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Direct Cash Transfer of Subsidies: A Game-Changer for India?

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From 1 January 2013, India rolled out the much-hyped direct cash transfer of subsidies scheme. Widely tipped as a 'game-changer', the scheme is being heavily discussed for both its economic and political significance. Economically, it is expected to be a significant reform measure for improving distribution of subsidies by eliminating 'leakages' from the existing system of transfer in kind. Politically, the ruling Congress hopes to capitalise on the scheme's spirit of 'Aapka Paisa, Aapke Haath' ('Your money in your hands') by publicising it is as a move pioneered by the Congress party for putting money directly in the hands of people.

The scheme was expected to roll out in 51 districts across 16 states of the country, covering almost 30 social welfare programmes of several central ministries. The latter include various ongoing programmes of the Ministries of Social Justice, Human Resource Development, Minority Welfare, Women & Child Development, Health & Family Welfare, Labour & Employment. But it has taken off on a much moderate scale. It is currently running in only 20 districts and covering subsidies for seven existing programmes pertaining mostly to student scholarships and stipends. By March 2013, however, the government plans to extend the scheme to the remaining identified districts and include more programmes.

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‘Aadhar’ and Bank Account

The limited beginning of the scheme highlights the operational difficulties of administering it. It has two essential pre-requisites. The beneficiaries must have a unique identity number, christened ‘Aadhar’. These numbers are being issued by the Unique Identification Authority of India (UIDAI). After identifying the beneficiaries from the UIDAI platform, the scheme aims to deposit money directly into their bank accounts. The second requirement therefore is the possession of a bank account. Beneficiaries of the scheme must have both the ‘Aadhar’ identity and the bank account. Having one of the two will not help. Having both also is not going to help immediately since bank accounts will have to be ‘Aadhar’-enabled for facilitating transfer of cash.

The main operational challenge is connecting the issued ‘Aadhar’ identity numbers to the bank accounts of the ‘Aadhar’ holders. Only bank branches equipped with Core Banking Solutions (CBS) are capable of doing so. The future progress of the scheme will be a function of the pace at which bank branches, particularly in rural areas, implement the CBS. It will also depend on the speed with which ‘Aadhar’ identity numbers are issued across the country.

Benefitting the Poor?

The scheme is not targeted exclusively towards the poor or the below-poverty-line (BPL) population of the country. ‘Aadhar’ identities are being issued across all income groups and are not confined to the BPL. Indeed, given that possession of both ‘Aadhar’ and a bank account is necessary for benefitting from the scheme, it is more likely that the non-poor segments will be the greater beneficiaries of the scheme, at least during its initial phase. The non-poor segments have more bank accounts than their poor counterparts. India’s limited financial inclusion has ensured that most poor in the country, particularly in rural areas, do not have access to formal banking facilities. The non-poor are also able to satisfy the documentation requirements of ‘Aadhar’ faster than the poor.

The scheme might create difficulties for the poor and those left out of it in another respect. It is expected to have an inflationary impact similar to the rural employment guarantee scheme, MGNREGA. Cash deposited into bank accounts of beneficiaries would be partly spent and saved. The spending would generate a fresh cycle of expenditure in the economy leading to some increase in prices. The early inflationary impact of MGNREGA was not entirely unwelcome, since it came at a time (2008-2009) when the economy was looking for demand-driven stimulus for revival following the slowdown inflicted by the global economic crisis. The current bout of fresh inflation might not be welcome given the already high consumer prices.

Finally, the impact of the scheme on the poor might be even more limited, because cash transfers are not covering the government’s biggest subsidies – food, fertilizer and petroleum.

Monthly rations of food and kerosene will continue to be distributed to poor households in kind through fair price shops. Leakages from the public distribution system in these respects will also continue the way they do now.

Where Goes the Cash?

The government's great enthusiasm in flagging off the scheme is on account of its potential to reduce leakages. Direct transfers would connect the subsidy-disbursing agencies to the beneficiaries. It would eliminate intermediaries, reduce corruption and ensure properly targeted distribution of subsidies. In the process, it should not only ensure that the beneficiary receives the full quantum of the subsidy but should also reduce the overall subsidy burden of the government by minimising distribution costs.

Theoretically, the scheme is capable of generating these benefits. There is, however, a different problem which might create complications. Subsidies delivered in kind cannot be used for any other purpose. Cash transfers are not so. Cash subsidies for student stipends deposited into bank accounts might end up being spent on purposes entirely different from education. There would be similar problems if the scheme in future is extended to food subsidies. There is little possibility of the scheme incorporating features for ensuring the usage of subsidies for specific and desired purposes only. In this respect, while the scheme can choke leakages, it might fail to achieve the basic objective of having subsidies in the first place.

Political Game-Changer ?

The political ramifications of the scheme were evident when the Election Commission expressed its unhappiness over the announcement of its rolling out few weeks before the Gujarat assembly elections in December 2012. A politically and morally battered Congress is banking upon the scheme for weaving electoral magic. Congress leader Rahul Gandhi's conviction that the scheme can win elections for his party if successfully implemented is a clear indication that the party will not spare any efforts to widen its scope during this year and in the run-up to the next Parliamentary elections.

For the Congress, the scheme marks fulfilment of a promise made before the 2009 elections. It expects the scheme to be as politically powerful as the MGNREGA. After the latter, the cash transfer scheme would be the Congress's most ambitious effort in promoting inclusive growth. The scheme will reduce the clout of local politicians with their constituencies, irrespective of the parties to which they belong, since beneficiaries of subsidies under different schemes often had to seek their interventions in availing the support. Direct transfers would reduce this possibility. While local Congress politicians would try to champion this as proof of the party's overwhelming concern for the common man, opposition politicians would need to think of other ways for countering the strategy. By introducing the scheme, the Congress also hopes to curb some of the flak it received for market-friendly controversial reforms, such as foreign direct investment in retail and correcting petroleum subsidies, which were touted as anti-people by the opposition parties and some allies.

Much would depend on how deep and wide the cash transfers can become within this year. With around 200,000 beneficiaries and seven ongoing schemes, they are too limited in scope right now to make any visible political impact. Faster issue of 'Aadhars' and tying them up with bank accounts is critical, as is coordination with various central government ministries for channelling their subsidies as cash. Ultimately, it is administrative and operational efficiency that will determine the scheme's emergence as a political game-changer. Doubts remain strong in this regard as operational and administrative efficiency in implementing schemes has hardly been a conspicuous virtue of the current government.

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