Freebies and Subsidies in India: Are They Leading to Fiscal Vulnerabilities?

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Abstract
Subsidies and freebies are tools, governments use to achieve economic and social objectives. They influence resource allocation, income distribution, and market outcomes. While subsidies aim to reduce costs and promote specific economic activities, freebies often cater to immediate political or social demands.
This paper examines the economic implications of subsidies and freebies, particularly in the context of India, and their effects on state budgets, fiscal health, and poverty alleviation. While subsidies are typically targeted financial transfers aimed at achieving specific policy objectives, freebies are indiscriminate handouts, often used as electoral tools. The study highlights the fiscal burden caused by freebies, which contribute to rising public debt, budget deficits, and market distortions. Although cash transfers and subsidies provide immediate relief, and can temporarily improve living standards but they often fail to address the root causes of poverty and can lead to long-term economic inefficiencies. In the context of a lack of credibility among political powers, political clientelism may crop up. The paper explores the concept of the poverty trap, and a sample case of 'Ladaki Bahin Yojana' used during the electoral campaign in the State of Maharashtra. The analysis calls for a balanced approach, advocating for targeted subsidies alongside broader development initiatives focused on education, job creation, and economic empowerment to foster long-term, sustainable growth.

Keywords: Subsidies, freebies, fiscal burden, electoral campaign, poverty trap, sustainable growth, etc.

INTRODUCTION
The term 'subsidy' is used rampantly in Economics, while a proper definition of it is seldom found. Even the World Trade Organization acknowledges that a narrow approach of determining subsidies will present an incomplete picture. The Cambridge Dictionary defines subsidy as 'money given as part of the cost of something, to help or encourage it to happen'. (Cambridge Dictionary, n. d.). Although the World Trade Report contends that mere fiscal transfer may be an insular approach to the concept, some features are still important here. Subsidy is essentially a transfer of some form of benefits from the government to its subjects, and it is carried out in a targeted manner. It may be done for a particular objective, and aimed at a niche beneficiary cohort. Subsidies often take form of availability of goods at reduced cost, interest subvention credit etc. As it is, completely waiving off fees of the goods are not characteristic to subsidies.
Freebies on the other hand, are true to their name. The entire charge on these goods is waived off, and they are given 'for free', hence the name. They are typically used as an election tool, aimed at appeasing the

voters to vote for a particular party. As is the case of subsidies, freebies are also not well-defined in Economics. However, unlike the former, freebies are not targeted tools, and no payment is exchanged in lieu of their consumption.

As can be inferred from above, both subsidies and freebies possess the risk of inculcating bad credit culture in the society. Subsidies are usually targeted, and are somewhat effective in achieving the set aim. Freebies on the other hand, are more often than not, just populist measures taken with electoral gains in mind. Freebies, more so than subsidies, put great burden on the fiscal conditions of the country. In 2019 Lok Sabha Election, Akhileash Yadav, President of Samajwadi Party in Uttar Pradesh, distributed free laptops without even cross-checking the status of one House-one Laptop. Obviously, households received 3 to 4 Laptops and then they were reselling them in the market to encash it. This is a typical example of freebies. Also distribution of Laptop did not take the appropriate users into consideration. The distribution was quite randomly done. Another form of Freebies is 'cash handouts' to the accounts of beneficiaries, a trump card in the hands of political parties as it serves the purpose of winning the elections.

There are two ways to look at it. One is of fiscal burden and the other is for the poverty eradication programme.

Budgetary burden – subsidies and freebies-

There is always a budgetary allocation for subsidies. For example, to reduce the drop- out rates in schools and also to improvise the children's nutrition intake, if the government decides to run a mid-day meal programme, then such a programme will surely have a plan and the required financial allocation accordingly.

Whereas in case of freebies, it would not have any budgetary allocation and the decision to distribute something free of cost to beneficiaries would be over and above the budgetary provisions. Avery recent example of this is, ' Ladki Bahin Yojana' which got declared in Maharashtra just before the VidhanSabha elections. For this on the spot announcement, no budgetary provision was in place and this random distribution of funds to poor ladies will certainly create a fiscal burden for the state. We get to see many such cases happening in different states at different time referring to this concern of fiscal burden.

There are freebies which come in the form of free distribution of goods (like Laptop in UP) before the election in anticipation that people would vote the respective political party. Cash handouts are also very common in this category. In this form of freebies, financial arrangement would take place through the political party budget which would mainly come from the corporates, for example, the Electoral Bond Scheme, 2024, but earlier also there were and even today there are number of ways in which corporate sector finance the electoral expenses of the political parties. The corporate support also happens in anticipation of future business related support if the same party wins the election. It is completely based on the give and take relation and these features of crony capitalism would not come into the focus unless and until the legal checks and balances are in place.

A promise of free supply of electricity, water and even free transportation, etc., political party would declare this before even winning the elections, assuming that such declarations will make them win it. Pre-winning announcements are done and then after winning the election, the party needs to keep its promise. Here comes the question of budgetary allocations, financial jugglery within the fiscal space of the state. Else the bad credit creation becomes habitual.

Assembly elections in Karnataka, Telangana, Himachal Pradesh and even in Punjab, were won by based on several such guarantees. 'Ladli Bahena' in Madhy Pradesh is another success story of fund transfers to beneficiaries and winning elections.

In Odisha, the BJP implemented the Subhadra Scheme to provide one crore women direct financial assistance of Rs. 50,000 over five years creating budgetary provision of almost Rs. 55,825 crore.

West Bengal has perhaps the largest number of such handout schemes, covering practically every section of voters, including its much-touted Lakshmir Bhandar under which 2.2 crore women get Rs. 1,200 or Rs. 1,000 every month in htier accounts, depending on whether they belong to the SC/ST category or not.

Digital Jan-Dhan connectivity has made implementing these promises involving direct benefit transfers a seamless process. When we discuss the inclusive development, implementing development schemes/projects and delivering their benefits to a large scale of population which would require many glitches to be fixed, but transferring cash to poor, vulnerable (could be so-called also) is rather easy and instant.

Fiscal Concern:

These handouts are pushing public debt to unsustainable levels. Gross Fiscal Deficit to nominal Gross State Domestic Product (GFD to GSDP) is an important metric to analyze the above premise. Responsibility of establishing financial discipline in the economy is equally there on States' shoulders. Going as per the recommendation of the 15th Finance Commission, the desirable level of 3% fiscal deficit to GSDP ratio has been crossed almost by 21 States in India during 2022-23 and continuing with the same trend in FY 2023-24 apparently.

Following table gives us the status of few States mentioned below:

Table-I

States	FY 2022-23	FY 2023-24
Andhra Pradesh	3.6	3.8
Karnataka	2.7	2.5
Kerela	3.5	3.4
Madhya Pradesh	3.6	3.8
West Bengal	4.0	3.8
Punjab	4.9	4.7
Maharashtra	2.7	2.5
Himachal Pradesh	6.4	4.6
All States	3.5	3.2
Centre	6.4	5.9

Source: Handbook of Statics on Indian Economy 2022-23

Karnataka's fiscal deficit is projected to swell from Rs. 42, 622 crore, or 2 percent of GSDP in FY 23, i.e. before election, to Rs. 82,980 crore, or 3 percent of GSDP, in FY 25.

States like Bihar, Kerala, Punjab, Rajasthan and West Bengal are majorly distressed, and have a high Debt-to-GSDP ratio.

Another metric of fiscal distress is Interest Payment to Revenue Receipts (IP-RR) ratio. It explains the debt-servicing capability of a State against its revenue. The higher the ratio, the worse is the fiscal management of the State.

An RBI paper, Mukherjee et al. (2022), analyzes the major causes of this distress. The authors have come up with some common but crucial reasons. They are: indiscriminate disbursal of freebies and subsidies, dysfunctional power distribution companies that frequently need bailing out, increasing natural disasters that need tending to, etc.

Share of subsidies and freebies in state finances has only grown in the past years. Subsidies against total revenue expenditure were 7.8% in 2019-20, which grew to 8.2% in 2021-22. States such as Jharkhand, Kerala, Odisha, Telangana and Uttar Pradesh saw the largest increase in this regard.

RBI data on states shows that states with high revenue deficit are Rajasthan, Tamil Nadu, Kerala, Andhra Pradesh and Punjab. Maharashtra, Uttar Pradesh, West Bengal, Tamil Nadu and Kerala have high interest payments components in their budgets. These states, with inclusion of Karnataka are also toppers in the list of States with highest social sector expenditure. However, since these are the states with highest GSDP figures, and highest capital expenditure figures, they often get away with spending more on revenue account.

For the entire country, expenditure on subsidies in the current financial year is given in the table below:

Table-II

	Actuals 2023-24	Budgeted 2024-25	Revised 2024-25	Budgeted 2025-26	% change (2024-25 RE to 2025-26 BE)
Food Subsidy	2,11,814	2,05,250	1,97,420	2,03,420	3.0%
Fertiliser subsidy	1,88,292	1,64,000	1,71,299	1,67,887	-2.0%
Interest subsidy	19,516	29,550	28,156	27,840	-1.1%
LPG subsidy	12,240	11,925	14,700	12,100	-17.7%
Other subsidies	3,037	17,698	16,294	14,969	-8.1%
Total	4,34,899	4,28,423	4,27,868	4,26,216	-0.4%

Sources: Expenditure Profile, Union Budget 2025-26; PRS

Freebies are a special cause for concern due to some of the following reasons-

- Handing out free goods undermines a good credit culture, and sets in bad economic habits.
- The cross-subsidization undergone in the process distorts prices. Naturally, the foundations of a well-functioning market are destabilized, and private sector is disincentivized from participating.
- Wage rates are manipulated and a general misallocation of resources is seen.
- Further, freebies with regards to water and electricity only encourage their overexploitation.

Some papers such as Sahoo et al. (2023), and Srivastava, D., Bhujanga Rao, C. (2002), suggest that targeted subsidies, which cater to provision of merit goods to all societal strata, are more useful in elevating the standard of living among people. However, instead of a sound vision, subsidies and freebies are seen more as an electoral tool aimed at appeasement of respective vote banks.

Monthly transfer of money to women, pilgrimage travel freebies to the elderlies, bus fair waive off to women etc. are some of the freebies offered. Experts believe that this will greatly increase the fiscal burden on the Government.

Removal of Poverty Trap-

A case of 'Ladki Bahin Yojana' in Maharashtra -

Ahead of Assembly elections in November 2024 in the State of Maharashtra a slew of freebies has been announced by the ruling coalition, with the opposition also chipping in their own likewise promises. A monthly cash transfer scheme for women is said to have played a significant role in the Mahayuti coalition's resounding history. Under the scheme, beneficiaries receive Rs. 1,500/- per month, with a promise by Mahayuti leaders during the election campign to increase the amount to Rs. 2,100/- According to the report, the scheme costs the State exchequer approximately Rs. 3,700 crore a month, projected to cost the State Rs. 46,000 crore annually. (Aiyar, 2024) The State Government Budget for FY 25, has pegged the state fiscal deficit at 2.6% of the GSDP. Experts attribute the entirety of this rise to the populist schemes. (Surabhi, 2024). With a heightened fiscal expenditure, economists fear that the brunt will be borne by a reduced capital expenditure, stunting the state growth in the long run.

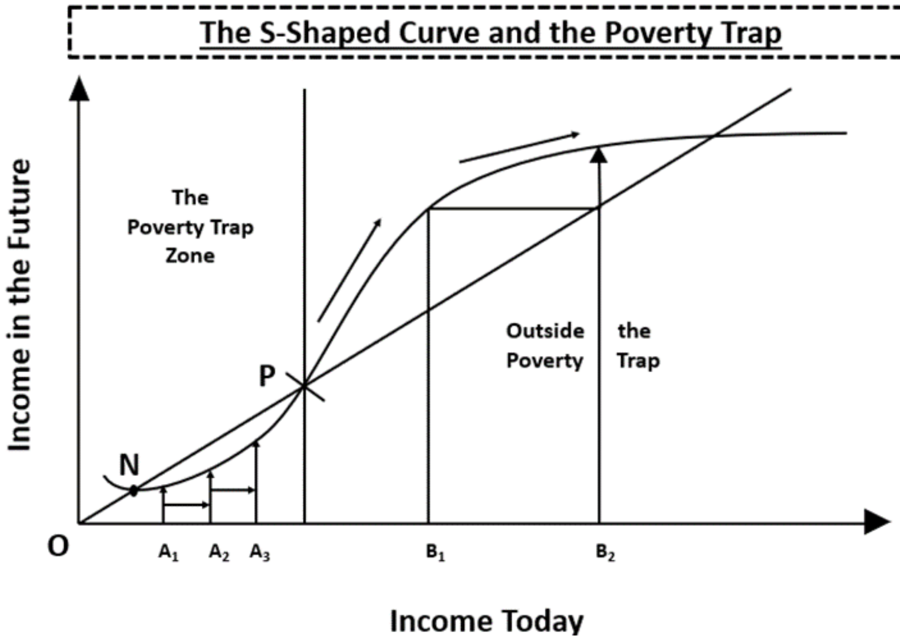
However, the credit rating agency ICRA is of the opinion that this increased Fiscal Deficit may not pose a serious threat to the State of Maharashtra. It suggests that since Maharashtra has been a more fiscally prudent state in the past (at least amongst its undertaken sample), the overall fiscal burden can be absorbed over time. (Business Standard, 2024).

The scheme has faced criticism as cash handouts offer only temporary relief. Skill development and job creation are the real solutions to poverty. Such schemes also risk fuelling inflation by boosting consumption demand. However, many countries, including Mexico (Oportunidades), Brazil (Bolsa Família), Kenya (GiveDirectly programme), the US as well as some countries in Europe, often turn to cash transfers. India, too, has a history of transferring maternal benefits, including the recent Covid-relief to women's accounts. Government transfers can be in two forms: Cash, like the Ladki Bahin scheme, or subsidised goods and services, such as free staples, cheaper LPG cylinders. While both aim to help the poor, they affect consumption differently. Direct cash transfers empower recipients to spend as they wish, enhancing purchasing power without interfering with market prices or consumer choice.

Gokhale Institute of Politics and Economics did a survey on the much debated ' Ladaki Bahin' scheme and found out that most women in the study used the money for groceries and medicines. Such spending boosts the local economy aligning with the objective of the scheme. Some also used it for travel or their husband's business, showing that it gave them an extra elbow room as per their consumption preference.

Can the small transfers to households uplift them from backwardness and poverty? These transfers are definitely profitable in electoral battles, comforting for the poor but may not be enough to end endemic poverty. Although it is designed to empower women economically, it has sparked an intense debate about its implementation and impact. While some critics argue that this amount is too meagre to make meaningful difference in the lives of poor women, others dismiss it as a misallocation of taxpayers' hard-earned money aimed at pleasing voters. A common thread in these debates is the criticism of "free doles" that are undesirable and unsustainable for the government's finances.

Theoretically, poverty eradication plan along with some financial direct transfers can be portrayed in the following manner.



Source: Poor Economics, Abhijeet v. Banerjee

When we refer to the poverty trap, the World looks like the above figure. Your income today influences what your income will be in the future (the future could be tomorrow, next month or even the next generation): what you have today determines how much you eat, how much you have to spend on medicines or on the education of your children, etc., and all this determines what you will have tomorrow.

The shape of the curve is key here. The rough S-shape of the above curve is the source of the poverty trap. On horizontal line, income today is measured and on vertical axis, income in the future is taken up. For the very poor who are in the poverty trap zone, income in the future is lower than income today. The curve below the diagonal line in the graph, showcases the poverty trap zone. This means that over time, those in this zone become poorer and poorer, and finally get trapped in poverty's vicious circle. As shown in the graph, if such poor group receives a onetime monetary gift or recurring financial support at point A1, then they would start heading towards point 'P'. Fixed amount of financial transfers to such groups, would surely change their consumption pattern. More access to nutritious food or education or health, though at crawling rate, but would help them improve their living standards. After reaching at point 'P', the given free finance push would help them move further on the graph above the diagonal line.

But this theoretical framework does not match up with the real life cases. Abhijit Banerjee in his book, 'Poor Economics' has given multiple examples of how free means worthless across the World. He puts it up in the form of 'psychological sunk cost' effect – people are more likely to make use of something they have paid for. In addition, free means inferior quality and people may judge quality by price. Things may be judged to be valueless precisely because they are cheap or because they are freely available, which then leads to diminishing utility hypothesis experience.

However, several studies that have tested whether people use things less because they got them for free found no evidence of such behaviour. Several studies observe that poor people would react differently to different subsidies and freebies. The poor seem to be trapped by problems such as, lack of information or half information, weak beliefs and procrastination, which is also very high among the poor.

Conclusion:

In conclusion, the debate surrounding subsidies and freebies underscores significant challenges faced by governments, particularly in terms of fiscal sustainability and long-term development. While subsidies are generally targeted and may serve as effective tools for achieving specific policy objectives, the indiscriminate distribution of freebies, often linked to electoral gain, poses a substantial risk to public finances. These free goods and services may temporarily alleviate hardship, but they often foster a culture of dependency, lead to market distortions, and escalate fiscal deficits.

The larger concern lies in the long-term impact on state budgets, where excessive spending on these populist measures strains resources and diverts funds from critical areas such as infrastructure and skill development. While cash transfers, as seen in various schemes like Maharashtra's "Ladki Bahin Yojana," may offer immediate relief, they often fail to address the underlying causes of poverty. True poverty alleviation requires comprehensive strategies focused on education, job creation, and economic empowerment, rather than reliance on one-time or short-term financial handouts.

Ultimately, a balanced approach is needed—one that integrates targeted subsidies with sustainable development initiatives, ensuring that immediate relief does not come at the expense of long-term economic health. Both governments and citizens must recognize the importance of fiscal discipline, strategic investments, and the creation of opportunities that break the cycle of poverty rather than perpetuate it.

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