

3. Government Expenditures: A Review

EXPENDITURES: BUDGETARY CLASSIFICATION

Trends in revenue expenditure, considered as a percentage of GSDP, have been summarised in table 3.1. Expenditure on social and economic services, has experienced a slight fall in terms of GSDP at the expense of a rise in non-development expenditure, i.e., general services. In fact, during 1985–86 to 1996–97, social, economic and general services have risen at the compound rate of growth of 12.66, 15.84 and 18.22 percent per annum respectively. This reveals that while the growth rate of general services has been the highest, it is the lowest for social services.

The rise of expenditure in general services is attributable to interest payments and pensions. Interest payment as a percentage of GSDP grew from 1.69 percent in 1985–86 to 3.31 percent in 1996–97 whereas pensions have grown from 1.60 percent to 2.55 percent during the same period as given in table 3.1. The overhang of debt with a gradually increasing reliance on market for borrowing has escalated the interest payments. Pensions work out to be a higher percentage of revenue expenditure in Kerala as compared to other States possibly because of the lower retirement age (55 as compared to 58/60 years). The other two components, viz., organs of State and fiscal services have remained more or less stable as shares in GSDP during the period under consideration.

A low retirement age (55 years) and a relatively high life expectancy is causing a substantial burden on the State exchequer as far as pensions are concerned. Even if a pension is commuted initially, it is fully restored after 12 years at the age of 67. It is advisable for the State and most of its important public enterprises to create separate pension funds and operate them off the budget while the State government may still contribute a significant amount. Clear guidelines should be prepared for appropriate investments of the pension funds so that they may become self-sustaining. The issue of raising the retirement age should also be reviewed. Central government and most other State governments are now having a retirement age of 58–60 years. A one-time adjustment is required in raising the retirement age. Since fresh recruitment in the government sector has to be reduced drastically, employment potential has to be created in the private sector.

With reference to the development sectors, social and economic, there is a perceptible structural shift in favour of the economic services. Among the social sectors, the fall in education is significant compared to near stagnancy in health and a marginal rise in water supply, sanitation and urban development. The shares of education and health in GSDP fell from 5.54 and 1.36 in 1985–86 to 4.84 and 1.30 in 1996–97 respectively. Water supply, sanitation and urban development registered a rise from 0.35 to 0.66 during the same period.

Table 3.1: Revenue Expenditure

	(Percent of GSDP)							
	1985-86	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
A. Developmental expenditure (1-2)	13.86	12.79	11.23	11.44	11.48	11.17	11.36	12.13
1. Social services	10.28	9.04	7.70	7.23	7.89	7.72	7.69	8.07
a. Education, sports, art and culture	5.54	5.50	4.77	4.57	5.09	5.01	4.78	4.84
b. Health and family welfare	1.36	1.51	1.27	1.15	1.26	1.27	1.32	1.30
c. Water supply, sanitation & urban development	0.35	0.58	0.51	0.44	0.50	0.47	0.48	0.66
2. Economic services	3.58	3.74	3.53	4.21	3.59	3.46	3.67	4.07
a Agriculture and allied	2.38	1.33	1.55	2.26	1.48	1.51	1.51	1.65
b Rural development	0.00	0.89	0.73	0.66	0.71	0.63	0.65	0.83
c Special area programmes	0.00	0.05	0.07	0.03	0.04	0.04	0.03	0.03
d Irrigation and flood control	0.18	0.46	0.36	0.36	0.41	0.38	0.41	0.35
e Energy	0.00	0.01	0.01	0.01	0.01	0.02	0.02	0.04
f Industry and minerals	0.25	0.27	0.22	0.33	0.32	0.32	0.35	0.44
g Transport and communications	0.44	0.49	0.43	0.40	0.46	0.38	0.50	0.49
h Science, technology and environment	0.00	0.03	0.02	0.02	0.02	0.02	0.02	0.04
i general economic services	0.33	0.21	0.16	0.15	0.14	0.15	0.16	0.19
B. Non-Developmental Expenditure								
3. General Services	5.32	7.02	6.96	6.70	7.32	7.36	7.79	7.86
a Organs of State	0.21	0.25	0.23	0.19	0.21	0.22	0.24	0.24
b Fiscal services	0.54	0.59	0.52	0.50	0.55	0.60	0.58	0.53
c Interest payments and servicing of debt	1.69	2.42	2.76	2.72	3.05	3.04	3.08	3.31
d Administrative services	1.28	1.40	1.23	1.12	1.19	1.18	1.23	1.23
e Pensions and miscellaneous general services	1.60	2.37	2.23	2.16	2.33	2.32	2.65	2.55

Source: CAG, relevant years

In economic services, the fall in the share of agriculture and allied activities from 2.38 to 1.65 during 1985–86 to 1996–97 is significant in relation to the increase in shares of irrigation and flood control, industry and minerals, transport and communications. Particularly, the rise is significant in case of irrigation and flood control (a rise from 0.18 to 0.35) and industry and minerals (0.25 to 0.44). Expenditure on energy and science, technology and environment continue to be low (table 3.1).

Historically, Kerala has assigned high priority to social and community sectors. This is evident from the fact that in 1985–86, education and health combined, accounted for 6.9 percent of GSDP compared to 3.58 percent for economic services as a whole. Though, there has been a gradual shift in favour of economic services, these two sectors continue to claim a higher share of budgetary resources (6.14 percent of GSDP) as compared to 4.07 percent of GSDP for economic services in 1996–97.

The contribution of the State government to capital formation in the State has been dismally low, and declining. Net of repayments, capital expenditure was 3.54 percent of GSDP in 1985–86 (table 3.2). By 1996–97, it had fallen to 2.89 percent. Correspondingly, capital outlay which was 2.74 percent of GSDP in 1985–86, fell to 1.87 percent in 1996–97. The impact has been felt by social services and economic services alike. While, for the former category, the fall was from 0.59 percent in 1985–86 to 0.25 percent in 1996–97, for the latter, it was from 2.04 percent to 1.52 percent during the same period.

Table 3.2: Capital Expenditure and Outlay

	(Percent of GSDP)							
	1985-86	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
Capital expenditure	4.65	3.62	3.35	2.88	3.42	3.31	3.65	3.46
Capital expenditure (net of repayments) of which	3.54	2.80	2.63	2.08	2.65	2.72	3.10	2.89
Capital outlay	2.74	1.82	1.63	1.39	1.61	1.65	1.88	1.87
Capital outlay on social and economic Services								
A. Social services	0.59	0.25	0.19	0.20	0.21	0.16	0.23	0.25
Education, sports, art and culture	0.11	0.14	0.10	0.12	0.11	0.08	0.07	0.08
Medical, public health & family welfare	0.19	0.07	0.05	0.05	0.06	0.05	0.07	0.06
Water supply, sanitation & urban development	0.25	0.02	0.01	0.01	0.01	0.01	0.05	0.03
B. Economic services	2.04	1.51	1.41	1.15	1.35	1.44	1.57	1.52
Agriculture and allied activities	0.21	0.23	0.25	0.15	0.11	0.17	0.20	0.17
Transport	0.54	0.42	0.39	0.34	0.39	0.43	0.47	0.42
Industry and minerals	0.31	0.30	0.25	0.17	0.26	0.31	0.30	0.33

Source: CAG, relevant years.

Within social services, capital expenditure on education, health and water supply, as a percentage to GSDP, have all fallen. This fall has been particularly severe for the latter two. Expenditure on medical and public health and water supply were 0.19 and 0.25 respectively in 1985–86. These shares plummeted to 0.06 and 0.03 respectively in 1996–97 as percentages of GSDP. With regard to economic services, barring industry and minerals which show a marginal rise from 0.31 to 0.33 during the same period, the other two major economic sectors, agriculture and allied activities and transport exhibit a decline. With regard to compositional shift pertaining to capital expenditure, economic services exceed social services by a large margin (as compared to the case of revenue expenditure).

ECONOMIC CLASSIFICATION: SELECTED ITEMS

This structure of government expenditure can also be viewed in terms of its economic classification. In this context, we focus attention on two major economic categories of government expenditure, *viz.*, maintenance and salaries.

As evident in table 3.3, there is a clear declining trend in maintenance expenditure which has fallen from 2.77 in 1985–86 to 1.13 in 1996–97. Though, the same trend is discernible for all the three sectors, social, economic and general services, it is more severe for social sectors.

Table 3.4 shows salary expenditure emanating from the budget for the years 1994–95, 1995–96 and 1996–97 as given in Appendix XI of the explanatory memorandum of the budget of 1998–99. Salary heads under revenue and capital heads are shown with an explicit reference to the teaching grants given to the aided private educational institutions (APEI). Like other States, Kerala is also revising the salary structure of its employees in

line with the recommendations of the Fifth Central Pay Commission. These increases are based on the recommendations of the State Pay Commission which has a periodicity of five years as compared to the centre where the cycle is of 10 years. According to a recent press release of the government, the additional annual burden is likely to be Rs. 904 crore including pensions, out of which Rs. 637 crore can be accounted for by revision of salaries, while the rest pertains to pensions. This implies an increase of about 20 percent over the existing pay package.

Table 3.3: Expenditure on Maintenance

(As percentage of GSDP)

	1985-86	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96
Maintenance	2.77	1.89	1.22	1.16	1.38	0.97	1.13
Social	0.93	0.85	0.54	0.50	0.63	0.40	0.34
Economic	0.65	0.57	0.38	0.37	0.41	0.31	0.48
General	0.54	0.35	0.22	0.20	0.26	0.26	0.31

Source: CSO, relevant years(a).

Table 3.4: Expenditure on Salaries and Number of Government Employees

(Rs. lakh)

	1994-95	1995-96	1996-97
Salary expenditure: revenue heads	142941	143199	172825
Salary expenditure: capital heads	1918	2188	2675
Total salary expenditure of government employees	144859	145387	175500
Teaching grants to APEI	74566	77653	86166
Total salary expenditure	219425	223040	261666
<i>Total salary expenditure as a percentage of GSDP</i>	<i>8.13</i>	<i>7.42</i>	<i>7.84</i>
<i>Total salary expenditure as a percentage of total expenditure</i>	<i>37.83</i>	<i>33.00</i>	<i>33.76</i>
Number of government employees	357203	362540	361115
Number of employees in APEI	141551	142044	142982
Total number of employees	498754	504584	504097
Memo: Total expenditure	580078	675795	775166

Source: GoK, DoF, relevant years.

AN INTER-STATE COMPARISON OF PER CAPITA EXPENDITURE

In per capita terms, Kerala spends relatively larger amounts through its budget, as compared to most other Indian States. A comparative picture is presented in table 3.5 for

the year 1995–96. The north-eastern States, and Jammu and Kashmir are not included in this comparison. We observe that Kerala ranks seventh among the fifteen general States with reference to development expenditure. With regard to non-development expenditure, there are only three States which spend more than Kerala in per capita terms.

Table 3.5: Comparison of Per Capita Expenditure: 1995-96

(Rupees)							
States	Develop- ment Expen- diture	Non-Develop- ment Expen- diture	Total Expen- diture	States	Develop- ment Expen- diture	Non-Develop- ment Expen- diture	Total Expen- diture
Andhra Pradesh	1248	510	1758	Madhya Pradesh	1048	397	1445
Bihar	549	381	930	Maharashtra	1849	677	2526
Goa	4191	3154	7345	Orissa	1177	511	1688
Gujarat	1659	612	2271	Punjab	1793	1118	2911
Haryana	1936	1466	3402	Rajasthan	1467	7369	2202
Karnataka	1529	577	2106	Tamil Nadu	1437	601	2038
Kerala	1504	785	2289	Uttar Pradesh	871	564	1435
				West Bengal	1000	462	1462

Source: RBI 1996-97

PLAN AND NON-PLAN EXPENDITURE

It is also notable that nearly three-fourths of the State government expenditure comprises non-Plan expenditure which is higher than average for the major States as shown in table 3.6. As such, the pattern of expenditure is tilted towards non-Plan, non-developmental items.

Table 3.6: Plan and Non-Plan Expenditure

(Percent of total expenditure)				
Year	Kerala Plan	Kerala Non-Plan	Major States Plan	Major States Non-Plan
1994-95	23.76	76.24	27.21	72.79
1995-96	25.08	74.29	28.43	71.57
1996-97	27.33	72.67	29.59	70.41

Source: GoK, SPB, 1997(a).

BUDGETARY SUBSIDIES

In order to obtain a comprehensive picture of the budgetary resources that are used for subsidising various social and economic services, it is appropriate to take into account both explicit and implicit subsidies. For this purpose, an estimate of budget subsidies was made for the year 1996–97, using the methodology described in Srivastava *et.al.*(1997) with

some modification.² In this methodology, subsidies are interpreted as unrecovered costs in the provision of services by the government through budgetary allocations. It is the excess of costs over recoveries which provide the estimate of subsidies. Current costs are taken as revenue expenditure on the services in addition to which an annualised cost of capital is also included. Receipts are in the form of revenue receipts, interests and dividends. A distinction is made between services provided directly by the government departments, and government investments in the form of equity and loans to various enterprises. Total subsidies in 1996–97 amount to Rs. 4541 crore which is 13.6 percent of GSDP. Some sectors produce a surplus which amount to about Rs. 97 crore. These sectors are mainly forestry and wildlife and petroleum. A summary of budgetary subsidies is given in table 3.7.

Table 3.7: Budgetary Subsidies in Kerala: 1996-97

Sector	(Rs. crore)							
	Revenue Expenditure	Aggregate Costs	Revenue Receipts	Aggregate Receipts	Unrecovered Variable Costs	Unrecovered Total Costs	Subsidy as a Percentage of GSDP	Recovery Rate (Percent)
Social services	2579.70	2743.70	38.82	44.26	2540.86	2699.41	8.09	1.61
Education, sports, etc	1615.09	1649.39	26.16	26.21	1588.93	1623.18	4.86	1.59
Health & family welfare	427.42	458.96	3.32	3.34	424.10	455.62	1.37	0.73
Other social services	537.17	635.32	9.34	14.71	527.83	620.61	1.86	2.32
Economic services								
A. Subsidised sectors	1222.30	1937.30	73.50	95.39	1148.81	1841.86	5.52	4.92
Agriculture & allied Activities	463.35	544.24	33.28	37.26	430.07	506.98	1.52	6.85
Rural development	239.12	239.43	0.49	0.52	238.63	238.91	0.72	0.22
Special area programmes	9.90	10.41	0.25	0.64	9.90	10.40	0.03	0.06
Irrigation and flood control	115.72	379.77	3.20	3.20	112.52	376.57	1.13	0.84
Energy	14.58	100.82	0.00	10.61	14.58	90.21	0.27	10.52
Industry and minerals	147.01	266.40	7.80	13.76	139.21	252.64	0.76	5.17
Transport	165.11	324.46	18.96	20.20	146.15	304.26	0.91	6.23
Other economic services	67.52	71.72	9.77	9.83	57.75	61.89	0.19	13.71
B. Surplus sectors	67.23	78.94	174.46	175.52	-107.23	-96.58	-0.29	222.35
Social and economic services (excluding surplus sectors)	3801.99	4680.92	112.32	139.65	3689.67	4541.27	13.61	2.98
Social and economic services (including surplus sectors)	3869.22	4759.86	286.78	315.17	3582.44	4444.69	13.32	6.62

Source (Basic Data): CAG, relevant years

It is evident that the total subsidies in social services, amounting to 8.09 percent of GSDP, are higher than those for economic services which amount to 5.52 percent of GSDP. The recovery rate in social services is 1.61 percent of the costs, and in economic services, it is 4.92 percent. It is clear that the huge amount of subsidies need to be brought down in both social and economic services where the recovery rates are abysmally low and the volume large. At first, those services should be targeted where the extent of externalities may not be significant and the benefits may largely accrue to the users of the services directly. For this purpose, we suggest that the following sectors should be targeted: (i) irrigation, (ii) energy, (iii) industry and minerals, (iv) transport, and (v) 'other' economic services. Next, some components of agriculture and allied activities, health services that are curative in nature, and education at the higher and technical ends including medical education may be targeted. A decomposition of the recovery rates with respect to major

heads and their components indicates that the share of variable (i.e., current) costs for direct services constitutes more than 95 percent of the total costs for many services. Sectors where it is relatively low are irrigation and flood control (30 percent) and transport (54.5 percent). In all other services, it is quite high. It is suggested that in the case of economic services, a target of recovering at least 50 percent of the variable costs should be set up in the first instance. The existing recovery rates with reference to variable costs are so low that a significant volume of revenues may be raised even through this modest target. The other component of these services is the investment made through budgetary resources in the form of equity and loans. Here, the recovery rates range from extremely low to about 12 percent. All sectors where the recovery rates are less than 10 percent should be targeted for improving recoveries, especially in the case of loans. Some of the suggested sectors for this purpose are plantations, industries, transport and tourism.