CASE STUDY

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Building an Urban Policy from the Ground Up: How Kerala Developed a State Urban Policy and What It Means for Municipal Finance

This case study demonstrates how a tradition of participatory local governance, combined with climate shocks and recognised governance failures, can catalyse the development of a comprehensive urban policy framework. Kerala shows how an autonomous, consultative process can generate analytically grounded and ambitious policy reforms.

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1. Overview and Purpose

Kerala's experience demonstrates how a state with deep roots in participatory local governance can translate that tradition into a structured urban policy framework. The trigger for the current urban policy was a combination of recognised governance failure and climate shock. Catastrophic flooding in 2018 and subsequent years exposed Kerala's urban areas as hotspots of vulnerability, and by the early 2020s there was an honest admission within government that existing frameworks were not working.

The Kerala Budget Speech of 2023 announced that a new Urban Policy would be formulated, and a Kerala Urban Policy Commission was constituted by government order in December of that year. Critically, the Commission was given full intellectual autonomy, such that its findings could not be altered by the bureaucracy or the state government, and its 24-month process engaged over 7,000 to 8,000 people across 53 stakeholder consultations, underpinned by 40 commissioned studies.

The resulting Kerala Urban Policy, passed in February 2026 and organised around ten pillars, makes Kerala the first state in India to develop a comprehensive urban policy. The most significant pillar for municipal finance purposes is Pillar 9 on Innovative and Sustainable Urban Finance, which proposes credit rating of ULBs, Kerala Municipal Bonds for the three largest corporations, pooled bonds for smaller municipalities, revision of the Kerala Municipality Accounts Manual, and the establishment of Project Initialisation Fund to support bankable project preparation. These proposals are more specific and more ambitious than the equivalent sections of most state urban policies, and they reflect a genuine analytical grasp of the fiscal challenge.

2. Urban Context and Structural Challenge

In 1996 the newly constituted Kerala State Planning Board launched the People's Planning Campaign, to empower panchayats and municipal bodies to design and implement their own development projects under India's Ninth Five-Year Plan (1997–2002).[1] The expectation was that 35 to 40 per cent of that Plan's budget would be devolved to local bodies to fund these projects. Over three million people attended local meetings in the first phase alone, and approximately 100,000 Local Resource Persons were trained across the state. Significantly, the Campaign cut across political lines, as around 40 per cent of local bodies at the time were opposition controlled. That experience left Kerala with substantive consultation culture, relatively strong local data systems and a working relationship between state agencies and Urban Local Bodies (ULBs) built on mutual engagement.

Yet that institutional foundation, built primarily around rural governance, was not designed for the scale and character of urbanisation that followed. Kerala is a state of approximately 35 million people with one of India's highest human development profiles, but studies project that over 90 per cent of its population will be urbanised by 2035.[2] What makes this distinctive is not simply the pace of urbanisation but its form: rather than the concentrated residential and commercial cores typical of Indian cities, Kerala has developed through dispersed settlements and ribbon development along transport corridors, creating governance challenges that do not map neatly onto existing administrative boundaries and for which the tools developed through the People's Planning Campaign were not calibrated.

[1] Isaac, T.M.T. and Harilal, K.N. (1997) 'Planning for empowerment: People's Campaign for decentralised planning in Kerala', Economic and Political Weekly, 32(1/2), pp. 53–58.
[2] Government of Kerala (2023) Formulation of State Urban Policy: Constitution of Kerala Urban Policy Commission. G.O. (Ms) No. 219/2023/LSGD. Thiruvananthapuram: Local Self Government (DC) Department, 22 December

The fiscal health of ULBs has deteriorated alongside this urban growth. Own-source revenue as a share of total revenue receipts has fallen. The introduction of the Goods and Service Tax (GST) is a significant part of the explanation: before GST, municipalities had access to a range of indirect tax instruments, but their consolidation into a single federal regime removed that fiscal space almost entirely, leaving property tax and profession tax as the principal levers available to ULBs.[3] The result is structural dependence on fiscal transfers, with these grants now constituting about 66 per cent of total ULB receipts.[4] This in turn exposes local investment programmes to the volatility of central and state transfer decisions and leaves municipalities with little autonomous capacity to plan or borrow for infrastructure.

This fiscal fragility was compounded by a structural mismatch between political cycles and the timescales that urban investment requires. Five-year municipal council terms, combined with frequent changes in political composition and limited institutional carry-over between administrations, create discontinuities in the long-term planning and investment commitments that urban infrastructure demands. A road network, a drainage system, or a municipal bond programme cannot be designed, financed, and delivered within a single electoral cycle, yet no legal instrument exists in Kerala to embed those commitments across administrations or to insulate capital investment programmes from the priorities of incoming councils.

By the early 2020s, the cumulative weight of these pressures had become impossible to ignore. Kerala had built a well-deserved reputation for rural governance and decentralised planning, but there was a growing recognition within government that the same tools and institutional approaches were not working in urban areas. Basic challenges, such as waste management, mobility, land use, service delivery, were proving resistant to existing frameworks, and government was finding it increasingly difficult to respond effectively. Climate change sharpened that sense of urgency further. Kerala had experienced catastrophic flooding in 2018 and again in subsequent years, events that exposed its urban areas as hotspots of vulnerability and demonstrated that existing governance and planning instruments were not adequate to the scale of climate risk that rapid urbanisation was concentrating in its towns and cities.

3. Project Approach and Experience

It was against that backdrop that the Kerala Budget Speech of 2023 announced that a new Kerala Urban Policy would be formulated. The Local Self Government Department issued Government Order G.O. (Ms) No. 219/2023/LSGD in December of that year, constituting the Kerala Urban Policy Commission and setting out its terms of reference. The Commission was deliberately structured to combine external credibility with local government voice: the Chair was an internationally recognised academic who brought both standing and distance from the internal politics of Kerala's urban governance, while the co-chair was the Mayor of Kochi and Chairperson of the Mayors' Council of Kerala, giving elected city government direct representation at the Commission's leadership level. Equally significant was the degree of intellectual autonomy the Commission was afforded as its members were free to build their arguments independently, its findings could not be altered by the bureaucracy or the state government, and no attempt was made to steer its conclusions from outside. The Commission's secretariat was housed at the Kerala Institute of Local Administration.

[3] Kannan, R. and Venkatachalam, P. (2024) 'Did the implementation of GST hurt municipal finances?', Economic and Political Weekly, 59(1)
[4] Comptroller and Auditor General of India (2024) Report on Urban Local Bodies, Kerala. New Delhi: CAG of India

The Commission was given a 24-month tenure, with terms of reference that were broad, covering urbanisation patterns, local governance frameworks, sustainable development, administrative reform, sectoral policy convergence, and regulatory change. It was explicitly asked to galvanise both spatial planning and local participatory democracy, and the process reflected that ambition in its reach: over 7,000 to 8,000 people were engaged across the course of the work, including all elected representatives, bureaucrats, media, and young people, a breadth of participation that the Commission regarded as essential to the credibility of its findings. This was underpinned by 40 commissioned studies that together resulted in comprehensively evidenced report, grounded in direct engagement with the full range of actors who would ultimately need to implement it.

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The resulting Kerala Urban Policy, passed in February 2026, is organised around ten pillars (see figure above). The most significant for municipal finance purposes is Pillar 9, on Innovative and Sustainable Urban Finance, which is more specific and more ambitious than the equivalent sections of most state urban policies and reflects a genuine analytical grasp of the fiscal challenge. Its proposals include:

- Mapping the full range of funding options available to ULBs across own sources, central and state devolution, domestic and international financing, and community and private sector contributions.
- Revision of the Kerala Municipality Accounts Manual of 2007 to bring financial reporting up to standards compatible with capital market requirements
- A financial health assessment of ULBs as the basis for credit rating
- The pursuit of Kerala Municipal Bonds for the three largest municipal corporations (Thiruvananthapuram, Kochi, and Kozhikode) to be issued directly

- Pooled bonds through KIIFB (Kerala Infrastructure Investment Fund Board, the state's infrastructure financing institution), KURDFC (Kerala Urban and Rural Development Finance Corporation, which channels finance to local bodies), or a new Special Purpose Vehicle for smaller corporations and larger municipalities that lack the scale or creditworthiness to issue bonds independently

- Creation of a Project Initialisation Fund to support preparation of viable, bankable projects

4. Key Lessons and Transferable Insights

What the Process Got Right

- The decision to establish an independent Commission with full intellectual autonomy and insulated from short-term political pressure, which gave the process a credibility that government-steered policy exercises rarely achieve.

- The breadth of the consultation and research process generated an evidence base substantial enough to support a 25-year policy framework, and the deliberate inclusion of youth reflected a recognition that the urban investment decisions embedded in the policy will shape the lives of a generation not yet in positions of institutional power.

- The policy treats finance both as a dedicated pillar and as a thread woven through its broader framework, connecting land use, climate resilience, governance reform, and economic development.

- The proposal to revise the Kerala Municipality Accounts Manual before attempting capital market financing is the prerequisite on which creditworthiness, investor confidence, and ultimately bond issuance all depend.

Challenges and Constraints

- The most significant risk facing Pillar 9 is the gap between policy ambition and implementation capacity as preparing a bond prospectus, managing a credit rating process, or administering a Project Initialisation Fund requires financial and legal expertise that most Kerala municipalities do not currently have on staff, and building that capacity may take years.

- The Commission's costs were met through a combination of fiscal grants, a World Bank Programme for Results grant, and state budget provisions, which is a structure that gave the process financial flexibility but also embedded external priorities into its agenda.

- Full public disclosure of the Commission's findings remains an outstanding issue as only a 37-page summary of the full policy has been made publicly available, even though it was funded largely from public sources.[5]

5. Key Takeaways

- Developing a comprehensive urban policy requires genuine political will at the highest level of government, which in turn gave the Commission the mandate, the resources, or the protection from interference that made its work credible.

[5] Thankachan, S. (2026) 'Kerala Urban Policy 2026–2050: Vision, transparency, and the need for a rights-based framework', *Mainstream Weekly*, February 2026. Available at: http://www.mainstreamweekly.net/article16526.html

- Commissioners were free to build their arguments without interference, which included the ability to name the fiscal and governance failures that had accumulated over decades, rather than producing a document that reflected what government wanted to hear.
- The breadth of Kerala's consultative process for the urban policy helped build the shared understanding and legitimacy that a 25-year investment agenda will need to survive political transitions and competing priorities.
- Integrating finance as a thread running through the entire urban policy, rather than treating it as a standalone technical annex, is what gives an urban policy document genuine traction in terms of its operationalisation that must now follow.

This Case Study was prepared by Tikender Panwar and Astrid R.N. Haas, by way of contribution to the work of the CSCC Urban Finance Action Group, March 2026.

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