

ISSN 2394-2

Metric
Engl
R.B.S

PURSUIT

(A Half Yearly International Peer Reviewed Multi-Disciplinary Research Journal)

Vol. III, Issue - VI (July 2016)

Prin. Dr. D. B. Shinde
Editor-in-Chief

Dr. S. K. Binnor
Executive Editor

Government Subsidies in India

Mr. Rajendra B. Shinde

Associate Professor

Head, Department of English

Arts, Science & Commerce College,

Ozar (MIG)

rbshinde2011@gmail.com

Introduction:

This paper attempts to study the benefits and drawbacks of government subsidies in India. 1) According to **Kishore Jethanandani**, "Subsidies are akin to steroids as prescriptions. Lazy doctors like to administer to their ignorant patients a dose of steroids to remedy the proximate cause of illness. Steroids provide quick relief but don't promise an enduring cure." 2) "Subsidy is an amount of money that the government or another organization pays to help to reduce the cost of a product or service." (Macmillan English Dictionary for Advanced Learners, 2009 edition)

Objectives:

Subsidies, by means of creating a wedge between consumer prices and producer costs, lead to changes in demand/ supply decisions. Subsidies are often aim :

1. To induce higher consumption/ production
2. To offset market imperfections including internalisation of externalities
3. To achieve social policy objectives including redistribution of income, population control, etc.
4. To study achievements and failures of government subsidies in India

Methodology:

Used secondary data for the analysis of objectives of the paper

Mr. P. Chidambaram, former Finance Minister of India, put the discussion paper entitled 'Government Subsidies in India' in his budget speech for 1996-97. The estimation of subsidies was based on a standard classification into three categories **i) Public goods:** national defence, police, general administration since these services are available to all. **ii) merit goods:** infectious diseases, environmental protection and minimum level of education (primary education) for all, roads and bridges, flood control and research pertaining to agriculture space, atomic energy, etc. **iii) non-merit goods:** These subsidies are beneficial for the individual consumers. Here are the ways of benefits to the individual consumer: **a) Cash Subsidies-** providing food or fertilizers at prices lower than those at which the govt. procures the commodities. **b) Interest or Credit Subsidies-** relate to loans given at the rate lower than market rates e.g. provided to small scale industries or priority sector loans to individuals to buy taxi, an auto-rickshaw or to set small enterprise. **c) Tax Subsidies** – can be in the form of tax exemption of medical expenses, postponing collection of tax arrears **d) In- Kind Subsidies** – provision of free medical services through govt. dispensaries, provision of equipment to physically handicapped persons. **e) Procurement Subsidies** – a good example is the purchase of foodgrains at an assured price which is higher than the prevailing market price. **f) Regulatory Subsidies** – fixation of prices of goods produced by the public sector at less than the cost with a view to providing inputs to industry or helping certain other categories. Examples are making steel, coal, or other minerals available to industry, providing electricity to farmers at a rate lower than the cost.

The Indian government has, since independence, subsidised many industries and products, from fuel to food. However, the argument against subsidies in India does not consider

that just agricultural and fisheries subsidies from over 40% of the EU budget (see Agricultural subsidy) although in Europe less than 10% of the people compared to India will be affected. This is also true of United States and most other Western countries.

In India subsidies now account for a significant part of government's expenditures although, like that of an iceberg, only their tip may be visible. These implicit subsidies not only cause a considerable draft on the already strained fiscal resources, but may also fail on the anvil of equity and efficiency as has already been pointed out above.

In the context of their economic effects, subsidies have been subjected to an intense debate in India in recent years. Issues like the distortionary effects of agricultural subsidies on the cropping pattern, their impact on inter-regional disparities in development, the sub-optimal use of scarce inputs like water and power induced by subsidies, and whether subsidies lead to systemic inefficiencies have been examined at length. Inadequate targeting of subsidies has especially been picked up for discussion.

Social security subsidies

The following table shows financial size of the social security subsidies in India funded by the Union government of India. The table does not cover other programs operated by various state governments, see public welfare in India. The social security benefits / subsidies offered by various state governments are estimated to be above Rs. 600 billion (US\$10 billion). Thus total subsidies become Rs. 3,600 billion (US\$60 billion).

Social security budget 2013-14:

Region	Social security program	Billion Rupee	Billion US\$
Pan India	Total subsidy for FY-2013-14 (approx)	3,600	60.00
Pan India	Food Security (PDS) (subsidy)	1,250	20.83
Pan India	Petroleum (subsidy)	970	16.17
Rural	Fertilizer (subsidy)	660	11.00
Rural	NREGA (non-subsidy)	330	5.50
Rural	Child development (ICDS) (non-subsidy)	177	2.95
Rural	Drinking water and sanitation (non-subsidy)	152	2.53
Rural	Indira Awaas Yojana (IAY) (non-subsidy)	151	2.52
Rural	Maternal and child malnutrition (non-subsidy)	3	0.05
States	Various programmes of state govts (subsidy/non-subsidy)	600	10.00

Transfers and Subsidies:

Transfers which are straight income supplements need to be distinguished from subsidies. An unconditional transfer to an individual would augment his income and would be distributed over the entire range of his expenditures. A subsidy however refers to a specific good, the relative price of which has been lowered because of the subsidised goods. Even when subsidy is consumption/ allocation decisions in favour of the subsidised goods. Even when subsidy is hundred percent, i.e. the good is supplied free of cost, it should be distinguished from an income-transfer (of an equivalent amount) which need not be spent exclusively on the subsidised good.

Transfers may be preferred to subsidies on the ground that i) any given expenditure of state funds will increase welfare more if it is given as an income-transfer rather than via subsidising the price of some commodities, and ii) transfer payments can be better targeted.

Effects of subsidies:

Economic effects of subsidies can be broadly grouped into:

1. Allocative effects: these relate to the sectoral allocation of resources. Subsidies help draw more resources towards the subsidised sector.
2. Redistributive effects: these generally depend upon the elasticities of demands of the relevant groups for the subsidised good as well as the elasticity of supply of the same good and the mode of administering the subsidy.
3. Fiscal effects: subsidies have obvious fiscal effects since a large part of subsidies emanate from the budget. They directly increase fiscal deficits. Subsidies may also indirectly affect the budget adversely by drawing resources away from tax-yielding sectors towards sectors that may have a low tax-revenue potential.
4. Trade effects: a regulated price, which is substantially lower than the market clearing price, may reduce domestic supply and lead to an increase in imports. On the other hand, subsidies to domestic producers may enable them to offer internationally competitive prices, reducing imports or raising exports.

Subsidy issues in India:

In the context of their economic effects, subsidies have been subjected to an intense debate in India in recent years. Some of the major issues that have emerged in the literature are indicated below:

- Whether the magnitude and incidence of subsidies, explicit and implicit, have spun out of control; their burden on government finances being unbearable, and their cost being felt in terms of a decline of real public investment in agriculture
- Whether agricultural subsidies distort the cropping pattern and lead to inter-regional disparities in development
- Whether general subsidies on scarce inputs like water and power have distorted their optimal allocation
- Whether subsidies basically cover only inefficiencies in the provision of governmental services
- Whether subsidies like (food subsidies) have a predominant urban bias
- Whether subsidies are mistargeted
- Whether subsidies have a deleterious effect on general economic growth of sectors not covered by the subsidies
- Whether agricultural subsidies are biased against small and marginal farmers
- How should government services be priced or recovery rates determined?
- What is the impact of subsidies on the quality of environment and ecology

Methodology for estimation of subsidies in India:

The estimates of budgetary subsidies are computed as the excess of the costs of providing a service over the recoveries from that service. The costs have been taken as the sum of:

1. revenue expenditure on the concerned service
2. annual depreciation on cumulative capital expenditure for the creation of physical assets in the service;
3. Interest-cost (computed at the average rate of interest actually paid by the respective governments) of cumulative capital expenditure, equity investments in public enterprises, and loans given for the service concerned including those to the public enterprises. The recoveries are the current receipts from a service, which are usually in the form of user charges, fees, interest receipts and dividends.

Central government subsidies:

Trends in the subsidies given by Central Government (Year 1994-95):

- The bulk of the Central Govt's subsidies arise on the provision of economic services, which account for 88% of the total subsidies (10% on merit services and 78% on non-merit).

- The recovery rates in the social end economic services are very low (around 10%).
- Subsidies on non-merit goods are more than five times those on merit goods, which reflects an unduly large and ill-directed subsidy regime.
- The bulk of subsidies on merit goods go for the construction of roads and bridges, followed by elementary education and scientific research.
- Amongst non-merit services, the biggest recipients are industries and agriculture and allied services.
- 78% of subsidies which go for non-merit economic services are amenable to economic pricing. Even if one allows for a part of these subsidies being given in the interest of redistribution or provision of human needs, a substantial part must be due to inefficiency costs of public provision of these services and/or inessential input or output subsidies.
- Subsidies to Central Public Enterprises are estimated separately as the excess of imputed return on the equity held and loans given by the central government to these enterprises, over actual receipts in the form of dividends and interests. Subsidy in this manner is calculated for each enterprise. They are aggregated according to cognate groups.

Recent trends:

Expenditure on major subsidies has increased in nominal terms from Rs. 95.81 billion in 1990-91 to Rs. 40, 4.16 billion in 2002-03. It was budgeted to increase by 20.3 percent to Rs. 48, 6.36 billion in 2003-04. Expenditure on major subsidies as per cent of revenue expenditure after declining from 13.0 per cent in 1990-91 to 8.7 per cent in 1995-96 started rising to reach a level of 9.6 per cent in 1998-99. In 2002-03, expenditure on major subsidies increased to 11.9 per cent from 10.0 per cent in 2001-02. With the dismantling of the administered price mechanism for petroleum products from 1 April 2002, subsidies in respect of LPG and kerosene distributed through the Public Distribution System are now explicitly reflected in the budget. This partially explains the spurt of 35.3 per cent in the expenditure on major subsidies in 2002-03. The spurt in major subsidies in 2002-03 was also because of an increase in food subsidy by Rs. 66.77 billion necessitated by the widespread drought in the country. Some of the major initiatives taken so far to rationalise the budgetary subsidies include targeted approach to food subsidy (BPL families under Public Distribution System, allowing Food Corporation of India (FCI) to access market loans carrying lower interest rates, encouraging private trade in food grains, liquidating excess food grain stocks, replacing unit based retention price scheme with a group based scheme in the case of fertiliser subsidies and proposed phasing out of subsidies on PDS kerosene and LPG. (Economic Survey for the year 2004-05).

Benefits of subsidies:

The relative distribution of the benefits of a subsidy may be studied with respect to different classes or groups of beneficiaries such as consumers and producers, as also between different classes of consumers and producers.

- In case of food subsidy, PDS suffers from considerable leakage and apart from a low coverage of poor; the magnitude of benefit derived by the poor is very small.
- In case of electricity, the subsidy rates have been rising for both agriculture and domestic sectors because the unit cost has been rising faster than the relevant tariff-rate. Also, there is considerable variation in the level of per capita electricity subsidy indicates that, in the richer States, the per capita subsidy is substantially higher as compared to that in the poorer States.
- In case of public irrigation, water has a very high marginal productivity when used in conjunction with HYV of seeds, chemical fertilisers, power and other related inputs. It is the richer farmers who may derive relatively larger benefits because of their capacity to use these allied inputs.

- Subsidies to elementary education form about half of the total subsidies on general education. However, this is not true for all individual States: the share of elementary education is lowest in the high income States and the highest in the low income States (Goa, Punjab and West Bengal actually give higher subsidies to secondary education than primary education). A negative correlation between the level of per capita income and the share of subsidies to elementary education is thus discernible. Most subsidies to higher education accrue predominantly to the better-off sections of society as they have an overwhelming advantage in competing out prospective candidates from the poorer sections in getting admission to courses that are characterised by scarcity of seats.
- For subsidies of health, the greater emphasis on curative health care expenditure often reflects a bias towards the better-off people whereas preventive health care expenditure with much larger externalities would clearly be of greater help to the economically weaker sections of the society.

Suggestions:

- Reducing the overall scale of subsidies
- Making subsidies as transparent as possible
- Using subsidies for well defined economic objectives
- Focusing subsidies to final goods and services with a view to maximising their impact on the target population at minimum cost
- Instituting systems for periodic review of subsidies
- Setting clear limits on duration of any new subsidy schemes

References:

1. Indian Economy (58th revised edition 2008) by Ruddar Datt, K.P.M. Sundharam
2. "India should redirect subsidies to those who need them". *The International Herald Tribune*. 2005.
3. http://www.moneycontrol.com/news/economy/budget-2013-food-security-gets-rs-10kcr-fy14-subsidy-at-rs-2311k-cr_832058.html
4. <http://www.firstpost.com/economy/budget-2013-rural-development-gets-46-hike-rs-33000-cr-for-mgnregs-643294.html>
5. "From famine to plenty, from humiliation to dignity."
6. Amanda Briney. "History and Overview of the Green Revolution".
7. Matt Rodell. "Satellite data show Indian water stocks shrinking.". *Nature*.
8. J. Carl Ganter. "Q&A: Upmanu Lall on India's Nexus of Energy, Food and Water.". *Circle of Blue*.
9. Eryn-Ashlei Bailey. "Incentives for Water Conservation in Gujarat.". *Water Wide Web*.
10. Government of India procured almost 2 billion condoms in 2004 (p.9, pdf)
11. Macmillan English Dictionary For Advanced Learners, 2009 edition