



Finance Department
Government of Kerala

MEDIUM TERM FISCAL POLICY & STRATEGY STATEMENT WITH MEDIUM TERM FISCAL PLAN FOR KERALA

2026-2027 to 2028-2029





**MEDIUM TERM FISCAL
POLICY & STRATEGY
STATEMENT WITH MEDIUM
TERM FISCAL PLAN FOR
KERALA**

2026-27 to 2028-29

FINANCE DEPARTMENT

2026



STATEMENT OF COMPLIANCE

✎ This 2026-27 Medium Term Fiscal Policy and Strategy Statement is placed before the Legislature in compliance with section 3 of the Kerala Fiscal Responsibility Act, 2003.

✎ Section 3 of the Act requires the Medium Term Fiscal Policy Statement to include the following elements all of which have been incorporated in the document.

- ✓ A Statement of recent economic trends and prospects for growth and development.
- ✓ An Assessment of sustainability relating to the revenue deficit and the use of capital receipts for generating productive assets.
- ✓ An evaluation of the performance against targets for 2024-25 and 2025-26.
- ✓ The medium term fiscal objectives of the Government.
- ✓ Three year rolling targets for fiscal indicators with specification of underlying assumptions.
- ✓ The strategic priorities and key policies of the Government.
- ✓ Policies of Government for the ensuing financial year relating to taxation, expenditure, borrowing, other liabilities etc.

FOREWORD

Over the past decade, Kerala has faced multiple shocks which include macroeconomic changes, structural changes and shocks arising out of natural disasters and Covid-19 pandemic. Notwithstanding these headwinds, economy has been resilient. States Own revenue constitute 75% of the total revenue of the State. Despite performing exceedingly well in resource mobilisation, Kerala is facing fiscal stress mainly due to the restrictions on eligible borrowing to the state and conditions imposed for the release of CSS by Union Government. The GST rationalisation and reciprocal tariff measures imposed by the United States, further weakened the tax base and growth of the State.

The GSDP is estimated to grow at 14.15 % in the FY 2026-27 keeping the growth momentum. The priority is on enhancing growth generating capital expenditure, without compromising social welfare spending, while maintaining fiscal consolidation.

Kerala is on the path of fiscal consolidation. The fiscal strategy underpins revenue-led fiscal consolidation. Kerala is of the firm view that Fiscal consolidation should not be achieved through expenditure compression but through revenue augmentation and expenditure efficiency

I present the Medium-Term Fiscal Policy and Strategy Statement before the august house seeking co-operation of all.

29.01.2026

K.N.Balagopal
Minister for Finance

Global Economy

As per the latest *World Economic Outlook*, published by IMF, global growth is projected at 3.3 % for 2025-26 and 3.2 % for 2026-27. The report projects growth to remain resilient amid divergent forces. Headwinds from trade policy shifts are offset by technological investments, fiscal and monetary support, accommodative financial conditions and adaptability of the private sector. Global inflation is expected to fall but US inflation will likely to return to the target more gradually. Key downside risks are re-evaluation of technology expectations and escalation of geo political tensions.

Indian Economy

India's real GDP growth is expected to rise sharply to 7.4 % in the current fiscal, according to the first advance estimate released by the NSO, on the back of a sharp rebound in manufacturing and service sector growth despite the uncertainties caused by the imposition of 50 % tariffs by US on Indian goods. The nominal GDP is projected at 8 % as per the Advance Estimates as against a nominal GDP growth rate of 10.10% projected originally in the Union Budget 2025-26.

While manufacturing is projected to expand by 7 % (at constant prices), agricultural growth is seen declining to 3.1 % from the 4.6 % level in 2024-25. The services sector is projected to expand by 9.1 %, with the impact of boost from Goods and Services Tax

(GST) rate cuts that came into effect in September 2025, and robust services exports.

On the expenditure side, while Private Final Consumption Expenditure (PFCE) is projected to be steady at 7% (at constant prices) in 2025-26 as against 7.2 % in 2024-25, Gross Fixed Capital Formation (GFCF) – a proxy for investments – is expected to rise to 7.8%, a slight improvement from 7.1% growth seen in last year. The Government's Final Consumption Expenditure (GFCE) is expected to be doubled to 5.2 % this year from 2.3 % recorded in 2024-25 led by Government capital expenditure.

Headline inflation rose to a three-month high of 1.33 % in December 2025 which is still below the lower comfort level of 2% set by RBI. Overall, the economy is on a stable footing, anchored by well-contained inflation, resilient domestic demand and supportive policy reforms, even as global uncertainties pose risk to growth outlook.

Kerala Economy & Finances

Over the past decade, Kerala has faced multiple shocks which include macroeconomic changes, structural changes and shocks arising out of natural disasters and Covid-19 pandemic. On the fiscal front, Kerala has demonstrated resilience and fiscal discipline

The share of State's Own Revenue in Total Revenue Receipts improved from 65.61% in 2022-23 to 74.59% in 2024-25. The

State's Own Tax Revenue (SOTR) in Total Revenue Receipts rose from 54.22% in 2022-23 to 61.38% in 2024-25. The SOTR-GSDP ratio remained stable at 6% underscoring consistent revenue mobilisation.

Kerala is facing fiscal stress due to cessation of GST compensation, RD grants, reduction in central share of Taxes and declining assistance from Centrally Sponsored Schemes. Central Transfers as percentage of Total Revenue Receipts (TRR) have declined from 44% in 2020-21 to 25% in 2024-25. The share of central taxes have declined from 3.875% in 10th FC to 2.5% in 14th FC and further to 1.925% in 15th FC. Since 2017, Union Govt have been imposing cut in the eligible borrowing of the state by treating Public Account accruals, borrowing by KIIFB and KSSPL as public debt. Even the commercial borrowing by KIIFB for commercial entities and their repayment made are not considered for replacement borrowing. The reduction in central transfers along with cut in the OMB have resulted in fiscal stress to the state despite the state performing exceedingly well in Own Revenue mobilization.

These pressures are compounded by the GST rationalisation and the recent reciprocal tariff measures imposed by the United States which threatens the State's ability to maintain essential services and honour committed liabilities. The GST rate rationalization has also resulted in substantial revenue losses for Kerala. The State, being heavily dependent on GST revenues,

faces an annual shortfall of approximately around Rs 8,000 crore during the Financial Year 2025-26. This reduction substantially narrows Kerala's fiscal space to sustain Welfare schemes and Developmental expenditure. Reciprocal tariff measures imposed by the United States are adversely impacting Kerala's export-oriented sectors, including Marine products, Spices, Cashew, Textiles, Other export commodities. This is estimated to result in an additional annual loss of approximately Rs. 2,500 crore, further weakening both the tax base and future growth outlook of the State. On the top of it, the State is facing a resource gap of Rs. 21000 crore in the current fiscal, of which Rs.17,000 crore is on account of direct cut from the borrowing space and Rs.4,250 crore due to GSDP estimation by the Ministry of Finance, which deviate from the methodology suggested by the Finance Commission.

The restructuring of MGNREGA into VB-G RAM G with a 60:40 Union-State cost sharing pattern and expanded scope has significant fiscal implication for the State. Kerala, whose wage contribution was negligible (below 2%) under the earlier framework will now have to bear 40% of the total scheme cost resulting in an additional burden of thousands of crores in the years to come.

In the World Economic Forum held in Daos in January 2026, the state has secured Expressions of Interest (EoIs) worth more than one lakh crore, which is expected to uplift demand and growth

of the economy. The most recent Free Trade agreement signed between India and the European Union is expected to benefit mainly the marine export from Kerala.

The total expenditure has increased from 1.02 Lakh crore in 2016-17 to 1.74 Lakh crore in 2024-25. The average annual expenditure during 2016-2021 is 1.17 Lakh crore and that of 2021-2025 is 1.64 Lakh crore.

About 60% of the Revenue Expenditure is met from State's Own Resources. The capital expenditure as a percentage of total expenditure is 10.50% (average for 4 years from 2021-2022 to 2024-2025). An amount of Rs.1,25,032 crore has been spent for capital expenditure for the period 2016-17 to 2024-2025 (excluding capital expenditure by local governments and KIIFB).

Debt-GSDP ratio declined from the pandemic peak of 38.47% in 2020-21 to 34.87% in 2024-25 which shows steady improvement towards the goal of fiscal sustainability. The debt outstanding for the year 2024-25 is 4.35 Lakh crore. The state has been able to arrest the trend of doubling of debt outstanding every five years. Had this trend been continued the debt outstanding would have reached 6 Lakh crore by end March 2026 as against the Budgeted figure of Rs.5.45 crore for 2026-27. That is, the debt stock is expected to be decreased by 0.55 Lakh crore. The GSDP growth

rate exceeds the effective interest rate of Debt which satisfies the Domar condition for debt sustainability.

Kerala is on the path of fiscal consolidation. The state is of the firm view that there should be a fine balance between fiscal prudence and developmental imperatives. Fiscal consolidation should not be achieved through expenditure compression but through revenue augmentation and expenditure efficiency.

Fiscal Performance 2024-25

State's Own Revenue constitute 75 % of total revenue receipts. State's Own Tax Revenue grew by 3.11 % in 2024-25 compared to the previous year. State's Non Tax Revenue grew by 0.86 % compared to the previous year due to stabilisation of receipts in Lotteries. Revenue Deficit and Fiscal Deficit as a percentage of GSDP stands at 2.49 % and 3.86 % respectively as against 1.60% and 3.02% recorded in the previous year. Revenue Deficit and Fiscal Deficit as a percentage of GSDP stands at 2.49% and 3.86% respectively as against 2.29% and 3.51%, in the MTFP target, due to decline in State's Own Tax and Non Tax Revenue due to the general slowdown in economy and higher developmental expenditure. Debt - GSDP ratio stands at 34.87% as against 34.22% in the MTFP target due to the utilisation of borrowing under Power Sector and decline in GSDP growth.

Review of 2025 - 2026

State' Own Tax Revenue grew by 9.25 % in 2025-26 RE compared to the previous year. State's NonTax Revenue grew by 13.79% compared to the previous year. Grand in Aid grew by 3.45 % in 2025-26 RE. Revenue Deficit and Fiscal Deficit as a percentage of GSDP stands at 2.58 % and 3.78 % respectively as against 1.90 % and 3.16% in 2025-26 BE due to decline in Central Transfers and the moderation in GST collection due to the recent rationalisation of GST by Government of India and the disbursement of DA/DR to the employees. Debt - GSDP ratio stands at 34.26 % as against 33.77% in 2025-26 BE. This is due to availment of borrowing under power sector which was not reckoned in the BE.

Three Year rolling Targets and underlying Assumptions

GSDP

Nominal GSDP is projected to grow at 14% keeping with the growth momentum. The prevailing high inflation in the state is reckoned for estimation of GSDP. As the MOSPI is in the process of changing the base year for estimation of GSDP from FY 2011-12 to 2022-23, the estimates of GSDP will undergo revision.

Revenue Receipts

State's Own Tax Revenue (SOTR) is estimated to grow at 12.27% compared to 2025-26 RE. States Own Non Tax Revenue

(SONTR) is estimated to grow at 8.5% over the previous year. The Action Taken Report of the 16th Finance Commission is expected to be placed in the Parliament in the current budget session. The State expects higher devolution of taxes and Grant – in -aid including RD Grant from the 16th FC recommendations. Share of Central Taxes is projected to grow at 53.80% in anticipation of higher devolution from 16th Finance Commission. Grant – in – Aid is estimated at a higher side over the Revised Estimate for 2025-26 anticipating higher allocation of Revenue Deficit (RD) Grant.

Revenue Expenditure

Revenue Expenditure is projected to grow at 25.05% due to increase in salary and pension expenditure and DA/DR disbursements.

Salaries & Pension

The increase in provision for salary and pension is for disbursement of pay revision and DA/DR.

Devolution to LSGs

Devolution to LSGs is made as per the recommendation of the 7th SFC. 6% each of Net SOTR (t-2) is provided as General Purpose Fund (of which 1.5% is statistical adjustment only) and Maintenance Fund. 28.50% of State Plan Outlay is provided as Development fund.

Revenue Deficit and Fiscal Deficit

Revenue Deficit and Fiscal Deficit as a percentage of GSDP is estimated at 2.12% and 3.40% respectively. Additional borrowing of 0.50% for Power reforms is also reckoned. Debt – GSDP is estimated at 33.44%. The Declining trend in Debt- GSDP is in line with fiscal consolidation efforts of the State.

Taxation

Kerala emerged as the front runner in GST administration, leveraging institutional and technological reforms. GST Department was restructured into Tax Audit, Tax payer services and Intelligence to enhance monitoring and tax payer facilitation. Kerala pioneered faceless adjudication and AI enabled return scrutiny systems, strengthening detection of evasion and improving voluntary compliance. GST council secretariat (2024-25) ranked Kerala No.1 among all States. Continued reforms are expected to narrow compliance gaps and enhance tax collection in future.

Strategic Priorities

- ✦ Enhance growth generating productive capital expenditure.
- ✦ Ensure welfare for the poor and vulnerable sections of the society.
- ✦ Sports & Youth, Elderly care
- ✦ Health, Education and Knowledge Economy will continue to be the priority areas.

- ✦ Skilling, R&D and Digital Infrastructure
- ✦ Innovation & Starts-ups, Tourism
- ✦ Sustainability and Green growth
- ✦ MSME, Infrastructure and connectivity
- ✦ Women empowerment

Forward Estimates and underlying Assumptions

GSDP

Nominal GSDP is projected to grow at 12 % for both 2027-28 and 2028-29.

Revenue Receipts

State Own Tax Revenue is estimated to grow at 12% in the forward estimate period. Non Tax Revenue is projected to grow at 9%.

Central Transfers

Share of Central Taxes and Grant -in- aid are estimated to grow at 10% and 5% respectively in the forward estimate period.

Borrowing, Public Debt and Other Liabilities

Borrowing ceiling is fixed at 3.5% of GSDP in the forward estimate period in anticipation of additional borrowing to the extent of 0.50% for Power sector reforms from 2026-27 onwards. Debt- GSDP ratio stands at 33.36% and 33.29% for 2027-28 and 2028-29 respectively.

Interest

Interest is worked out by applying effective interest at the rate of 7% on outstanding debt.

Subsidies

An allocation of Rs.2000 cr. each is provided for Subsidies for both the years.

Devolution to LSGs.

The recommendations of the first report of the 7th SFC covers only the Financial Year 2026-27. The recommendations for the subsequent years is yet to be submitted. Therefore, the recommendations for the year 2026-27 is adopted for the estimation. However, the Development Fund is kept at the level of 28.5% itself for the forward estimate period.

Capital Expenditure

Capital Expenditure is projected to grow at 14% and 16% for the years 2027-28 and 2028-2029 excluding capital spending by KIIFB and LSGs.

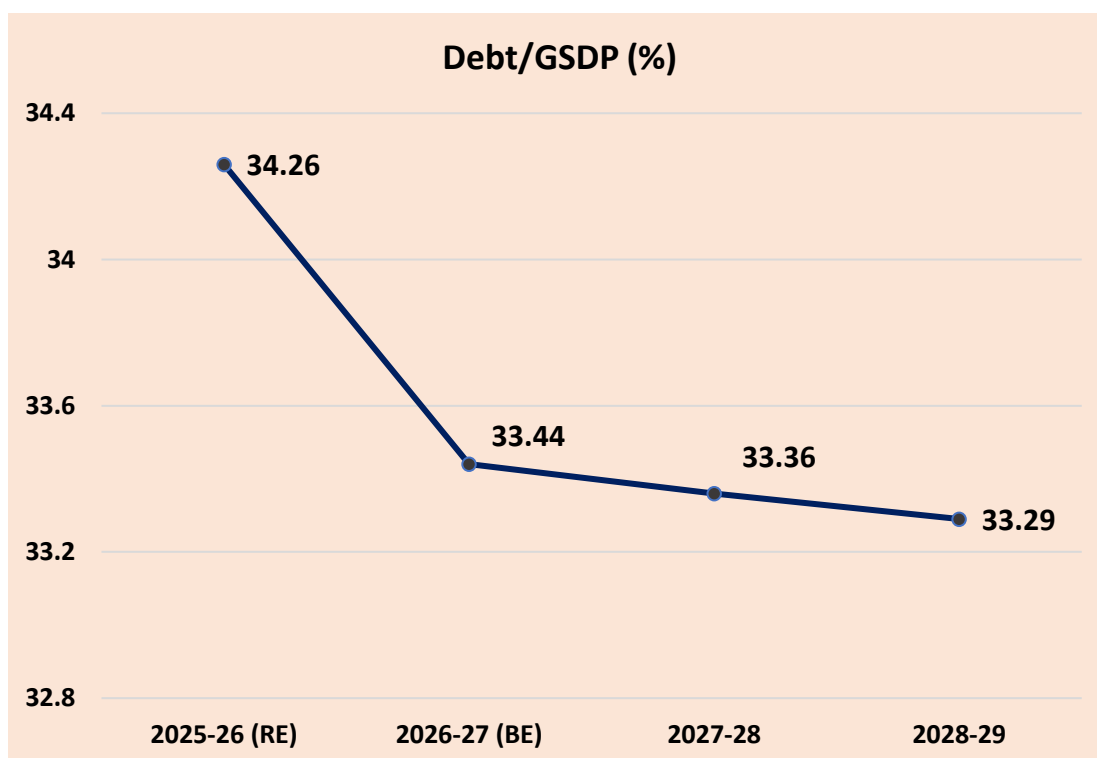
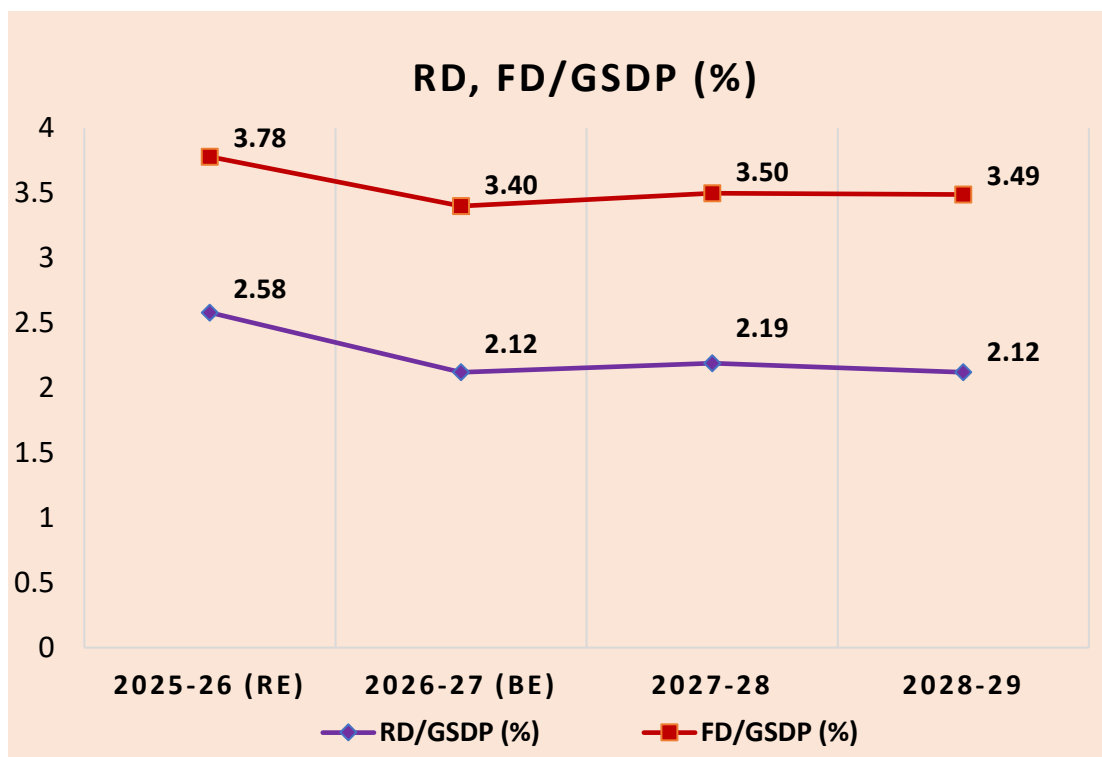
Revenue Deficit and Fiscal Deficit

Revenue Deficit as a percentage of GSDP is projected at 2.19% and 2.12 % in the forward estimate period. Fiscal Deficit as a percentage of GSDP is projected at 3.50% and 3.49 % in the forward estimate period. Debt – GSDP as a percentage of GSDP is projected at 33.36% and 33.29 % in the forward estimate period of 2027-28 and 2028-29.

MTFP Targets

ITEM	2025-26	2026-27	2027-28	2028-29
	RE	BE	Forward Estimates	
RD/GSDP (%)	2.58	2.12	2.19	2.12
FD/GSDP (%)	3.78	3.40	3.50	3.49
Debt/GSDP (%)	34.26	33.44	33.36	33.29

Fiscal Consolidation Path



State's Fiscal Plan 2026-27

(Rs. In Crores)

Item	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
	Accounts	Accounts	Accounts	RE	BE	Forward Estimate	
Revenue Receipts	132724.65	124486.15	124861.07	137082.61	182972.10	201620.82	222275.46
State's own tax revenue	71968.16	74329.01	76642.19	83730.96	94002.47	105282.77	117916.70
Non Tax Revenue	15117.96	16345.96	16486.62	18760.72	20355.77	22187.79	24184.69
Resources from Centre	45638.54	33811.18	31732.25	34590.93	68613.86	74150.27	80174.07
Revenue Expenditure	141950.94	142626.34	155920.79	173971.80	217558.76	241490.22	265639.25
Non-Interest Revenue Expenditure	116774.58	115640.12	126782.56	142155.79	183182.74	201116.83	220527.47
Interest	25176.36	26986.22	29138.23	31816.01	34376.02	40373.39	45111.78
Salaries	37902.84	38572.85	39903.81	43889.87	57564.15	60442.36	63464.48
Pension	26090.04	25644.24	27875.21	29414.60	38669.12	40602.58	42632.70
Non SPI Revenue Expenditure	52781.70	51423.03	59003.54	68851.32	86949.47	100071.90	114430.29
Subsidies	1542.50	1446.77	1490.42	1690.42	2382.14	2000.00	2000.00
Devolution to LSGs	10838.47	9021.07	14010.05	14257.59	17901.45	18610.76	20116.33
Revenue Expenditure excld SPI, subsidies & Devol.to LSGIs	40400.73	40955.19	43503.07	52903.31	66665.88	79461.14	92313.96
Revenue Surplus/Deficit	-9226.29	-18140.19	-31059.72	-36889.19	-34586.66	-39869.40	-43363.79
Capital Expenditure	16787.49	16880.17	17886.77	18483.80	22348.38	25555.78	29677.17
Capital Outlay	13996.56	13584.45	15082.41	15670.22	19451.16	22368.83	26171.54
Loan disbursements	2790.93	3295.72	2804.36	2813.58	2897.22	3186.94	3505.64
<i>Non Debt Capital Receipts</i>	<i>459.23</i>	<i>762.31</i>	<i>698.36</i>	<i>1423.49</i>	<i>1515.53</i>	<i>1667.08</i>	<i>1750.44</i>
Fiscal Deficit/Surplus	-25554.54	-34258.05	-48248.14	-53949.50	-55419.51	-63758.09	-71290.52
Primary Deficit/Surplus	-378.18	-7271.83	-19109.90	-22133.49	-21043.49	-23384.70	-26178.75
End of the period Debt	348916.52	377063.06	413623.94	462112.08	516871.70	576762.71	644453.93
Debt Service	25176.36	26986.22	29138.23	31816.01	34376.02	40373.39	45111.78
Salary+Pension+Interest	89169.24	91203.31	96917.25	105120.48	130609.29	141418.32	151208.96
Debt Stock	362191.89	391934.23	435313.65	488910.50	544832.89	608692.53	680215.33
Government Guarantees	50374.49	62387.93	73799.14				
Interest/Revenue Receipts (%)	18.97	21.68	23.34	23.21	18.79	20.02	20.30
Debt/Revenue (%)	272.89	314.84	348.64	356.65	297.77	301.90	306.02
(Salary+Pen+Interest)/Revenue (%)	67.18	73.26	77.62	76.68	71.38	70.14	68.03
(Salary+Pen+Interest)/GSDP (%)	8.58	8.03	7.76	7.37	8.02	7.75	7.40
(Salary+Pen)/GSDP (%)	6.16	5.66	5.43	5.14	5.91	5.54	5.19
Rev Deficit/Rev Receipt (%)	6.95	14.57	24.88	26.91	18.90	19.77	19.51
RD/GSDP (%)	0.89	1.60	2.49	2.58	2.12	2.19	2.12
FD/GSDP (%)	2.46	3.02	3.86	3.78	3.40	3.50	3.49
Debt Stock/GSDP (%)	34.87	34.52	34.87	34.26	33.44	33.36	33.29
GSDP	1038734	1135372	1248533	1427145	1629073	1824561	2043509
Nominal GSDP Growth Rate (%)	12.36	9.30	9.97	14.31	14.15	12.00	12.00

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