

AP is losing sight of fiscal prudence

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Of concern Building a capital by acquiring farmland is not a good idea V RAJU - V Raju

The State is clamouring for more funds from Centre even as it undertakes an overly ambitious Amaravati project

The fiscal position of the bifurcated State of Andhra Pradesh (AP), formed in 2014, continues to be weak. The Fourteenth Finance Commission (FFC) has recommended a fiscal deficit ceiling of 3 per cent for States. States whose debt to GSDP (gross state domestic product) ratio is below 25 per cent and whose interest payments are lower than 10 per cent of revenue receipts (RR) have the flexibility to rack up an additional 0.25 per centage points fiscal deficit each, thereby increasing the effective fiscal deficit ceiling to 3.5 per cent.

AP's 2017-18 (RE) debt to GSDP and interest payments to RR ratios stood at 28.4 per cent and 11.8 per cent, respectively. The State's applicable fiscal deficit ceiling is 3 per cent, which it has breached.

The sole positive aspect of AP's fiscal profile is that its ratio of capital expenditure (capex) to GSDP up to 2016-17 was higher than that of comparable States. At 7.2 per cent in 2016-17, the ratio was higher than those of Telengana (5.1 per cent), Karnataka (3.2 per cent), Maharashtra (1.8 per cent), Gujarat (3.3 per cent), and Tamil Nadu (2.5 per cent).

But even this has not been sustainable. AP's own estimates indicate that its capex-to-GSDP ratio declined to 4.1 per cent in 2017-18 (RE) and is projected to improve to 4.7 per cent in 2018-19 (BE).

The Central Government used to grant special category state (SCS) status based on multiple factors, including hilly and difficult terrain, low population density, low resource base, strategic location along India's border, economic and infrastructure backwardness, unsustainable finances, and sizeable share of tribal population.

The AP Reorganisation Act 2014 includes demand for SCS status. This is underpinned by AP's weak fiscal position and, thereby, access to higher devolutions and grants from the Centre, concessional excise duty and tax breaks, and eligibility for debt swapping and debt relief schemes. Concessional excise duty and tax breaks would enhance AP's attractiveness as an investment destination.

The large gap between AP's demand for ₹16,078 crore grants-in-aid to fund the 2014-15 revenue deficit and the Centre awarding ₹6,283 crore, is another bone of contention. The 14th Finance Commission did allocate ₹1,94,820 crore grants-in-aid to 11 States (AP, Assam, HP, J&K, Kerala, Manipur, Meghalaya, Mizoram, Nagaland, Tripura, and West Bengal) to enable them bridge their revenue deficits for the five-year period 2015-16 to 2019-20.

AP's share at ₹22,113 crore (11 per cent of the pool) is the third highest among the 11 States, behind those of J&K (31 per cent) and HP (21 per cent). AP's revenue grants-in-aid receipts are projected to more than double to ₹50,700 crore in 2018-19 (BE) from ₹21,800 crore in 2014-15.

Finance Minister Arun Jaitley committed a 'SCS-like' financing package for centrally-sponsored schemes (CSS) in AP. The Centre finances 60 per cent and 90 per cent of the CSS implemented in general States and SCSs, respectively. Jaitley assured AP that the Centre will finance 90 per cent of CSS in AP during 2015-20. The Centre does appear correct in this instance by following the 14th Finance Commission recommendations in letter and spirit and not according AP SCS status, while simultaneously extending grants-in-aid and favourable financing packages to ease its birth pangs.

While States require higher tax devolutions and grants-in-aid to finance their capital expenditure, they must not lose sight of fiscal prudence. AP's wages, salaries and pensions consume almost 45 per cent of its revenue expenditure. The State's wages and salaries was 30.6 per cent of its 2016-17 revenue expenditure; 7.16 percentage points above the 23.4 per cent ratio of wages and salaries to revenue expenditure recorded by all States, excluding AP and including NCT Delhi and Puducherry.

AP's ratio of pensions to revenue expenditure was the highest among peer States at 14.1 per cent in 2016-17, followed by Tamil Nadu (12.7 per cent), Gujarat (9.5 per cent), Karnataka (9.3 per cent), Telengana (8.9 per cent), and Maharashtra (8.5 per cent).

Snapshot of AP's finances

	Revenue receipts (₹ billion)	Own tax revenues/ RR (%)	Revenue (Surplus) deficit/ GSDP (%)	Gross fiscal deficit/ GSDP (%)	Wages & salaries/ RR (%)	Pensions/ RR (%)	Interest payments/ RR (%)	Debt/ GSDP (%)	Capital expenditure/ GSDP (%)
2009-10	647	54.4	-0.5	5.1	26.9	9.8	13.8	45.2	7.9
2010-11	810	55.7	-0.8	3.7	28.9	11.9	11.9	43.6	6.9
2011-12	936	57.0	-0.8	4.1	28.7	11.9	11.3	39.7	6.7
2012-13	1,038	57.7	-0.3	4.3	24.8	11.6	11.2	42.4	6.5
2013-14	1,107	57.9	-0.1	3.9	29.2	12.4	11.7	41.9	5.6
Post bifurcation									
2014-15	907	42.4	2.7	2.3	30.8	11.0	11.0	23.0	2.4
2015-16	886	45.0	-0.1	3.6	35.3	10.8	12.6	28.5	8.9
2016-17	990	44.6	-2.5	4.4	35.3	16.3	11.8	28.8	7.2
2017-18*	1,233	42.8	-0.1	3.5	NA	NA	12.0	28.4	4.1
2018-19**	1,555	42.1	0.1	2.8	NA	NA	9.7	28.7	4.7

Source: RBI State Finances: A Study of Budgets, <http://nfti.gov.in/state-statistics>; Andhra Pradesh Budget at a Glance 2015-16 to 2018-19; and author's calculations

Revenue deficit = revenue receipts less revenue expenditure

Gross fiscal deficit = Aggregate disbursements (net of debt repayments) less revenue receipts, non-debt capital receipts and recovery of loans and advances NA: Not available *RE **BE

Amaravati project

Another worrisome development is Chief Minister Chandrababu Naidu's initiative to build a new capital city, Amaravati, scheduled to be completed by 2029.

The two key concerns regarding the Amaravati project are the ecological implications of converting agricultural land into a planned city and the project's funding mix.

The project is estimated to cost anywhere between ₹58,000 crore and ₹1 lakh crore. The Centre has released ₹2,500-crore grant and another ₹1,000 crore is in the pipeline. HUDCO and the World Bank have extended a ₹14,200-crore funding package. And, AP plans to issue bonds worth ₹2,000 crore. Assuming that the project cost is at the lower end of the range — ₹58,000 crore — monetising 4,000 acres (16.19 square kilometres) of prime land holds the key to raising the balance ₹38,300 crore or 66 per cent of the project cost. The Amaravati project hinges on the AP government implementing the land monetisation in a fair, transparent and timely manner. Embarking on a project of this magnitude on agricultural land will impact the livelihoods of thousands of farmers and their families.

Crucial questions Chandrababu Naidu and the TDP need to ask themselves are: Can the ecological risks associated with the Amaravati project be mitigated? And, is the State equipped to undertake a project of this magnitude given its embattled finances? Empire building aspirations have, after all, caused the downfall of many a head of state and CEO.

The writer is an independent analyst and co-author of 'The Singapore Blue Chips'.