borrowing by State Governments. The growth rate of interest payments of State Governments exceeded the growth rate of revenue expenditure during the period of study. This raises the issue of sustainability of debt and the term structure and mix of State Governments debts. The interest payment-debt servicing ratio is also high, pointing to the fact that the burden of State Government debt comes more from interest payments than from repayment obligations. The net loan availability of State Governments is lower than that of the Central Government on account of a high debt servicing-gross loan ratio for the State Governments. Debt servicing payments of Central loans created a situation of '*reverse flow*' of funds from the States to the Centre. The State wise analysis of debt burden of Central loans also reveals the inequality

in the spread of the burden of debt, which is shouldered invariably by the low and special category States. The high interest rates and short maturity of loans to State Governments have contributed heavily towards increased burden of Central loans. Similarly market borrowings of State Governments have not been distributed consistently on the basis of any objective principle. In the context of financial sector reforms, State Governments may find it difficult to finance a part of their fiscal deficits through market borrowings.

References:

1. Thimmaiah, G. (1985), *Burning Issues in Center-State Financial Relations*, Ashish, New Delhi.
2. George, K.K. (1988), *Centre-State Financial Flows and Inter-State Disparities*, Criterion Books, Delhi.

CHAPTER 5

PUBLIC DEBT OF KERALA (1974-75 TO 1996-97)

5.1 Introduction

Public debt of State Governments and their fiscal situation are closely linked. An analysis of the public debt of Kerala is attempted to trace the two way relation between State's debt and fiscal crisis. The growth and composition of the debt receipts of the Government of Kerala from 1974-75 to 1996-97 is presented in this chapter. The various aspects of the components of States' debt such as Central loans to State Government, market borrowing of the State Government, negotiated loans and provident funds and small savings receipts of Kerala are examined to capture the entire public debt scenario of the State Government.

5.2 Growth and composition of the Outstanding Debt of the Government of Kerala: 1974-75 to 1996-97.

The outstanding debt of the Government of Kerala increased both in absolute and per capita terms during the period of study (Tables 5.1 & 5.2). The magnitude of the total debt outstanding increased from Rs. 565

crores in 1974-75 to Rs 914 crores by the end of the Fifth Five Year Plan. By the end of the Sixth Five Year Plan period (1984-85) the total debt outstanding registered a three fold rise, compared to the 1974-75 level. Thereafter, it doubled every four years. By 1996-97, the final year of the Eighth Five Year Plan, it reached a level of Rs. 11671 crores.

TABLE 5.1: COMPOSITION OF THE OUTSTANDING DEBT OF THE KERALA, 1974-75 TO 1996-1997

(Rs. Corers)

YEAR 31 ST MARCH 1	INTERNAL DEBT 2	LOANS & ADVANCES FROM THE CENTRE 3	PF and SMALL SAVINGS (etc.) 4	TOTAL DEBT 5=2+3+4
1974-75	92(16.3)	396(70.1)	77(13.6)	565(100)
1975-76	118(19.2)	409(66.5)	88(14.3)	615(100)
1976-77	131(17.2)	430(66.2)	104(16.6)	665(100)
1977-78	112(15.8)	460(66.0)	129(18.2)	710(100)
1978-79	128(15.0)	547(63.9)	181(21.1)	856(100)
1979-80	145(15.9)	604(66.1)	165(18.0)	914(100)
1980-81	167(16.5)	660(65.5)	181(18.0)	1008(100)
1981-82	275(25.3)	606(55.7)	207(19.0)	1088(100)
1982-83	251(20.0)	769(58.5)	238(19.3)	1258(100)
1983-84	353(22.0)	914(57.8)	314(19.9)	1581(100)
1984-85	520(28.0)	955(51.4)	383(20.6)	1858(100)
1985-86	374(16.7)	1382(61.8)	481(21.5)	2237(100)
1986-87	466(18.7)	1496(60.2)	526(21.1)	2488(100)
1987-88	604(21.3)	1616(55.5)	610(22.9)	2830(100)
1988-89	718(21.5)	1495(51.2)	705(24.2)	2918(100)
1989-90	928(26.5)	1654(47.2)	920(26.3)	3502(100)
1990-91	1100(24.8)	2166(48.8)	1176(26.4)	4442(100)
1991-92	1323(25.5)	2435(46.9)	1433(27.6)	5191(100)
1992-93	1554(26.3)	2721(46.1)	1630(27.6)	5905(100)
1993-94	1735(24.1)	3114(43.3)	2356(32.6)	7199(100)
1994-95	2079(23.6)	3726(42.8)	3016(32.8)	8821(100)
1995-96	2511(24.8)	4258(41.3)	3539(34.3)	10309(100)
1996-97	3004(25.7)	4815(41.3)	3852(33.0)	11671(100)

Note: Figures in brackets are percentage to total outstanding debt

Source: RBI report on Currency and Finance, various issues.

The per capita outstanding debt was only Rs 248 in 1974-75. It had been doubling every five years till 1990 and then during the seven year period ending in 1996-97, it registered a three fold rise to reach Rs. 3710. While All States average rose by 103 per cent between 1991 and 1997, the increase in the case of Kerala was 149 per cent. Kerala, which was the 8th highest indebted State in early 1990s is now third in the list¹.

**TABLE 5.2: PER CAPITA OUTSTANDING DEBT OF KERALA
1974-75 TO 1996-1997**

(Rs. percapita)				
YEAR 31 ST MARCH	INTERNAL DEBT	LOANS & ADVANCES FROM THE CENTRE	PF AND SMALL SAVINGS (etc.)	TOTAL DEBT
1	2	3	4	5=2+3+4
1974-75	40.3	173.6	33.8	247.7
1975-76	50.8	175.9	37.8	264.5
1976-77	55.3	181.6	43.9	280.8
1977-78	46.5	191.0	53.5	294.7
1978-79	52.2	223.3	73.9	349.5
1979-80	58.3	242.9	66.3	367.5
1980-81	66.2	261.6	71.7	399.5
1981-82	107.6	236.9	80.9	425.3
1982-83	96.7	296.1	91.6	484.4
1983-84	134.0	346.9	119.2	600.0
1984-85	194.5	357.3	143.3	695.1
1985-86	138.0	510.0	177.5	825.5
1986-87	169.6	544.6	191.5	905.7
1987-88	217.0	580.7	219.2	1016.9
1988-89	254.8	530.5	250.2	1035.5
1989-90	325.2	579.7	322.5	1227.5
1990-91	381.1	750.3	407.3	1538.6
1991-92	452.5	832.8	490.1	1775.3
1992-93	523.9	917.4	549.6	1990.9
1993-94	569.0	1021.3	772.4	2361.1
1994-95	672.6	1205.4	975.7	2853.8
1995-96	807.7	1369.6	1138.3	3315.9
1996-97	954.9	1530.5	1224.4	3709.8

Source: RBI, Report on Currency and Finance, various issues.

The rise in outstanding debt is marked by significant changes in the composition of debt. Central loans outstanding which contributed 70 per cent of total outstanding debt in 1974-75 declined to 41.3 per cent in 1996-97. But in the case of All States, Central loans constituted 61.3 per cent of total outstanding debt in 1996-97. The fall in the Central loan component of Kerala's debt is more pronounced and occurred much earlier than All States. The fall in the share of Central loans outstanding is matched by steady increase in the share of internal debt and provident funds. Their shares in total debt outstanding increased from 16.3 per cent in 1974-75 to 25 per cent in 1996-97. Similarly, the share of provident funds and small savings outstanding steadily increased from 13.6 per cent in 1974-75 to 33 per cent in 1996-97.

5.2.1 Outstanding Debt-SDP Ratio

The growth of the outstanding debt of Kerala when expressed in relation to State Domestic Product (SDP) makes the analysis more meaningful (Table 5.3). Between 1974-75 and 1979-80, the ratio ranged between 29 per cent and 31.8 per cent. It was only 26.4 per cent in 1980-81. But from 1985-86 onwards, the State's outstanding debt formed more than one-third of its domestic product (SDP). This rising outstanding debt/SDP ratio continued throughout the nineties and in 1996-97, it reached the all time high of 40.9 per cent.

TABLE 5.3: OUTSTANDING DEBT/SDP RATIO 1974-75 TO 1996-1997

YEAR 31 ST MARCH (1)	TOTAL DEBT (Rs Crores) (2)	% INCREASE OVER PREVIOUS YEAR (3)	SDP AT CURRENT PRICES (4) (Rs crores)	% INCREASE OVER PREVIOUS YEAR (5)	TOTAL DEBT AS % of SDP (6)
1974-75	565	-	1942.2	-	29.1
1975-76	615	8.9	2098	8.0	29.3
1976-77	665	8.1	2250.7	7.3	29.6
1977-78	710	6.8	2422.5	7.6	29.3
1978-79	856	20.6	2692.7	11.8	31.8
1979-80	914	6.8	2874.3	6.8	31.8
1980-81	1008	10.3	3823	33.0	26.4
1981-82	1088	7.9	3697	-3.3	29.4
1982-83	1258	15.6	4567	23.5	27.6
1983-84	1581	25.7	5465	19.7	28.9
1984-85	1858	17.5	6152	12.6	30.2
1985-86	2237	20.4	6503	5.7	34.4
1986-87	2488	11.2	7354	13.1	33.8
1987-88	2830	13.8	8258	12.3	34.3
1988-89	2918	3.1	9182	11.2	31.8
1989-90	3502	20	10668	16.2	32.8
1990-91	4442	26.8	12173	14.1	36.5
1991-92	5191	16.7	15102	24.1	34.4
1992-93	5905	13.8	17175	13.7	34.4
1993-94	7199	21.9	19688	14.6	36.6
1994-95	8821	22.5	22024	11.9	40.1
1995-96	10309	16.9	24819	12.7	41.5
1996-97	11671	13.2	28479	8.5	40.9
Annual average growth rate		14.9		12.9	

Note: SDP Figures: Statewise Net Domestic Product at factor cost (at current prices) from various issues of RBI, Report on Currency and Finance 1974-75 to 1996-97.

Source: RBI, Report on Currency and Finance, various issues.

All States data in this regard show that, it is now higher than that of Kerala. The estimates for March 1997 shows that outstanding debt constitutes 55 per cent of the State's domestic product in India. For States like Jammu and Kashmir, Manipur, Orissa, Nagaland and Arunachal Pradesh, at several points of time, outstanding debt exceeded or equalled their SDP. While the ratio from 1994-95 onwards stood at over 40 per

cent in Kerala, the average for the major States was well below this figure. In 1994-95, it was 30.75 per cent which increased to 32.23 per cent in 1995-96. However, by 1996-97, the 16 States average shot up to 40.16 per cent and next year further to 42.04 per cent². With regard to Kerala it remained almost at the level of 1994-95. The aggregate liabilities of the Central Government, as noted earlier, as percentage of GDP increased considerably and came upto 58.2 per cent in March 1997, a level higher than the All States' average.

5.2.2 Growth of Kerala's Public Debt and its Fiscal Crisis

Almost all State Governments in India are saddled with fiscal crisis in one form or another. But the frequency and magnitude of the crisis is much more for Kerala than for other states (Table 5.4). The magnitude of deficits, especially revenue deficits, was much larger for Kerala than for other States. In 1987-88, revenue deficits formed 10.9 per cent of the total revenue expenditure of Kerala against 2.4 per cent for All States. In 1990-91, it was 14.9 per cent for Kerala while the figure for All States was just half of it. The situation remained more or less the same in 1996-97, with Kerala having a revenue deficit of 13.5 per cent to its revenue expenditure, while the figure for All States was 9.2 per cent only.

TABLE 5.4: RATIO OF REVENUE SURPLUS/ DEFICITS TO REVENUE EXPENDITURE OF KERALA AND ALL STATES, 1974-75 TO 1996-1997

(in percentage)

YEAR	KERALA	ALL STATES
1974-75	0.1	6.5
1975-76	-1.0	13.9
1976-77	-0.8	13.8
1977-78	7.0	11.4
1978-79	9.0	10.8
1979-80	10.9	12.8
1980-81	-4.1	10.8
1981-82	12.7	8.1
1982-83	3.4	4.4
1983-84	-5.9	0.9
1984-85	-1.2	-3.3
1985-86	-5.1	2.0
1986-87	-9.2	0.1
1987-88	-10.9	-2.4
1988-89	-8.0	-3.5
1989-90	-10.9	-6.1
1990-91	-14.9	-7.4
1991-92	-11.3	-7.2
1992-93	-9.2	-5.2
1993-94	-8.6	-3.5
1994-95	-7.9	-4.8
1995-96	-6.9	-5.7
1996-97	-13.5	-9.2

Source: RBI Bulletin, various issues related to Finance of State Governments: 1974-75 to 1996-97

5.2.3 Revenue Deficit/SDP

Revenue deficit of the State Government account occurred for the first time in 1975-76 and in 1976-77. Though this situation was averted for the next three years, revenue deficit appeared again in 1980-81 and 1983-84 and worsened with the passage of time and has become a permanent feature of Kerala's budgetary operations. Revenue deficits as a percentage

of state domestic product (SDP) increased from 1.1 per cent in 1983-84 to a high of 3.5 per cent in 1990-91. It later came down and stabilised at less than 2 per cent in the early nineties. In 1996-97 it increased to 2.3 per cent of state domestic product (Table 5.5)

TABLE 5.5: REVENUE DEFICITS / SDP RATIO (KERALA)

YEAR	REVENUE DEFICIT (Rs. Crores)	SDP (Rs. Crores)	DEFICIT AS PERCENTAGE OF SDP (%)
1983-84	58	5465	1.1
1984-85	16	6152	0.3
1985-86	74	6503	1.2
1986-87	152	7354	2.1
1987-88	194	8258	2.4
1988-89	163	9182	1.8
1989-90	250	10668	2.5
1990-91	422	12173	3.5
1991-92	364	15102	2.4
1992-93	337	17175	2.0
1993-94	371	19688	1.9
1994-95	399	22024	1.8
1995-96	402	24819	1.6
1996-97	643	28479	2.3

Source: RBI Bulletin, various issues

In Kerala, the deficit has its genesis largely in the revenue account. Kerala had 17 years of revenue deficit during the 23 year period (Fifth to Eighth Plan) of study. All the years of the Seventh and Eighth Plan period witnessed revenue deficits for Kerala. During the same period All States had revenue deficits for only 11 years and the trend was visible only from 1987-88 and developed into a regular feature only thereafter. On the other hand All States had capital deficits during 12 out of 23 years against 8 years for Kerala. Thus Kerala during many years, had been carving out

surpluses in its capital account in order to finance, at least partly, its recurrent revenue deficits. All States during the same period had been utilizing their revenue surpluses to meet capital deficits. But by 1987-88, deficits of All States had also started following the Kerala pattern (See Appendix 5.1).

Kerala's mounting and recurrent revenue deficits have become increasingly a charge on the State's capital receipts. This is evident from Table 5.6. In 1986-87, revenue deficits absorbed 25.9 per cent of the capital receipts of Kerala, including loans from Centre, market borrowing and negotiated loans. The situation shows no signs of improvement. By the end of the Seventh Plan (1989-90) revenue deficit as a percentage of capital receipts increased to 30.7 per cent. This came up to 44.1% in 1990-91 and thereafter it came down and by 1995-96 it reached 25.7 per cent. The situation in 1996-97, however, shows that 55.2 per cent of the capital receipts are diverted to finance the revenue deficits of the State. It was only from 1987-88 that on a continuous basis, capital receipts have been diverted to finance the revenue deficits of All State Governments. The proportion of capital diversion to feed revenue deficit in Kerala is high when compared with the All States situation. The practice of financing revenue deficits with capital receipts naturally reduces the capacity of the State Government to incur capital expenditure, given the constraints of a State Government in raising its capital receipts. Besides,

almost all capital receipts are interest bearing. The diversion of the costly capital receipts for current consumption is therefore bound to accentuate the problem of debt servicing in future years.

TABLE 5.6: RATIO OF REVENUE SURPLUS/ DEFICITS TO TOTAL CAPITAL RECEIPTS AND RECEIPTS IN PUBLIC ACCOUNTS OF KERALA AND ALL STATES 1974-75 TO 1996-1997

(in percentage)

YEAR	TOTAL CAPITAL RECEIPTS		RECEIPTS IN PUBLIC ACCOUNTS	
	KERALA	ALL STATES	KERALA	ALL STATES
1974-75	0.3	18.2	1.2	148.8
1975-76	-3.6	32.5	-5.3	261.2
1976-77	-2.7	38.0	-13	223.2
1977-78	22.1	31.9	93.4	176.9
1978-79	25.2	22.1	106.8	133.5
1979-80	14.7	36.2	231	225.5
1980-81	-18.7	36.6	-102.6	140.6
1981-82	55.4	22.6	313.8	130.5
1982-83	12.3	12.4	45.6	60.6
1983-84	-16.0	2.3	-60.4	11.7
1984-85	-3.7	-8.5	-19.3	-48.7
1985-86	-10.3	5.0	-65.2	30.3
1986-87	-25.9	0.3	-127.8	1.6
1987-88	-29.6	-7.0	-89.8	-16.6
1988-89	-2.9	-10.6	-102.7	-25.4
1989-90	-30.7	-18.3	-116.9	-41.6
1990-91	-44.1	-21.4	-143.8	-48.8
1991-92	-33.0	-22.4	-170.5	-38.0
1992-93	-29.8	-17.0	-72.1	-30.1
1993-94	-28.2	-13.3	-77.3	-26.8
1994-95	-23.6	-14.1	-58.6	-58.5
1995-96	-25.8	-18.8	-89.4	-64.6
1996-97	-55.2	-33.2	-196.6	-157.1

Notes: Public Accounts include Small savings, Trust and Endowment Funds, Insurance and Pension Funds, Resesrve Funds, Deposits and Advances, Suspense and Miscellaneous, Remittances and Cash Balances.

Source: RBI Bulletin, various issues.

Another disturbing aspect of Kerala's fiscal crisis can be brought out by examining the ratio of revenue deficits to its Public Accounts (Table 5.6). In fact, four years during the eighties (1980-81, 1986-87, 1988-89 and 1989-90) revenue deficits exceeded net receipts into the government's Public Accounts. During three years of the nineties (1990-91, 1991-92 and 1996-97), this was repeated. The diversion of these funds for current consumption may impair the government's capacity to meet in time, its fiduciary obligations. All States data in this connection shows that revenue deficit exceeded the net receipts in the Public Accounts of State Governments only from 1987-88 onwards on a regular basis. The ratio remained low for most of the period for other States compared to Kerala, except between 1989-90 and 1992-93.

5.2.4 Gross Fiscal Deficit of Kerala

The fiscal crisis of Kerala, rooted in the revenue deficit, can be expressed in terms of Gross Fiscal Deficit (GFD) of the State (Table 5.7). Gross Fiscal Deficit (GFD) is the total additional borrowing by the Government in a given period of time. GFD was 24.9 per cent of aggregate government expenditure in 1990-91. Though there is marginal decline in this ratio, it exceeded 20 per cent during most of the years during the nineties. In 1990-91, the GFD was 6.6 per cent of State domestic product and declined marginally till 1995-96. But in 1996-97, it

**TABLE 5.7: GROSS FISCAL DEFICIT MOVEMENT OVER YEARS
(KERALA AND ALL STATES)**

(Rs. crores)

Year	Kerala				All States			
	Expend- iture	Surplus(+)/ Deficit(-)	(2) as % of (1)	(2) as % of SDP	Expend- iture	Surplus(+)/ Deficit(-)	(6) as % of (5)	(6) as % of SDP
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1990-91	3201.4	-798.5	-24.9	-6.6	8523.7	-18786.9	-22.0	-4.8
1991-92	3655.5	-803.4	-22.0	-5.3	99935.8	-18900.1	-18.9	-4.6
1992-93	4050.7	-732.0	-18.1	-4.3	11982.4	-20891.3	-18.7	-4.1
1993-94	4857.3	-935.2	-19.3	-4.8	126159. 7	-20596.7	-16.3	-3.4
1994-95	5575.1	-1108.7	-19.9	-5.0	149980. 3	-27696.6	-18.5	-4.0
1995-96	6726.3	-1302.7	-19.4	-5.2	168229. 2	-31425.8	-18.7	NA
1996-97	8490.4	-1944	-23.9	-7.1	199059. 8	-41844.6	-21.0	NA

Note: GFD is the difference between aggregate disbursements net of debt repayments and recovery of loans, revenue receipts and non-debt capital receipts.

Source: R.B.I. Bulletin, various issues

was 7.1 per cent of SDP. The Gross Fiscal Deficits of Kerala in relation to expenditure were always larger than those for All States during the nineties. Even though international financial institutions stipulate 3 per cent as the ideal level of GFD, it is considered too low a figure for developing countries. The Central Government's GFD runs currently at around 5-6 per cent and the combined deficit of Central and State Governments stands at 9-10 per cent of GDP³. In 1995-96, Kerala became the fourth in the list of States with the highest GFD. However, in 1996-97, the GFD of Kerala fell below the All States average though it still ranked sixth in the list. But Kerala has the highest GFD among all the southern States⁴. The quantum jump in the GFD of Kerala in the past has resulted in the growing debt of the Government in the form of loans and other capital receipts. Thus the growth of the public debt of Kerala is

closely linked to the fiscal crisis of the State manifested in the form of growing Gross Fiscal Deficit (GFD).

5.2.5 Uses of Gross Fiscal Deficits

The decomposition of Gross Fiscal Deficit (GFD) shows how the borrowed funds are utilised by the Government. It is used to meet revenue deficits, capital outlay and net lending. But the striking aspect of Kerala's fiscal deficit is that an increasing proportion goes for financing revenue deficit (Table 5.8). In 1990-91, 52.8 per cent of GFD was

TABLE 5.8:USES OF GROSS FISCAL DEFICITS (KERALA AND ALL STATES)

(Rs. Crores)

YEAR	KERALA				ALL STATES			
	REVE- -NUE DEFI- CIT	CAPI- TAL OUT- LAY	NET LENDING	GFD	REV- ENUE DEFI- CIT	CAPI- TAL OUT- LAY	NET LEND- ING	GFD
1990-91	422 (52.8)	256 (32.0)	121 (15.1)	799 (100)	5309 (28.3)	9223 (49.1)	4255 (22.6)	18787 (100)
1991-92	364 (45.3)	286 (35.60)	153 (19.0)	803 (100)	5651 (29.9)	10096 (53.4)	3153 (16.7)	18900 (100)
1992-93	337 (46.0)	278 (38.0)	117 (16.0)	732 (100)	5114 (24.5)	10655 (51.0)	5123 (24.5)	20892 (100)
1993-94	371 (39.7)	363 (38.8)	201 (21.4)	935 (100)	3813 (18.5)	12450 (60.4)	4333 (21.0)	20596 (100)
1994-95	400 (36.1)	466 (40.1)	262 (23.7)	1109 (100)	6156 (22.2)	17351 (62.6)	4180 (15.1)	27697 (100)
1995-96	402 (30.9)	564 (43.3)	337 (25.9)	1303 (100)	8201 (26.1)	18496 (58.9)	4731 (15.1)	31426 (100)
1996-97	643 (33.1)	623 (32.1)	678 (34.8)	1944 (100)	11466 (27.4)	21341 (51.2)	9038 (22.2)	41845 (100)

Note: Figures in brackets are % to total

Source: RBI Bulletin, various issues.

utilised for meeting the revenue deficits. This increased to 39.7 per cent in 1993-94. Thereafter it declined and in 1996-97 revenue deficit formed only 33.1 per cent of GFD. The average for All States was only 28.3 per cent in 1990-91 but declined to 18.5 per cent in 1993-94. In 1996-97, revenue deficit of All States increased and formed only 27.4 per cent. The increase in revenue deficit component of GFD reduces the availability of borrowed funds for capital outlay and for advancing loans. Using loans to finance revenue expenditure has wide ramifications. It adds to the interest liability, which once again increases the revenue deficits. This develops into a typical debt trap scenario.

5.2.6 Larger Revenue Component of Expenditure

As noted earlier, the origin of Kerala's fiscal crisis lies in its revenue account. This is partially due to the predominance of revenue expenditure in total expenditure (Table 5.9). The share of revenue expenditure was higher for Kerala than for All States during the period of study. The revenue component of the non plan expenditure was considerably higher than that of plan expenditure during all years, both for Kerala and for All States. Similarly the revenue expenditure in plan expenditure of Kerala was higher than that of All States except for six years in the twenty three year period of study. Further examination of

expenditure shows that in the case of Kerala, the revenue content of developmental expenditure was larger than for All States. One of the reasons for the higher revenue content of Kerala's development expenditure is the dominance of social and community services over economic services in total expenditure. But, the revenue content of its expenditure on economic services too is higher than that of All States (George 1994)⁴.

TABLE 5.9: SHARE OF REVENUE EXPENDITURE IN TOTAL EXPENDITURE

(In percentage)

YEAR	NON-PLAN		PLAN		TOTAL	
	KERALA	ALL STATES	KERALA	ALL STATES	KERALA	ALL STATES
1974-75	85.0	84.6	34.1	29.5	76.4	70.3
1975-76	85.6	81.9	30.0	31.2	76.5	67.9
1976-77	83.9	84.3	41.4	33.0	74.4	67.5
1977-78	90.1	85.3	39.0	31.7	75.6	67.5
1978-79	89.1	84.7	45.1	35.5	76.8	67.1
1979-80	88.9	85.2	36.0	33.6	75.2	67.6
1980-81	92.9	81.6	46.0	37.8	78.0	67.0
1981-82	79.4	84.2	42.9	38.2	69.5	68.8
1982-83	91.3	86.5	44.4	41.0	78.6	71.2
1983-84	90.6	85.4	44.8	44.9	75.5	71.5
1984-85	81.9	82.1	48.2	48.4	72.4	71.6
1985-86	82.5	85.0	43.6	46.6	73.4	73.0
1986-87	88.1	86.7	41.2	48.5	76.5	73.6
1987-88	88.3	88.7	49.1	50.6	79.1	75.3
1988-89	89.3	90.0	56.1	53.2	81.8	77.9
1989-90	89.5	90.6	47.0	50.5	79.5	78.4
1990-91	93.0	90.2	51.6	52.4	83.7	78.8
1991-92	88.1	91.4	50.0	51.3	80.3	79.9
1992-93	90.3	90.9	58.9	54.2	83.4	80.6
1993-94	92.4	91.6	53.7	53.7	83.6	81.2
1994-95	94.8	92.5	53.8	49.7	85.0	79.5
1995-96	93.3	92.8	55.3	51.9	84.2	81.7
1996-97	94.7	93.3	60.4	56.4	85.8	82.7

Source: R.B.I. Bulletin(s); various issues

5.2.7 Pattern of Plan Financing of Kerala: Sixth to Eighth FYP (1980-1997)

The sources of finance for the State's plan consist of the State's own budgetary resources, Central assistance, market borrowings and funding by institutional agencies. From the Sixth FYP (1980-85) onwards the importance of the State's own resources in financing the Plans steadily declined (Table 5.10). From 71.4 per cent in Sixth FYP, it came down to 53.2 per cent in the Seventh FYP. In the two Annual Plans that followed, it was only 42.9 and 38.6 per cent. The share of revenue surplus in financing Kerala's Public Sector Plan outlay, which was 15.3 per cent of the State's own resources in the Sixth FYP, turned into revenue deficits, from the Seventh FYP onwards. The amount came upto Rs. 1031 crores and formed 75.2 per cent of the State own resources. The situation further deteriorated during the Annual Plans (1990-92). In the Eighth FYP, the revenue deficit constituted 50 per cent of total resources and 178 per cent of the State's own resources, which amounted to Rs. 2743 crores. So the surplus from current revenue for financing FYPs was negative for Kerala since the Seventh FYP. This among other things, compelled the State to go in for borrowing to finance its public sector Plan outlay.

TABLE 5.10: PATTERN OF PLAN FINANCING OF KERALA VITH TO VIIITH FYP (1980-1997)
(Rs. Crores)

MODE OF FINANCING		VI th PLAN 1980-85	VII th PLAN 1985-90	A.P. 1990-91	A.P. 1991-92	VIII th PLAN 1992-97
1.	Balance from current revenues	186.9 (10.9)	-1030.8 (-40)	-403.3 (-65)	-327.7 (-40.6)	-2743 (-50.2)
2.	Contribution of Public enterprises	-113.7 (-0.7)	-170.8 (-6.7)	-24.8 (-)	-33.4 (-1.4)	550 (10.1)
3.	Loans from the market by state government	122.03 (7.1)	497.7 (19.3)	152.0 (24.5)	194.5 (24.1)	972.0 (17.8)
4.	Share of Small Savings	73.5 (4.3)	352.6 (13.7)	154.0 (24.8)	188.4 (23.4)	976.8 (17.9)
5.	State PFs etc	256.7 (15)	307.5 (12)	201.1 (32.4)	140.0 (17.4)	1461 (26.8)
6.	Miscellaneous capital receipts	-108.9 (-6.4)	-460.9 (-17.9)	-60.6 (-9.8)	-106.4 (-13.2)	-544.6 (-10)
7.	Adl. Resource Mobilization	364 (21.3)	1313.2 (51)	131 (21.1)	164.77 (20.4)	1841.1 (33.7)
8.	Negotiated Loans	82 (4.8)	312.2 (12.1)	62.9 (10.1)	70.5 (8.7)	500 (9.2)
9.	Market Borrowing by KSEB & Others	81.5 (4.8)	95.8 (3.7)	21.3 (3.4)	21.3 (2.6)	-
10.	Withdrawal from cash balances	275.9 (16.1)	143.2 (5.6)	32.7 (5.3)	-	-
11	Total State's own resources (1 to 10)	1220.8 (71.4)	1369.2 (53.2)	266.2 (42.9)	311.9 (38.7)	1541.4 (28.2)
12	Central Assistance.	488.3 (28.6)	1204.6 (26.8)	298.1 (48.1)	495.1 (61.3)	3918 (71.8)
	TOTAL RESOURCES (11+12)	1709.1 (100)	2573.8 (100)	620.01 (100)	807.0 (100)	5460 (100)

Source: Kerala State Planning Board.

5.3 Growth of Debt Receipts of the Government of Kerala: 1974-75 to 1996-97

On the basis of the recommendations of the Second Report of the Team on Reforms in the Structure of Budgets and Accounts, constituted by the Government of India in 1969, the State's public debt has been reclassified into three major heads from 1974-75 onwards.

- a) Internal Debt consisting of 'Market loans', loans from financial institutions and compensation and other bonds.
- b) 'Loans and advances from the Centre' given for plan as well as for non-plan purposes and
- c) 'Provident funds (etc)' account for state provident funds, small savings receipts, trusts and endowments, insurance and pension funds.

In absolute terms, total annual debt receipts of the government of Kerala increased from Rs. 82.9 crores in 1974-75 to Rs. 1749 crores in 1996-97, registering an annual average growth rate of 20.5 per cent (Table 5.11). Between 1974-75 and 1979-80, the total debt receipts increased from Rs 83 crores to Rs 114 crores. But during 1975-76 and 1979-80 it recorded 13.9 and 20.9 per cent decline. All the years during the Sixth Plan period (1980-85) showed an increasing trend in the debt receipts of the State. In 1984-85, debt receipts increased to Rs 341 crores, showing a three fold increase within a period of 5 years. Except for 1986-87, the same trend prevailed during the Seventh Plan period (1985-90). By 1989-90, total debt receipts increased to Rs. 801 crores — having more than doubled in five years. During the nineties also except for 1992-93 and 1995-96, total debt receipts of the State Government showed an increasing trend. In 1996-97, it reached Rs.1749 crores. So far, during the 23 year

period of study, only 5 years have recorded a decline in the growth of the debt receipts, of the Government of Kerala.

TABLE 5.11: GROWTH AND COMPOSITION OF THE DEBT RECEIPTS OF THE GOVERNMENT OF KERALA, 1974-75 TO 1996-97.

(Rs crores)

YEAR 1	IDEBT 2	LACG 3	PF AND SMALL SAVINGS (ETC) 4	TOTAL DEBT 5
1974-75	13 (15.49)	48.8 (58.88)	21.3 (25.63)	82.9 (100)
1975-76	11 (15.90)	48.5 (67.97)	11.5 (16.13)	71.4 (100)
1976-77	14 (13.89)	68.8 (69.58)	16.4 (16.53)	98.9 (100)
1977-78	16 (14.53)	69.4 (63.31)	24.3 (22.16)	109.6 (100)
1978-79	21 (11.29)	71.0 (60.07)	52.4 (28.64)	144 (100)
1979-80	23 (20.19)	73.4 (64.45)	17.5 (15.36)	113.9 (100)
1980-81	28 (23.72)	74.8 (62.80)	16.1 (13.48)	119.1 (100)
1981-82	36 (21.37)	93.5 (56.07)	37.6 (22.56)	166.7 (100)
1982-83	40 (18.93)	108.5 (51.56)	62.1 (29.51)	210.4 (100)
1983-84	47 (14.63)	199.7 (62.75)	72.0 (22.62)	318.2 (100)
1984-85	59 (17.38)	213.0 (62.42)	68.9 (20.20)	341.2 (100)
1985-86	94 (14.95)	425.8 (67.80)	108.3 (17.25)	627.9 (100)
1986-87	104 (22.65)	284.8 (61.88)	71.2 (15.47)	460.2 (100)
1987-88	122 (22.95)	301.6 (56.58)	109.1 (20.47)	533 (100)
1988-89	162 (26.52)	289.2 (47.35)	159.6 (26.13)	610.8 (100)
1989-90	237 (29.61)	349.3 (43.62)	214.4 (26.77)	800.8 (100)
1990-91	194 (21.62)	408.4 (45.61)	293.5 (32.77)	895.5 (100)
1991-92	231 (21.73)	575.0 (54.09)	257.0 (24.18)	1063 (100)
1992-93	296 (28.51)	529.6 (50.94)	213.6 (20.55)	1040 (100)
1993-94	271 (20.31)	595.9 (44.64)	467.8 (35.05)	1335 (100)
1994-95	377 (21.03)	749.4 (41.82)	665.7 (37.15)	1792 (100)
1995-96	428 (29.36)	655.5 (44.5)	373.5 (25.64)	1457 (100)
1996-97	543 (31.01)	742.7 (42.47)	462.6 (26.45)	1749 (100)

Note:

1. Figures in brackets are percentage to total
2. IDEBT = Internal Debt includes market loans and loans from other institutions
3. LACG = Loans and Advances from Centre
4. PF etc = State Provident Funds and Small savings, Deposits, Trust and Endowments, Insurance Funds and Pension funds

Source: RBI Bulletins; Issues related to "Finances of State Governments", 1974-75 to 1996-97.

The increase in per capita debt receipts of Kerala shown in Table 5.12 can also bring out the magnitude of the growth of public debt of the State Government. Per capita debt receipts of Kerala which was Rs. 36.4 in 1974-75 increased to Rs. 46 in 1979-80. During the Sixth Plan period

(1980-85) per capita debt receipts recorded a threefold increase and came up to Rs. 128. In the next five year period ending in 1989-90, the per capita debt receipts more than doubled and came upto Rs.281. During the nineties, per capita debt steadily increased and reached the all time high of Rs. 588 in 1994-95 and in 1996-97, it was estimated at Rs. 556. An analysis of the total debt receipts of Kerala reveals that both the absolute amount and per capita debt receipts are rising fast.

TABLE 5.12: PER CAPITA DEBT RECEIPTS OF KERALA , 1974-75 TO 1996-97
(Rs. per capita)

YEAR 1	IDEBT 2	LACG 3	PF AND SMALL SAVINGS (ETC) 4	TOTAL DEBT 5
1974-75	5.63	21.40	9.32	36.35
1975-76	4.88	20.86	4.95	30.70
1976-77	5.80	29.07	6.90	41.77
1977-78	6.61	28.81	10.08	45.50
1978-79	8.43	44.88	21.40	58.82
1979-80	9.25	29.52	7.03	45.80
1980-81	11.2	29.66	6.36	47.22
1981-82	13.93	36.55	14.71	65.18
1982-83	15.33	41.77	23.90	81.00
1983-84	17.67	75.78	27.33	120.77
1984-85	22.19	79.68	25.78	127.65
1985-86	34.63	157.11	39.97	231.71
1986-87	37.94	103.67	25.92	167.53
1987-88	43.96	108.36	39.21	191.53
1988-89	57.48	102.62	56.63	216.73
1989-90	83.11	122.44	75.14	280.68
1990-91	67.07	141.47	101.65	310.18
1991-92	78.99	196.66	87.90	363.55
1992-93	99.91	178.54	72.02	350.48
1993-94	90.18	198.15	155.58	443.91
1994-95	123.61	245.79	218.34	587.75
1995-96	137.55	210.82	120.14	468.51
1996-97	172.74	236.07	147.04	555.85

Note: Population used for working out the per capita figures are estimated mid-year population, from RBI Report on Currency & Finance , various issue.

Source: Based on Table 5.11

The rate of growth of internal debt and other liabilities of the Central Government, as noted earlier, during 1980s was only 19.5 and 17 per cents respectively. Similarly, All States data on outstanding public debt, show that the growth rate was only 10.2 per cent in the 1970s. But the eighties and the first half of the nineties registered an annual average growth rate of 14.7 and 14.2 per cents. So a comparison of the rates of growth of debt of the Central and State Governments reveals that Kerala's debt receipts are growing at a comparatively higher rate.

5.4 Composition of the debt receipts of the Government of Kerala: 1974-75 to 1996-97.

5.4.1 Internal Debt.

Internal debt receipts comprise mainly of market borrowings of the State Government, loans taken by the State Government from autonomous agencies like Life Insurance Corporation, SBI and other Banks, National Agricultural Credit Fund of RBI, National Co-operative Development Corporation, and Land compensation and other Bonds.

Internal debt receipts of the Government of Kerala increased during the period of this study. It has been steadily rising from Rs 13 crores in 1974-75 to Rs 237 crores in 1989-90. But during 1990-91 and 1993-94 there was 18.3 and 8.5 percentage fall in internal debt receipts.

Thereafter it started rising and in 1996-97 it remain at Rs. 543 crores. During the 23 year period, internal debt registered an annual average growth rate of 20.5 per cent (Table 5.11). With the steady increase in the magnitude of internal debt receipts, except for two years (1990-91 and 1993-94), its percentage contribution to total debt receipts of Kerala also increased. Between 1974-75 and 1979-80, (Fifth Plan period) the share of internal debt receipts increased from 15.5 per cent to 20.2 per cent. But in the Sixth Plan (1980-85) its share marginally declined and came down to 17.4 per cent. This trend was completely reversed in the Seventh Plan period (1985-90) and the proportion of internal debt receipt in total debt receipts of the State rose to 29.6 per cent. During the early years of the nineties there was decline in the share, but in 1995-96 it came up to 29.4 per cent again. In the final year of the Eighth Plan, 1996-97, it reached 31 per cent, the highest percentage share for internal debt in the 23 year period of the study. Similarly per capita internal debt of the Government of Kerala as shown in Table 5.10 also increased in the same period. It was Rs. 6 in 1974-75 and by 1979-80, it increased to Rs. 9. Between 1980-81 and 1984-85, it doubled to Rs. 22. In the next 5 year period ending in 1989-90, per capita internal debt registered a four fold growth and came up to Rs. 83. During the nineties, there were fluctuations in this growth and in 1996-97 it reached Rs. 173.

5.4.2 Provident Fund and Small Savings

The debt item Provident funds (etc) comprises mainly of the balances at the credit of government servants and aided school employees in funds, such as state provident funds, Insurance funds, pension funds and the balances in the savings deposits in treasuries. Provident fund and other debt receipts during the period of study registered an annual average growth rate of 27.4 per cent. The rate of growth of this component of debt receipts far exceeded the growth rate of internal debt receipts and Central loans. The growth of these receipts was marked by wide fluctuations throughout the 23 year period of study. In 1974-75, provident fund and other similar debt receipts amounted to Rs. 21.3 crores. It declined to Rs. 11.5 crores and Rs. 16.4 crores in the next two years. In 1977-78 and 1978-79, it came up to Rs. 24.3 crores and Rs. 52.4 crores respectively. In 1979-80, it came down to Rs. 17.5 crores. The same trend was witnessed during the Sixth FYP (1980-85). In 1980-81, it was only Rs. 160 crores. But it gradually increased till 1983-84 to decline in the next year. The Seventh Plan period (1985-90) saw substantial increase in the provident fund and other debt receipts of the State. By 1989-90, it had come up to Rs. 214.4 crores, a near doubling in a five year period. During the nineties, growth of this debt receipt was marked by wide fluctuations. In 1991-92, 1992-93 and 1995-96, it actually declined by 12.4, 16.9 and 43.9 per cent respectively. The year

1993-94 recorded the second highest growth rate of 119 per cent for provident funds and other receipts.

In per capita terms, provident funds and other debt receipts increased gradually during the period of study. But this increase was not continuous. In 1974-75, it was only Rs. 9, but by the end of 1978-79 it reached Rs. 21, to fall in the next year to a low of Rs. 7. But during the eighties, the trend was clear and by 1989-90, it reached a high of Rs. 75, nearly 10 fold increase in a decade. During the nineties also per capita debt receipts of provident fund and other receipts increased except for three years, and reached the high of Rs. 218 in 1994-95. In 1996-97, it was estimated as Rs. 147.

As a proportion of Kerala's total debt receipts, provident funds and other debt receipts constituted nearly one fourth. During the 23 year period of study, in 13 years it dipped below this level, and in the other 10 years it exceeded the level. Though the fast growth of this debt item is an All States phenomenon, the growth rate of the same debt item in Kerala, exceeded the All States level.

A further disaggregation of the data into provident funds and small saving receipts of Kerala and All States (Table 5.13) reveals some distinct aspects of this debt item of Kerala. In Kerala, State provident funds which

TABLE 5.13: GROWTH OF STATE PROVIDENT FUNDS AND SMALL SAVINGS - KERALA AND ALL STATES: 1974-75 TO 1996-97
(Rs. Crores)

YEAR	KERALA			ALL STATES		
	STATE PROVIDENT FUND 2	SMALL SAVINGS* 3	TOTAL 4=2+3	STATE PROVIDENT FUND 5	SMALL SAVINGS* 6	TOTAL 7=5+6
1974-75	13 (62.2)	8 (37.8)	21 (100)	125 (87.0)	19 (13.0)	144 (100)
1975-76	5 (39.2)	7 (60.8)	12(100)	132 (88.2)	18 (11.7)	150 (100)
1976-77	9 (51.9)	8 (48.1)	17(100)	176 (87.9)	24 (12.0)	200 (100)
1977-78	12 (48.3)	13 (51.7)	25(100)	209 (85.5)	36 (14.5)	245 (100)
1978-79	15 (28.6)	34 (65.6)	49(100)	222 (75.4)	73 (24.6)	295 (100)
1979-80	16 (93.6)	1 (6.4)	17(100)	282 (87.7)	40 (12.3)	322 (100)
1980-81	17 (108.2)	-1 (-8.2)	16(100)	284 (88.8)	59 (17.2)	343 (100)
1981-82	22 (58.6)	16 (41.4)	38(100)	374 (81.1)	87 (18.9)	461 (100)
1982-83	31 (50.3)	31 (49.7)	62(100)	593 (81.2)	137 (18.8)	730 (100)
1983-84	41 (56.9)	31 (43.1)	72(100)	653 (81.9)	144 (18.1)	797 (100)
1984-85	39 (56.6)	30 (43.4)	69(100)	783 (83.9)	149 (16.0)	932 (100)
1985-86	71 (65.3)	38 (34.7)	109(100)	753 (77.5)	218 (22.5)	971 (100)
1986-87	55 (77.5)	16 (22.5)	71(100)	816 (78.3)	226 (21.7)	1042 (100)
1987-88	54 (49.6)	55 (50.4)	109(100)	1295 (79.6)	333(20.5)	1628 (100)
1988-89	93 (58.3)	67 (41.7)	160(100)	1631 (81.5)	370 (18.5)	2001 (100)
1989-90	108 (50.5)	106 (49.5)	214(100)	1889 (81.8)	418 (18.1)	2307 (100)
1990-91	202 (68.7)	92 (31.3)	294(100)	2489(81.1)	582 (18.9)	3071 (100)
1991-92	143 (55.6)	114 (44.4)	257(100)	2355(80.9)	555 (19.1)	2910 (100)
1992-93	67 (31.4)	147 (68.6)	214(100)	2990 (82.5)	632 (17.5)	3622 (100)
1993-94	323 (69.1)	145 (30.9)	468(100)	3649 (84.3)	681 (15.7)	4330 (100)
1994-95	345 (51.8)	321 (48.2)	666(100)	3787 (79.2)	992 (20.8)	4779 (100)
1995-96	288 (76.9)	86 (23.0)	374(100)	4201 (85.7)	701 (14.3)	4902 (100)
1996-97	313 (67.6)	150 (32.4)	463(100)	4468 (82.9)	923 (17.1)	5391 (100)
Annual average growth rate (%)	33.1	-36.6	27.4	18.8	23.9	18.9

Note: Figures in the brackets are percentage to total

* This head includes State insurance and pension funds and Trust and Endowments.

Source: RBI Bulletins; various issues.

constituted 62.2 per cent of total in 1974-75, increased to 67.6 per cent in 1996-97. But at the All States' level, share of provident funds declined from 87 per cent in 1974-75 to 82.9 per cent in 1996-97. Similarly, the growth rate of State provident funds in Kerala at 33.1 per cent per annum exceeded the All States' growth rate of 18.8 per cent.

5.4.3 Loans & Advances from Central Government (LACG)

As seen in the case of other States Central loans constitute the major component of Kerala's debt receipts. Central loans to the Government of Kerala in absolute terms, increased during the 23 year period of study. But it was marked by fluctuating trends. Between 1974-75 and 1979-80, Central loans to Kerala, increased from Rs. 49 crores to Rs. 73 crores. In the Sixth Plan period (1980-85) Central loans receipts reached Rs. 213 crores. During the Seventh Plan period (1985-90) Central loan receipts fluctuated widely between Rs. 426 crores in 1985-86 and Rs. 285 crores in 1986-87. The period of the Annual and Eighth Five Year Plan period, (1990-97) saw minor variations in the amount of Central loan receipts of Kerala. In 1990-91, it was Rs. 408 crores and by 1996-97, it reached Rs. 743 crores. The annual average growth rate of Central loans during the 23 year period was only 16.6 per cent, less than the growth rate for internal debt and provident fund (etc). The percentage share of Central loan receipts too has shown wide variations.

Kerala, like other States, is also dependent on the Centre for the mobilization of its debt receipts or capital receipts. Central loans receipts as a percentage of total State debt receipts were at their peak levels during the Fifth Plan period (1974-79). It was 58.9 per cent in 1974-75 and in 1976-77 it reached 69.6 per cent, the highest level in the 23 years period of the study. Thereafter, it declined and came down to 64.5 per cent in 1979-80. In the Sixth Plan period, (1980-85) this proportion marginally declined and was 62.4 per cent in 1984-85. In 1985-86, it rose to 67.8 per cent to decline in the following four years consecutively and by the end of Seventh Plan (1989-90), the proportion of Central loans in the State debt was as low as 43.6 per cent. In the nineties, the first four years marked some increase in this proportion. But in 1994-95, the share of Central loans declined to 41.8 per cent, lower than the 1989-90 level. The situation remained the same at the end of the Eighth Plan period (1996-97) and Central loan receipts stagnated at 42.5 per cent of Kerala's total debt receipts.

Per capita Central loan receipts during the period also increased (Table 5.12), though there were fluctuations. In 1974-75, it was only Rs. 21, but by the end of the Fifth FYP (1978-79), it more than doubled to Rs. 45. The early years of the eighties saw a decline in the per capita Central loans to the State. It was only Rs.30 in 1979-80. In 1981-82, it rose to

Rs. 37. But by 1984-85, it nearly doubled to Rs.80 from the 1978-79 level. During the Seventh Plan period (1985-90), per capita Central loans to the State fluctuated between a high of Rs. 157 in 1985-86 and low of Rs.103 in 1988-89. During the nineties, though the Central loan receipts as a per centage of the States' total debt receipts were falling, the percapita Central loans had been rising, though marked by fluctuations. In 1992-93, the per capita Central loan receipts declined to Rs.179 from the previous year's level of Rs. 197. It rose to Rs. 246 in 1994-95 and in the final year of the Eighth Plan (1996-97) it reached the level of Rs. 236.

Central loans to State Governments which formed 74.1 per cent of the total outstanding debt of All States in 1974-75, declined to 61.3 per cent in 1996-97 and still forms the single largest component of State debt in India. But for Kerala, the internal debt receipts and small savings and provident fund receipts formed 57.5 per cent of its total debt receipts. In other words, though Central loans, forms the single largest item of debt receipts, Kerala's debt mobilization effort depends more on the State's internal debt receipts and provident fund and small savings receipts. These are costly items of borrowing and consequently the burden of State public debt will be higher for Kerala.

5.5 Relative Importance of Central Loans in Transfer of Resources from the Centre to Kerala.

The declining share of Central loans in total transfers noted in Chapter 3 is also reflected in the case of Kerala (Table 5.14). Expressed as a percentage of total transfers, Central loans to Kerala remained almost

TABLE 5.14: TOTAL TRANSFER OF RESOURCES FROM CENTRE TO KERALA AND THE RELATIVE IMPORTANCE OF CENTRAL LOANS 1974-75 TO 1996-97

(Rs. Crores)

YEAR	SHARED TAXES	CENTRAL GRANTS	CENTRAL LOANS	TOTAL TRANSFER	CENTRAL LOAN AS PERCENTAGE OF TOTAL TRANSFER
1	2	3	4	5	6
1974-75	47.1	62.1	48.8	158.1	30.7
1975-76	61.7	67.3	48.5	177.5	27.3
1976-77	65.0	66.9	68.8	200.7	34.3
1977-78	69.1	81.9	69.4	220.3	31.5
1978-79	75.2	100.7	71.0	246.9	28.8
1979-80	136.7	42.2	73.4	252.2	29.1
1980-81	151.4	52.4	74.8	278.6	26.9
1981-82	170.8	73.2	93.5	337.5	27.7
1982-83	185.9	69.5	108.5	363.9	29.8
1983-84	209.5	119.7	199.7	528.9	37.8
1984-85	233.3	136.6	213	582.9	36.5
1985-86	208.5	290.5	425.8	924.7	46.0
1986-87	339.2	185.6	284.8	809.6	35.2
1987-88	289.3	183	301.6	773.9	39.0
1988-89	436.8	213.4	289.2	939.4	30.8
1989-90	455.9	184.8	349.3	990.0	35.3
1990-91	486.3	367.5	408.4	1262.2	32.4
1991-92	576.4	367.0	575.0	1518.5	37.9
1992-93	687.0	204.8	529.6	1421.3	37.3
1993-94	751.2	502.8	595.9	1849.8	32.2
1994-95	838.4	632.6	749.4	2220.4	33.8
1995-96	1037.0	468.4	655.5	2160.8	30.3
1996-97	1218.0	746.9	742.7	2707.3	27.4

- Note
1. Shared Taxes = Income Tax, Estate duty, Union Excise duty
 2. Central Grants (a) State plan schemes, (b) Central plan schemes, (c) Centrally sponsored schemes, (d) Special plan schemes Non-Plan Grants = (a) Statutory grants, (b) Grants for natural calamity, (c) Non-plan non-statutory grants.
 3. Central Loans = (a) plan loans, (b) non-plan loans.

Source: RBI Bulletins; Finance of State Governments, various issues.

stagnant during the 23 year period of study. The Seventh FYP period was an exception in the sense that it was during this period that Central loans in total transfers to Kerala, marginally increased. Plan wise, analysis shows that during the Fifth FYP period (1974-75) Central loans to Kerala formed 30.6 per cent of total fiscal transfers from the Centre. It was only 29.1 per cent during the Annual Plan Period of 1979-80. During the Sixth FYP period (1980-85), it marginally rose to 31.7 per cent. The Seventh FYP period (1985-90) witnessed, the highest share of 37.3 per cent of Central loans in total fiscal transfers to Kerala. Thereafter, loans from the Centre as a proportion of total transfers to Kerala declined steadily. In the Annual Plan period (1990-92), this share came down to 35.1 per cent. By the end of the Eighth FYP period (1992-97), Central loans in total resource transfers had come down to 31.8 per cent. This is almost equal to the share that prevailed during the Fifth FYP period. Thus during the 23 year period of study, Central loans constituted nearly one-third of the total fiscal transfers to Kerala. In the 1990's the share of Central loans in total transfers showed decline.

5.5.1 Net Central Loan Receipts of Kerala

Table 5.15 details the various aspects of Central loan receipts of the Government of Kerala between 1974-75 and 1996-97. Net loan from Centre to the State is calculated by deducting the sum of repayment and

TABLE 5.15: CENTRAL LOANS TO KERALA AND ALL STATES: 1974-75 TO 1996-97

YEAR	KERALA					ALL STATES				
	1	2	3	4	5	6	7	8	9	10
	GROSS LOANS	NET LOANS	TOTAL CAPITAL RECEIPTS	TOTAL DEBT RECEIPTS	GROSS LOANS AS % OF CAPITAL RECEIPTS	GROSS LOANS AS % OF DEBT RECEIPTS	PER CAPITA LOAN RECEIPTS (Rs.)	TOTAL CAPITAL RECEIPTS	GROSS LOANS	GROSS LOANS AS % OF TOTAL CAPITAL RECEIPTS
1974-75	48.82	13.21	100.64	82.91	48.51	58.88	21.40	217.13	1075.18	49.5
1975-76	48.51	-6.44	96.49	71.37	50.27	67.97	20.86	2593.77	1294.30	49.9
1976-77	68.82	1.07	122.63	98.91	56.12	69.58	29.06	283.31	1446.16	50.2
1977-78	69.40	17.76	131.43	109.62	52.80	63.31	28.81	3433.84	1989.98	58.0
1978-79	109.90	55.24	170.45	182.95	64.48	60.07	44.88	5141.48	3229.69	63.0
1979-80	73.41	32.09	139.08	113.90	52.78	64.45	29.52	4272.34	2668.53	62.5
1980-81	74.82	34.09	145.78	119.14	51.32	62.80	29.66	5579.32	3021.85	54.2
1981-82	93.48	-80.75	173.21	166.73	53.97	56.07	36.54	6095.97	3372.47	55.3
1982-83	108.47	46.55	217.08	210.36	49.97	51.56	41.77	7150.91	4165.40	58.2
1983-84	199.68	99.82	364.64	318.24	54.76	62.75	75.78	9093.05	4902.57	53.9
1984-85	212.98	-12.96	369.59	341.22	57.63	62.45	79.68	10882.38	5909.68	54.3
1985-86	425.77	136.70	718.08	627.94	59.29	67.80	157.11	13133.08	8368.28	63.7
1986-87	284.78	9.16	488.13	460.20	58.34	61.88	103.67	30302.71	7702.77	25.4
1987-88	301.57	11.26	658.54	533.04	45.79	56.58	108.36	15585.21	9034.20	58.0
1988-89	289.18	-5.22	576.97	610.75	50.12	47.35	102.62	17052.51	9936.66	58.0
1989-90	34931	16.92	816.87	800.77	42.76	43.62	122.44	20113.65	11258.64	58.2
1990-91	408.42	131.51	957.10	895.50	42.67	45.61	141.47	24846.75	13974.29	56.0
1991-92	575.03	37.96	1105.00	1063.02	52.04	54.09	196.66	27953.97	13069.01	56.2
1992-93	529.55	401.81	1134.10	1039.51	46.69	50.94	178.54	30072.91	13099.61	43.6
1993-94	595.85	365.02	1315.69	1334.83	45.29	44.64	198.15	28623.10	14409.73	50.3
1994-95	749.42	281.13	1691.90	1792.05	44.29	41.82	245.79	43737.84	19252.48	44.0
1995-96	655.45	94.13	1563.30	1456.61	41.93	45.00	210.82	39328.98	21017.73	53.4
1996-97	742.69	8269	1824.09	1748.70	40.72	42.47	236.07	42734.72	23122.07	54.1

Note 1. Net loans = Gross loans minus the sum of repayment and interest payments on Central loans

2. Debt Receipts include internal debt, LACG and PF and small Savings etc.

3. Total Capital Receipts = Internal debt + LACG + Recovery of loans and advances + Public Accounts.

Source: RBI Bulletins; various issues.

interest payments on Central loan in a particular year from gross loans received in that year. Net loans have been fluctuating widely during the period of study. As the amount of Central loans to the State increases, the repayments also will increase in the subsequent years and this affects the net loan availability of the State. During the Fifth Plan period (1974-79), the net loan available to the State was meager, and in one year (1975-76) it was negative to the tune of Rs. 6.4 crores. This implies that the State during the year repaid to the Centre more funds than it received as loans. During the period 1979-80 and 1984-85, the net loans fluctuated widely. It was negative in two years during the Sixth Plan, (1981-82 and 1984-85) and showed marginal improvement during the remaining years of the Plan. It was during the Seventh Plan period (1985-90) that net loan availability to the State was severely reduced to a fraction of gross loans. In 1988-89, it was negative again.

The net loan available to Kerala remained low during the Annual Plans (1990-92) and the Eighth Plan period (1992-97). As pointed out in the previous chapter, the burden of debt servicing of States on Central loans increased with the progressive rise in debt financing of Plan outlays and increase in interest rates. As seen in the previous chapter, the rate of interest increased from 4.8 per cent on pre-1979 consolidated State Plan loans to 9 per cent on loans outstanding as at the end of 1989-90.

The rate of interest on other non-plan loans went up from 7.5 per cent to 12 per cent on loans to States during June 1984 and May 1995. The rate of interest on small savings loans increased from 6.25 per cent in July 1974 to 14.5 per cent in May 1997. Earlier, the maturity period of States loans from the Centre had been shorter than that of Central Government's own loans.

5.5.2 Gross Central Loans as a Percentage of Capital Receipts of Kerala and All States

The contribution Central loans to total State debt receipts and capital receipts can highlight the extent of State Government dependency on the Centre, in the mobilization of debt receipts and capital expenditure. As a percentage of total capital receipts of Kerala, Central loans form the single most important component (Table 5.15). During the period of study, the percentage share of gross loans from the Centre in the capital receipts of Kerala, declined substantially. In the Fifth FYP period (1974-79), the share of Central loans in Kerala's capital receipts was around 50 per cent and for All States in India this was 54.1 per cent. In the Sixth FYP period (1980-85), for Kerala, share of Central loans marginally increased to 53.5 per cent of its total capital receipts and for All States this constituted 55.2 per cent of capital receipts. There was marginal decline in this share during the Seventh FYP period (1985-90); for Kerala, it was only 51.3 per cent and for All States it was 52.7 per cent. The

declining percentage share of gross Central loans in the capital receipts of Kerala continued unabated during the Annual Plan (1990-92) and the Eighth FYP period (1992-97). The share was only 47.4 and 43.8 during these periods. The respective figures for All States were higher at 56.1 and 49.1 per cent. Thus, during the period of study, though gross loans from the Centre constituted the major source of capital receipts of Kerala, the percentage share of it had been falling since the Sixth FYP period. Another aspect of Central loans to Kerala is that, the State's share of Central loans in its capital receipts, throughout the period of study, remained well below the All States average. This is indicative of the declining contribution of Central loans in mobilizing investable funds for the State Government in Kerala.

5.6 Composition of Loans and Advances from the Central Government

Central loans to States are mainly given for plan and non-plan purposes. Under the plan schemes Central loans are distributed for State plan schemes, Central plan schemes and Centrally sponsored schemes (Table 5.16). The proportion of loans given for plan schemes are greater than for non-plan schemes. In the case of Kerala, 71.8 per cent of Central loans had been given for plan purpose during the Fifth FYP period (1974-79). But the composition of Central loans underwent considerable change

TABLE 5.16: COMPOSITION OF CENTRAL LOANS TO KERALA 1974-75 TO 1996-97
(Rs. Crores)

YEAR	STATE PLAN LOANS 2	CENTRAL PLAN LOANS 3	CENTRALLY SPONSORED SCHEMES 4	TOTAL PLAN LOANS 5	SMALL SAVINGS LOANS 6	TOTAL NON- PLAN LOANS 7	TOTAL CENTRAL LOANS 8
1974-75	25.0 (51.0)	1.5 (3.1)	2.76 (5.7)	29.2 (59.9)	7.02 (14.4)	18.6 (38.0)	48.8 (100)
1975-76	30.9 (63.7)	2.8 (5.8)	3.6 (7.4)	37.3 (77.0)	4.08 (8.4)	11.7 (23.0)	48.5 (100)
1976-77	33.9 (46.3)	3.2 (4.7)	4.99 (7.3)	42.1 (61.2)	3.86 (5.6)	6.7 (9.0)	68.8 (100)
1977-78	50.4 (72.6)	5.4 (7.8)	2.84 (4.1)	58.6 (84.4)	4.13 (6.0)	10.8 (15.6)	69.4 (100)
1978-79	74.9 (68.2)	6.5 (9.2)	2.46 (3.5)	83.9 (76.4)	6.22 (8.8)	25.9 (23.6)	70.9 (100)
1979-80	58.5 (79.7)	3.6 (4.9)	2.12 (2.9)	64.2 (87.5)	6.74 (9.2)	9.2 (12.5)	73.4 (100)
1980-81	55.6 (74.3)	3.7 (5.0)	2.42 (3.2)	61.7 (82.4)	10.81 (14.5)	13.2 (17.6)	74.8 (100)
1981-82	73.2 (78.3)	3.9 (4.5)	2.38 (2.5)	79.4 (85.0)	10.57 (11.3)	14.1 (16.0)	93.5 (100)
1982-83	69.2 (63.8)	4.0 (3.7)	1.56 (1.4)	74.8 (69.0)	14.83 (13.7)	18.7 (17.2)	108.5 (100)
1983-84	97.5 (45.8)	4.0 (2.0)	3.69 (1.8)	105.2 (52.7)	13.33 (6.7)	79.1 (39.6)	199.7 (100)
1984-85	69.2 (32.5)	2.5 (1.2)	3.51 (1.6)	75.2 (35.3)	23.91 (11.2)	27.8 (13.0)	212.9 (100)
1985-86	193.6 (45.5)	2.5 (0.6)	3.03 (0.7)	199.1 (46.8)	48.65 (11.4)	53.2 (12.5)	425.8 (100)
1986-87	185.3 (65.1)	3.3 (1.2)	2.66 (0.9)	191.3 (67.2)	58.32 (20.5)	60.8 (21.4)	284.8 (100)
1987-88	167.2 (55.4)	3.5 (1.2)	2.65 (0.9)	173.4 (57.5)	94.2 (31.2)	100.3 (33.3)	301.6 (100)
1988-89	167.3 (57.9)	1.3 (0.5)	2.51 (0.9)	171.2 (59.2)	111.3 (38.5)	115.8 (40.0)	289.2 (100)
1989-90	161.7 (46.3)	2.4 (0.70)	4.04 (1.2)	168.3 (50.0)	144.4 (41.3)	149.0 (42.7)	349.3 (100)
1990-91	199.2 (48.8)	2.1 (0.5)	8.54 (2.1)	209.8 (49.3)	154 (37.7)	157.7 (38.5)	408.4 (100)
1991-92	228.2 (39.7)	3.1 (0.5)	2.76 (0.5)	234.0 (40.7)	139.8 (24.3)	140.2 (24.4)	575.0 (100)
1992-93	277.1 (52.3)	0 (0.0)	3.76 (0.7)	280.8 (53.0)	112.3 (21.2)	115.3 (21.7)	529.6 (100)
1993-94	340.0 (57.0)	0.1 (0.02)	12.8 (2.1)	352.9 (59.2)	167.3 (28.1)	168.9 (28.4)	595.9 (100)
1994-95	354.3 (47.3)	0.1 (0.01)	1.41 (0.2)	355.9 (47.5)	393.2 (52.5)	393.6 (52.5)	749.4 (100)
1995-96	312.6 (47.7)	0.2 (0.03)	3.05 (0.5)	315.9 (48.2)	338.4 (51.6)	339.6 (51.8)	655.5 (100)
1996-97	418.0 (56.3)	-	23.9 (3.2)	441.9 (59.5)	300 (40.4)	300.8 (40.5)	742.7 (100)

Note: Figures in brackets are % to total
Source: RBI Bulletins; various issues.

during the successive Plan periods. The share of Central loans for plan purposes decreased and that for non-plan purposes increased. The proportion of plan loans in Central loans came down to 64.9 and 56.1 per cent during the Sixth and Seventh FYP periods. During the Annual Plans (1990-92) and Eighth FYP period, plan loan component in Central loans reached 45 and 42.9 per cent respectively. At the same time, the proportion of non-plan loans in Central loans nearly doubled. It increased from 21.8 per cent in the Fifth FYP period to 39 per cent in the Eighth FYP period. As a result of this, the Central loan component in financing Kerala's FYP's declined considerably. In the Fifth FYP, 61 per cent of the Central loans received by Kerala were for the State Plan. But this proportion gradually declined. Kerala's Sixth and Seventh FYPs received only 59.5 and 54 per cent of Central loans. During the Annual Plan (1990-92) and Eighth FYP period (1992-97) the proportion of Central loans in State Plan came down to 44.3 and 42.3 per cent. So the decline in Central loans to Kerala, is reflected in a reduction in the total plan loans and also in the State Plan. The transfer of Central loans for Kerala under Central Plan and Centrally Sponsored Scheme which was very low became insignificant during this period.

5.6.1 Plan outlay and market borrowings of Kerala (Fifth to Eighth Five Year Plan)

As with other States, market borrowings constitute the major share of the internal debt of Kerala. They are loans raised in open markets and

having a maturity of more than twelve months. The market loans of Kerala Government are floated by the Reserve Bank of India. Table 5.17 shows that from the Fifth Five Year Plan (1974-79), market borrowings as a proportion of Plan outlay of the State, have increased steadily and substantially. It financed only 7.4 per cent of the Plan outlay during the Fifth Five Year Plan period. But by the Seventh Five Year Plan Period (1985-90) it showed a threefold rise to 24.9 per cent. By the end of the Annual Plan period (1991-92) market borrowings nearly reached 30 per cent of the State's Plan outlay. During the Eighth Plan period it came down steeply to 20.7 per cent of the Plan outlay.

**TABLE 5.17: PLAN OUTLAY AND MARKET BORROWINGS OF KERALA
1974-75 TO 1996-97**

Plan Period	(Rs. crores)						
	V th PLAN 1974-79	A.P. 1979-80	VI th PLAN 1980-85	VII th PLAN 1985-90	A.P. 1990-91	A.P. 1991-92	VIII th PLAN 1992-97
Plan Outlay	569	393	1550.4	2299	596	672	6862
Market Borrowing	42.2	34.6	166.4	571.2	152.2	200.9	1421.5
% to Plan Outlay	7.42	8.79	10.73	24.85	25.54	29.89	20.72

Source:

1. RBI Report on Currency and Finance
2. Kerala State Planning Board

The increase in the market borrowing of Kerala during Plan periods can be attributed to, among other things, the declining Central loans to Kerala. As noted earlier, loan component in total fiscal transfers from the Centre to States in India have been falling. In the case of Kerala, this fall in Central loans was of a higher order compared to the All States

position. Secondly, the non-plan component of Central loans for Kerala has been rising. But small savings loans, a component of non-plan Central loans, received by Kerala, is below the All States average. All these factors create a situation in which, the State in order to have a larger plan size, resorts to increased market borrowings.

TABLE 5.18: PERCENTAGE SHARE OF KERALA IN ALL STATES MARKET BORROWING 1974-75 TO 1996-1997

YEAR 1	ALL STATES TOTAL MARKET BORROWING (Rs crores) 2	MARKET BORROWING OF KERALA (Rs crores) 3	% SHARE OF KERALA 4	PERCAPITA MARKET BORROWING OF KERALA (Rs) 5
1974-75	311.3	9.8	3.2	4.3
1975-76	274.5	9.9	3.6	4.3
1976-77	283.3	10.6	3.7	4.5
1977-78	283.7	12.4	4.4	5.2
1978-79	282.9	16.3	5.8	6.7
1979-80	305.9	17.7	5.8	7.1
1980-81	333.2	22.4	6.7	8.6
1981-82	506.9	27.1	5.4	10.6
1982-83	556.0	29.8	5.4	11.5
1983-84	763.0	37.4	4.9	14.2
1984-85	1301.3	50.9	3.9	19.1
1985-86	1414.2	81.9	5.8	30.3
1986-87	1446.4	88.6	6.1	32.3
1987-88	1789.2	103.4	5.8	37.2
1988-89	2284.9	137.1	6.0	48.6
1989-90	2554.9	158.8	6.2	55.7
1990-91	2568.7	152.2	5.9	52.7
1991-92	3364.3	192.9	5.7	66.0
1992-93	3805.0	215.0	5.7	72.5
1993-94	4145.0	219.6	5.3	72.0
1994-95	5123.0	295.6	5.8	95.6
1995-96	6274.0	345.9	5.5	111.6
1996-97	6298.8	380.2	6.0	120.8

Source: RBI Report on Currency & Finance
RBI Bulletins, various issues.

As the share of market borrowing in financing plan outlay increased, the share of Kerala in All States market borrowings also increased.

During the Fifth Five Year Plan period (1974-79), it remained below 5 per cent except in 1978-79. The first year of Sixth Five Year Plan witnessed a marginal increase in this proportion, when it came up to 6.7 per cent. But in subsequent years, it declined and came down to the lowest level of 3.9 per cent in 1984-85. The Seventh Five Year Plan period (1985-90) was notable for the comparatively high share of State's market borrowings, when it often exceeded 6 per cent. In the nineties, the share of Kerala's market borrowings remained at 5.5 per cent except in 1996-97, when it came up to 6.1 per cent (Table 5.18).

Per capita market borrowings of Kerala, however increased remarkably reflecting the absolute increase in these receipts. Between 1974-75 and 1979-80, it remained less than Rs 9. By the end of the Sixth Plan period (1984-85) it had gone up to Rs.19. During the Seventh Plan (1985-90) period, it registered a nearly threefold rise because it was during this period that the share of Kerala in All States borrowings improved. The same trend continued in the nineties and by the end of the Eighth Five Year Plan (1996-97) it came up to Rs. 121.

5.6.2 Maturity Pattern of the Market Loans of Kerala

The period of maturity of the State loans of Kerala increased steadily during the period of study. Between 1974-80, the period of maturity of the State loans floated in the market was only 10 years (Table

5.19). It increased considerably from 1980s onwards. During the Sixth Plan period (1980-85) the maturity of State Government loans increased considerably. During 1980-82, it was 12 years. In 1983-84 it increased to

TABLE 5.19: OPEN MARKET BORROWING OF KERALA : PERIOD OF MATURITY AND REDEMPTION YIELD; 1974-75 TO 1996-1997

YEAR 1	GROSS MARKET BORROWINGS (Rs. Crores) 2	PERIOD OF MATURITY (No. of Years) 3	REDEMPTION YIELD AT ISSUE PRICE (%) 4
1974-75	9.81	10	6.14
1975-76	9.93	10	6.14
1976-77	10.60	10	6.14
1977-78	12.44	10	6.07
1978-79	16.32	10	6.25
1979-80	17.65	10	6.50
1980-81	22.37	12	6.75
1981-82	27.10	12	7.00
1982-83	29.76	15	7.50
1983-84	37.43	17	8.75
1984-85	50.93	15	9.00
1985-86	81.91	13	9.75
1986-87	88.60	15	11.00
1987-88	103.41	15	11.00
1988-89	137.08	20	11.50
1989-90	158.81	20	11.50
1990-91	152.23	20	11.50
1991-92	192.92	20	12.00
1992-93	215.01	15	13.00
1993-94	219.64	10	13.50
1994-95	295.61	10	12.50
1995-96	345.92	10	14.00
1996-97	380.17	10	13.85

Source: RBI Bulletins; various issues
RBI. report on Currency and Finance.

17 years from 15 years in 1982-83. Between 1989-90 and 1991-92 the maturity period was 20 years for State Government loans. Then it declined to 15 years in 1992-93. During all the remaining four years of the Eighth Plan, loans were raised with a maturity of 10 years. The maturity

period of the State's market loans increased steadily till 1991-92. Loans with longer maturity period can lessen the burden of loan repayment by the State. But to attract more fund into the State market loan issue, the maturity period has to be shortened to become more attractive to the capital market. With liberalization of the economy in India State Governments will have to approach competitive financial markets to secure loans. They may be compelled to pay market related rate of interest, which may prove costly and accentuate the burden of State debt in future.

5.6.3 Yield Pattern of State Government Loans of Kerala

The yield pattern or coupon rates of States' market loans are important for two reasons. Firstly, it determines the attractiveness of State Government market loans to the investors in the capital market. Secondly, it also reflects the cost of market borrowings to the State Governments. During the period of study, redemption yield on State market loans floated by the Government of Kerala, nearly doubled from 6.14 in 1974-75 to 13.9 per cent in 1996-97 (Table 5.19). These yield rates remained fixed at nearly 6 per cent for 7 years up to 1980-81. It gradually increased and came up to 9 per cent in 1984-85. The cost of borrowing increased from 9.8 per cent in 1985-86 to 11.5 per cent in 1990-91. By 1995-96 it reached the high rate of 14 per cent to decline

slightly to 13.9 per cent in the next year. The increase in the yield rates, coupled with the decrease in the period of maturity of market loans during the recent years, make the State Government loans attractive to institutional investors but burdens the State Government.

When compared with Central loans the rate of interest of the State Governments market borrowings is high. As noted in the previous chapter, State Plan loans were given at a rate interest of 4.75 per cent until 1979. By 1984 it increased to 6.75 per cent. As per the Tenth Finance Commission Report (1995), the maximum rate of interest charged in 1989-90 was only 9 per cent. Similarly the rate of interest on small savings loans to State Governments was only 6.25 per cent in August 1974, and it increased to 14.5 per cent in September 1993. So Kerala, with its declining Central loans has to resort to market borrowings to finance its Plan outlay. This increases the problem of debt servicing of the State. The decision to phase out 91 day treasury bills restricts the capacity of Government to raise funds easily and at lower cost. With liberalisation of the financial markets, both the Central Government and State Governments will have to offer market-related rate of interest for their securities. The maturity period of these securities will have to be reduced in order to attract investors. These two aspects, namely, high rate of interest and short maturity period will increase the burden of debt.

5.6.4 Negotiated Loan Receipts of Kerala (1974-75 to 1996-97)

Apart from the market borrowings, negotiated loans receipts constitute a significant portion of the internal debt receipts of the State Governments in India. They are loans received by the State Governments from Central autonomous bodies and financial institutions, such as Life Insurance Corporation of India, State Bank of India and other Banks, National Agricultural Credit Fund of RBI, National Co-operative Development Corporation, Khadi and Village Industries Commission and Central Warehousing Corporation.

The increase in negotiated loans receipts and the share of it in internal debt receipts of Kerala are shown in Table 5.20. During the 23 year period from 1974-75 to 1996-97, negotiated loan receipts registered an annual average growth rate of 32 per cent. In absolute amount it was only Rs 3 crores at the beginning of the Fifth Five Year Plan and increased only to Rs. 4.3 crores by the end of the Plan period. The increase was steady till 1982-83. But in the next two years it declined. All the five years of Seventh Plan period (1985-90) recorded steady rise. During the nineties also there were wide fluctuations in the absolute amounts of negotiated loans received by the Kerala. In the final year of the Eighth Plan, the negotiated loans amounted to Rs. 163.3 crores.

TABLE 5.20: NEGOTIATED LOAN RECEIPTS OF KERALA 1974-75 TO 1996-1997
(Rs. Crores)

YEAR 1	IDEBT 2	NEGOTIATED LOANS 3	NEGOTIATED LOANS AS A PERCENTAGE OF IDBET 4(3/2*100)
1974-75	13	3.0	23.60
1975-76	11	1.4	12.51
1976-77	14	3.1	22.85
1977-78	16	3.4	21.34
1978-79	21	4.3	20.97
1979-80	23	5.4	23.26
1980-81	28	5.9	20.84
1981-82	36	8.5	23.94
1982-83	40	10.1	25.26
1983-84	47	9.1	19.59
1984-85	59	8.4	14.14
1985-86	94	11.9	12.72
1986-87	104	15.6	14.99
1987-88	122	18.9	15.47
1988-89	162	24.9	15.38
1989-90	237	78.3	33.02
1990-91	194	41.4	21.38
1991-92	231	38.1	16.48
1992-93	296	81.3	27.44
1993-94	271	51.5	19.00
1994-95	377	81.3	21.57
1995-96	428	81.7	19.11
1996-97	543	163.3	30.04
Annual average % change		31.95	

Note Negotiated Loans include loans from LIC, SBI and other Banks, National Agricultural Credit Fund of RBI, loans from National Co-operative Development Corporation, Khadi and Village Industries Commissions, Central Warehousing Corporation etc.

Source: RBI Bulletins; various issues

Negotiated loan receipts constituted nearly one fifth of the internal debt receipts of Kerala till 1981-82 except in 1975-76. In 1983-84 it formed 25.3 per cent of internal debt receipts. After that, the share of negotiated loan receipts declined substantially and came down to 15.4 per cent in 1988-89. It exceeded the one-third level in 1989-90. All the 7

years of the nineties saw wide variations ranging between 16.5 and 30 per cent.

5.7 Conclusion

The outstanding debt/SDP ratio of Kerala is below the All State average. But it is the third highly indebted State in India. The growth of the public debt of Kerala is closely linked to the fiscal crisis of the State. This is manifested in the form of revenue deficit and measured in terms of Gross Fiscal Deficit. This is nothing but the resource gap of the State and is equivalent to the public debt of the State. Decomposition of GFD shows that borrowed funds are increasingly used to finance revenue deficit. This diversion of costly borrowed funds reduces the capital outlay and net lending. This again reduces the growth of the economy and its revenue on the one hand and increases the burden of debt servicing. This forces the State Government to go in for further borrowing. A vicious circle of revenue deficit and increased debt is at the centre of Kerala's fiscal crisis. The increase in the share of internal debt consisting of market borrowings and negotiated loans shows that the burden of debt servicing for Kerala will be higher in the future. Similarly the rise in the share of provident funds and small savings in total debt receipts may pose severe strain on the revenue account of the State in the form of increased interest payment. These and other aspects like growth and composition of

capital disbursements and debt receipts utilization of the Government of Kerala are discussed in the next chapter.

References

1. Economic Review, Governemnt of Kerala 1998
2. Ibid
3. Ibid
4. K.K.George (1993), *Limits to Kerala Model Development*, Centre for Development Studies, Trivandrum.

CHAPTER 6

GROWTH AND COMPOSITION OF CAPITAL DISBURSEMENTS AND DEBT RECEIPTS UTILIZATION OF GOVERNMENT OF KERALA 1974-75 TO 1996-97.

6.1 Introduction

After analysing the various aspects of the total debt receipts of Kerala, this chapter looks into the utilization of debt receipts largely through capital disbursements. State Governments, apart from providing basic services like health, education, housing, and social welfare have to provide for the development of infrastructure as also agriculture and industry. This necessitates capital investment in the sphere of irrigation, power, transport, etc. Debt receipts mobilized by the State Governments are meant to finance these capital expenditures and hence both are related. Against this background, the chapter studies the growth and composition of the capital disbursements and debt receipts utilization of the Government of Kerala for the period 1974-75 to 1996-97.

6.2 Aggregate Disbursements of the Government of Kerala

As a consequence of the adoption of economic planning and factors like rise in state income, population, etc., the total expenditure (Revenue +Capital) of Kerala has been registering a steady growth over the years. The growth of total disbursements of Kerala is set out in Table 6.1. The total disbursements which was modest at Rs. 376 crores during 1974-75 had gone up to Rs. 8713 crores in the year 1996-97 registering an annual growth rate of 15.5 per cent. In total disbursements, the share of revenue expenditure has steadily increased compared to the share of capital expenditure. The share of the former was high even in 1974-75 accounting for nearly 76.4 per cent and this proportion remained unchanged till the end of Fifth Five Year Plan (1978-79). During the latter half of the eighties, the share of revenue expenditure almost reached 80 per cent in total disbursement. This trend continued in all the years of the Eighth Plan period (1992-97) and revenue expenditure reached the all time high of 85.7 per cent of total disbursement.

But capital disbursement as a proportion of total disbursement declined during the same period, i.e. from 23.6 per cent to 14.2 per cent. This trend in Kerala is in line with the trend in other States.

**TABLE 6.1: GROWTH & COMPOSITION OF THE TOTAL DISBURSEMENTS
1974-75 TO 1996-97.**

(Rs. Crores)

YEAR	REVENUE EXPENDITURE	CAPITAL DISBURSEMENTS	TOTAL DISBURSEMENTS	REVENUE EXPENDITURE AS PERCENTAGE OF TOTAL DISBURSEMENTS	CAPITAL DISBURSEMENTS AS PERCENTAGE OF TOTAL DISBURSEMENTS
1	2	3	4	5	6
1974-75	288	89	377	76.4	23.6
1975-76	355	109	464	76.5	23.5
1976-77	390	134	524	74.4	25.6
1977-78	416	137	553	75.3	24.7
1978-79	479	148	627	76.5	23.6
1979-80	534	176	710	75.2	24.8
1980-81	668	188	856	78.0	22.0
1981-82	755	331	1086	69.5	30.5
1982-83	784	213	997	78.6	21.4
1983-84	992	329	1321	75.1	24.9
1984-85	1139	433	1572	72.4	27.6
1985-86	1445	523	1968	73.4	26.6
1986-87	1655	507	2162	76.6	23.5
1987-88	1780	470	2250	79.1	20.9
1988-89	2061	460	2521	81.8	18.2
1989-90	2298	591	2889	79.6	20.5
1990-91	2825	552	3377	83.7	16.3
1991-92	3216	789	4005	80.3	19.7
1992-93	3656	707	4363	83.8	16.2
1993-94	4293	845	5138	83.6	16.4
1994-95	5066	892	5958	85.0	15.0
1995-96	5826	1096	6922	84.2	15.8
1996-97	7472	1240	8712	85.8	14.2
Annual average growth rate (%)	15.90	14.89	15.49		

Source: RBI Bulletin, various issues

A study of public expenditure trends in India during 1970-85 showed that the growth of capital expenditure at the State level suffered a decline in the first half of the 1 terms, capital disbursements of States grew at only 3.9 per cent per annum between 1980-81 and 1985-86, while revenue expenditure grew at 8.8 per cent (Govinda Rao and

Tulasidhar (1991))¹. Another study shows that the current expenditure in real terms increased at 8 per cent per annum in the 1980s. Expenditure on capital formation, however, increased only by 4.7 per cent (Govinda Rao, 1992)². The ratio of government expenditure to SDP for Kerala was higher than for All States, in all the 23 years except in 1982-83. The State's ratio of capital expenditure to SDP was lower than that of All States except in 1981-82. Similarly Kerala's ratio of revenue expenditure to SDP has been consistently higher than that of All States (George 1994)³.

6.2.1 Ratio of Expenditure to State Domestic Product.

The ratio of total government expenditure (Revenue + Capital) to SDP which was 19.9 per cent in 1974-75 steadily increased to 31 per cent by 1996-97 (Table 6.2). As noted earlier this ratio is higher for Kerala than for other States. The margin of difference between Kerala's ratio and All States' ratio coming down in recent years. Break-up of the ratio of budgetary expenditure to state domestic product, shows that the State's ratio of capital disbursement to SDP was lower, than the All States level. The State's ratio of revenue expenditure to SDP was higher. It was only 14.8 per cent in 1974-75 and increased to 26.6 per cent in 1996-97. The revenue expenditure of Kerala takes away one-

fourth of the State's domestic product, for current consumption alone.

The State's aggregate expenditure took away nearly one-third of its domestic product in 1996-97.

TABLE 6.2: RATIO OF EXPENDITURE TO STATE DOMESTIC PRODUCT (KERALA)

(Rs. Crore)

YEAR	REVENUE EXPENDITURE	CAPITAL DISBURSEMENTS	TOTAL DISBURSEMENTS	SDP AT CURRENT PRICES	PERCENTAGE OF REVENUE EXPENDITURE TO SDP	PERCENTAGE OF CAPITAL DISBURSEMENTS TO SDP	PERCENTAGE OF TOTAL EXPENDITURE TO SDP
1	2	3	4	5	6	7	8
1974-75	288	89	377	1942	14.8	4.6	19.4
1975-76	355	109	464	2098	16.9	5.2	22.1
1976-77	390	134	524	2250	17.3	6.0	23.3
1977-78	416	137	553	2423	17.2	5.6	22.8
1978-79	479	148	627	2693	17.8	5.5	23.3
1979-80	534	176	710	2874	18.6	6.1	24.7
1980-81	668	188	856	3823	17.5	4.9	22.4
1981-82	755	331	1086	3697	20.4	9.0	29.4
1982-83	784	213	997	4567	17.2	4.7	21.8
1983-84	992	329	1321	5465	18.2	6.0	24.2
1984-85	1139	433	1572	6152	18.5	7.0	25.6
1985-86	1445	523	1968	6503	22.2	8.0	30.3
1986-87	1655	507	2162	7354	22.5	6.9	29.4
1987-88	1780	470	2250	8258	21.6	5.7	27.3
1988-89	2061	460	2521	9182	22.5	5.0	27.5
1989-90	2298	591	2889	10668	21.5	5.5	27.1
1990-91	2825	552	3377	12173	23.2	4.5	27.7
1991-92	3216	789	4005	15102	21.3	5.2	26.5
1992-93	3656	707	4363	17175	21.3	4.1	25.4
1993-94	4293	845	5138	19688	21.8	4.3	26.1
1994-95	5066	892	5958	22024	23.0	4.1	27.0
1995-96	5826	1096	6922	24819	25.1	4.4	29.5
1996-97	7472	1240	8712	26919	26.6	4.4	31.0
Annual average growth rate (%)	15.90	14.89	15.49	12.94		12.94	

Source: RBI Bulletin, various issues.

5.2.2 Economic Classification of Expenditure

The economic classification of the State budget provides a correct picture of aggregate expenditure on consumption and capital formation (Table 6.3). The share of consumption expenditure in the State's final outlay (direct expenditure on consumption as well as capital formation) is very high. The share of capital formation is correspondingly low. The share of consumption expenditure which was 79.6 per cent declined to 67.3 per cent in 1979-80. Thereafter consumption expenditure increased considerably and in 1996-97, 90.9 per cent of Kerala's budgetary expenditure was used for consumption purpose. The share of gross capital formation declined from 20.4 per cent in 1975-76 to just 9.1 per cent in 1990-91. The increase in the share of consumption expenditure was largely due to the steep increase in the share of consumption in the final outlay on economic services. This in turn was a reflection of the increasing revenue component of expenditure on economic services (George 1994)³. Within consumption expenditure, the share of compensation for employees increased from 65.5 per cent in 1975-76 to 74 per cent in 1990-91. Similarly the net purchases of commodities also increased from 14.1 per cent to 16.9 per cent during the same period. All these factors together reduced the budgetary resources for capital formation in Kerala.

TABLE 6.3: COMPONENTS OF FINAL OUTLAY OF KERALA 1975-76 TO 1990-91.

YEAR	TOTAL CONSUMPTION EXPENDITURE	COMPENSATION FOR EMPLOYEES			NET PURCHASE OF COMMODITIES & SERVICES	GROSS CAPITAL FORMATION	FINAL OUTLAY
		1	2	3			
		WAGES & SALARIES	PENSIONS	TOTAL (2+3)			
1975-76	79.6	62.6	2.9	65.5	14.1	20.4	100
1976-77	78.6	61.4	3.0	74.4	14.2	21.4	100
1977-78	74.2	58.2	2.9	61.1	13.1	25.8	100
1978-79	70.2	58.4	2.8	61.2	9.0	29.8	100
1979-80	67.3	52.8	3.5	56.3	11.0	32.7	100
1980-81	78.1	56.2	7.5	63.7	14.4	21.9	100
1981-82	77.9	53.3	8.8	62.2	15.7	22.1	100
1982-83	82.1	54.0	10.8	64.8	17.3	17.9	100
1983-84	84.9	51.2	10.0	61.2	23.7	15.1	100
1984-85	83.9	58.1	11.1	69.3	14.6	16.1	100
1985-86	81.2	52.6	11.1	63.7	17.5	18.8	100
1986-87	83.6	50.9	16.1	67.1	16.5	16.4	100
1987-88	86.5	56.1	16.9	72.9	13.6	13.5	100
1988-89	86.6	57.5	14.9	72.3	14.2	13.4	100
1989-90	89.7	59.2	13.4	72.6	17.2	10.3	100
1990-91	90.9	59.1	14.9	74.0	16.9	9.1	100

Source: Economic cum Functional Classification of Budget. Bureau of Economics and Statistics, Government of Kerala.

6.2.3 Sources of Capital Receipts

The capital receipts of States are mainly debt financed. This is evident from the composition of its capital receipts (Table 6.4). As seen in the previous chapter, the increase in the revenue deficit component of Gross Fiscal Deficit (GFD) over the years reduced the availability of borrowed funds. This in turn reduced the share of debt receipts in the

YEAR	INTERNAL DEBT	CENTRAL LOANS	PS. SMALL SAVINGS (etc)	RECOVERY OF LOANS AND ADVANCES	RESERVE FUND	DEPOSITS AND ADVANCES	CURRENTS*	TOTAL DEBT RECEIPTS	TOTAL NON DEBT RECEIPTS	TOTAL CAPITAL RECEIPTS
1	2	3	4	5	6	7	8	9	10	11
1974-75	13 (13.0)	49 (49.0)	21 (21)	12 (12.0)			5 (5)	83 (83)	17 (17.0)	100 (100)
1975-76	11 (11.5)	49 (51.0)	12 (12.5)	16 (17.0)			8 (8.3)	72 (75)	24 (25.0)	96 (100)
1976-77	14 (11.4)	69 (56.1)	16 (13)	15 (12.0)			9 (7.3)	99 (80.5)	24 (19.5)	123 (100)
1977-78	16 (12.2)	69 (52.7)	24 (18.3)	12 (9.2)			10 (7.6)	109 (83.2)	22 (16.8)	131 (100)
1978-79	21 (12.3)	71 (41.5)	52 (30.4)	10 (5.8)			17 (9.9)	144 (84.2)	27 (15.8)	171 (100)
1979-80	23 (16.5)	73 (52.5)	17 (12.2)	10 (7.2)			16 (12.0)	113 (81.3)	26 (18.7)	139 (100)
1980-81	28 (19.2)	75 (51.4)	16 (11.0)	11 (7.5)			16 (11.0)	119 (81.5)	27 (18.5)	146 (100)
1981-82	36 (20.8)	93 (53.8)	38 (22.0)	16 (9.2)			-10 (-6.0)	167 (96.5)	6 (3.5)	173 (100)
1982-83	40 (18.4)	108 (49.8)	62 (28.6)	15 (6.9)			-8 (-4.0)	210 (96.8)	7 (3.2)	217 (100)
1983-84	47 (12.9)	200 (54.8)	72 (19.7)	15 (4.1)			31 (8.5)	319 (87.4)	46 (12.6)	365 (100)
1984-85	59 (15.9)	213 (57.6)	69 (18.6)	21 (5.7)			8 (2.2)	341 (92.2)	29 (7.8)	370 (100)
1985-86	94 (13.1)	426 (59.3)	108 (15.0)	18 (2.5)	2.8 (0.4)	3.0 (0.4)	66.2 (9.2)	628 (87.5)	90 (12.5)	718 (100)
1986-87	104 (21.3)	285 (58.4)	71 (14.5)	32 (6.6)	2.9 (0.6)	3.5 (0.7)	-10.4 (-2.0)	460 (94.3)	28 (5.7)	488 (100)
1987-88	122 (18.5)	302 (45.8)	109 (16.5)	18 (2.7)	.8 (0.1)	4.3 (0.7)	102.9 (16)	533 (80.9)	126 (19.1)	659 (100)
1988-89	162 (28.1)	289 (50.1)	160 (27.7)	22 (3.8)	.5 (0.1)	5.3 (0.9)	-61.8 (-11)	611 (106)	-34 (-5.9)	577 (100)
1989-90	237 (29.0)	349 (42.7)	214 (26.2)	19 (2.3)	1.1 (0.1)	5.8 (0.7)	-8.9 (-1)	800 (97.9)	17 (2.10)	817 (100)
1990-91	194 (20.3)	408 (42.6)	293 (30.6)	18 (1.9)	3.2 (0.3)	7.1 (0.7)	33.7 (3.5)	895 (93.5)	62 (6.5)	957 (100)
1991-92	231 (20.9)	575 (52.0)	257 (23.3)	22 (2.0)	3.6 (0.3)	9.0 (0.8)	7.4 (0.7)	1063 (96.2)	42 (3.8)	1105 (100)
1992-93	296 (26.1)	530 (46.7)	214 (18.9)	20 (1.8)	5.1 (0.4)	8.7 (0.8)	60.2 (5.3)	1040 (91.7)	94 (8.3)	1134 (100)
1993-94	271 (20.6)	596 (45.3)	468 (35.6)	33 (2.5)	3.8 (0.3)	8.6 (0.7)	-64.4 (-5.0)	1335 (101)	-19 (-1.4)	1316 (100)
1994-95	377 (22.3)	749 (44.3)	666 (39.4)	26 (1.5)	5.2 (0.3)	11.8 (0.7)	-143 (-8.0)	1792 (106)	-100 (-5.9)	1692 (100)
1995-96	428 (27.4)	655 (41.9)	374 (23.9)	32 (2.0)	40.4 (2.6)	11.8 (0.8)	21.8 (1.4)	1457 (93.2)	106 (6.8)	1563 (100)
1996-97	543 (29.8)	743 (40.7)	463 (25.4)	31 (1.7)	11.8 (0.6)	45.2 (2.5)	-13 (-1)	1749 (95.9)	75 (4.1)	1824 (100)

Note: 1. Reserve Funds include depreciation/ renewal reserve funds, development and welfare funds, general and other reserve funds under public account

2. Deposits and Advances include deposits of local funds, civil deposits, and civil advances under public Account.

3. *Others include and miscellaneous, appropriation to contingency fund, miscellaneous capital receipts and remittances which were negative in some years

Source: RBI Bulletin, various issues

capital receipts of Kerala. The share of non-debt items in capital receipts declined from 17.6 per cent in 1974-75 to 4.2 per cent in 1996-97. The major non-debt item of capital receipts namely recovery of loans and advances by State Government declined from the low of level at 11.7 per cent in 1974-75 to 1.7 per cent in 1996-97. The other items of capital receipts like Reserve Funds, Deposits and Advances remained low during the period of study.

The extent of financing of capital disbursements by the public debt receipts shown in Table 6.5 can present a picture of debt receipts utilization by the Government of Kerala. Debt receipts contributed nearly 81 per cent of the capital receipts of the State during the Fifth Plan period (1974-79). The proportion steadily increased during the Sixth and Seventh Plan period and reached 90 per cent. During the Eighth Plan period (1992-97) capital receipts of the State was almost equal to the debt receipts of the State of Kerala. In 3 years during the period of study debt receipts exceeded the capital receipts implying diversion of funds on account of deficits in suspense and miscellaneous, remittances and appropriation to contingency. In 1988-89, the total debt receipts was Rs. 611 crores, while total capital receipts was shown as Rs. 577 crores. This means that total debt receipts formed 105.9 per

TABLE 6.5: FINANCING OF CAPITAL DISBURSEMENTS BY PUBLIC DEBT IN KERALA: 1974-75 TO 1996-97.

(Rs. crores)

YEAR	DEBT RECEIPTS	CAPITAL RECEIPTS	CAPITAL DISBURSEMENTS	DEBT AS PER CENTAGE OF CAPITAL DISBURSEMENTS	CAPITAL RECEIPTS AS PERCENTAGE OF CAPITAL DISBURSEMENTS
1	2	3	4	5	6
1974-75	82.9	100.6	88.8	93.40	113.37
1975-76	71.4	96.5	109.3	65.29	88.272
1976-77	98.9	122.6	134.2	73.69	91.365
1977-78	109.6	131.4	136.6	80.25	96.222
1978-79	144.0	170.5	147.6	97.60	115.5
1979-80	113.9	139.1	176.1	64.67	78.964
1980-81	119.1	145.8	187.8	63.43	77.613
1981-82	166.7	173.2	331.1	50.35	52.31
1982-83	210.4	217.1	212.9	98.81	101.96
1983-84	318.2	364.6	329.4	96.61	110.7
1984-85	341.2	369.6	433.1	78.78	85.334
1985-86	627.9	718.1	523.3	119.10	137.22
1986-87	460.2	488.1	507.0	90.78	96.286
1987-88	533.0	658.5	470.4	113.32	140
1988-89	610.8	577.0	459.9	132.79	125.45
1989-90	800.8	816.9	590.9	135.53	138.25
1990-91	895.5	957.1	551.5	162.38	173.54
1991-92	1063.0	1105	788.7	134.78	140.11
1992-93	1039.5	1134.1	706.6	147.11	160.5
1993-94	1334.8	1315.7	844.9	157.99	155.73
1994-95	1792.1	1691.9	892.4	200.81	189.59
1995-96	1456.6	1563.3	1095.5	132.96	142.7
1996-97	1748.7	1824.1	1240.2	141.00	147.08

Note: Total Debt Receipts = Internal debt plus Loans and advances from Centre plus provident fund and small savings ETC..

Debt receipts are lower than capital receipts in some years due to Revenue Account and overall deficit.

Source: RBI Bulletin; various issues

cent of the total capital receipts during that year. The same situation was repeated in 1993-94 and 1994-95, when debt receipts exceeded the total capital receipts (101.5 and 105.9 per cent respectively). This can

be partly attributed to reduced recovery of amounts from various institutions to which the State Government have advanced loans. The amount of arrears of recovery (principal and interest) overdue at the end of March 1997, comes up to Rs. 931 crores (Table 6.7). The Kerala State Electricity Board and Road Transport Corporation owed Rs. 627 crore and Rs. 81 crores by way of principal and interest amount to the Government of Kerala in March 1997. The other leading defaulters are the Kerala Water Authority (Rs. 204 crores) and Kerala State Housing Board (Rs. 7 crores). An amount of Rs. 12 crore had to recovered from other institutions in March 1997. This situation also reduced, as noted earlier, the non-debt component of Kerala's capital receipts to an insignificant level.

6.3 Financing of Capital Disbursements

Capital disbursement is mainly financed through the mobilization of public debt receipts. In addition, surplus from the revenue account, recovery of loans and advances by the state government, contingency fund receipts, reserve funds receipts, deposits and advances are also used to meet the total capital disbursement of the State Governments. However debt receipts mobilization by the State Governments is the single largest and main source of funds for capital disbursements because

other components of capital receipts as noted earlier are meager. There was no revenue surplus in recent years.

TABLE 6.6: ARREARS IN RECOVERY OF AMOUNTS OVERDUE AT THE END OF MARCH 1997

		(Rs. Lakhs)	
		PRINCIPAL	INTEREST
1	Kerala State Road Transport Corporation	4140.08	3963.82
2	Kerala State Electricity Board	16092.22	46586.35
3	Kerala Water Authority	9118.60	11280.73
4	Kerala State Housing Board	383.66	290.61
5	Other Institutions	552.72	684.61
Total		93093.40	

Source: Finance Accounts of Kerala 1996-97.

6.3.1 Diversion of Capital Receipts

Capital disbursements of the State were highly debt financed (Table 6.5). Debt receipts were less than capital disbursements till 1984-85. Thereafter it exceeded capital disbursements till 1996-97. The only exception was 1986-87, when debt receipts was only 90.8 per cent of capital disbursements. This implies that only a portion of the debts receipts was used for capital disbursement by the State Government. The other portion of the debt receipts was used up to finance the deficit on the revenue account of the State budget. A surplus in the capital account was created by deliberate compression of the capital disbursements of the State. The surplus so created in the capital account was nothing but borrowed funds meant to fill the deficit in the revenue

account which is the difference between revenue expenditure and revenue receipts. This is clear from the Seventh Plan onwards, when debt receipts exceeded the total capital disbursement of the State on a regular basis. Thus revenue deficit is the root cause of fiscal deficit which shows the difference between total expenditure and non-debt receipts of the Government. This is equal to the public debt of the State Government.

Diversion of capital receipts is also reflected in the high proportion of capital receipts in capital disbursements (Table 6.5). During 15 years, total capital receipts exceeded the capital disbursements and in the other 8 years capital receipts financed nearly 80 per cent of capital disbursement except in 1981-82, when it was only 52.3 per cent. This means that during most of the time a surplus in the capital account was created to finance the revenue deficit of the State budget. This points to the declining investment effort of the State on the one hand and diversion of the costly debt financed capital receipts on the other hand.

6.4 Growth and Composition of the Capital Disbursements

Total capital disbursements consist of

- a) Capital outlay (developmental and Non-developmental)
- b) Repayment of debt of the State Government
- c) Loans and advances by the State Government to third parties and institutions like loans for social services(education, health, housing, urban development, social welfare), economic services (agriculture, rural development, energy, industry, transport) and loans to Government servants.

Total capital disbursements of the Government of Kerala increased from Rs. 89 crore in 1974-75 to Rs 1240 crore in 1996-97. It registered an annual average growth rate of 14.9 per cent per annum during the 23 year period of study. The growth was marked by fluctuations, especially during the Seventh Plan period (1985-90) when it declined consecutively in three years (1986-89) (Table 6.7).

6.4.1 Share of Capital Outlay and Loans and Advances in Total Capital Disbursements.

The actual investments made by the State Government out of its total capital disbursements consist of total capital outlay and loans and advances made by the State Government. The third component of the State's capital disbursements namely, repayment of debt is actually the leak from the State's inevitable funds. Revenue deficits increase this

TABLE 6.7: GROWTH AND COMPOSITION OF THE CAPITAL DISBURSEMENTS OF KERALA - 1974-75 TO 1996-97.

YEAR	(Rs. Crores)								
	2	3	4	5	6	7	8	9	
	TOTAL CAPITAL DISBURSEMENT	TOTAL CAPITAL OUTLAY	REPAYMENT OF MARKET LOANS	REPAYMENT OF LOANS TO CENTRE	REPAYMENT TO AUTONOMOUS INSTITUTIONS AND OTHERS	TOTAL REPAYMENTS	LOANS AND ADVANCES BY STATE GOVERNMENT	CAPITAL OUTLAY & LOANS AS % OF TOTAL CAPITAL DISBURSEMENTS	
1974-75	88.8 (100)	32.1 (36.2)	3.9 (4.39)	19.9 (22.4)	2.2 (2.44)	26.0 (29.3)	3069 (34.57)	70.7	
1975-76	109.3 (100)	47.4 (42.4)	0.2 (0.14)	35.6 (32.6)	1.6 (1.45)	37.4 (34.2)	2454 (22.45)	65.8	
1976-77	134.2 (100)	56.8 (40.9)	4.2 (3.11)	47.6 (35.5)	1.2 (0.90)	53.0 (39.5)	2445 (18.22)	60.5	
1977-78	136.6 (100)	72.9 (52.3)	3.9 (2.88)	30.3 (22.2)	1.3 (0.92)	35.5 (26.0)	2615 (20.61)	72.5	
1978-79	147.6 (100)	67.1 (44.2)	3.7 (2.52)	31.3 (21.2)	1.4 (0.91)	36.4 (24.7)	4104 (29.84)	73.3	
1979-80	176.1 (100)	104.2 (58.0)	4.2 (2.37)	16.7 (9.5)	1.6 (0.89)	22.4 (12.7)	4956 (28.14)	87.3	
1980-81	187.8 (100)	121.9 (62.9)	5.0 (2.67)	18.7 (10.0)	1.8 (0.96)	25.6 (13.6)	4041 (21.51)	86.4	
1981-82	331.1 (100)	132.9 (38.6)	7.1 (2.13)	147.7 (44.6)	2.2 (0.67)	157.0 (47.4)	4123 (12.45)	52.6	
1982-83	212.9 (100)	128.5 (58.9)	6.6 (3.11)	39.3 (18.5)	2.5 (1.18)	48.5 (22.8)	3597 (16.90)	77.2	
1983-84	329.4 (100)	208.1 (62.1)	9.0 (2.72)	59.7 (18.1)	2.9 (0.87)	71.6 (21.7)	4771 (14.48)	77.7	
1984-85	433.1 (100)	167.1 (37.4)	18.0 (4.14)	169.4 (39.1)	6.2 (1.44)	193.6 (44.7)	7248 (16.73)	55.3	
1985-86	523.3 (100)	205.8 (37.8)	12.8 (2.44)	240.5 (46.0)	3.6 (0.69)	256.8 (49.1)	6064 (11.59)	50.9	
1986-87	507.0 (100)	211.1 (39.7)	10.9 (2.16)	171.3 (33.8)	4.4 (0.87)	186.7 (36.8)	10923 (51.55)	63.2	
1987-88	470.4 (100)	167.4 (34.2)	13.0 (2.76)	181.5 (38.6)	4.7 (1.00)	199.2 (42.3)	10378 (22.06)	57.7	
1988-89	459.9 (100)	180.3 (37.7)	15.6 (3.39)	168.0 (36.5)	5.7 (1.24)	189.3 (41.2)	9036 (19.65)	58.8	
1989-90	590.9 (100)	232.3 (38.4)	19.8 (3.36)	190.6 (32.3)	7.5 (1.27)	218 (36.9)	14059 (23.79)	63.1	
1990-91	551.5 (100)	256.0 (45.1)	0.1 (0.02)	138.6 (25.1)	18.6 (3.38)	157.3 (28.5)	13825 (25.07)	71.5	
1991-92	788.7 (100)	286.1 (35.5)	0.02 (0.002)	305.9 (38.8)	21.5 (2.72)	327.4 (41.5)	17514 (22.21)	58.5	
1992-93	706.6 (100)	277.9 (38.0)	21.7 (3.07)	243.3 (34.4)	26.6 (3.77)	291.6 (41.3)	13710 (19.40)	58.7	
1993-94	844.9 (100)	363.3 (41.7)	26.4 (3.13)	202.7 (24.0)	18.5 (2.19)	247.6 (29.3)	23396 (27.69)	70.7	
1994-95	892.4 (100)	446.0 (48.4)	0.21 (0.02)	137.6 (15.4)	20.1 (2.25)	157.9 (17.7)	28848 (32.33)	82.3	
1995-96	1095.5 (100)	563.5 (52.2)	0.02 (0.003)	143.3 (13.2)	20.7 (1.96)	163.9 (15.0)	36811 (30.31)	85.0	
1996-97	1740.2 (100)	682.6 (55.1)	0.03 (0.003)	165.9 (14.0)	25.6 (1.95)	191.4 (11.0)	36619 (26.43)	60.3	
Annual average growth rate (%)	14.89	16.57	175.27	43.88	17.78	3.2	14.90		

Note: Figures in brackets are percentage to total

Source: RBI Bulletin: Finances of State Government 1974-75 to 1996-97.

leak. The ratio of capital outlay and loans and advances to total capital disbursements reflect the proportion of capital resources that has gone into investment in the State (Table 6.7). During the Fifth and Sixth FYP periods, this ratio remained more or less stable at 68.5 and 69.8 per cents respectively. But capital disbursements on these two heads declined during the Seventh FYP period, as it came down to 58.7 per cent. In the Annual Plans of 1990-92, it marginally increased to 64.7 per cent. The eighth FYP period achieved commendable capital investments because nearly three-fourth (75.5 per cent) of capital disbursements of Kerala have gone into capital outlay and loans and advances by the State Government. This is mainly on account of a fall in the total repayment of debt especially during the latter half of the Eighth FYP period.

6.4.2 Share of Capital Outlay

Capital outlay of the State Government is incurred on general services (Public works, stationery and printing) Social services (education, health, water supply, housing, social security) and Economic services (agriculture and allied activities, transport, irrigation, energy, industry). Composition of total capital disbursements of Kerala shows the increasing share of capital outlay, of both developmental and non-

developmental nature. The share of this item which was only 36.2 per cent of total capital disbursement in 1974-75 formed 55.1 per cent by 1996-97 (Table 6.7). During this period, it registered a growth rate of 16.6 per cent per annum, higher than the growth of capital disbursements itself. During the Fifth Plan period (1974-79), it increased to the high of 52.3 per cent to fall to 44.2 per cent in the final year of the Plan. This implies that the State Government is getting directly involved with the development process by its increasing investment. This also reduces the capacity of the State Government to advance loans to institutions engaged in developmental activities. The Sixth Plan period (1980-85) witnessed the high of 62.1 per cent in 1980-81 but the final year of the PLAN marked the beginning of the decline in capital outlay of the State as a proportion of its capital disbursements. The same trend continued till the beginning of the Eighth Plan (1992-97) and of late capital outlay has constituted more than half of the State's capital disbursements.

6.4.3 Share of Loans and Advances

Loans and advances, for social and economic services, made by the Government of Kerala is an important component of the capital disbursements of the State. In absolute terms, it increased from Rs. 31 crore in 1974-75 to Rs. 366 crore in 1996-97 recording a growth rate of

9 per cent per annum equaling the rate of growth of capital disbursements of the State (Table 6.7). As a proportion of total capital disbursements, State Government's loans and advances formed 34.6 per cent at the beginning of the Fifth Plan period. But in the Sixth Plan period it came down to an average level of 16.4 per cent. In the Seventh and Eighth Plan periods, the proportion of State Government loans and advances increased steadily and formed 23.4 and 27.2 per cent respectively. These loans are mainly given for developmental purposes to institutions engaged in the development of power, transport, housing and local bodies. Sectoral disaggregation of loans and advances by State Government is discussed in the subsequent sections of the chapter.

6.4.4 Total Repayments and Capital Disbursements

Repayment of debt is an important component of total capital disbursements of the State. Total repayment of Kerala which was only Rs.26 crores in 1974-75, increased to Rs.196 crores in 1996-97, registering an annual average growth rate of 34.3 per cent (Table 6.7). Total repayment of debt consists of repayment of loans to the Central Government and repayment of the internal debt of Kerala. In internal debt repayment, repayment of market loans are larger than repayment of negotiable loans from the autonomous institutions. During the Fifth and

Sixth FYP periods, repayment of debt took away nearly one-third (31.5 and 30.2 per cent) of the total capital disbursements of Kerala. The repayment burden increased during the Seventh FYP period when 41.3 per cent of Kerala's capital resources were used to repay old debts. This situation changed by the end of the Eighth FYP period. During the Annual Plan period 1990-92, only 35.3 per cent of the State's capital funds were used to make repayments. During the Eighth FYP period, repayment of debt consumed only 24.5 per cent of Kerala's investable funds. This means that even today, one fourth of Kerala's capital disbursements are marked for repayment of its accumulated public debt. But this is an improvement when compared with the repayment burden the State experienced during the earlier Plan periods. This fall in the repayment burden of Kerala can be attributed to the existence of long maturity loans in the State's borrowings and debt rescheduling effected by the Ninth and Tenth Finance Commissions. Discharge of internal debt as a whole, takes away only less than 5 per cent of the capital disbursements of Kerala during the 23 year period of study. Repayment of loans to the Centre has registered a growth rate of 44 per cent per year. But as a proportion of the State's capital disbursements it showed wide fluctuation and of late it has been falling.

6.5 Capital Outlays and Loans and Advances by the Government of Kerala as Percentage of Debt

As noted earlier capital outlays and loans and advances made by the state government accounted for the major share of the total capital disbursements of Kerala which are mostly debt financed. To understand the utilization of debt receipts, the capital outlay-debt, loans-debt, and finally capital outlay and loans to debt ratios are examined.

6.5.1 Capital Outlay-Debt Ratio

The total capital outlay of Kerala expressed as a percentage of total debt receipts declined considerably during the Plan periods (Table 6.8). During the Fifth FYP period, nearly 55.1 per cent of Kerala's total debt was utilised for capital outlay. In the Sixth FYP period, 71.5 per cent of the debt was used for financing capital outlay. But from the Seventh FYP period onwards, the proportion of borrowed funds used for investment declined considerably. During the Seventh FYP and the Annual Plan periods (1990-92) only 33.7 and 27.7 per cent of Kerala's total debt receipts were utilized on capital outlay. In the Eighth FYP period also capital outlay out of debt receipts utilization remained at a low of 30.7 per cent. Thus in spite of the decline in the repayment

burden during the Eighth FYP period, only less than one-third of debt utilization went into capital outlay.

6.5.2 Loans and Advances-Debt Ratio

Loans and Advances by the State Government for Developmental and Non-Developmental purposes constitute an important item of the Government's total capital disbursements. These are mainly given for social and economic services under developmental purposes. The debt financed loans and advances by the State Government declined steadily during the period of study (Table 6.8). In the Fifth FYP period, nearly 29.7 per cent of loans and advances made by the State Government was out of its total debt receipts. But in the Sixth FYP period, this proportion came down to 22.4 per cent. A higher proportion of capital outlay in debt receipts might have contributed to this low share of loans out of debt receipts. In the Seventh FYP and Annual Plan (1990-92), loans and advances as a proportion of Kerala's total debt receipts declined further to 17 and 16 per cent respectively. In the Eighth FYP period only 17.1 per cent of borrowed funds were used for loans and advances by the State Government.

**TABLE 6.8: DEBT AS PERCENTAGE OF CAPITAL OUTLAY AND LOANS & ADVANCES MADE BY THE GOVERNMENT OF KERALA
1974-75 TO 1996-97.**

YEAR	2	3	4	5	6	7	8
	TOTAL DEBT	TOTAL CAPITAL OUTLAY	TOTAL CAPITAL OUTLAY AS PERCENTAGE OF TOTAL DEBT	LOANS AND ADVANCES BY STATE GOVERNMENT	LOANS AND ADVANCES AS OF TOTAL DEBT	CAPITAL OUTLAY PLUS LOANS AND ADVANCE	CAPITAL OUTLAY PLUS LOANS AND ADVANCE AS PERCENTAGE OF TOTAL DEBT
1974-75	83	32	38.6	31	37.3	63	75.9
1975-76	71	47	66.2	25	35.2	72	101.0
1976-77	99	57	57.6	24	24.2	81	81.8
1977-78	110	73	66.4	26	23.6	99	90.0
1978-79	144	67	46.5	41	28.5	108	75.0
1979-80	114	104	91.2	50	43.9	154	135.0
1980-81	119	122	103	40	33.6	162	136.0
1981-82	167	133	79.6	41	24.6	174	104.0
1982-83	210	128	61.0	36	17.1	164	78.1
1983-84	318	208	65.4	48	15.1	256	80.5
1984-85	341	167	49.0	72	21.1	239	70.1
1985-86	628	206	32.8	61	9.71	267	42.5
1986-87	460	211	45.9	109	23.7	320	69.6
1987-88	533	167	31.3	104	19.5	271	50.8
1988-89	611	180	29.5	90	14.7	270	44.2
1989-90	801	232	29.0	141	17.6	373	46.6
1990-91	896	256	28.6	138	15.4	394	44.0
1991-92	1063	286	26.9	175	16.5	461	43.4
1992-93	1040	278	26.7	137	13.2	415	39.9
1993-94	1335	363	27.2	234	17.5	597	44.7
1994-95	1792	446	24.9	288	16.1	734	41.0
1995-96	1456	544	37.4	368	25.3	912	62.6
1996-97	1749	683	39.1	366	20.9	1049	60.0

Source: RBI Bulletin: issues related to Finances of state government 1974-75 to 1996-97.

6.6 Ratio of Developmental Capital Outlays and Developmental Loans to Capital Disbursements

The pace of capital formation in the State depends on the share of total developmental outlay and developmental loans in the total capital disbursements. Total developmental funds consist of developmental capital outlay and developmental loans made by the state government to autonomous bodies and institutions. These mainly include investment on social and economic services like education, health, housing agriculture, irrigation, energy, industry, transport, etc. The growth and magnitude of these investment in total capital disbursements, ultimately determine the pace of economic development of a State.

During the Fifth Plan period (1974-79) total developmental outlays and developmental loans as a proportion of total capital disbursements increased from 67.2 to 70.1 per cent. But in the Sixth Plan period after reaching the high of 82.9 per cent at the beginning, declined to 53.1 per cent by the final year of the Plan period (Table 6.9). The decline in investment was more pronounced during the Seventh Plan period when total developmental outlay and loans declined to a level of 56.7 per cent. But the share of total loans increased from 1990 and in the Eighth Five Year Plan (1992-97), developmental loans increased to 74 per cent of the total capital disbursements of Kerala.

**TABLE 6.9 : DEVELOPMENTAL CAPITAL OUTLAY AND DEVELOPMENTAL LOANS
AS PERCENTAGE OF TOTAL CAPITAL DISBURSEMENT OF KERALA
1974-75 TO 1996-97.**

(Rs. crores)

YEAR	DEVELOPMENTAL CAPITAL OUTLAY	DEVELOPMENTAL LOAN	TOTAL LOANS	TOTAL CAPITAL DISBURSEMENT	DEVELOPMENTAL CAPITAL OUTLAY AND DEVELOPMENTAL LOANS AS PER CENTAGE OF TOTAL CAPITAL DISBURSEMENT	DEVELOPMENTAL CAPITAL OUTLAY AND DEVELOPMENTAL LOANS AS PER CENTAGE OF CAPITAL OUTLAY AND LOANS AND ADVANCES
1	2	3	4 (2+3)	5	6	7
1974-75	31	28	59	89	66.3	95.0
1975-76	46	22	68	109	62.4	94.8
1976-77	55	21	76	134	56.7	98.7
1977-78	71	23	94	137	68.6	95.8
1978-79	65	38	103	148	69.6	95.6
1979-80	102	47	149	176	84.7	96.7
1980-81	118	37	155	188	82.4	95.9
1981-82	128	38	166	331	50.2	95.2
1982-83	125	32	157	213	73.7	90.2
1983-84	205	43	248	329	75.4	96.5
1984-85	162	68	230	433	53.1	95.8
1985-86	198	55	253	523	48.4	95.0
1986-87	201	104	305	507	60.2	95.2
1987-88	161	103	264	470	56.2	97.2
1988-89	173	89	262	460	57	96.8
1989-90	227	139	366	591	61.9	98.2
1990-91	248	137	385	552	69.7	97.7
1991-92	280	172	452	789	57.3	90.1
1992-93	268	133	401	707	56.7	96.8
1993-94	353	229	582	845	68.9	97.4
1994-95	432	284	716	892	80.3	97.5
1995-96	540	363	903	1096	82.4	96.9
1996-97	649	360	1009	1240	81.4	96.2
Annual average growth rate	16.8	17.0	15.4	14.9		

Source: RBI Bulletin: various issues

6.6.1 Developmental Capital Outlays and Developmental Loans as a Percentage of Total Capital Outlays and Loans and Advances

A more accurate measure of the investment realised in the State can be gauged by the percentage of developmental capital outlays and loans that has come out of the sum of Capital outlays and loans and advances by the State Government. In 1974-75, 95 per cent of the State's capital outlays and loans and advances was of developmental nature (Table 6.9). This high proportion of developmental capital outlay and loans remained unchanged throughout the period of study, and in 1996-97, 96.2 per cent of the State's investable funds were utilized for developmental purpose. During this period the ratio fluctuated between the high of 98.2 (1989-90) and the low of 90.2 per cent (1982-83).

6.7 Progressive Capital Outlay and Outstanding Loans and Advances as Percentage of Outstanding Public Debt of Kerala.

The capital formation that has taken place in Kerala as a result of government borrowings over a period of time can be gauged by the ratio of progressive capital outlays and outstanding loans by the State Government to the outstanding debt of Kerala. The progressive growth of capital outlay and outstanding loans exceeded the growth of outstanding public debt of Kerala until 1984-85. But after 1987-88, the situation changed and the ratio came down and outstanding debts of

TABLE 6.10: OUTSTANDING PUBLIC DEBT OF KERALA AS PERCENTAGE OF PROGRESSIVE CAPITAL OUTLAY 1974-75 TO 1996-97.

(Rs. Crore)

YEAR	OUTSTANDING PUBLIC DEBT	PROGRESSIVE CAPITAL OUTLAY	PROGRESSIVE CAPITAL OUTLAY AS PERCENTAGE OF OUTSTANDING PUBLIC DEBT 4	OUTSTANDING LOANS & ADVANCES BY STATE GOVERNMENT	OUTSTANDING LOANS & ADVANCES AS PERCENTAGE OF OUTSTANDING PUBLIC DEBT 6	PROGRESSIVE CAPITAL OUTLAY & OUTSTANDING STATE LOANS AS PERCENTAGE OF OUTSTANDING PUBLIC DEBT 7
1	2	3		5		
1974-75	565	385	68.1	233	41.2	109.4
1975-76	615	432	70.3	241	39.2	109.5
1976-77	665	489	73.6	251	37.7	111.3
1977-78	710	562	79.2	266	37.5	116.6
1978-79	856	629	73.5	296	34.6	108.1
1979-80	914	733	80.2	332	36.3	116.5
1980-81	1008	855	84.8	362	35.9	120.7
1981-82	1088	988	90.8	386	35.4	126.3
1982-83	1258	1117	88.8	402	32	120.8
1983-84	1581	1325	83.8	433	27.4	111.2
1984-85	1858	1491	80.3	463	24.9	105.2
1985-86	2237	1698	75.9	505	22.6	98.5
1986-87	2488	1912	76.8	583	23.4	100.3
1987-88	2830	2079	73.5	649	22.9	96.4
1988-89	2918	2198	75.3	708	24.3	99.6
1989-90	3502	2439	69.7	814	23.2	92.9
1990-91	4442	2715	61.1	931	21.0	82.1
1991-92	5191	3004	57.9	1084	20.9	78.8
1992-93	5905	3282	55.6	1201	20.3	75.9
1993-94	7199	3645	50.6	1401	19.5	70.1
1994-95	8821	4091	46.4	1664	18.9	65.2
1995-96	10309	4685	45.4	1967	19.1	64.5
1996-97	11671	5370	46	2250	19.3	65.3
Annual average growth rate	7.45	6.01	10.95			

Source: RBI, Report on Currency & Finances
Finance Accounts of Kerala, 1974-75 to 1996-97.

Kerala, exceeded the growth of capital formation in the State in the form of capital outlays and loans by the State Government. In the Annual

Plan (1990-92) and Eighth FYP period, this ratio further declined to 80.4 and 68.2 per cent. This points to the deceleration of capital formation efforts on the one hand and growing accumulation of public debt on the other hand. Debt servicing problems may develop if the income or revenue yielding investments fall short of the growth of outstanding debt. This also points to the increasing diversion of borrowed funds normally meant for capital formation. In the Eighth Plan period, more than half of the accumulated debt was not on account of the growth of productive investment in Kerala. The borrowed funds were diverted either to fill the revenue deficit or to repay old debts of the State Government.

6.8 Composition of Capital Outlays

Capital outlays and loans and advances by the State Government form major components of total capital disbursements. Table 6.11 presents a profile of the composition of capital outlays of the Government of Kerala from 1974-75 to 1996-97. Total capital outlays, are classified into developmental and non-developmental capital outlays. Composition of the total capital outlays shows that developmental capital outlay formed nearly 95 to 98 percentage of the total capital invested during the period of study. Non developmental capital outlays

YEAR	SECTOR WISE CLASSIFICATION OF CAPITAL OUTLAY OF KERALA										(RS. CRORES)	
	1	2	3	4	5	6	7	8	9	10	TOTAL DEVELOPMENTAL CAPITAL OUTLAY	TOTAL NON DEVELOPMENTAL CAPITAL OUTLAY
1974-75	10.2 (31.7)	8 (2.4)	8.1 (25.1)	21.3 (66.3)	0.9 (2.7)	10.5 (32.7)	31.5 (98.0)	6 (2.0)	32.1 (100)			
1975-76	12.5 (26.5)	9 (1.8)	10.2 (21.5)	33.9 (71.4)	3.0 (6.3)	16.8 (35.5)	46.4 (97.9)	1.0 (2.1)	47.4 (100)			
1976-77	10.6 (18.6)	1.8 (3.1)	9.4 (16.6)	44.3 (78.0)	0.2 (0.3)	25.2 (44.4)	54.9 (96.6)	1.9 (3.4)	56.8 (100)			
1977-78	13.6 (18.3)	2.9 (3.8)	9.5 (12.7)	59.4 (79.8)	0.4 (5.4)	35.0 (47.0)	73.0 (98.0)	1.5 (2.0)	74.5 (100)			
1978-79	-23.3 (-3.5)	4.1 (6.1)	-8.7 (-12.9)	67.5 (100.5)	5.2 (7.6)	41.5 (61.8)	65.2 (97.1)	2.0 (2.9)	67.1 (100)			
1979-80	18.5 (17.8)	2.8 (2.7)	14.0 (13.4)	83.6 (80.2)	4.8 (4.6)	42.9 (41.2)	102.1 (98.0)	2.1 (2.0)	104.2 (100)			
1980-81	23.0 (18.8)	3.2 (2.6)	17.4 (14.3)	95.2 (78.1)	9.6 (7.9)	48.9 (40.1)	118.2 (97.0)	3.7 (3.0)	121.9 (100)			
1981-82	32.2 (24.2)	5.9 (4.4)	23.4 (17.6)	95.6 (71.9)	5.0 (3.8)	53.6 (40.3)	127.8 (96.1)	5.2 (3.9)	132.9 (100)			
1982-83	33.2 (25.8)	4.1 (3.2)	26.6 (20.7)	92.2 (71.7)	5.3 (4.1)	54.6 (42.5)	125.4 (97.6)	3.1 (2.4)	128.5 (100)			
1983-84	90.4 (43.0)	4.4 (2.1)	77.4 (36.8)	114.3 (54.4)	7.1 (3.4)	65.2 (31.0)	204.6 (97.4)	5.5 (2.6)	210.1 (100)			
1984-85	45.3 (27.1)	4.8 (2.9)	35.4 (21.2)	116.6 (69.8)	8.9 (5.3)	69.1 (41.4)	162.0 (97.0)	5.1 (3.1)	167.1 (100)			
1985-86	44.7 (21.7)	8.1 (4.0)	14.5 (7.1)	153.3 (74.5)	17.2 (8.4)	70.4 (34.2)	198.0 (96.2)	7.8 (3.8)	205.8 (100)			
1986-87	56.5 (26.8)	7.8 (3.7)	19.9 (9.4)	144.8 (68.6)	20.1 (9.5)	60.6 (28.7)	201.2 (95.4)	9.8 (4.7)	211.1 (100)			
1987-88	44.1 (26.4)	3.6 (2.2)	17.7 (10.6)	116.8 (69.8)	4.1 (2.4)	55.5 (33.1)	160.9 (96.1)	6.5 (3.9)	167.4 (100)			
1988-89	23.0 (12.8)	4.6 (2.6)	12.8 (7.1)	150.1 (83.3)	14.2 (7.9)	64.6 (35.9)	173.2 (96.1)	7.1 (4.0)	180.3 (100)			
1989-90	25.6 (11.0)	6.8 (2.9)	11.3 (4.9)	201.1 (86.6)	22.6 (9.7)	86.4 (37.2)	226.6 (97.6)	5.7 (2.4)	232.3 (100)			
1990-91	35.2 (13.8)	19.5 (7.6)	9.2 (3.6)	213.2 (83.3)	32.8 (12.8)	76.7 (30.0)	248.4 (97.0)	7.6 (3.0)	256.0 (100)			
1991-92	32.6 (11.4)	17.9 (6.3)	9.1 (3.2)	247.7 (86.6)	43.6 (15.2)	90.8 (31.7)	280.3 (98.0)	5.9 (2.0)	286.1 (100)			
1992-93	39.1 (14.1)	23.3 (8.4)	9.1 (3.3)	229.1 (82.5)	30.9 (11.1)	95.6 (34.4)	268.2 (96.5)	9.7 (3.5)	277.9 (100)			
1993-94	47.7 (13.1)	25.9 (7.1)	14.2 (3.9)	304.9 (83.9)	24.9 (6.8)	131.5 (36.2)	352.6 (97.0)	10.8 (3.0)	363.3 (100)			
1994-95	44.3 (9.9)	21.7 (4.9)	13.4 (3.0)	387.5 (86.2)	44.7 (10.0)	137.4 (30.8)	431.8 (96.8)	14.2 (3.28)	446.0 (100)			
1995-96	69.0 (12.2)	22.5 (4.0)	18.3 (3.2)	471.0 (83.19)	58.9 (10.4)	170.5 (30.1)	540.0 (95.4)	23.4 (4.6)	563.5 (100)			
1996-97	88.0 (13.0)	29.3 (4.3)	17.5 (2.6)	560.7 (82.58)	66.2 (9.75)	204.3 (30.1)	648.7 (95.5)	33.9 (4.5)	682.6 (100)			
Annual average growth rate (%)	-30.42	27.18	-9.58	17.48	144.77	15.77	16.83	25.87	16.85			

Note: Figures in brackets are percentage to total.

Source: RBI Bulletin: Finances of State Government 1974-75 to 1996-97.

on general services and loans to Government employees constituted a very insignificant (less than 5 per cent) portion of total capital outlays of Kerala.

6.8.1 Developmental Capital Outlay

Developmental capital outlays are on social and economic services. Under social services, investments in education, medical and public health, water supply, housing, urban development, social security and welfare of backward classes are included. Economic services include agriculture and allied activities, industry, water and power development, transport and communication, science and technology, etc.

6.8.2 Economic Services

The composition of developmental capital outlay shows the increasing share of economic services. The beginning of the Fifth Plan period (1974-75), economic services formed 66.3 per cent of the total developmental outlay. It steadily increased and during the Sixth Plan period reached 70 per cent in 1984-85. During the Seventh and Eighth Plan periods, economic services got 77 and 83 per cent of the developmental capital outlay of the State.

6.8.3 Outlay on Water and Power Development

Among the various items under economic services, it is the investments in irrigation, flood control and power development that takes away a major portion of the developmental outlay of the State. During the Fifth Plan period, nearly 44 per cent of the developmental capital outlays was spent on water and power development. But the investment on these gradually declined in the subsequent Five Year Plans in Kerala. It was only 39 per cent in the Sixth Five Year Plan period. But during the Seventh and Eighth Five Year Plan periods, Kerala's investment on the development of water and power came down further to 34 and 33 per cent respectively.

6.8.4 Outlay on Agriculture and Allied Activities

Agriculture and allied activities as a whole did not get adequate investment in the State Government scheme of developmental outlay during the period of study. In the Fifth and Sixth Five Year Plan periods, agriculture and allied activities received only 4.5 per cent of total developmental outlay. The investment on these heads marginally improved in the subsequent Plans. During the Seventh and Eighth Plan periods, outlay on agriculture and allied sectors increased to 7.6 and 9.6

er cent. The low priority accorded to this vital sector is evident from the less than 10 per cent investment made in successive Plans by the State Government.

6.8.5 Outlay on Industry and Minerals

The developmental capital outlay on industry and minerals was very low compared to the investment in other sectors. In 1985-86, the investment on this sector was only 9 per cent of the total capital outlay. But it increased to 14.6 per cent by 1989-90 and the increase in the nineties was marginal. In 1996-97 it reached 16.2 per cent (Appendix 6.1). This low level of capital outlay on industry reflects Kerala's past priorities in favour of social services at the expense of economic services. This partly explains the state of present economic stagnation. The growth of Kerala's social infrastructure (education and health) was not supplemented by adequate State investment in the industrial sector to trigger off an industrial development. So the low investment in industry by the State Government along with the declining of developmental outlay in water and power development and the insignificant investment in agriculture and allied sectors may partly explain the state of industrial backwardness and agricultural stagnation prevalent in Kerala.

6.8.6 Outlay on Transport

The developmental capital outlay on transport is distributed among various areas like ports, lighthouses, shipping, civil aviation, roads, bridges, road transport, inland water transport, etc. The developmental capital outlay on this sector was high when compared with industrial sector. In 1985-86, it was 16.2 per cent and by 1989-90 it came up to 24.4 per cent. But in the nineties, State investment declined and by 1996-97, it reached 20.8 per cent of the total capital outlay (Appendix 6.1).

6.9 Social Services

Developmental capital outlay on social services was lower compared to outlay on economic services. Kerala economy, notable for the development of social and community services, interestingly, is now faced with a situation of falling developmental capital outlay on these items. During the Fifth Plan period social services received 23 per cent of the developmental capital outlay. But the Sixth Plan period saw the highest share of 27.8 per cent. After that, investments in social services declined rapidly to 19.7 and 12.4 per cent during the Seventh and Eighth Plan periods. This set limits to the State's lead in social services. The

declining share of developmental capital outlay on social services reflects the inability of the State to undertake new schemes and service earlier schemes. The underutilisation of capacities built in the past leads to waste of public expenditure.

6.9.1 Education and Related Services

The decline in the developmental outlay in social services as whole kept the share of education and related services at a low level. During the Fifth Plan period education, sports, arts and culture accounted for only 3.4 per cent of the capital outlay incurred by Kerala. The share of this sector declined further during the Sixth and Seventh Five Year Plan period to 2.5 and 3.1 per cent respectively. But during the Annual Plan period (1990-92) and Eighth Plan periods (1992-97), though the share of social services as whole declined in total capital outlay, education and related services received increased allocation of 7.3 and 5.7 per cent of capital outlay. During the 23 year period of study, capital investment on education and related services registered an annual average growth rate of 27.2 per cent.

6.9.2 Medical, Public Health and Family Welfare

The share of medical and public health services in total capital

outlay was considerably high till the Sixth Five Year Plan. In 1974-75, it was at the level of 25.1 per cent and by the end of 1984-85, it came down to 21.2 per cent. During the period 1974-75 to 1984-85, nearly 80 per cent of resources in social services were utilized for medical and public health services by the Government of Kerala. In the Seventh Plan period the proportion declined, though it still remained higher than the share of education and other social services. By the beginning of the 1990s, capital outlay on medical and finally health declined to 3 per cent, a level lower than that of education and related services in social services. On the whole, public investments in these sectors recorded a negative growth rate of 9.6 per cent per annum. Thus social services as a whole received falling public investment share and in social services outlay on education and related services increased from its low initial base and the share of medical and public health services declined considerably from the initial high level to a negligible low level. But loans and advances made by the Government of Kerala to third parties can also influence the level of investment in social and economic services of the State. This has other implications on the Kerala model of development. The impressive infrastructure built up by the State, in terms of hospitals and medical personnel may remain underutilised at a time when the expenditure requirements on health are rising. The State's relatively high quantitative achievements in the field of literacy

and general education has been at the cost of quality. The educational institutions in the State lack adequate facilities. A cut in expenditure on education may strike at the very root of the Kerala model of development.

6.10 Composition of Loans and Advances

Loans and advances are given for a variety of purposes like housing, co-operatives, power projects, village and small scale industries, etc. These advances form a major part of debt financed capital disbursement, and repayment of these loans back to the State Government reduces the net repayment burden of State public debt. The aggregate loans and advances made by the Government of Kerala increased from Rs.31 crores in 1974-75 to Rs.366 crores in 1996-97 showing an annual average growth rate of 15 per cent (Table 6.12).

Loans for developmental purposes are predominant in the aggregate loans and advances made by the Government of Kerala. During the Fifth Plan period, it formed nearly 90 per cent of the aggregate loans and advances. This high proportion gradually increased and by the end of the Eighth Plan period, 98 per cent of the State Government's loans and advances were developmental in nature. These are distributed among social and economic services.

TABLE 6.12: NET BORROWING: CUMULATIVE AID FROM GOVERNMENT AND ADVANCES 1974-75 TO 1996-97.
(Rs. Crores)

YEAR	LOANS FOR DEWENT PURPOSES	2	3	4	5	6	7	8	9	10	11
1974-75	28.1 (91.7)	2.7 (8.8)	0.5 (1.6)	25.5 (82.93)	3.6 (11.7)	7.8 (25.30)	11.3 (36.9)	2.6 (8.3)	2.5 (8.1)	30.7 (100)	
1975-76	21.8 (89.0)	2.6 (10.4)	0.7 (2.9)	19.3 (78.57)	5.5 (22.3)	3.1 (12.50)	9.3 (37.7)	2.7 (11.0)	2.5 (10.3)	24.5 (100)	
1976-77	21.7 (88.9)	5.7 (23.1)	0.8 (3.2)	16.1 (65.81)	5.0 (20.5)	4.4 (18.10)	3.6 (14.7)	2.7 (11.1)	2.5 (10.3)	24.5 (100)	
1977-78	23.5 (88.5)	5.7 (21.6)	1 (3.7)	17.7 (66.83)	6.0 (22.6)	5.1 (19.20)	2.8 (10.6)	3.1 (11.5)	3.0 (11.4)	26.5 (100)	
1978-79	38.3 (93.2)	10.0 (24.4)	2.2 (5.4)	28.2 (68.81)	3.0 (7.3)	2.4 (5.73)	7.4 (18.1)	2.8 (6.8)	2.8 (6.8)	41.0 (100)	
1979-80	46.6 (94.1)	7.2 (14.5)	1.4 (2.9)	39.5 (79.64)	3.3 (6.7)	3.1 (6.15)	1.8 (3.6)	2.9 (5.9)	2.9 (5.9)	49.6 (100)	
1980-81	37.5 (92.8)	10.1 (25.1)	3.1 (7.7)	27.4 (67.71)	5.6 (13.9)	2.7 (6.78)	5.2 (12.9)	2.9 (7.2)	2.9 (7.2)	40.4 (100)	
1981-82	38.1 (92.4)	9.8 (23.8)	3.6 (8.8)	28.3 (68.54)	6.2 (15.1)	3.8 (9.22)	2.4 (5.7)	3.1 (7.6)	3.1 (7.6)	41.2 (100)	
1982-83	31.7 (88.1)	7.9 (22.1)	2.3 (6.5)	23.8 (66.03)	9.3 (25.7)	2.8 (7.78)	NA NA	4.3 (11.9)	4.3 (11.9)	36.0 (100)	
1983-84	42.7 (89.5)	6.8 (14.3)	1.4 (2.9)	36.2 (75.83)	15.4 (32.3)	3.4 (7.17)	1.0 (2.1)	5.0 (10.5)	5.0 (10.5)	47.7 (100)	
1984-85	67.7 (93.4)	8.3 (11.5)	1.8 (2.5)	59.3 (81.84)	8.0 (11.0)	3.8 (5.28)	34.8 (48.0)	4.8 (6.7)	4.8 (6.7)	72.5 (100)	
1985-86	55.3 (91.1)	21.5 (35.4)	1 (1.7)	33.8 (55.72)	5.3 (8.8)	1.1 (1.85)	5.5 (9.0)	5.4 (8.9)	5.4 (8.9)	60.6 (100)	
1986-87	109.2 (95.2)	34.4 (30.0)	4.3 (3.8)	69.3 (60.42)	1.7 (1.5)	2.1 (1.80)	30.5 (26.6)	5.5 (4.9)	5.5 (4.9)	114.7 (100)	
1987-88	102.6 (98.8)	35.3 (34.0)	0.3 (0.3)	67.3 (64.82)	2.1 (2.0)	6.1 (5.83)	32.6 (31.4)	1.2 (1.2)	1.2 (1.2)	103.8 (100)	
1988-89	89.26 (98.8)	30.8 (34.1)	0.9 (0.96)	58.4 (64.66)	3.0 (3.3)	4.6 (5.07)	11.7 (12.9)	1.1 (1.2)	1.1 (1.2)	90.4 (100)	
1989-90	139.5 (99.2)	28.7 (20.4)	1 (0.72)	110.8 (78.80)	6.7 (4.8)	3.4 (2.39)	68.4 (48.7)	1.1 (0.8)	1.1 (0.8)	140.6 (100)	
1990-91	136.8 (99.0)	34.7 (25.1)	1.8 (1.27)	102.1 (73.84)	5.7 (4.2)	4.1 (2.96)	59.7 (43.2)	1.4 (1.0)	1.4 (1.0)	138.3 (100)	
1991-92	172.4 (98.5)	47.2 (27.0)	2 (1.15)	125.2 (71.48)	8.8 (5.0)	6 (3.40)	57.5 (32.8)	2.7 (1.6)	2.7 (1.6)	175.1 (100)	
1992-93	133.3 (97.3)	59.0 (43.0)	0.2 (0.13)	74.3 (54.22)	6.4 (4.7)	5.7 (4.16)	20.4 (14.8)	3.8 (2.7)	3.8 (2.7)	137.1 (100)	
1993-94	229.2 (98.0)	74.2 (31.7)	7.3 (3.12)	155.0 (66.26)	15.1 (6.5)	9.8 (4.19)	70.4 (30.1)	4.7 (2.0)	4.7 (2.0)	234.0 (100)	
1994-95	284.3 (98.5)	84.2 (29.2)	8.3 (2.89)	200.1 (69.36)	15.3 (5.3)	3 (1.04)	81.0 (28.1)	4.2 (1.5)	4.2 (1.5)	288.5 (100)	
1995-96	362.7 (98.5)	80.4 (21.9)	4.7 (1.29)	282.2 (76.67)	6.23 (1.7)	1.4 (0.37)	134.3 (36.5)	5.4 (1.5)	5.4 (1.5)	368.1 (100)	
1996-97	360.2 (98.4)	99.3 (27.1)	5.1 (1.38)	260.9 (71.3)	22.2 (6.1)	4.4 (1.19)	81.1 (22.1)	6.0 (1.7)	6.0 (1.6)	366.2 (100)	
Annual average growth rate (%)	17.04	23.59	208.31	18.03	20.43	12.24	208.87	9.35	9.75	15.08	

Note: Figures in the brackets are percentage to total.

Source: RBI Bulletin: issues related to Finances of state government 1974-75 to 1996-97.

Loans for developmental purposes under social services are given mainly for housing. These loans increased from Rs.3 crores in 1974-75 to Rs.99 crores in 1996-97 showing a growth rate of 23.6 per cent per annum. The growth of these loans were marked by fluctuations until the end of the Seventh Plan period. As a proportion of total developmental loans, the share of social services increased steadily over the Five Year Plan period. During Fifth and Sixth Five Year Plan periods, social services received only 17.7 and 19.3 per cent of State Government loans. But during the Seventh and Eighth Plan periods, its share increased to 30.8 and 30.6 per cent respectively.

Total loans given by the State Government for housing to various agencies like co-operatives and housing boards increased in absolute amount during the period of study. But as a proportion of total developmental loans, these loans declined after the Sixth Plan period even from its initial low level. By the end of the Eighth Plan period, loans for housing purposes declined to less than 2 per cent of total developmental loans (Table 6.12).

3.1 Developmental Loans for Economic Services

Developmental loans advanced by the State Government increased considerably during the period of study. It increased from Rs.26 crores in 1974-75 to Rs.261 crores in 1996-97 recording a growth rate of 18 per cent per annum. The share of economic services in total developmental loans made by the Government of Kerala, declined from 72 per cent in the Seventh Plan onwards. During the Fifth and Sixth Plan periods, economic services as a group received 72 per cent of the State Government's loans. This came down to 64.9 and 67.5 per cent during the Seventh and Eighth Plan periods.

Among the various economic services, agriculture and allied activities, power projects and co-operatives received the major share of the loans advanced by the State Government. Loans to power projects are loans advanced by the State Government to the public sector, Kerala State Electricity Board for its various activities like generation and distribution of power. Loans to the State Electricity Board varied considerably between the Fifth and Eighth Five Year Plan periods. During the Fifth Plan period, 23.5 per cent of the total developmental loans went into the power sector. But in the Sixth Plan period, the share of it came down to 17.1 per cent. Though economic services as a whole

received less developmental loans, power projects in that group received an increased share of 25.7 and 26.3 per cent of the developmental loans of Kerala during the Seventh and Eighth FYPs.

The loans for agriculture, targeted mainly at crop husbandry and soil and water conservation, declined considerably as a proportion of aggregate loans and advances during the period of study. Between 1974-75 and 1996-97, it registered only a growth rate of 12.2 per cent, less than the average growth rate of aggregate loans and developmental loans of Kerala during the period. It declined from 15 per cent in the Fifth Plan period to 7.2 per cent during the Sixth Plan period. But the Seventh and Eighth Plan periods witnessed a sharp decline in the share of developmental loans in agriculture to 3.4 and 2.2 per cent of aggregate loans made by the Government of Kerala.

Another sector which experienced a similar drop in State Government loans, was the co-operative. In absolute terms, loans to co-operative societies mainly in the form of capital contribution increased from Rs. 4 crores in 1974-75 to Rs 22 crores in 1996-97 setting a growth rate of 20.4 per cent per annum. As a proportion of aggregate loans, its share declined steadily from the Fifth to Eighth Five Year Plans. During the Fifth and Sixth Five Year Plans, share of co-

operatives in total loans was 12.3 and 19.6 per cent. But in the Seventh and Eighth Plan periods, this came down to 4.1 and 4.8 per cent. Thus agriculture and co-operation were the candidates for cut when economic services received a declining share of government's aggregate loans during the period of study.

6.10.2 Non-Developmental Loans by the State Government

Non-developmental loans by the Government of Kerala are mainly loans given as house building advances and advances for motor conveyance to its employees. These loans increased from Rs 3 crores in 1974-75 to Rs 6 crores in 1996-97 registering an annual average growth rate of 9.4 per cent. As a proportion of aggregate loans and advances, non-developmental loans declined considerably during the 23 year period of study.

The composition of the loans advanced by the Government of Kerala between 1974-75 and 1996-97 reveals that the developmental loans are predominant. The rise in the share of social services in aggregate loans from the Seventh Five Year Plan has been at the expense of the share of economic services. But the fall in the share of economic services does not act as a limiting factor for increasing the loans to the

power sector. Non- developmental loans have been reduced to an insignificant level by the end of the Eighth Plan period.

6.11 Conclusion

The expenditure pattern of Kerala during the period of study highlights the predominance of consumption expenditure over capital formation. The basic reason for this high level of consumption expenditure in aggregate expenditure stems from the high revenue component of Kerala's budgetary operations. The revenue deficit of Kerala measured in terms of the Gross Fiscal Deficit (GFD) is financed by borrowing. In other words, the expenditure pattern of Kerala shows diversion of borrowed funds on a regular basis for meeting current consumption. The State is unable to spend adequately not only on economic services, but also on social and community services. Thus the fiscal crisis of the State manifested in the form of revenue deficit financed by borrowing may set limits to Kerala's present development pattern and future prospects of economic growth. The diversion of borrowed funds for consumption and the inadequate yield from debt financed capital outlay may pose severe problems in the servicing of Kerala's public debt.

References:

1. Govinda Rao, M. and Tulasidhar,U.B., *Public Expenditure in India: Emerging Trends*. NIPFP working papers, No. 5 National Institute of Public Finance and Policy, New Delhi, 1991.
2. Govinda Rao, M., *A proposal for State level budgetary reforms*, EPW Feb I, 1992.
3. George,K.K., *Limits to Kerala Model of Development*, Centre for Development Studies, Trivandrum, 1993.

CHAPTER 7

DEBT SERVICING BURDEN AND DEBT RELIEF

1.1 Introduction

Growth of public debt brings along with it the problem of debt servicing. Servicing of debt includes the repayment of debt and interest payments. This has implications to both the revenue and capital accounts of the State's budget. In the past amortization/sinking fund methods were used to service debt. It was formerly customary to build up a sinking fund by paying into it a certain sum each year from government revenue for the eventual redemption of the debt. On the basis of the advice given by the Reserve Bank of India, no sinking fund is maintained for loans floated by Government from 1975 onwards. Debt becomes a burden when debt financed investments or projects do not yield sufficient returns to meet the interest and repayment obligations. The growth of income or output is a crucial factor that increases or lessens the burden of debt in an economy. This chapter attempts to explain the debt-servicing burden of

Kerala in the background of the growing outstanding debt of the State. The debt reliefs recommended by various Finance Commissions to Kerala also have been taken up. During the period of study, as noticed in Chapter Five, the Government of Kerala borrowed funds on an increasing scale not only to finance its capital disbursements but also to meet revenue deficit. Consequently, the outstanding debt liabilities of the Government of Kerala increased considerably. Composition of outstanding debt between 1974-75 and 1996-97 shows that outstanding loans from the Centre form the major portion of the total outstanding debt liabilities. The share of outstanding internal debt and outstanding provident funds and small savings increased substantially during the same period.

7.2 Growth and Composition of Interest Payments of the Government of Kerala: 1974-75 to 1996-97

7.2.1 Gross Interest Payments

The gross interest payments of the Government of Kerala increased from Rs 25 crores in 1974-75 to Rs 1107 crores in 1996-97, registering a growth rate of 23 per cent per annum (Table 7.1). The rise in gross interest payments has been steady and continuous. During the Fifth Plan period, it increased at an annual average rate of 13.2 per cent. In the Sixth Plan period, it registered the highest growth rate of 23.3 per cent per annum. In the Seventh and Eighth Plan periods, though there was a

marginal fall, gross interest payments increased at 19.8 and 18.1 per cent per annum respectively.

7.2.2 Interest Payments on Loans from the Centre

Interest payments on Central loans constitute the major portion of the gross interest payments of Kerala. In absolute magnitude, it increased from Rs 16 crores in 1974-75 to Rs 482 crores in 1996-97 showing a growth rate of 22.7 per cent per annum (Table 7.1). This is lower than the growth rate of gross interest payment as a whole. During the Fifth Plan period, it recorded an average growth rate of 8.5 per cent per year. But by the Sixth, Seventh and Eighth Plan periods, it rose to 22.8, 27.5 and 26.8 per cent respectively. As a proportion of the gross interest payments, interest payments on Central loans steadily declined. In the Fifth Plan period, it was as high as 60.4 per cent. But in subsequent plans, it declined, and in the Sixth and Seventh Plan periods, it was 45 and 53.7 per cent of gross interest payments. In the final year of the Eighth Plan, it came down to 43.5 per cent. This can be attributed to the debt relief granted by the Ninth and Tenth Finance Commissions. The other reason is the fall in the share of Central loans to the State as noted in the previous chapters.

**TABLE 7.1: GROWTH AND COMPOSITION OF INTEREST PAYMENTS
1974-75 TO 1996-97.**

(Rs. Crores)

YEAR	INTEREST ON INTERNAL DEBT	INTEREST ON LOANS FROM THE CENTRE	INTEREST ON PF, SMALL SAVINGS AND OTHERS	GROSS INTEREST PAYMENT
1	2	3	4	5
1974-75	4.9 (19.89)	15.7 (63.74)	4.1 (16.36)	24.7 (100)
1975-76	5.8 (19.18)	19.3 (64.30)	4.9 (16.52)	30.0 (100)
1976-77	7.3 (21.75)	20.2 (60.10)	6.1 (18.15)	33.6 (100)
1977-78	9.1 (23.95)	21.3 (56.11)	7.6 (19.94)	38.0 (100)
1978-79	7.0 (17.37)	23.3 (57.88)	10.0 (24.75)	40.3 (100)
1979-80	7.9 (17.69)	24.7 (55.44)	12.0 (26.87)	44.5 (100)
1980-81	9.4 (20.62)	22.0 (48.24)	14.2 (31.13)	45.6 (100)
1981-82	13.2 (23.16)	26.5 (46.49)	17.3 (30.35)	57.0 (100)
1982-83	20.8 (33.90)	22.6 (36.84)	18.0 (29.26)	61.4 (100)
1983-84	24.3 (26.52)	45.2 (49.36)	22.1 (24.11)	91.5 (100)
1984-85	40.0 (33.05)	53.8 (44.47)	27.2 (22.48)	121.1 (100)
1985-86	42.1 (38.18)	48.6 (44.05)	36.7 (17.76)	127.5 (100)
1986-87	29.4 (18.75)	104.3 (66.53)	43.6 (14.72)	177.3 (100)
1987-88	50.5 (25.25)	108.8 (54.38)	53.9 (20.37)	213.2 (100)
1988-89	56.7 (24.77)	126.5 (55.28)	61.2 (19.96)	244.5 (100)
1989-90	78.8 (26.92)	141.8 (48.39)	72.4 (24.69)	293.0 (100)
1990-91	97.6 (28.64)	138.3 (40.61)	104.8 (30.74)	340.6 (100)
1991-92	124.6 (25.78)	231.2 (47.82)	127.7 (26.40)	483.4 (100)
1992-93	149.8 (30.52)	127.6 (25.98)	265.1 (43.51)	542.5 (100)
1993-94	180.9 (26.33)	278.2 (40.48)	228.1 (33.19)	687.2 (100)
1994-95	216.4 (26.40)	330.7 (40.35)	272.6 (33.25)	819.7 (100)
1995-96	271.3 (28.19)	418.1 (43.44)	273.1 (28.37)	962.4 (100)
1996-97	336.9 (30.44)	481.8 (43.54)	287.9 (26.02)	1106.6 (100)
Annual average growth rate	23.50	22.65	23.41	23.04

Note: Figures in the brackets are percentage to total

Source: RBI Bulletins various issues

7.2.3 Interest Payments on Internal Debt

Interest payments on internal debt, comprising of market loans and negotiable loans, increased both in absolute amount and as a proportion of gross interest payments during the period of study. It increased from Rs. 5

crores in 1974-75 to Rs.337 crores in 1996-97 registering an annual average growth rate of 23.5 per cent (Table 7.1). The share of interest payments on market borrowings which was only 15.4 per cent of gross interest payments in 1985-86 increased to 24.4 per cent in 1996-97. But the share of interest payments on negotiated loans declined from 17.6 to 4.3 per cent during the same period. So increase in the growth of interest payment on internal debt is mainly on account of the growth of interest payment on market borrowings of Kerala (see Appendix 7.1).

7.2.4 Interest Payments on Provident Fund and Small Savings

These payments comprise mainly the interest on the balances at the credit of government employees in state provident funds, State Government's insurance funds, family pension funds and balance in the savings deposits in treasuries. In absolute terms, these interest payments increased from Rs 4 crores in 1974-75 to Rs 288 crores in 1996-97 showing a growth rate of 23.4 per cent per annum. As a proportion of gross interest payments, interest on provident fund and small savings formed 19.1 and 27.4 per cent during the Fifth and Sixth Plan periods. It came down to 19.5 per cent in the Seventh Five Year Plan period. In the Eighth Plan, interest payments on provident funds and small savings came up to 32.8 per cent of the State's gross interest payments. At this level,

the proportion of interest payment on provident funds and small savings exceeded the same on internal debt of Kerala.

Interest payment on State Provident Fund which constituted 21.5 per cent of gross interest payments in 1985-86 declined to 19.4 per cent in 1996-97. During the same period, the share of interest payments on Small Savings remained at 6.7 and 5.6 per cent. The interest payment on other items like insurance funds, and family pension funds constituted only around 2 per cent of gross interest payments of the State (see Appendix 7.1).

7.3 Gross and Net Interest Payments of Kerala: 1974-75 to 1996-97

Gross interest payments of Kerala increased with the increase in the State's public debt. At the same time, the State Government receives interest payments from various sources as non-tax revenue forming part of the revenue receipts. These interest receipts come from

- a) Interest from Departmental Commercial Undertakings.
- b) Interest from cultivators.
- c) Interest realised on investment of cash balances
- d) Interest from public sector and other undertaking

- e) Interest from local bodies and
f) Interest from co-operative societies.

TABLE 7.2: GROSS AND NET INTEREST PAYMENTS 1974-75 to 1996-97.

(Rs. Crores)

YEAR	GROSS INTEREST PAYMENTS	INTEREST RECEIVED	NET INTEREST PAYMENTS	INTEREST PAYMENTS/SDP RATIO	INTEREST RECEIVED AS PERCENTAGE OF GROSS INTEREST PAYMENTS
1	2	3	4	5	6
1974-75	24.7	13.5	11.1	1.3	54.7
1975-76	30.0	9.6	20.4	1.4	32.0
1976-77	33.6	7.9	25.7	1.5	23.5
1977-78	38.0	13.3	24.7	1.6	35.0
1978-79	40.3	17.5	22.8	1.5	43.4
1979-80	44.5	38.0	6.5	1.5	85.4
1980-81	45.6	9.0	36.6	1.2	19.7
1981-82	57.0	3.9	53.2	1.5	6.8
1982-83	61.4	10.2	51.2	1.3	16.6
1983-84	91.5	9.5	82.0	1.7	10.4
1984-85	121.1	30.6	90.4	2.0	25.3
1985-86	127.5	24.1	103.4	2.0	18.9
1986-87	177.3	35.5	141.8	2.4	20.0
1987-88	213.2	38.4	174.8	2.6	18.0
1988-89	244.5	26.1	218.4	2.7	10.7
1989-90	293.0	17.9	275.1	2.7	6.1
1990-91	340.6	21.4	319.2	2.8	6.3
1991-92	483.4	19.5	463.9	3.2	4.0
1992-93	542.5	23.1	519.4	3.2	4.3
1993-94	687.2	27.6	659.6	3.5	4.0
1994-95	819.7	37.8	781.9	3.7	4.6
1995-96	962.4	55.2	907.2	3.9	5.7
1996-97	1106.6	55.7	1048	3.9	5.0
Annual (%) average growth rate	23.04	22.94	39.9		

Source: RBI bulletin various issues

The interest from public sector and other undertakings declined steadily. But the interest from Departmental Commercial Undertakings

reased during the same period. Similarly interest realised on investment of Cash Balances and interest from Co-operative Societies are other items of receipts which increased during the period (Appendix 7.2).

Net interest payment of the State Government is calculated as gross interest payment liability of the State Government minus interest received from the Government of Kerala during the same period (Table 7.2).

3.1 Ratio of Interest Receipts to Outstanding Loans Advanced by Kerala: 1974-75 to 1996-97

The ratio of interest receipts to outstanding loans advanced by the State Government declined considerably during the plan periods. (Table 4.3). The ratio was 4.8 per cent during the Fifth FYP period. It declined to 3 per cent in the Sixth FYP. The situation slightly improved during the Seventh FYP period when it came to 4.5 per cent. The interest receipts on State Government loans were reduced to a trifle during the nineties. During the Annual Plan (1990-1992) period, it was only 2 per cent. In the Eighth FYP period it remained at a low level of 2.3 per cent.

A detailed examination of the interest receipts of Kerala shows that the interest from public sector and other undertakings which formed 50.3 per cent of total interest receipts in 1985-86, declined to 20.6 per cent in 1989-90 and by 1996-97 its share was only 8.2 per cent (see Appendix

TABLE 7.3: RATIO OF INTEREST RECEIPTS TO OUTSTANDING LOANS OF THE GOVERNMENT OF KERALA, 1974-75 TO 1996-97.

(Rs. Crores)

YEAR 1	OUTSTANDING LOANS 2	INTEREST RECEIPTS 3	RATIOS (%) 4
1974-75	233	13.5	5.8
1975-76	241	9.6	4.0
1976-77	251	7.9	3.2
1977-78	266	13.3	5.0
1978-79	296	17.6	5.9
1979-80	331.9	38	11.4
1980-81	361.8	9.0	2.5
1981-82	385.6	3.9	1.0
1982-83	402.4	10.2	2.5
1983-84	433	9.5	2.2
1984-85	462.9	30.6	6.6
1985-86	505	24.1	4.8
1986-87	582.7	35.5	6.1
1987-88	649	38.4	5.9
1988-89	707.8	26.1	3.7
1989-90	814	17.9	2.2
1990-91	931	21.4	2.3
1991-92	1084	19.5	1.8
1992-93	1201	23.1	1.9
1993-94	1401	27.6	2.0
1994-95	1664	37.8	2.3
1995-96	1967	55.2	2.8
1996-97	2250	55.7	2.5

Source: RBI Bulletins and Finance Account of Kerala

7.2). Similarly, interest from Departmental Commercial Undertakings stagnated, and remained at 30.5 per cent in 1996-97, a level very close to what prevailed in 1985-86 (28.3 per cent). But interest receipts on investment of cash balances which was only 10 per cent in 1985-86 and remained low till 1993-94, increased to 38.5 per cent of total interest receipts in 1996-97. As noted in the previous chapter, the arrears in recovery of amounts overdue to the State Government at the end of March

1997 was Rs. 931 crores. This include Rs.303 crores by way of principal and Rs. 628 crores as interest. The amount due from the Kerala State Road Transport Corporation (KSRTC) (principal Rs. 41 crore + interest Rs. 40 crores), Kerala State Electricity Board (KSEB) (principal Rs. 161 crore + interest Rs. 466 crores) and Kerala Water Authority (KWA) (principal Rs. 91 crore + interest Rs. 113 crores) can partly explain the decline in the ratio interest receipts to total outstanding loan of Kerala. In the case of KSRTC, the State Government had to write off dues from the corporation to the tune of Rs. 84 crores during 1980-81 and 1986-87.

3.2 Gross Interest Payments /SDP Ratio

Gross interest payments/SDP ratio remained at less than 2 per cent till 1983-84. From 1984-85 the ratio gradually increased and came up to 2.8 per cent in 1990-91. In the early nineties interest payments increased and reached 3.9 per cent of SDP in 1996-97 (Table 7.2).

3.4 Growth and Composition of Repayment of Debt

Rising debt of the State Government brings along with it the problem of repayments of debt. These repayments are made out of the capital receipts of the State Government. Faced with persisting revenue

ficits, Kerala cannot operationalise other methods of debt repayments
e amortization sinking fund which is based on revenue surplus. So the
agnitude of debt repayment has a financial impact on the capital
bursements of the State Government. The repayment of Central loans
fects the net availability of these loans to the State. Table 7.4 analyses
e growth and composition of the repayment burden of the State
overnment debt. Total repayment of Kerala increased from Rs 26 crores
1974-75 to Rs 190 crores in 1996-97 recording a growth rate of 34.8
er cent. This growth in repayments was marked by wide fluctuations
uring the period of study.

4.1 Repayment to Centre

This growth in repayment was mainly on account of the rapid
growth of repayment to the Centre. Repayment to the Centre increased
from Rs.20 crores in 1974-75 to Rs.167 crores in 1996-97 showing an
average growth rate of 44.6 per cent per annum.

Composition of total repayments shows that repayment to Centre
constitutes the major portion of the total repayment of Kerala during the
period of study. It formed 76.6 per cent of total repayment in 1974-75
and by 1996-97 it came up to 87.7 per cent. During the Fifth and Sixth

Plan periods repayments to the Centre formed 86.6 and 83.7 per cent of the total repayments. But during the Seventh and Eighth Plan periods, 90.5 and 85.6 per cent of Kerala's repayments were on account of Central loans. This had drastically reduced the net availability of Central loans to the State.

TABLE 7.4: GROWTH AND COMPOSITION OF REPAYMENTS

(Rs crores)

YEAR	REPAYMENT OF INTERNAL DEBT	REPAYMENTS TO THE CENTRE	TOTAL REPAYMENTS	REPAYMENTS TO CENTRE AS PERCENTAGE OF TOTAL REPAYMENTS
1	2	3	4	5
1974-75	6.1 (23.4)	19.9 (76.6)	26.0 (100)	76.6
1975-76	1.7 (4.7)	35.6 (95.3)	37.4 (100)	95.4
1976-77	5.4 (10.2)	47.6 (89.8)	53.0 (100)	89.8
1977-78	5.2 (14.6)	30.3 (85.4)	35.5 (100)	85.4
1978-79	5.1 (13.9)	31.3 (86.1)	36.4 (100)	86.1
1979-80	5.7 (25.6)	16.7 (74.4)	22.4 (100)	74.4
1980-81	6.8 (26.7)	18.7 (73.3)	25.6 (100)	73.3
1981-82	9.3 (5.9)	147.7 (94.1)	157.0 (100)	94.1
1982-83	9.1 (18.9)	39.3 (81.1)	48.5 (100)	81.1
1983-84	11.8 (17.8)	54.7 (82.2)	66.6 (100)	82.2
1984-85	24.2 (12.3)	172.1 (87.7)	196.3 (100)	87.7
1985-86	16.4 (6.4)	240.5 (93.6)	256.8 (100)	93.6
1986-87	15.3 (8.2)	171.3 (91.8)	186.7 (100)	91.8
1987-88	17.7 (8.9)	181.5 (91.1)	199.2 (100)	91.1
1988-89	21.3 (11.3)	168.0 (88.7)	189.3 (100)	88.7
1989-90	27.4 (12.6)	190.6 (87.4)	218.0 (100)	87.5
1990-91	18.7 (11.9)	138.6 (88.1)	157.3 (100)	88.1
1991-92	21.5 (6.6)	305.9 (93.4)	327.4 (100)	93.4
1992-93	48.3 (16.6)	243.3 (83.4)	291.6 (100)	83.4
1993-94	44.9 (18.1)	202.7 (81.9)	247.6 (100)	81.9
1994-95	20.3 (12.9)	137.6 (87.1)	157.9 (100)	87.1
1995-96	21.4 (12.9)	143.4 (87.1)	164.8 (100)	87.0
1996-97	23.3 (12.3)	166.5 (87.7)	189.8 (100)	87.7
Annual average (%) growth rate	23.04	44.60	34.82	

Source: RBI Bulletins, various issues.

7.4.2 Repayment of Internal Debt

Repayment of internal debt consists of discharge of maturing market borrowings and repayments to autonomous bodies and financial institutions. This was only Rs.6 crores in 1974-75 and by 1996-97 it came up to Rs.23 crores setting a growth of 19 per cent per annum. As a percentage of total repayments, repayment of internal debt remained at 13.4 and 12.3 per cent during the Fifth and Sixth Plan periods. During the Seventh Plan period it came down to 9.5 per cent of the total repayments to rise in the next plan to 14.4 per cent.

Thus the data (Table 7.4) analysis of the 23 year period shows, that repayment of Central loans formed nearly four-fifth of Kerala's total repayments, right from the beginning of the Fifth Plan period. The repayment of internal debt remained low throughout the Plans.

7.5 Gross and Net Repayments

Gross repayments consist of repayment of internal debt and repayment of Central loans. The financial burden of repayments can be better appreciated with the help of the concept of net repayments. State Government loans and advances to autonomous bodies and institutions, as

**TABLE 7.5: GROSS AND NET REPAYMENT OF DEBT BY GOVERNMENT OF KERALA
1974-75 TO 1996-97**

YEAR	GROSS REPAYMENTS	NET REPAYMENTS	TOTAL CAPITAL RECEIPTS	TOTAL CAPITAL DISBURSEMENTS	GROSS REPAYMENTS AS PERCENTAGE OF TOTAL CAPITAL DISBURSEMENTS	NET REPAYMENTS AS PERCENTAGE OF TOTAL CAPITAL DISBURSEMENTS MINUS GROSS REPAYMENTS
1	2	3	4	5	6	7
1974-75	26.0	8.12	100.6	88.8	29.23	12.93
1975-76	37.4	19.3	96.5	109.3	34.20	26.83
1976-77	53.0	32.97	122.6	134.2	39.47	40.58
1977-78	35.5	18.72	131.4	136.6	26.01	18.52
1978-79	36.4	21.14	170.5	147.6	24.67	19.02
1979-80	22.4	6.65	139.1	176.1	12.72	4.33
1980-81	25.6	8.23	145.8	187.8	13.61	5.072
1981-82	157.0	131.2	173.2	331.1	47.41	75.36
1982-83	48.5	24.38	217.1	213.0	22.76	14.83
1983-84	71.6	40	364.6	329.4	21.72	15.51
1984-85	193.6	164.6	369.6	433.1	44.70	68.73
1985-86	256.8	240	718.1	523.3	49.08	90.07
1986-87	186.7	170.6	488.1	507.0	36.82	53.25
1987-88	199.2	180.7	658.5	470.4	42.35	66.63
1988-89	189.3	145.5	577.0	459.9	41.15	53.76
1989-90	218	171.8	816.9	590.9	36.89	46.08
1990-91	157.3	120.9	957.1	551.5	28.52	30.67
1991-92	327.4	283.8	1105.0	788.7	41.52	61.52
1992-93	291.6	222.9	1134.1	706.6	41.27	53.70
1993-94	247.6	169.2	1315.7	844.9	29.30	28.33
1994-95	157.9	111.9	1691.9	892.4	17.70	15.23
1995-96	164.8	116.6	1710.0	1088.4	15.15	12.62
1996-97	189.8	135.8	1745.9	1188.8	15.96	13.59
Annual average growth rate	34.8	90.5				

Note: 1. Gross Repayment = Discharge of Internal debt + Repayment of Central loans

2. Net Repayment = Gross Repayment to the Centre - Recovery of loans and advances by State Government.

Source: RBI Bulletins; various issues

part of capital disbursements are mainly debt financed. Repayment of these loans back to the State Government by these autonomous bodies and institutions augment the capital receipts of the State. Thus net repayments can be calculated by deducting the recoveries of loans and advances by the State Government from gross repayments to the Centre. Net repayment of Kerala increased from Rs 8 crores in 1974-75 to Rs 136 crores in 1996-97 registering a growth rate of 90.5 per cent annum (Table 7.5). The growth was marked by wide fluctuations. To measure the financial burden of debt repayment the following measures are used.

7.5.1 Gross Repayment/Capital Disbursement Ratio

The gross repayment - capital disbursement ratio remained at 30.7 and 30 per cent during the Fifth and Sixth Plan periods. But during the Seventh Plan period, 41.3 per cent of the capital expenditure was used to repayment of old debts (Table 7.5). During the Eighth Plan period the repayment burden of State loans as a percentage of its capital disbursement came down to 23.9 per cent. As noted earlier, this was partly on account of the debt relief recommended by the Ninth Finance Commission.

7.5.4 Net Repayment/Capital Disbursement Ratio

Net capital disbursement shows the quantum of funds available for capital outlay and for loans and advances at the disposal of the State Government. During the Fifth and Sixth Plan period, net repayments formed 23.6 and 25.9 per cent of the net capital disbursement of Kerala (Table 7.5). But during the Seventh Plan period, net repayments formed 62 per cent of the capital disbursement. This implies that more was spent on repayment than on investment and loan purpose by the State Government from its available capital during the period. The situation improved during the Eighth Plan period and net repayments formed 24.7 per cent of the net capital disbursements of Kerala.

Thus the study reveals that after the initial high levels, both gross and net repayment burden of the State debt have been falling when considered in relation to its capital disbursements. The burden of servicing the debt of Kerala in recent years comes more from interest payments than from repayments obligations.

7.6 Aggregate Debt Servicing Burden of Kerala

Servicing of debt refers to repayment of debt with interest charges. This is considered as the burden of debt. There are several indices to

measure this rising burden of State debt. They include

- a) Debt servicing/SDP ratio
- b) Interest payment/ Revenue Expenditure Ratio
- c) Debt servicing/ Total Expenditure Ratio
- d) Per capita debt servicing

7.6.1 Debt servicing - State Domestic Product (SDP) Ratio

The availability of financial resources for debt servicing depends on the growth of income or output in the economy. If debt servicing charges as a percentage of state domestic product (SDP) keep on rising over a period of time, then the burden of debt can be said to be rising. Gross debt servicing, consisting of gross repayments and gross interest of the Government of Kerala, increased from Rs 51 crores in 1974-75 to Rs 1296 crores in 1996-97 registering an annual average growth rate of 22.8 per cent (Table 7.6). Gross debt servicing as a percentage of State Domestic Product (SDP) of Kerala increased from 2.6 to 4.6 per cent during the same period. Plan-wise analysis of the same shows that during the Fifth and Sixth Plan periods, the ratio remained at 3.1 and 3.6 per cent respectively. It increased to 5.1 per cent during the Seventh Plan period. At the Eighth Plan period witnessed a marginal decline in this ratio to 4.7 per cent.

**TABLE 7.6: DEBT SERVICING/SDP RATIO OF GOVERNMENT OF KERALA
1974-75 TO 1996-97** (Rs Crores)

YEAR	STATE DOMESTIC PRODUCT AT CURRENT PRICES	GROSS DEBT SERVICING	NET DEBT SERVICING	GROSS DEBT SERVICING AS PERCENTAGE OF SDP	NET DEBT SERVICING AS PERCENTAGE OF SDP
1	2	3	4	5	6
1974-75	1942.2	50.7	19.3	2.6	1.0
1975-76	2098.0	67.4	39.7	3.2	1.9
1976-77	2250.7	86.6	58.6	3.9	2.6
1977-78	2422.5	73.5	43.4	3.0	1.8
1978-79	2692.7	76.7	44.0	2.9	1.6
1979-80	2874.3	66.9	13.2	2.3	0.5
1980-81	3823	71.1	44.9	1.9	1.2
1981-82	3697	214	184.4	5.8	5.0
1982-83	4567	109.8	75.6	2.4	1.7
1983-84	5465	163	122.0	3.0	2.2
1984-85	6152	314.7	255.1	5.1	4.2
1985-86	6503	384.3	343.4	5.9	5.3
1986-87	7354	364	312.3	5.0	4.3
1987-88	8258	412.4	355.5	5.0	4.3
1988-89	9182	433.7	363.9	4.7	4.0
1989-90	10668	511	446.9	4.8	4.2
1990-91	12173	497.9	440.1	4.1	3.6
1991-92	15102	810.9	747.7	5.4	5.0
1992-93	17175	834.1	742.28	4.9	4.3
1993-94	18837	934.8	828.79	5.0	4.4
1994-95	21358	977.6	893.79	4.6	4.2
1995-96	24559.8	1127	1023.8	4.6	4.2
1996-97	28241.6	1296	1194.5	4.6	4.2
Annual average growth rate (%)	13.17	22.78	41.15		

Note: 1. Gross Debt Servicing = Gross Repayment + Gross interest payment

2. Net Debt Servicing = Net repayment + Net interest payment

Source: RBI Bulletins; various issues.

Net debt servicing payments comprising of net repayments and net interest payments increased from Rs 19 crores in 1974-75 to Rs 1194 crores in 1996-97 setting a growth rate of 41.2% per annum. Net debt servicing payments of Kerala increased at a higher rate. Expressed as a

percentage of GDP, it increased from less than one percentage to 4.2 per cent during the period of study. During the Fifth and Sixth Plan periods, it increased to 1.8 and 2.8 per cent. In the Seventh and Eighth Plan periods it came closer to the gross debt servicing/GDP ratio, to 4.4 and 4.3 per cent respectively. The gross and net debt servicing/GDP ratios of Kerala during the period of study had been rising and are in line with all India trend in State Finances as noted in Chapter Four.

6.2 Interest Payment/Revenue Expenditure Ratio

The increase in the interest payments of the Government of Kerala leads to the growth of the non-developmental revenue expenditure of the State. This reduces the quantum of funds available for developmental purposes. In this context, increase in interest payments of the State Government, poses a severe constraint on the State Government finances. As shown in Table 7.7, the growth in the revenue expenditure of Kerala was only 15.9 per cent between 1974-75 and 1996-97. But during the same period its gross and net interest payments recorded higher and faster growth rate in percentage terms (19.4% and 39.9%). In the case of Kerala, during the period of study both gross and net interest ratio to total revenue expenditure were high.

Gross interest payments as a percentage of total revenue expenditure of Kerala increased from 8.6 per cent in 1974-75 to 15.5 per cent in 1996-97. Plan wise analysis of data indicates that during the Fifth and Sixth Plan periods, it remained around 8.6 and 8.4 per cent of the State's total revenue expenditure. But the Seventh and Eighth Plan periods recorded a rise in the ratio to 11.2 and 15.6 per cent. Thus by the final year of the Eighth Plan, gross interest payments constituted nearly one-sixth of Kerala's revenue expenditure.

Net interest payment ratio during the 23 year period of study also comes close to that of gross interest payment. It increased from 3.9 per cent in 1974-75 to 14.8 per cent in 1996-97. Plan wise analysis shows that the difference between gross and net interest payment ratio to revenue expenditure has narrowed down from the Sixth Plan period onwards. As noticed earlier, this indicates the declining returns on State Government investments and loans on its debt financed capital disbursement programme. During the Fifth and Sixth Plan periods net interest payments took away only 5.4 and 7.1 per cent of Kerala's revenue expenditure. But during the Seventh and Eighth Plan periods, it rose to 9.6 and 14.9 per cent of the State's revenue expenditure. Thus the above analysis reveals that both gross and net interest payments as a proportion of revenue expenditure are high and in recent years, the gap between these

two has been coming down. This emphasises the need for the generation of surpluses by debt financed projects and enterprises at the State level to contain the increasing non-developmental expenditure on interest payments.

TABLE 7.7: DEBT SERVICING/EXPENDITURE RATIO OF THE GOVERNMENT OF KERALA 1974-75 TO 1996-97.

(Rs. Crores)

YEAR	TOTAL REVENUE EXPENDITURE	GROSS INTEREST PAYMENT AS PERCENTAGE OF TOTAL REVENUE EXPENDITURE	NET INTEREST PAYMENT AS PERCENTAGE OF TOTAL REVENUE EXPENDITURE	RATIO OF GROSS DEBT SERVICING TO TOTAL EXPENDITURE (Rev. + Cap.)
1974-75	288	8.58	3.87	13.46
1975-76	355	8.45	5.76	14.51
1976-77	389	8.62	6.59	16.53
1977-78	416	9.14	5.94	13.31
1978-79	479	8.42	4.77	12.24
1979-80	534	8.34	1.22	9.42
1980-81	668	6.83	5.49	8.32
1981-82	755	7.56	7.05	19.71
1982-83	783	7.83	6.53	11.02
1983-84	992	9.22	8.26	12.33
1984-85	1139	10.63	7.94	20.02
1985-86	1445	8.82	7.15	19.52
1986-87	1655	10.71	8.57	16.84
1987-88	1781	11.97	9.82	18.32
1988-89	2061	11.86	10.59	17.21
1989-90	2298	12.75	11.97	17.69
1990-91	2825	12.06	11.30	14.75
1991-92	3216	15.03	14.42	20.25
1992-93	3656	14.84	14.21	19.12
1993-94	4293	16.01	15.36	18.19
1994-95	5066	16.18	15.43	16.41
1995-96	6226	15.46	14.57	15.41
1996-97	7147	15.48	14.81	15.55

Source: RBI bulletins various issues

7.6.3 Debt Servicing/Total Expenditure Ratio

Debt servicing payment as a percentage of total State Government expenditure (revenue + capital) also can measure the burden of debt (Table 7.7). Debt servicing involving both interest payments and repayments increases the total expenditure of the State Government. Gross debt servicing as a percentage of total state expenditure steadily increased except during the Eighth Plan period. During the Fifth and Sixth Plan periods, it remained at 14 and 14.3 per cent of the State's total expenditure. The Seventh Plan period saw a rise in this ratio to 17.9 per cent. But during the Eighth Plan period, debt servicing State expenditure ratio marginally declined to 16.9 per cent. This means that nearly one sixth of the State's total expenditure is used to pay back, its old debt.

7.6.4 Per Capita Debt Servicing Burden.

The increase in debt servicing payments can be described in per capita terms (Table 7.8). Per capita gross debt servicing of Kerala remained low at Rs. 22 at the beginning of the Fifth Plan period (1974-75). It gradually increased to Rs 31 by the end of the Plan period. But by the end of the Sixth Plan period, it came up to Rs. 118. By the final year

of the Seventh and Eighth Plan periods, the figure reached Rs. 179 and Rs 412 respectively. The growth in debt servicing burden in per capita terms was more pronounced during the Sixth and Eighth Plan periods.

TABLE 7.8: PER CAPITA DEBT SERVICING.

(Rs Per capita)

YEAR 1	POPULATION IN KERALA (In Lakhs) 2	PER CAPITA GROSS DEBT SERVICING 3	PER CAPITA NET DEBT SERVICING 4	PER CAPITA DEBT SERVICING OF CENTRAL LOANS 5
1974-75	228.1	22.21	8.44	15.61
1975-76	232.5	28.98	17.09	23.63
1976-77	236.8	36.55	24.76	28.61
1977-78	240.9	30.52	18.03	21.44
1978-79	244.9	31.33	17.95	22.32
1979-80	248.7	26.90	5.30	16.61
1980-81	252.3	28.20	17.78	16.14
1981-82	255.8	83.66	72.10	68.11
1982-83	259.7	42.29	29.10	23.84
1983-84	263.5	61.87	46.29	39.80
1984-85	267.3	117.70	95.43	83.52
1985-86	271.0	141.80	126.70	106.67
1986-87	274.7	132.50	113.70	100.33
1987-88	278.3	148.20	127.75	104.32
1988-89	281.8	153.90	129.12	104.51
1989-90	285.3	179.10	156.63	116.50
1990-91	288.7	172.50	152.45	95.916
1991-92	292.4	277.30	255.71	183.68
1992-93	296.6	281.20	250.26	125.03
1993-94	300.7	310.90	275.62	159.90
1994-95	304.9	320.60	293.14	153.59
1995-96	310.9	362.60	329.29	181.66
1996-97	314.6	412.10	379.68	209.74

Note: Mid-year population figures from RBI Report on Currency & Finance
Source: RBI Bulletins; various issues.

Per capita debt servicing burden of Central loans (gross) also increased during the same period. It increased from Rs. 15.6 in 1974-75

Rs. 209.7 in 1996-97. Plan wise analysis of the data shows that per capita debt servicing burden of Central loans remained low during the fifth and Sixth Plan periods. It was Rs. 22.3 and Rs 83.5 by the end of these Plans. But by the end of Seventh and Eighth Plans, it came up to Rs.116.5 and Rs.209.7 respectively.

7.7 Servicing of Central Loans of the Government of Kerala, 1974-75 to 1996-97

As noted earlier, of the outstanding total debt of the government of Kerala, Central loans formed 66.2 per cent in the Fifth Plan period and it came down to 42.8 per cent by the end of the Eighth Plan period. In absolute terms, it increased from Rs 396 crores in 1974-75 to Rs.4815 crores in 1996-97. This indicates the dependency of the government of Kerala on Central loans for debt receipt mobilization. The growth in Central loans outstanding has also increased the problem of servicing these Central loans. The mounting debt servicing burden of Central loans has reduced the net loans available to states in India and a situation has arisen where most of the states in India have fallen into 'debt traps', a situation wherein fresh Central loans are necessary to service old loans (George, 1988)¹.

TABLE 7.9: GROSS AND NET TRANSFER (LOANS) FROM THE CENTRE TO THE GOVERNMENT OF KERALA 1974-75 TO 1996-97.

(Rs Crores)						
YEAR	GROSS LOANS AND ADVANCES FROM CENTRE	REPAYMENT OF CENTRAL LOANS	INTEREST ON CENTRAL LOANS	GROSS REPAYMENT OF CENTRAL LOANS AS PERCENTAGE OF GROSS LOANS	NET LOANS FROM THE CENTRE	NET LOANS AS PERCENTAGE OF GROSS LOANS & ADVANCES
1	2	3	4	5	6	7
1974-75	49	20	16	40.78	13	27.06
1975-76	49	36	19	73.47	-6	-13.28
1976-77	69	48	20	69.14	1	1.55
1977-78	69	30	21	43.72	18	25.59
1978-79	110	31	23	28.52	55	50.26
1979-80	73	17	25	22.69	32	43.71
1980-81	75	19	22	25.05	34	45.56
1981-82	93	148	27	158.0	-81	-86.38
1982-83	108	39	23	36.25	47	42.92
1983-84	200	55	45	27.4	95	47.49
1984-85	213	172	54	80.81	-10	-4.82
1985-86	426	240	49	56.48	137	32.11
1986-87	285	171	104	60.17	9	3.22
1987-88	302	182	109	60.19	11	3.73
1988-89	289	168	127	58.08	-5	-1.84
1989-90	349	191	142	54.57	17	4.84
1990-91	408	139	138	33.93	132	32.20
1991-92	575	306	231	53.2	38	6.60
1992-93	530	243	128	45.94	159	29.97
1993-94	596	203	278	34.01	115	19.30
1994-95	749	138	331	18.36	281	37.51
1995-96	676	143	418	21.22	114	16.91
1996-97	643	167	482	25.89	-5	-0.83

Source: RBI bulletins various issues

Given the above situation of Indian states, as noted in Chapter Four, the gross and net transfer of funds from the Centre to the Government of Kerala are analysed. Gross repayment of Central loans as percentage of gross loans from the Centre increased from 51.1 per cent during the Fifth Plan to 65.5 per cent in the Sixth Plan (Table 7.9). But

From the Seventh Plan onwards the Central loan availability improved. It was only during the Eighth Plan period that the burden of repayment was lessened when it came down to 29.1 per cent of gross Central loans of Kerala. This was partly on account of debt relief recommended by the Ninth Finance Commission. The increase in the maturity period of Central loans to States during this period also contributed to the lessening of repayment burden.

7.2 Net Loans from the Centre

Interest payments and repayment of Central loans by the Government of Kerala have led to lesser inflow of Central funds to Kerala. During the Fifth Five Year Plan period, net loans received by the State was only 18.2 per cent of the gross loans. In 1975-76, net loans were negative, in the sense that debt servicing payments of the Central loans were more than the gross loans received by the State. In the Sixth and Seventh Plan period, net loan position further deteriorated to 9 and 14 per cent of gross loans. It was negative for two years (1981-82, 1984-85) of the Sixth Plan and one year (1988-89) of the Seventh Plan. Despite being negative in the final year of the plan, net loans improved to 20.6 per cent in the Eighth Plan period. Thus from the above analysis, it is clear that, debt servicing of Central loans has reduced the net availability of

Central loans to Kerala to negative and insignificant levels, during the period of study. The debt relief provided by successive Finance Commissions should be viewed in this context.

1.8 Review of Debt Relief recommended by Finance Commissions.

1.8.1 Need for Debt Relief

The mounting debt burden of States especially that of Central loans has forced the Central Government to refer the issue of State debt to the Finance Commissions. Fears are often expressed that any substantial debt relief might adversely affect the Centre's financial position. But to the extent debt relief leaves the States with revenue and capital surpluses, the demand for Central assistance will be reduced. It is argued some times that debt servicing payments by States add to the Centre's pool of resources, which can be redeployed in favour of poorer States (Sixth Finance Commission Report). This is based on the wrong assumption that repayments are due more from the richer States.

1.8.2 Second Finance Commission

The Second Finance Commission was the first to be asked to look into the problem of state indebtedness in view of the mounting Central

loans to the States. Between 1947 and 1956, Central loans to States increased from Rs 44 crores to Rs 900 crores. The Commission was asked to suggest modifications if any in the rate of interest and the terms of repayment of the loans made to various States by the government of India between 15th August 1947 to the 31st day of March 1956 (Second Finance Commission Report (1956))². On the interest rate structure, the Commission noted that the policy of giving loans interest free or at a concessional rate of interest is open to objection, because such a concession conveys a wrong impression about the interest burden which has to be met. In order to rationalise the interest rate structure, the Commission suggested only two rates, 3 per cent and 3.5 per cent and recommended a 2.5 per cent interest rate for outstanding loans carrying interest rate below 3 per cent.

7.8.4 Third Finance Commission

The Third Finance Commission was not specifically asked to look into the problem of state indebtedness. The Commission as a part of its general observations commented on the rising interest liabilities of State Governments on Central loans. It considered that revenue gaps of State Governments are partly attributable to interest charges arising out of Central loans. It noticed that the position would worsen in the foreseeable

future (FC 1961)³. The commission did not make any specific suggestions on state debt.

7.8.4 Fourth Finance Commission

The Fourth Finance Commission was asked to assess the extent of assistance required by the States for servicing their debt. It was requested to examine the desirability of the 'creation of a fund out of the excess if any, over a limit to be specified by the Commission of the net proceeds of the estate duty on property other than agricultural land accruing to the states in any financial year for the payment of States' debt to the Union Government'. (Fourth Finance Commissions Report, 1965)⁴. The Commission recommended that both interest charges and amortisation should be treated as items of revenue expenditure for the purpose of working out budgetary gaps in order to recommend grants in aid under article 275(1). The Commission rejected the idea of creation of sinking fund because, the net proceeds of estate duty on property other than agricultural land would prove to be inadequate. It justified the plea for debt readjustment and recommended an overall assessment of the system of inter-governmental debt operation by an expert body to find out the solution for growing debt of State Governments.

1.8.5 Fifth Finance Commission

The problem of states overdraft was referred to the Fifth Finance Commission⁵ for its consideration. The Commission in its study commented that the basic problem was caused by chronic imbalance between resources available to the States and their responsibilities under the constitution. Secondly, manipulation of taxes by the Central Government in its favour had compounded the problem of resource inadequacy of the States. As a result of these, States resorted to unauthorized overdrafts to meet their plan expenditure and increasing burden of Central loans. The remedial measures to deal with the problem of overdrafts were

- a) RBI should issue notice to the States having problems of overdrafts and dishonour their cheques.
- b) RBI should bring this to the notice of the Union government and Union government should clear the overdraft.
- c) If despite these measures, the State Governments continue to overdraw from the RBI, the Commission recommended that Central government should invoke constitutional provision to keep the solvency of the concerned state.

These measures were not accepted by the Central government. But the Central government took over a certain percentage of outstanding overdrafts in 1972-73 and 1973-74 through special medium term loans to the State Governments which minimised the problem of unauthorized overdrafts in the short-run.

7.8.5 Sixth Finance Commission

Assessment of non-plan capital gaps of States and provision of debt relief was part of the terms of reference of the Sixth Finance Commission⁶. The Commission estimated that 19 out of the 21 States would have non-plan capital gaps. It recommended adjustments through

- a) consolidation of some loans into uniform type
- b) extension of period of repayment of some loans
- c) moratorium on the repayment of some loans and
- d) writing off some loans

The Sixth Commission recommended debt relief aggregating Rs 1970 crores (Table 7.10), for the entire Fifth Plan period mostly in the form of rescheduling. The debt relief recommended for Kerala during the

Fifth Plan period (1974-79) amounted to Rs 109.77 crores, which was 5.6% of the aggregate debt relief. This came under various loans categories. For non plan loans, the relief was Rs 26.12 crores for Kerala which was 9.8 per cent of the total non plan relief. A relief of Rs 11.69 crores was given for specific purpose plan loans which formed 5.4 per cent of the total in this category. The largest amount of debt relief for Kerala came for other loans amounting to 71.96 crores forming 4.8 per cent of the total relief under this category.

TABLE 7.10: AGGREGATE DEBT RELIEF RECOMMENDED BY THE VITH FINANCE COMMISSION 1974 to 1979 (Rs. Crores)

STATES	NON PLAN LOANS	SPECIFIC PURPOSE PLAN LOANS	OTHER LOANS	AGGREGATE DEBT RELIEF
Andhra Pradesh	31.99	19.11	140.10	191.20
Assam	24.76	5.72	131.99	162.40
Bihar	10.18	19.47	130.10	133.35
Gujarat	1.25	14.25	20.71	36.25
Haryana	10.20	3.28	19.12	33.14
Himachal Pradesh	0.04	0.99	33.54	34.57
Jammu & Kashmir	16.09	1.24	116.10	133.43
Karnataka	29.35	15.39	82.30	127.04
Kerala	26.12	11.69	71.96	109.77
Madhya Pradesh	0.71	14.62	71.83	87.16
Maharashtra	2.00	23.81	40.77	66.58
Manipur	0.04	0.24	14.95	15.23
Meghalaya	0.01	-	7.63	7.64
Nagaland	-	0.24	5.60	5.84
Orissa	2.54	10.16	144.62	157.32
Punjab	0.30	4.53	10.35	15.18
Rajasthan	44.29	8.00	205.85	258.14
Tamil Nadu	28.98	20.95	37.12	87.05
Tripura	-0.02	-0.10	14.47	14.35
Uttar Pradesh	18.67	29.39	102.71	150.77
West Bengal	19.36	13.51	110.25	148.12
Total	266.88	217.07	14.8567	1969.62
Relief to Kerala as % of Total Debt Relief	9.79	5.39	4.84	5.57

Source: Sixth Finance Commission's Report.

1.8.7 Seventh Finance Commission

The Seventh Finance Commission⁷ was asked to make an assessment of the non-plan capital gap of the States on a uniform and comparable basis for five year ending 1983-84 and a general review of the States' debt position. It recommended measures linking the repayment period

TABLE 7.11: DEBT RELIEF RECOMMENDED BY THE VIITH FINANCE COMMISSION
1978-84 (Rs. Crores)

STATES	ESTIMATED DEBT RELIEF DURING 1978-84
Andhra Pradesh	135.63
Assam	112.20
Bihar	182.65
Gujarat	108.02
Hariyana	38.29
Himachal Pradesh	30.07
Jammu & Kashmir	133.79
Karnataka	39.53
Kerala	115.09
Madhya Pradesh	147.34
Maharashtra	160.78
Manipur	11.85
Meghalaya	5.94
Nagaland	18.59
Orissa	96.48
Punjab	60.57
Rajasthan	137.98
Sikkim	0.66
Tamil Nadu	49.93
Tripura	10.55
Uttar Pradesh	367.13
West Bengal	191.93
Total	2155.80
Relief to Kerala as % of Total Debt Relief	5.34

Source: Report of the VII Finance Commission, 1978.

suitably with the purpose for which Central loans have been used by the states (productive and non-productive). The relief recommended by the Seventh Finance Commission for the five year period (1979-84) was in the order of Rs 2155.80 crores (Table 7.11). Kerala received a debt relief of Rs.115.09 crores during the period. This formed 5.3 per cent of the aggregate debt relief recommended by the Seventh Finance Commission. The Sixth and Seventh Finance Commissions' recommendations together reduced the total volume of All States debt by Rs 4125.42 crores.

7.8.8 Eighth Finance Commission

Like the Sixth and the Seventh Finance Commissions, the Eighth Finance Commission⁸ was asked for an assessment of the non-plan capital gap of the States and to suggest remedial measures to reduce the gap. The Commission noted that growing expenditure needs and insufficient revenue resources with the states, made them dependent on the Centre to finance their revenue expenditure. To finance developmental expenditure, the States resorted to borrowing. The Commission thus recognized the context of increasing indebtedness of the State Governments. But the Commission opposed the idea of writing off loans on the ground that it would reduce the resources available for recycling from the Centre to the states. The commission unfolded a total debt relief of Rs.2285.39 crores

consisting of rescheduling of Central loans and write-off. While considering rescheduling of repayment as a measure of debt relief, the Eighth Finance Commission felt that rescheduling should not exceed thirty years. Developed States were given debt relief to the extent of 35 to 55 per cent of their non-plan capital gaps. The poorer States were given debt relief to the extent of 75 to 85 per cent of their non-plan capital gap.

As shown in Table 7.12, total debt relief covered 59.3 per cent of the estimated non-plan capital gap of the States during 1984-89. Debt relief on the basis of rescheduling totalled 1880.19 crores, which came upto 82.3 per cent of the total debt relief and 48.8 per cent of the non-plan capital gap of State Governments. An amount of Rs.405 crore of Central loans of 12 States was written off. Of this, 5 States cornered Rs.386 crores. Kerala's share of debt relief of Rs.54 crores came under the loan rescheduling programme recommended by the Commission. The amount covered only 50 per cent of its estimated non-plan capital gaps because the State was grouped among the developed States by the Eighth Finance Commission. Kerala's non-plan capital gap formed 2.8 per cent of the total non-plan capital gap of all the States. So its share of debt relief was kept at the same level of total debt relief during 1984-89. Thus the share of debt relief of Kerala came down by 50 per cent with the

Eighth Finance Commission's recommendation from the level recommended by the Sixth and the Seventh Commissions.

TABLE 7.12: DEBT RELIEF RECOMMENDED BY THE VIIITH FINANCE COMMISSION, 1984-89

(Rs. Crores)					
STATES	NON-PLAN CAPITAL GAP	DEBT RELIEF ON THE BASIS OF RESCHEDULING	DEBT RELIEF ON THE BASIS OF WRITE OFF	TOTAL DEBT RELIEF	PERCENTAGE OF DEBT RELIEF TO NON-PLAN CAPITAL GAP
Andhra Pradesh	384.97	204.64	-	204.64	53.20
Assam	274.00	155.75	49.75	205.50	75.00
Bihar	441.3	254.53	76.45	330.98	75.00
Gujarat	81.78	17.80	-	17.80	21.80
Haryana	98.79	31.79	-	31.79	33.90
Jharkhand	19.44	10.92	5.60	16.52	8.00
Jammu & Kashmir	250.24	127.62	85.10	212.72	85.00
Karnataka	177.32	48.45	-	48.45	27.30
Kerala	107.78	53.80	-	53.80	49.90
Madhya Pradesh	294.07	143.65	-	143.65	48.80
Maharashtra	82.87	27.88	-	27.88	33.80
Manipur	13.13	7.63	3.55	11.18	85.10
Meghalaya	7.54	3.49	2.90	6.39	84.80
Mizoram	9.21	6.01	1.80	7.81	84.80
Nissa	260.81	119.12	76.50	195.62	75.00
Punjab	118.86	38.71	-	38.71	32.60
Rajasthan	319.20	141.56	97.85	239.41	75.00
Sikkim	3.63	2.47	0.60	3.07	84.60
Tamil Nadu	95.59	28.19	-	28.19	29.50
Uttar Pradesh	3.05	2.17	0.40	2.57	84.30
Uttarakhand	653.44	337.92	-	337.92	51.70
West Bengal	161.21	116.14	4.70	120.84	75.00
Total	3852.64	1880.19	405.20	2285.39	59.30
Debt Relief to Kerala as % of Total Debt Relief	2.79	2.86	-	2.86	

Source: Report of the Eighth Finance Commission, GOI, New Delhi, Annexure, XIV-6, P.268

7.9 State Wise Outstanding Central Loans and Debt Relief as per VI, VII & VIII Finance Commissions

The State wise data of outstanding Central loans and debt relief provided to the State are given in Table 7.13. All States outstanding Central loans increased from Rs 8578 crores in March 1974 to Rs.27059 crores in March 1984. The debt relief provided by the three Finance Commissions as a percentage of total Central loans outstanding declined considerably. The debt relief provided by the Sixth Finance Commission was 23 per cent of the State outstanding Central loans. But the debt relief provided by the Seventh and Eighth Finance Commissions formed only 16 and 8.4 per cent of outstanding Central loans of States.

In the case of Kerala, outstanding Central loans as on March 1974 was Rs 366 crores and it increased to Rs 535 crores in 1979 and Rs. 859 crores in 1984. However, the debt relief provided to the Government of Kerala by the Sixth, Seventh and Eighth Finance Commissions was only Rs. 110 crores (for 1974-79), Rs.115 crores (for 1979-84) and Rs 54 crores (for 1984-89). Thus debt relief as a percentage of Kerala's outstanding central loans declined steadily from 30.1 per cent during 1974-79 to 21.5 and 6.3 per cent during 1979-84 and 1984-89. So in the case of Kerala, the debt relief scheme of these Finance commissions has not lessened the burden of Central loans on the State.

RECOMMENDATIONS

(Rs. Crores)

STATES	CENTRAL LOANS OUTSTANDING AS ON 31 ST MARCH			DEBT SERVICING RELIEF PROVIDED BY			DEBT SERVICING RELIEF AS PERCENTAGE OF OUTSTANDING CENTRAL LOANS		
	1974	1979	1984	VI th FC (74-79)	VII th FC (79-84)	VIII th FC (84-89)	VI th FC	VII th FC	VIII th FC
Andhra Pradesh	692	1051	1860	191	136	205	27.6	12.9	11.0
Assam	*392	597	1306	163	112	205	41.6	18.8	15.7
Bihar	721	1187	2612	133	183	331	18.4	15.4	12.7
Gujarat	349	521	1419	36	108	18	10.3	20.7	1.3
Haryana	234	304	635	33	38	32	14.1	12.5	5.0
Himachal Pradesh	140	150	215	35	30	16	25.0	20.0	7.4
Jammu & Kashmir	330	612	918	134	134	213	40.6	22.0	23.3
Karnataka	452	677	1077	127	39	48	28.1	5.8	4.4
Kerala	366	535	859	110	115	54	30.1	21.5	6.3
Madhya Pradesh	417	712	1643	87	147	144	20.9	20.6	8.8
Maharashtra	687	978	2545	67	161	28	9.8	16.5	1.1
Manipur	44	57	124	15	12	11	34.1	21.1	8.9
Meghalaya	19	24	45	7	6	6	36.8	25.0	13.3
Nagaland	25	41	52	6	19	8	24.0	46.3	15.4
Orissa	515	706	1215	157	96	196	30.5	13.6	16.1
Punjab	242	380	682	15	61	39	6.2	16.1	5.7
Rajasthan	762	967	1803	258	138	239	33.9	14.3	13.3
Sikkim	-	6	16	-	1	3	-	16.7	18.8
Tamil Nadu	426	754	1399	87	50	28	20.4	0.7	2.0
Tripura	38	40	69	15	10	2	39.5	25.0	2.9
Uttar Pradesh	916	1824	3532	151	368	338	16.5	20.2	9.6
West Bengal	811	1342	3038	143	192	121	17.6	14.3	4.0
Total (All States)	8578	13465	27059	1970	2156	2285	23.0	16.0	8.4
Total debt relief as % of outstanding Central loans				23	16	8.4			

Source: Report of the VI, VII, VIII Finance Commission

7.9.1 Debt Relief by the Ninth Finance Commission.

The Ninth Finance Commission⁹ adopted an approach different from that of the previous three Commissions. Unlike in the case of the Eighth Commission, the Ninth Commission was not asked to estimate the likely non-plan capital gaps of States. The Commission was asked to review the entire debt position of the states and not the States' debt position with particular reference to Central loans. The total debt of State Government was estimated as Rs.8961 crores on March 1989 of which liabilities to the Central Government formed about 63 per cent (Rs.5645 crore).

The Commission was against debt rescheduling or write off as such. It linked the extent of relief to the performance of the States in respect of their investment in two important sectors namely power and road transport. The total debt relief recommended by the commission during 1990-95 in respect of loans outstanding at the end of 1989-90 came up to Rs.975.62 crores (Table 7.14). The quantum of relief was less than that provided by the Eighth Finance Commission. This was mainly due to the basic difference in the terms of reference of the Eighth and the Ninth Commissions. The Ninth Commission was not asked to suggest measures to deal with the non plan capital gap. Kerala received only Rs 16.43 crores during 1990-95 as debt relief. This formed only 1.7 per cent of the

total debt relief. This constituted only 10 per cent of its outstanding Central loans at the end of 1989-90.

TABLE 7.14: DEBT RELIEF RECOMMENDED BY THE NINTH (1990-95) & TENTH FINANCE COMMISSIONS (1900-2000)

STATES	ESTIMATED DEBT RELIEF DURING 1990-95 (in Cr.)	ESTIMATED DEBT RELIEF DURING 2000 STIPULATED UNDER GENERAL INCENTIVE SCHEME	
		5%	10%
		(Rs. Crores)	
Andhra Pradesh	43.74	42.9	85.89
Assam	49.69	14.5	28.91
Arunachal Pradesh	117.31	3.16	6.33
Bihar	27.64	44.5	89.08
Gujarat	82.67	52	104.01
Goa	28.84	4.06	8.12
Haryana	7.96	12.1	24.17
Himachal Pradesh	4.57	5.94	11.88
Jammu & Kashmir	43.25	11.7	23.41
Karnataka	26.27	28.4	56.77
Kerala	16.43	23.2	46.31
Madhya Pradesh	130.72	25	50.01
Maharashtra	40.41	56.2	112.47
Manipur	1.61	1.26	2.51
Meghalaya	1.30	1.01	2.01
Mizoram	51.72	1.57	3.1
Nagaland	2.18	1.33	2.67
Orissa	28.69	17.5	35.0
Punjab	6.45	11.4	22.85
Rajasthan	143.98	26.6	53.13
Sikkim	0.95	0.78	1.56
Tamil Nadu	34.31	31.2	62.34
Tripura	1.77	2.92	5.83
Uttar Pradesh	71.91	104	208.66
West Bengal	11.25	42.4	84.78
Total	975.62	566	1131.8
Relief to Kerala as % of Total Debt Relief	1.68	4.09	4.09

Source: Report of the Ninth and Tenth Finance Commissions

7.9.2 Debt Relief by the Tenth Finance Commission

The Tenth Finance Commission¹⁰ too was required, according to its terms of reference, to assess the debt position of the States and suggest corrective measures. The Commission estimated the total debt of the States at Rs 209159 crores at the end of March 1995. According to the Commission's estimates, 62 per cent of States' debt was in the form of loans from the Centre (Table 7.14).

7.9.3 Quantum and Form of Debt Relief- Disinvestment Route

The Tenth Finance Commission made two important recommendations to reduce the burden of state debt. It suggested that the State Governments should make substantial disinvestment from their public sector enterprises. The proceeds of these should be used to repay Central loans and the Centre should write – off an equivalent amount. It suggested the sale of at least 20 per cent of the equity of state public sector enterprises and Centre's write off of loans was limited to a maximum of 20 per cent of equity disinvested.

There is an incentive element in this recommendation. As the Centre itself has been using the proceeds of its disinvestment to bolster its revenue position, it seems unlikely that States will use similar revenue to reduce their debt burden. Given the uncertainties of the capital market

and accumulated loss of state public sector enterprises, the proposed disinvestment route may not yield sufficient funds for debt repayment, at the State level. Kerala Government is totally opposed to this idea of public sector disinvestment and is unlikely to get any relief on this count.

7.9.4 Reward for Revenue Improvement

The second recommendation of the Tenth Finance Commission, if implemented is likely to result in a larger reduction of the debt of the States. The idea behind this recommendation is that the Centre should 'reward' those States which take steps to improve their revenue account. The ratio of revenue receipts to revenue expenditure in a given year is compared with the average of this ratio in the preceding three years. If in a State, the revenue receipts to revenue expenditure ratio in a year has increased by three percentage point over the average ratio in the three preceding years, then the Centre will write off six per cent of what the State has to repay in the next financial year. The extent of write off is limited to a minimum of 5 per cent of repayment in each year and a maximum of 10 per cent. Debt relief, at a minimum of 5 per cent will be Rs 566 crores and the maximum equivalent to 10 per cent of repayment will be Rs 1132 crore during 1995-2000 (Table 6.16). For Kerala, the estimated debt relief under the general incentive scheme, at a minimum of 5 per cent and at a maximum of 10 per cent will be Rs 23.16 crores and Rs

46.31 crores respectively. Under both schemes, debt relief to Kerala forms 4.1 per cent of the total debt relief during 1995-2000. However, since the improvement in the revenue account that is needed to qualify for retiring a part of repayment is substantial, there will not be many cases of States being able to qualify for this scheme. Thus the two recommendation of the Tenth Finance Commission, it is argued, will result only in "incremental relief". This is so because the revenue deficits of the State Governments are on the rise as noted in Chapter Six.

The burden of Central loans persisted even after rescheduling and write off by successive Finance Commissions (Appendix 7.3). The Ninth Finance Commission estimated the central loans outstanding at the end of March 1989 as Rs 56051 crores. But it recommended only Rs 975.62 crores as total debt relief during 1990-95 forming only 1.74 per cent of the outstanding Central loans. The Tenth Finance Commission estimated the outstanding Central loans as Rs 56587 crores. With its novel methods of debt relief, its debt relief ranged between the minimum of Rs 56591 crores and the maximum Rs 113183 crores during 1995-2000. As a percentage of total outstanding Central loans of State Governments, it came between 1 per cent and 2 per cent. Recent estimates of the outstanding Central loans show that it has reached the level of Rs 150568 crores by 1996-97.

The above analysis of debt relief granted by various Finance Commissions reveals the following aspects of its working. One of the major failures of the Finance Commissions has been their inability either due to the terms of reference or due to other constraints to take equity consideration to their logical ends. Except the Eighth, they did not even take an integrated look at the non-plan revenue and capital gaps. The right approach would be to merge the revenue surpluses with the capital gaps and then to relate the debt relief to the overall surplus/ deficit. Even after the debt relief, all the deficit States continued to be deficit States. Thus while the debt relief continued to add to the surpluses of already surplus States, it failed to cover fully the overall gaps of the deficit States. Debt relief recommended as a proportion of the outstanding Central loans to States especially by the Ninth and Tenth Finance Commissions declined. Debt servicing relief provided as a percentage of outstanding Central loans of Kerala declined steadily from 30 per cent in the Sixth Finance Commission to 4 per cent in Tenth Finance Commission period. In the analysis of the Tenth Finance Commission, Kerala is not regarded as a high distress State to qualify for higher debt relief.

7.10 Conclusion

The State Governments are heavily dependent on borrowing to finance their revenue deficits and capital outlay. The diversion of

borrowed funds from investment to current consumption and the low investment yield from debt financed projects adversely affect the debt servicing capacity of the Kerala Government. The debt relief given through the awards of Finance Commissions though providing temporary succour, does not provide any permanent solution to the problem of mounting Central loans to States. The indiscriminating application of the same formula to all States with regard to loan-grant composition of Central plan assistance without reference either to the level of development of the State or the nature of the State's spending has created very difficult debt servicing situation for a State like Kerala. The large revenue component of State expenditure, the remarkable development of the social sector and economic backwardness of Kerala, must find a place in the scheme of debt relief to the State. The availability of resources for future investments crucially depends on the productive use of the borrowed funds, by the States. Only through prudent fiscal management, adequate provision for amortisation can be made to liquidate the past loans. This applies to Kerala also.

References:

1. George, K.K., *Center-State Financial Flow and Inter-State Disparities*, Criterion Books, Delhi, 1988, Chapter 8.

2. Second Finance Commission Report, Government of India New Delhi, 1956.
3. Third Finance Commission Report, Government of India New Delhi, 1961.
4. Forth Finance Commission Report, Government of India New Delhi, 1965.
5. Fifth Finance Commission Report, Government of India New Delhi, 1969.
6. Sixth Finance Commission Report, Government of India New Delhi, 1973.
7. Seventh Finance Commission Report, Government of India New Delhi, 1979.
8. Eighth Finance Commission Report, Government of India New Delhi, 1984.
9. Ninth Finance Commission Report, Government of India New Delhi, 1990.
10. Tenth Finance Commission Report, Government of India New Delhi, 1994.

CHAPTER 8

CONCLUSIONS AND RECOMMENDATIONS

8.1 Introduction

Kerala is a State which has been exposed to a unique development experience. The pattern of development known as the Kerala Model of Development is characterized by spectacular improvements in the quality of life and the slow growth of income and employment. The peculiar pattern of public expenditure, weighted in favours of social services has been one of the major contributory factors to this lopsided pattern of development. However, the Government of Kerala has been running into recurrent fiscal crises almost throughout the eighties. Fiscal crisis has become in a way systemic to the Kerala Model of Development. The crisis is rooted in the revenue account and that too in the non-plan account of the State budget. The mounting and recurrent revenue deficit have become

increasingly a charge on the State's capital receipts. It is true that budgetary deficit has become a common problem for all States in India. The frequency and magnitude of the fiscal crisis are much more for Kerala than for other States. As noted earlier, the origin of Kerala's revenue deficits dates back to the Fifth FYP period itself. While Kerala had been carving out surpluses in its capital account to finance revenue deficits, other States had been utilising their revenue surpluses to meet recurrent capital deficits. In recent years, deficits of All States have also started following the Kerala pattern.

8.2 Major Findings of the Study

- (i) Public debt of India comprising of the aggregate liabilities of the Central and State Governments excluding Central loans to States as a percentage of GDP nearly doubled during the period between 1950-51 and 1996-97. This is attributed to the high growth of internal debt of the Central Government. The growth of market loans and bonds during this period considerably influenced the growth of internal debt. The external governmental liabilities forms only a small portion of the aggregate liabilities of the Central Government. The growing burden of debt servicing may place severe strain on the finances of the Central Government in the near future.

- ii) The public debt of the State Governments increased at a rate of 15 per cent per annum and formed 21 per cent of GDP in 1996-97. The composition of State debt shows the preponderance of Central loans in total debt. The debt servicing payments of these loans have created a situation of reverse flow of funds from the States to the Centre. But of late, the share of Central loans in total transfers is falling and that of non-debt transfers are on the rise. Similarly State Governments are gradually moving from low cost to high interest bearing items of borrowings like Provident funds and Small savings. The high interest rates and short maturity of State Governments loans have contributed to the increased burden of State debt. But with the financial sector reforms in the nineties, the interest rate and maturity pattern of State Governments' market borrowing are moving in line with that of the Central Government.
- (iii) The growth of public debt of Kerala and its fiscal crisis are closely linked. The recurring revenue deficit of Kerala is increasingly financed by public borrowing. The diversion of borrowed funds for meeting revenue deficits reduces the capital outlay and loans of the State Government. It adds to the interest liability which again increases the revenue deficit. This develops into a debt trap situation for the State. The general decline in

Central loans to States, affected Kerala in a greater measure. However, Central loans to Kerala is still the single largest component of State debt. The corresponding increase in the high cost component of Kerala's debt receipts such as market borrowings, Provident Funds and Small Savings may pose severe strain on the debt servicing capacity of the State.

- (iv) The share of revenue expenditure in aggregate expenditure remained high in the budgetary operations of Kerala. One main reason for this situation is the preponderance of non-plan expenditure in Kerala's expenditure. Capital disbursements of Kerala are highly debt financed. Part of the borrowed funds are used to finance revenue deficit. Capital disbursements on capital outlay and loans declined steadily.
- (v) The substantially higher share of social and community services in total expenditure compared to economic services explains the genesis of the Kerala model of development. However, the share of social services shows a steady declining trend in recent years. This has affected the outlay on education and allied services and medical and health services adversely in the social sector. This may in course of time, erode the positive aspects of Kerala model of development. The dominance of social sector in the

State's expenditure implies that the share of consumption expenditure in the State's final outlay is quite high. Within consumption expenditure, it is the share of compensation for employees that has been very high. The share of capital formation is correspondingly low.

- (vi) The share of economic services in developmental outlay increased from the Sixth FYP onwards. The investment in irrigation, flood control and power development formed the major portion of the developmental outlay of Kerala. But the investment in these sectors declined from the Sixth FYP onwards. Agriculture and allied activities did not get adequate investment in the developmental outlay of the State. The public investment in industry and transport was low throughout the period of study. These may partly explain the agricultural stagnation and industrial backwardness of the State. Loans to power projects received an increased share in the developmental loans of Kerala during the Seventh and Eighth FYs.
- (vii) The pattern of capital disbursements, has created several difficulties in debt servicing. The outstanding debt of Kerala, in relation to its capacity to service debt, as indicated by the state domestic product has been one of the highest among States in

India. The composition of debt shows that Kerala has been relying more on high cost market loans and provident funds. Kerala's reliance on relatively low interest bearing funds like Reserve Funds and Deposits and Central loans has been considerably lower than that of other States. Interest receipts on State Government loans are meager and falling. Repayments increased at a faster rate than interest payments indicating the existence of large proportion of short maturity loans in the overall borrowings of the State. The mounting debt servicing burden of Central loans has reduced the net loan availability of Kerala. Debt relief provided by the various Finance Commissions as a proportion of outstanding Central loans of Kerala declined steadily from 30 per cent by the Sixth Finance Commission to 4 per cent by the Tenth Finance Commission. It is unlikely that Kerala's debt servicing burden will be lessened in the near future as the root of the problem lies in the massive deficits the state has been incurring every year. It appears that the State is caught in a vicious circle of deficits, debt servicing payments and more deficits.

1.3 Suggestions

- (i) Unproductive loans of the States outstanding as on 31 March 1997 should be rescheduled over a longer period. The investments which will neither bring direct returns nor will have direct income generation effect in future may be defined as unproductive. Expenditure on meeting emergencies like drought, flood and famine conditions are a few instances.
- (ii) Loans for different purposes should not have the same maturity period and carry the same interest rates.
- (iii) The Government of Kerala will have to exercise greater fiscal discipline because the practice of financing revenue deficit with costly borrowed funds meant for investment will accentuate the problem of debt servicing which is already high.
- (iv) There is definitely scope for Kerala raising more non-tax revenues from its public sector. The interest arrears due from State public sector enterprises are a major untapped source of non-tax revenue. This calls for better management of State public sector.
- (v) The benefits of Kerala's past expenditure on social services, particularly education can be reaped fully if the State can conceive

of a new strategy of growth which calls for further investment in human resources development.

(vi) The Finance Commission's debt relief to Kerala should be related to the State's development pattern which has led to present fiscal crisis and debt accumulation. The State is a victim of its success in attaining above average standards in social services. The second generation problems induced by Kerala's success in attaining higher standards in social services with serious fiscal implications have to be considered while the issue of outstanding Central loans and debt relief to Kerala, are decided.

(vii) In the changed economic environment, there is need to move on to an auction based system of State Government bonds under which financially sound States may have direct access to markets at market determined rates, while ensuring a stipulated level of borrowing for the less developed States.

SELECT BIBLIOGRAPHY

Books

Abbot, C.C., (1953), *The Federal Debt Structure and Impact*, New York, McGraw-Hill Book Company.

Anderson, William, (1960), *Intergovernmental Relations in Review*, University of Minnesota Press, Minneapolis.

Bajaj, J.L., Sinha, K.S. and Agarwal, O.P., (1985), *Finance commission and Backward States: An Appraisal*, Print House, Lucknow.

Banerjee, P.N. (1960), *Indian Public Finance*, George Allen and Unwin, London.

Bhargava, P.K., (1978), *Essays in Indian Public Finance*, Chug Publishers, Allahabad.

Break, George, F., (1967), *Intergovernmental Fiscal Relations in the United States*, Brookings, Washington.

Buchanan, James, M., (1970), *Public Finances*, R.D. Irwin, Illinois.

Barman, K., (1978), **India's Public Debt and Policy Since Independence**, Allahabad: **Chaug Publications**.

Bastable, C.F., (1895), **Public Finance**, London: **Macmillan**.

Bhargava, R.N., (1979), **Some Issues in Public Finance – Theory and Practice**, Allahabad: **Chaug Publications**.

Buiter, W.H. and U.R. Patel, (1994), 'Debt, Deficits and Inflation: An Application to the Public Finance of India', in A Bagchi and N. Stern (eds.), **Tax Policy and Planning in Developing Countries**, Delhi: **Oxford University Press**.

Chakravarthy, Sukhomy, (1987), **Development Planning: The Indian Experience**, **Oxford University Press**, New York.

Chanda, Ashok, (1965), **Federation in India**, **George Allen and Unwin**, London.

Chatterji, Amiya, (1971), **The Central Financing of State Plans in the Indian Federation**, **Firma, K.L. Mukhyopadhyay**, Calcutta.

Chelliah, R.J. and Narain, Sinha, (1982), **State Finances in India: Measurement of Tax Effort of State Governments 1973-76**, **World Bank**, Washington.

Chelliah, R.J., (1983), An Economic and Equity Aspect of the distribution of Financial Resources between the Centre and the States in India, National Institute of Public Finance and policy.

Chelliah, R.J., (1992), "Growth of India Public Debt", in Bimal, Jalan, (Ed.), (1992), The Indian Economy: Problems and Prospects, Viking Penguin India.

Dar, R.K., (1981), Recent Developments in India Federal Finance, Centre for Federal Financial Relations, Australian National University, Canberra.

Dass, Radhika, (1966), Finances of the Indian Union since 1947, Central Book Depot, Allahabad.

Domar, E.D., (1957), Essays in the Theory of Economic Growth, Oxford University Press, London.

Friedrich, C.J., (1968), Trends of Federalism in Theory and Practice, Pall Mall Press, London.

Ferguson, J.M., (1965), Public Debt and Future Generations, Chapel Hill: University of North Carolina.

Gadgil, D.R., (1965), Planning and economic Policy in India, Gokhale Institute of Politics and Economics, Pune.

Gopal, M.H., (1963), *Studies in Indian Public Finance*, Rao and Raghavan, Mysore.

Gulati, I.S.,(1979), *Centre-State Financial Relations: An Assessment of the Role of Finance Commissions*, University of Baroda, Baroda.

Guar, A.K., (1985), *Centre-State Financial Relations and Finance Commissions*, Chug Publishers, Allahabad.

Hemlata, Rao, (1981), *Centre-State Financial Relations*, Allied, New Delhi.

Hemlata, Rao, (1994), *Federal State Financial Relations*, Ashish, New Delhi.

Lakdawala, D.T., (1972), *Mobilisation of State Resources (Sir William Meyer Endowment Lectures in Economics 1969-70)*, University of Madras, Madras.

Lal, S.N., (1978), *Problems of Public Borrowing in Under-developed Countries*, Allahabad: Chugh Publications

Misra, B.R., (1954), *Indian Federal Finance*, Orient Longmans, Bombay.

Musgrave, R.A., (1959), *The Theory of Public Finance*, McGraw Hill, New York.

Musgrave, R.A., (1961), *Approaches to a Fiscal Theory and Political Federation*, in National Bureau of Economic Research, *Public Finances: Needs, Sources and Utilisation*, New York.

Musgrave, R.A. (Ed.), (1977), *Essays in Fiscal Federalism*, Greenwood, Westport.

Mushkin, Selma, J. and Cotton, John, F., (1969), *Sharing Federal Funds for State and Local Needs*, Praeger, New York.

Nanjundappa, D. M., (1976), *Studies in Public Finance*, Asia Publishing House, Bombay.

Oates, Wallance, E., (1972), *Fiscal Federation*, Harcourt Brace, New York.

Rao, Annanda, G., (1992), *Finance Commissions in India*, Deep and Deep Publishers, New Delhi.

Rao, Govinda, M., (1981), *Political Economy of Tax and Expenditure Determinants – A Case Study of Four Indian States*, Allied, New Delhi.

Rao, V.K.R.V., (1973), Centre-State Financial Relations in India, Institute for Social and Economic Change, Bangalore.

Reddy, K.N. (1972), Growth of Public Expenditure in India, 1872-1968, (A secular and Time Pattern Analysis), Sterling, New Delhi.

Santhanam, K., (1967), Union-State Relations in India, Asia Publishing House, Bombay.

Sharma, J.N., (1974), Union and The States- A Study in Fiscal Federalism, Sterling, New Delhi.

Singh, B.P. (1988), Fiscal Transfers -The working of Finance Commissions in India, Amar Prakashan, New Delhi.

Sinha, R.K., (1987), Fiscal Federalism in India, Sterling, New Delhi.

Sinha, R.K., Das, D.K. and Sinha, A.K., (Eds.), (1992), Development Paradigms – India's Development Experiences, Deep and Deep publishers, New Delhi.

Thimmaiah,G., (1975), "The Role of the Finance Commission- A Critique", in V.K. Nataraj and L.N. Sastry, (Eds.), New Perspectives in Centre – State Relations in India, Mysore University, Mysore.

Thimmaiah,G., (1977), Burden of Union Loans on the States, New Delhi: Sterling Publishing Co. Ltd.

Thimmaiah,G., (1981), A critique of the Finance Commission, New Delhi: Wheeler Publishing Co. Ltd.

Thimmaiah, G. and Rao, Hemalata, (1984), Finance Commission and Centre State Financial Relations, Ashish, New Delhi.

Venu, S., (1978), Finance Commissions of India, Institute for Financial Management and Research, Madras.

Reports and Monographs

Gulati, I.S. and K.K.George, (1988), Eighth Finance Commission's Award', in Essays in Federal Financial Relations, Monographs Series, Trivandrum: Centre for Development Studies.

Gulati, I.S. and K.K.George, (1988), Centre-State Resource Transferes, 1951-84, in Essays in Federal Financial Relations, Monographs Series, Trivandrum: Centre for Development Studies.

Gulati, I.S. and K.K.George, (1988), Sixth Finance Commission's Award: An Appraisal in Retrospect, Monographs Series, Trivandrum: Centre for Development Studies.

Gulati, I.S. and K.K.George, (1988), Seventh Finance Commission's Award: Inter-State Redistribution-Through Budgetary Transfers, Monographs Series, Trivandrum: Centre for Development Studies.

Gulati, I.S. and K.K.George, (1988), Eighth Finance Commission's Award: Inter-State Redistribution-Through Budgetary Transfers, Trivandrum: Centre for Development Studies.

Rao, Govinda, M., (1987), "Fiscal Imbalances in Indian Federalism, A paper presented at the seminar on Comparative Federalism, India, Canada, March, National Institute of Public Finance and Policy, New Delhi.

Rao, Hemlata, (1993), Measuring Taxable Capacity and Tax Efforts of Indian States, Mimeo, Institute for Social and Economic Change, Bangalore.

Rao, V.K.R.V., (1983), " Key Note Address",in seminar on Centre-State Relations, August 5-7, Institute for Social and Economic Change, Bangalore.

Journals

Ahuja, S.P. (1968), "Fiscal Disparities among States", The Indian economic Journal, Vol XV, No.5, PP. 560-8.

Ansari, M.M., (1983), "Financing of the States' Plans: A Perspective for Regional Development", Economic and Political Weekly, Voll XVIII, No. 49, PP. 2077-82.

Bagchi, Amaresh, Sen, Tapan and Tulasidhar, V.B., (1988), " Issues before Ninth Finance Commission", Economic and Political Weekly, Vol XXIII, No. 19, PP. 955-64.

Bhattacharaya, B.B. and S.Guha, (1990), "Internal Debt of Government of India: Growth and Composition", Economic and Political Weekly, XXV, April.

Chelliah, R.J., (1991), "The growth of India Public Debt-Dimensions of the Problem and Correctives Measures", I.M.F. Working Paper No. 72, Washington D.C.: International Monetary Fund.

Dandekar, V.M., (1994), " Assets and Liabilities of Government of India". Economic and Political Weekly, XXIX, 41-50.

George, K.K., (1987), "Discretionary Budgetary Transfers: A Review", Economic and Political Weekly, Vol. XXI, No.46, PP.1993-98.

George, K.K., (1987), "Centre-State Resource Transfers: An Appraisal", Economic and Political Weekly, Vol. XX, No.7, PP.287-296.

George, K.K. and Gualti, I.S., (1985), "Central Inroads into State Subjects: An Analysis of Economic Services", Economic and Political Weekly, Vol. XX, No.14, PP.592-603.

Guhan, S., (1997), "Centre-State Fiscal Transfers: Beyond the Tenth Finance Commission", EPW, Vol. XXXII, No. 7, PP. 353-56.

Gulati, I.S., (1977), "VIth F. C's Award- An Appraisal in Retrospect", Economic and Political Weekly, Vol. XII, No.67 and 68, PP.287-96.

Gulati, I.S., (1998), "Tackling the Growing Burden of Public Debt", Economic and Political Weekly, Vol. XXVIII, No.18, PP.883-86.

Lakdawala, D.T., (1972), "Evolution of Union – State Financial Relations", Commerce, Vol. 125, No.3198, PP. 82-9.

Lakdawala, D. T., (1984), "Eighth Finance Commission's Recommendations", Economic and Political Weekly, Vol. XIX, No.35, PP. 1529-34.

Lakdawala,D.T.,(1990), "Ninth Finance Commission's Award: An Overview", Economic and Political Weekly, Vol. XXV, No.23, PP. 1260-2.

Lakdawala,D.T.,(1990), "Indian Public Debt", Artha Vijnana, 32: 1-24.

Lerner, A.P., (1948), Income, Employment and Public Policy, New York: W.W.Norton and Co.

Lerner, A.P., (1961), "The Burden of Debt", Review of Economics and Statistics, XLIII: 139-141.

Masson, P.R., (1985), "The Sustainability of Fiscal Deficits", I.M.F. Staff Papers, XXXII: 577-605.

Rao, Hemalata (1978), "Federal Fiscal Transfers Criteria and their Application", Artha Vignana, Vol XX, No. 4, PP 333-52.

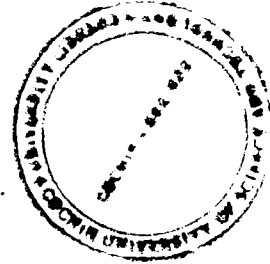
Rao, V.K.R.V., (1973), "Centre-State Relations in India", Southern Economist, Vol. XI, No. 18, PP 9-24.

Ratchford, B.U., (1986), "A formula for Limiting State and Local Debts", Quarterly Journal of Economics, Vol. II, PP 71-89.

Ray, Amal, (1988), "The Sarkaria Commission's Perspective", Economic and Political Weekly, Vol. 23, No. 22, PP. 1131-33.

2. Government of Kerala.

- (a) Economic Review, various issues
- (b) Budget document, various years
- (c) Finance Accounts of Government of Kerala.



3. Reserve Bank of India

- (a) RBI Bulletins, various issues
- (b) Report on currency and Finance, various issues.