IMPACT OF ECONOMIC LIBERALISATION ON KERALA ECONOMY – A PRELIMINARY ASSESSMENT

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In our discussions on economic reforms in India, very little attention is bestowed on their possible impact on different states in the country. Discussions on reforms in Kerala too have failed to focus on their direct impact on the state's economy. Even when such attention is paid, it is largely confined to the issue, how liberalisation and globalisation are going to threaten the state's public distribution system, social service sectors, cash crops and the few existing industries. But liberalisation, besides posing certain threats, is also envisaged to bring in some opportunities for investment. The newly conferred freedoms on the domestic entrepreneurs as well as foreign investors are expected to lead to resurgence of investments. But what has been the regional direction of these investments flows since 1991, the year in which liberalization process has been initiated? And, But what has been the impact of these investment flows on the state's economy?

No doubt, it is a little too early to assess the impact of reforms on the state's economy. Firstly, liberalisation, through initiated in 1991 has yet to gather full momentum and is yet to cover all sectors of the economy. Secondly, for making state-wise assessment of the impact, we require data on SDP or industrial and agricultural growth in different states. Such data are not yet available. What we have attempted is to find out the flow of industrial investment to different states, by piecing together scattered information on investment intentions and decisions as also investments in the pipeline. One of the limitations of this paper is that due to the non-availability of data, investments in agriculture could not be included in our analysis.

KERALA IN PRE-LIBERALISATION ERA

Before we examine Kerala's position in the post reform period, it may be of interest to examine its position in the pre-reform era. This becomes all the more necessary as many people in the state, while discussing economic reforms, become nostalgic about the by-gone era of central planning. But the centralised planning system, despite having a wide array of instruments of economic policy with their avowed objective of narrowing regional disparities failed miserably to check the downward slide of Kerala economy. The fact that Kerala's per capita SDP in 1950-51, the year when planning was introduced in India, was higher than the all-states average, has not received due attention in Kerala among the public as also among the academics. Fifties saw marginal decline in Kerala's position according to NCAER estimates. According to C.S.O. estimates, Kerala's SDP in 1960-61 was only 84 per cent of the All States average per capita SDP. Sixties saw some improvement in Kerala's position. But the trend was reversed in the seventies. Eighties witnessed only tardy growth in Kerala economy, as a result of which its per capita SDP in 1991-92 was only 80 per cent of the All India average. In the matter of per capita SDP. Kerala's relative position among states fell from 5th to 9th. Today, it belongs to the poor income category along with Orissa, Madhya Pradesh, Uttar Pradesh, Rajasthan and Bihar.

If we take the deviation of Kerala's per capita SDP from that of the top ranking state, the fall in Kerala’s per capita income was 65 per cent of the per capita income of West Bengal, the then top ranking state. Today, Kerala's SDP is only less than half that of Punjab, the present top ranking state in India. It is in this context of the failure of the past system of centralised planning that we are examining whether at least the newly liberated market forces, have been helping the poorer states like Kerala.

The decline in relative economic position, no doubt, is not peculiar to Kerala IN 1960-61, there were seven major states with above average per capita SDP. By 1991-92, their number shrank to just 4 (Punjab, Haryana, Maharashtra and Gujarat). All these states improved their position relative to all states average while the position of all others came down. In other words, under the Nehruvian model, despite its professed sympathy for backward states and regions, four states emerged as `Asian Tigers' in India while others slided down.

STATE-WISE POSITION OF INVESTMENTS

We have been able to piece together scattered state-wise information on the quantum of Foreign Direct Investments (FDI), Industrial Financial Institutions (AIFIs) and the Commercial Banks in the post liberalisation period . Data on the distribution of plants proposed to be set up by companies entering capital market as also the number of foreign collaborations is also collected. We have also made use of the date of the survey conducted by the Centre for monitoring India Economy (CMIE) covering 2664 large investment projects (exceeding Rs. 5 crores) in mining, manufacturing, electricity and irrigation for which investment decisions have been taken and which are in various stages of approval or implementation. Our findings are presented in Table 1.

FOREIGN DIRECT INVESTMENT (FDI)

Attracting foreign investment - both direct and portfolio - is one of the cornerstones of the New Economic policy. Between January 1993 and October 1994, 1650 Foreign Direct Investment proposals for investments totalling Rs. 19,607 crores had been approved by India. Of the 14 major states, Kerala's position with respect to the quantum of FDIs was only the last. It received just 20 proposals amounting to Rs. 35.2crores.The quantum of investments was less than those received by less populous states and Union Territories like Goa, Delhi and Chandigarh.

FOREIGN COLLABORATIONS

Foreign collaborations is another means identified by the Government of India to attract foreign funds and technology. According to the answer given to a parliamentary question, 9893 collaborations had been concluded between August 1991 and June 1993. In this, Kerala's share was just 71(0.7 per cent). In the number of foreign collaborations, even Union Territories like Delhi, Dadra and Nagar Haveli had been able to attract more. In fact, Kerala attracted just as many collaborations as Daman and Dieu. In the number of foreign collaborations in relation to population, Kerala's rank was just 12, among the 14 major states of India.

INDUSTRIAL ENTREPRENEUR MEMORANDUM SIGNED (IEMS)

IEMS indicate the investment intentions of the entrepreneur. From August 1991 to December 1994, 17064 IEMS for aggregate investment of Rs. 34493 crores had been signed. Of this, Kerala's share was just 145 covering Rs. 355 crores which represent only 1.0 per cent of the total investment. IEMS signed for Kerala was one of the lowest among the states, except Orissa, Goa, North Eastern States and Jammu and Kashmir. As in the case of FDIs and Foreign collaborations, the investment proposed under IEMS in Kerala was even lower than those for Delhi and Himachal Pradesh. The 145 IEMs signed are envisaged to generate employment for 27.751 persons. Of the total employment potential of investments proposed under these IEMS. Kerala's share comes to only 0.9 per cent.

COMPANIES RAISING CAPITAL FROM THE PRIMARY MARKET

Capital market has today emerged as the principal mobiliser and allocator of capital funds. According to the Prime Issue Monitor, 518 companies raised capital from the primary market in 1993-94. The state-wise location of plants of these companies shows a very low position for Kerala. Only 8 companies representing just 1.5 per cent of the total number had proposed their plants in Kerala, through Kerala continues to be a major supplier of funds in the primary market. In this respect, Kerala's position was lower than even those of Delhi and Dadra and Nagar Haveli.

INVESTMENTS IN THE OFFING

The survey by the Centre for Monitoring Indian Economy (CMIE) covers 2664 large investment projects in mining, manufacturing, electricity and irrigation for which investment decisions have been taken and which are in various stages of approval or implementation. The combined investments envisaged by these projects amount to Rs. 6,34,793 crores. Of this, mining and manufacturing account for 48.9 per cent and irrigation for 10.8 per cent.

Of the total investments in mining and manufacturing amounting to Rs. 3,10,551 crores, Kerala's share was only 4.204 crores (1.35 per cent). Of the total investments in electricity sector totalling Rs. 2,42,393 crores, Kerala's share was just Rs. 807 crores (0.33 per cent). In investments in irrigation totalling Rs. 68,545 crores, Kerala's share was just Rs. 1,019 crores (1.48 per cent). Of the aggregate investments totalling Rs. 6,34,793 crores, Kerala's share was only Rs. 6, 030 crores (0.95 per cent).

ALL INDIA NON-BANK FINANCIAL INSTITUTIONS (AIFIs)

These financial institutions in the government sector which portray themselves as development finance institutions still have sizeable investment funds at their command, despite the increasing role of the capital market. Their role in Kerala was very limited in the past. In 1980-81, Kerala accounted for only 3.2 per cent of the assistance disbursed by these institutions. During 1991-92, 1992-93 and 1993-94, the first three post - liberalisation years. Kerala's share has come down to just 1.7 per cent. From the seventies, these institutions have been operating a concessional scheme for backward areas. Kerala has been by-passed even under this scheme. Kerala's share in assistance under these schemes came down from 2.4 per cent in 1980-81 to 2.1 per cent during the last three years.

COMMERCIAL BANK CREDIT

In the matter of incremental public sector bank credit during 1993-94, Kerala's position was less than the All India average. Besides as in the pre-liberalisation era, public sector banking system continues to act as conduits for outflow of funds from the state. This is borne out by the very low incremental credit deposit ratio for the state in 1993-94. The ration was just 15 per cent for Kerala against the All India average of 31 per cent.

DISTRIBUTION OF INVESTMENTS BY INDUSTRY

One of the characteristics of Kerala's existing industrial structure is that it is not well diversified. The pattern of investments revealed by the CMIE date shows that this position is unlikely to change in the post liberalisation period (See Table II). A large number of industry groups have not been attracting any investment at all in the state. The share of electricity generation in the total investment in Kerala has been only 13.4 per cent against 38.2 per cent for the country as a whole. The comparative low investment in electricity generation may pose serious problems for the future industrialisation of the state unless the state follows an industrialisation strategy based on low fuel intensive industries. But unfortunately the industries which have attracted substantial share of investments in Kerala are refinery products, mineral products and chemicals, all of which are likely to be fuel intensive. Besides, these industries, going by the past experience, have little or no backward linkages in the state. Forward linkages are also very weak.

Our discussions so far show that economic liberalisation has not led to an upsurge of investment in Kerala. In almost all indicators of investment. Kerala's already low ranks (9) in per capita SDP and per Capita SDP originating in industry (8). Assuming that Kerala's capital output ratio is not lower than that of other states, Kerala's position with respect to per capita SDP and per capita industrial income in future is likely to slide down further. The process of economic decline which started during the days of Central Planning is likely to gather further momentum during the post liberalisation era. This is true not only for Kerala but also for most of the poor states. As for Kerala, it is the only state in South India which was by passed by liberalisation. Even its neighbouring Union Territories have done much better. Again, it is the only state on the West Coast which is being by-passed by liberalisation.

A larger study by the author shows that only those states which have already got higher than average per capita income or per capita income of industrial and mining origin have attracted above average quantum and number of investment proposals. Those states with higher proportion of income originating from industry and mining also benefited from liberalisation. The major beneficiaries of liberalisation have been Maharashtra, Gujarat, Haryana, Punjab, Tamil Nadu, and Karnataka. Some of the small states and Union Territories adjoining these states like Goa, Delhi, Chandigarh, Daman and Dieu, Dadra and Nagar Haveli and Pondicherry have also benefited.

WHY KERALA GETS BY-PASSED

How come that economic liberalisation is by-passing a state like Kerala? It may be noted that we have not yet got an answer to the question why the benefits of centralised economic planning did not reach the state. In fact, there had not been any comprehensive study at all seeking to explain the paradox of the state's economic under-development despite high levels of social development.

According to conventional wisdom, there are many factors favourable to the economic growth of the state. For instance, going by the experience of Japan and some of the East Asian `Tigers' a state which had implemented radical land reforms should have made great strides in agricultural growth which in turn should have triggered off industrial growth. But, for Kerala, there has been only stagnation in agricultural and industrial sector after Land Reforms. The reasons for this paradox too are not clear.

Again, conventional wisdom supported by the experience of Asian Tigers suggests that a state with its first position in physical quality of life index should have been the first to attract investments under liberalisation. Our analysis however shows that there is no strong correlation between physical quality of life index and the various indicators of investment. Is it that our educational attainments and health status lack some vital developmental inputs? Or are there any other inhibiting factors which override the advantages of the better physical quality of life of Keralites?

Kerala is well ahead of other states in the matter of physical infrastructure. Even this lead has not enabled it to attract industrial investments either during Nehruvian era or during Manmohan Singh's era.

Again, Kerala is second in the matter of household consumption. This should have generated a demand led industrialisation in the state. But this has not happened in the past. Nor is it happening at present. In fact, our analysis of the correlation between per capita consumption expenditure and investment indicators reveal a weak correlation. Only the latter's correlation with per capita SDP is quite strong.

From time immemorial, Kerala economy had developed strong linkages with international markets as a result of which the state's economy became export-import oriented. This process of export-import orientation got disrupted only during the plan era, when domestic industries were insulated from international competition. With the dismantling of protective walls, one would expect that an export oriented state like Kerala, with its historical connections with and proximity to international commodity and labour markets, will be able to attract larger investments. The presence of Malayalee NRIs around the globe also should have facilitated this process. But these expectations too are belied and we have no explanation yet for this.

Our earlier study covering the liberalisation's impact on all the states shows that indicators of investment during the post liberalisation era are having a high correlation with per capita state government expenditure. Though Kerala's ranking in per capita SDP was only 9th, its ranking in per capita government expenditure in the state, one would have expected that larger private investments would follow. Again, this has not happened.

One reason for the failure of the relatively high state government expenditure to attract private investment may lie in some of the qualitative dimensions of the state's high public expenditure. Much of the expenditure in the state are current expenditure, especially non-plan expenditure. Only a small portion of this expenditure gets transformed into investment. While Kerala’s rank in non-plan public expenditure which represents the current maintenance spending is 4th, its rank in per capital plan expenditure (which represents the fresh investment spending) was only 10th. Its rank in per capita state plan outlay was also the same. While Kerala's position in per capita expenditure on social services was second among the fourteen major sates, its position with regard to expenditure on economic services was only eleventh. It may be noted that in respect of state government's investments, Kerala's rank is the lowest among 13 major states (excluding Madhya Pradesh).

The State's failure to attract private investment is also due to its failure to attract central government investments. In the matter of private sector investment, (and state government investment) Kerala's rank is again the lowest among the 13 major states. Its rank in Central investment is only a shade better (11th). Studies had shown that there is a strong correlation between private sector investment and state government investment (rank correlation coefficient was 0.796).4 If we take the correlation between private investment and total government investment (central government and state government) the coefficient works out to 0.703.

If this analysis holds good our enquiry into the reasons for Kerala's failure to attract private investments during the Nehruvian era as well as during the liberalisation era should be shifted to the factors which crippled the state government's capacity to transform its large expenditure to investments. These factors have been already identified elsewhere. 5 As for the failure of central investment in a resource starved state like Kerala, this points an accusing finger at the existing Centre-State Relationship as also at the economic management of the country, whether it is under centralised planning system or under market system.

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Table - 1

SHARE OF KERALA IN INVESTMENTS DURING THE POST LIBERALISATION PERIOD

(Figures in percentage) Type of investment	Share of Kerala
1. Foreign Direct Investments Approved (1)	
a. Number	1.2
b. Amount of investment	0.2
II. No. of Foreign Collaborations Approved (2)	0.7
III. Industrial Entrepreneur Memoranda Signed (3)	
a. Number	0.8
b. Amount of Investments proposed	1.0
c. Employment potential	0.9
IV. No. of Companies Raising Capital (4)	1.5

Table - I (Contd…..)

V. Disbursement by All India Financial Institutions (5)	1.7
VI. Incremental Public Sector Bank Credit (6)	2.9
VII. Incremental Credit Deposit Ratio	15.8
VIII. CMIE Survey (7)	
a. Investments in Mining and Manufacturing	1.4
b. In electricity Generation	0.3
c. In Irrigation	1.5
d. Total	0.95

Notes and References:

1. Relates to the period, January 1993 to October 1994.
Source: Economic and Political Weekly (EPW), March 11. 1995.

2. Relates to the period, August 1991 to June 1993.
Source: Answer to Rajya Sabha, Question No. 45, Question 4313.

3. Relates to August 1991 - December 1995.
Source: EPW, March 18, 1995.

4. Relates to 1993-`94.
Source: Prime Issue Monitor, Delhi.

5. Relates to 1991-`92, 1992-`93 and 1993-`94
Source : IDBI, Report on Development Banking in India, 1993-`94.

6. Relates to 1993-`94.
Source: CMIE, Basic Statistics: States, Sept. 1994.
The Shape of Things to Come, December 1993.

Table II

DISTRIBUTION OF VOLUME OF INVESTMENT: INDUSTRY BY STATE

(Figures in percentage) Industries	Kerala	All States	No. of Projects
Coal & Lignite	---	2.1	2.1
Crude oil and Gas	---	3.6	0.7
Refinery Products	8.0	7.0	1.4
Mineral Products	8.4	1.3	1.5
Aquaculture	0.2	0.1	0.9
Sugar	----	0.2	1.6
Other Food Products	4.1	0.4	3.7
Vegetable oil	---	0.1	1.4
Vanaspathi	---	0.0	0.5
Beer & Alcohol	0.3	0.2	1.7
Cotton & Blended Textiles	0.9	0.8	5.7
Textile Products	0.1	0.2	1.7
Man Made Fibres	---	1.1	2.3
Other Textiles	---	0.1	0.5
Leather products	---	0.0	0.5
Wood products	0.8	0.0	0.3
Pulp & Paper products	2.0	1.2	2.1
Organic Chemicals	24.8	6.7	6.3
Alkalies	0.9	0.3	1.0
Inorganic Chemicals	12.4	0.7	2.6
Drugs & Pharmaceuticals	0.4	0.4	2.8
Fertilisers	---	2.4	1.2
Pesticides	---	0.0	0.3
Paints & Dyes	---	0.0	0.5
Other Chemicals	0.5	0.1	0.6
Plastic products	---	0.2	1.9
Tyres & Tubes	---	0.5	0.4
Rubber products	0.2	0.0	0.1
Cement & Cement products	---	2.0	2.7
Glass & Glass products	0.4	0.3	0.6
Granite	---	0.1	0.9
Non-metalic mineral products	2.3	0.2	1.3
Pig Iron & Sponge Iron	0.4	1.4	1.8
Steel	---	0.3	4.4
Ferro Alloys	0.2	0.2	0.6
Castings & Forgings	---	0.1	0.7
Tubes & Pipes	---	0.2	0.6
Non-ferrous metals	0.7	2.1	1.9
Metal products	---	0.1	1.0
Non-Electrical Machinery	0.4	0.3	0.9
Agri & Indl. Machinery	---	0.2	1.1

Table – II (Contd…..)

Electrical Machinery	---	0.2	1.4
Electronics	1.3	0.5	2.6
Transport Equipment	---	0.9	1.4
Miscellaneous products	---	0.2	0.8
Electricity	13.4	68.2	10.4
Railways	---	2.1	2.6
Irrigation	16.9	10.8	16.8
Cotton & Blended Textiles	0.9	0.8	5.7
Textile Products	0.1	0.2	1.7
Man Made Fibres	---	1.1	2.3
Other Textiles	---	0.1	0.5
Leather products	---	0.0	0.5
Wood products	0.8	0.0	0.3
Pulp & Paper products	2.0	1.2	2.1
Organic Chemicals	24.8	6.7	6.3
Alkalies	0.9	0.3	1.0
Inorganic Chemicals	12.4	0.7	2.6
Drugs & Pharmaceuticals	0.4	0.4	2.8
Fertilisers	---	2.4	1.2
Pesticides	---	0.0	0.3
Paints & Dyes	---	0.0	0.5
Other Chemicals	0.5	0.1	0.6
Plastic products	---	0.2	1.9
Tyres & Tubes	---	0.5	0.4
Rubber products	0.2	0.0	0.1
Cement & Cement products	---	2.0	2.7
Glass & Glass products	0.4	0.3	0.6
Granite	---	0.1	0.9
Non-metalic mineral products	2.3	0.2	1.3

Source: Centre for Monitoring Indian Economy, Shape of Things to Come Dec.1993.

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