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Financing Rights: The Macroeconomics of Social Welfare Programmes

Over the years, many social welfare programmes in India have been recast as rights resulting in debates surrounding the means to finance these rights. There is a persistent tension in the allocation of finances between capital expenditure for big infrastructure and spending on social welfare policies. Critics see welfare expenditure as a net cost to society, inducing rigidities in the labour market. However, it has been observed that increased spending on social welfare policies has both short and long-term positive impacts for economic development. In the short term, it reduces poverty and inequalities while in the long run by creating a more educated and healthier workforce it contributes to higher productivity and growth. Welfare spending in India has been inadequate, although there exists a strong economic rationale to increase it and this can be achieved through a more progressive tax regime including wealth and inheritance taxes.

Financing Rights: The Macroeconomics of Social Welfare Programmes

Jayati Ghosh

Social spending in general refers to public and private expenditure aimed at enhancing social well-being, reducing multidimensional poverty, improving health and education outcomes and promoting greater equality. Welfare programmes are typically understood as part of social spending or social policy programmes, encompassing interventions such as healthcare, education, food and nutrition support, old-age pensions, disability support, child support and family benefits, unemployment benefits and housing support. The concept of a ‘social protection floor’ seeks to guarantee minimum well-being and basic standards across the life cycle, implying differentiated provisions, including those based on gender. Proponents of such an approach have increasingly used a rights-based framework in which public provision may be required to ensure essential social and economic rights, such as the rights to life and livelihood, food, housing, health, education and social security against shocks.

A significant part of such welfare spending also covers activities that are broadly described as ‘care activities’. Many of these continue to be performed in unpaid fashion, mainly by women and girls within households. There is a strong link between the extent of good-quality public service provision and the availability of recognised and good-quality care services.

A framework for social welfare spending that is based on essential human rights obviates the need for economic justification, since it posits the realisation of such rights as a social goal that must be met. The economy must therefore be made to conform to this goal through public action. In other words, economic arrangements, institutions and policies should serve the needs of the society, within planetary limits, rather than the other way around.

In purely economic terms, social welfare spending or social protection can be seen as an investment in human capabilities, which makes it a major contributor to the economy. At the same time, it is also quite different from other public expenditures, such as those on infrastructure or industrial policies for development. It can also have positive macroeconomic effects, as considered below, in terms of demand management, macroeconomic stabilisation and countercyclical economic policies.

In this context, the economic implications of such public spending have been the subject of debate for a very long period. In recent decades, opponents of social spending, and in particular of various social protection programmes, have made

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arguments that are part of a more general critique of the welfare state (summarised in Atkinson 1999). Essentially, such spending is seen as a net cost to society, generating ‘inefficiencies’ by crowding out what is presumed to be more efficient private sector investment, and introducing ‘rigidities’ in the labour market. These include reducing the incentives for unemployed workers to seek

employment, and thereby generating greater tendencies for open unemployment. These arguments explicitly or implicitly rely on perceived trade-offs between equity and efficiency, or between equity and growth. Fiscal deficits that arise due to such spending are therefore seen as not only unsustainable but inefficient.

These short-run macroeconomic arguments against social policy have their counterpart in longer-run approaches to economic development. Since such spending is seen as a cost, simply paying for consumption, this implies a diversion of resources away from productive investment, thereby reducing the potential for economic growth. At best, social welfare programmes are then justified only as a residual category of ‘safety nets’ that are designed to respond to shocks, counteract policy failures or adjust for development-related negative impacts. These arguments

remain strongly embedded in the attitudes of policy makers in many countries, including in India, where the attitude to social spending has been relatively niggardly and its deployment has been for political purposes rather than expected economic gains.

Yet the evidence is strong that such arguments are not valid, and that social spending—and welfare expenditure in particular—has strong positive effects on economic activity in the short run, as well as positive developmental impacts over the medium and long run. Therefore, it is not just positive for ‘beneficiaries’, but extends beyond that to wider economic benefits, because of the positive externalities that result. Some short-run effects are obvious, such as the reduction of absolute poverty, reducing economic inequalities and the positive countercyclical effects that reduce the intensity and length of economic slumps. Macroeconomically, since such spending is disproportionately directed to lower-income sections of society, the multiplier effects tend to be significantly larger than most other forms of public spending.

In addition, there are important long-term impacts that are crucial to the development process, not only because of the clear benefits to an economy of a healthier, better-educated work force, but because such spending also helps in managing the conflicts and contradictions of a development process that necessarily involves change. Social security works positively on development through effects on demographics, distribution and incentives. In particular, greater equity—or the reduction of vertical and horizontal inequalities by improving conditions of life and access to opportunities for the entire population—plays a significant, albeit under-acknowledged, role in both speeding up and easing the development process.

Mkandawire (2001) argued that social policy ‘should be conceived as involving overall and prior concerns with social development, and as a key instrument that works in tandem with economic policy to ensure equitable and socially sustainable development.’ He identified social policy as the set of collective interventions that directly impact social welfare (such as adequate and secure livelihoods and incomes), social institutions (the structures, rules and constraints that shape social interaction) and social relations (ranging from the micro to the global levels, encompassing intra-household relations of class, community, ethnicity, gender, etc.). He noted that these are important determinants of economic development, which, in turn, facilitate achievements in these areas through positive feedback loops.

The importance of the role played in conflict management and improving social cohesion should also not be ignored. This promotes greater social stability through a process of accumulation that can involve dislocation and rapid change. The greater openness of economies in the period of globalisation has intensified economic and social vulnerability and added external shocks to those generated

internally. That is why [Rodrik \(1998\)](#) argued that institutions of conflict management are a necessary complement to economic openness, and that failure to manage internal conflict can magnify the negative effects of external shocks. Indeed, this argument now appears prescient for many countries, across all levels of per capita income: ‘every trade regime implies particular patterns of income distribution, and this in turn implies social policies either to sustain those patterns of distribution or to correct their social or political failures. Failure to do so can lead to integration into the world system that engenders social disintegration at the national level, with the distinct possibility of policy reversal toward protectionism’ ([Mkandawire 2001, 24](#)). Therefore, conflicts over distribution in the course of a development process require a role of the state as a mediator or as a partner in social concertation to strike acceptable bargains on income distribution ([Vartiainen 1999](#)).

Obviously, different political economy configurations will result in different social policy regimes, just as they also produce different political capacities for the extraction of resources necessary for financing social programmes. But this does not divide simply along democratic/authoritarian lines. Eventually, every state, including the most authoritarian, has to be concerned with some degree of popular legitimacy, especially when the accumulation process can impact national cohesion. This is why it has been argued that ‘the pursuit of social policies that enhance accumulation while securing the state the necessary legitimacy for political stability has constituted the cornerstone of developmental management’ ([Mkandawire 2001, 19](#)).

A range of factors affects how social policy acts to induce economic and political stability to assist or induce growth. It is also evident that different patterns of accumulation for economic growth, with corresponding distributional effects, have varying results in terms of meeting the spectrum of social goals that are now on both national and international agendas, such as the Sustainable Development Goals.

2.1

Cross-country empirical evidence

Increased public welfare expenditure that is universal, or effectively targeted to the poor without unwarranted exclusion, improves income distribution in obvious ways by improving the conditions of life of the poor. Yet there is a body of literature that argues that such moves towards greater equity are in contradiction with a rapid accumulation process: in microeconomic terms, because inequality is supposed to act as an incentive for investment and innovation; and in macroeconomic terms, because the rich tend to save more, which releases more domestic resources for investment. However, this position has been discredited by recent research, which points to a negative relationship between economic inequality and growth. It is now more widely accepted that reducing inequality can be good for economic performance (see [Stiglitz 2012](#) for a more extensive discussion).

Inequality results in lower aggregate demand, as those at the bottom spend a larger fraction of their income than those at the top. Deficient aggregate demand and a smaller and more sluggish expansion of the domestic market cause unemployment and underutilisation of other resources. These can have dynamic negative multiplier effects, leading to losses of potential aggregate income over time. The lack of income and access to essential social services among lower-income groups has knock-on effects for overall economic performance: hunger or malnourishment, lack of adequate healthcare and children who may not receive the education they need to live up to their potential. All this affects current economic performance and, even more, future growth prospects (Ferreira and Peragine 2015).

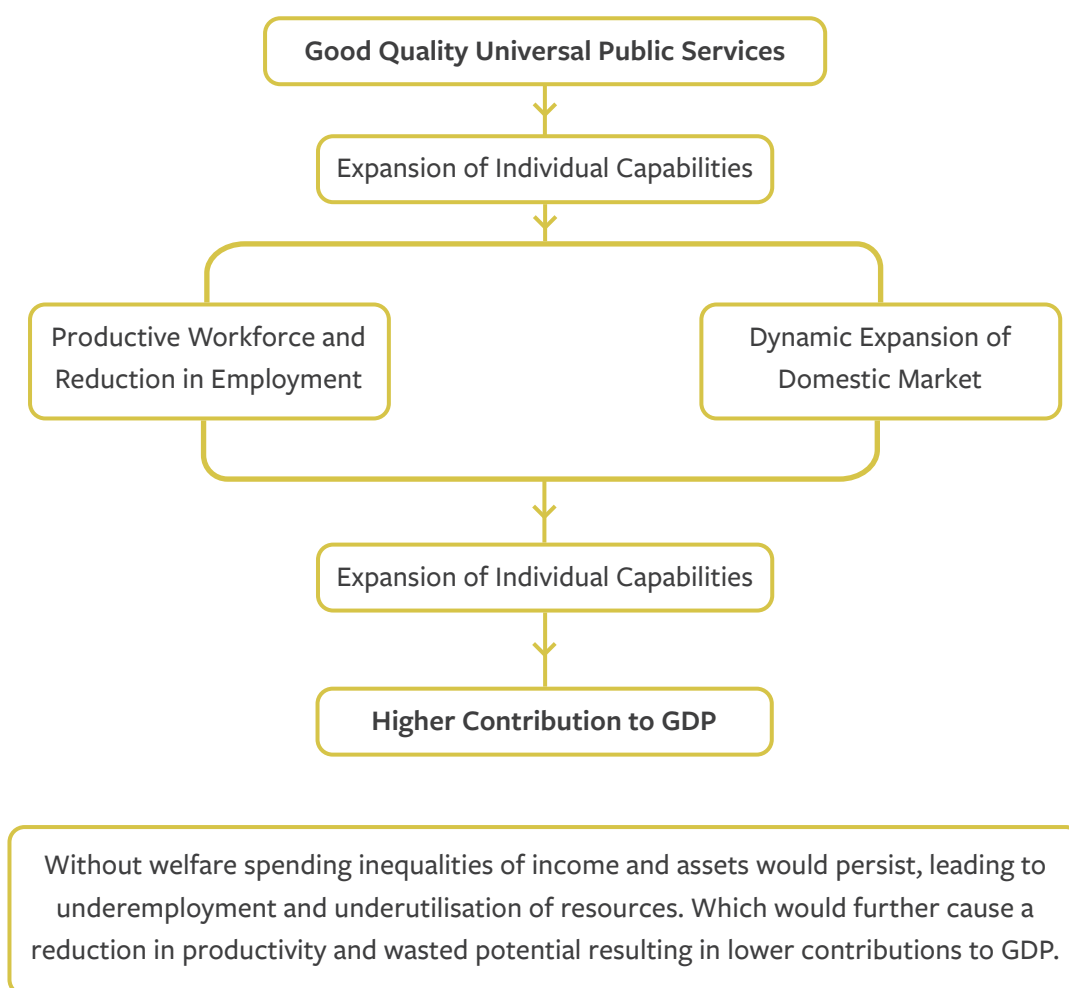
Specifically for this discussion, those at the bottom or in the informal sector, especially in countries with weak systems of social protection, are highly vulnerable to adverse shocks. These require coping mechanisms and survival strategies that may reduce productivity immediately and make it more difficult to make the long-term investments and other decisions that might improve it.

Inequalities of incomes and assets, in the absence of compensating social spending, both reflect and further reinforce inequality of opportunity, wasting the potential of those at the bottom. When good-quality public services are not universally provided, those who are better off can access the best privatised education and healthcare, while others—usually the bulk of the population—cannot. This undermines their chances of progress.

A substantial amount of recent research has found positive relationships between public social spending and the gross domestic product (GDP), both in the short term and over a longer period. Furthermore, this relationship has been found across different levels of base-period per capita income. It can also be argued that correlation is not causation. However, the argument that was widely prevalent in policy circles earlier—that increased social spending is a luxury that poor countries cannot afford, and that such spending would be an outcome of the growth process rather than one of the factors driving it—is not validated by empirical studies.

One study involving researchers from the International Monetary Fund (IMF) (Furceri and Zdzienicka 2012) used a panel of Organisation for Economic Co-operation and Development (OECD) countries from 1980 to 2005 to find that social spending had expansionary effects on GDP. In that study, an increase of 1 per cent in social spending increased GDP by about 0.1 percentage points, which, given the share of social spending in GDP, suggested a multiplier of about 0.6. The effect, while similar to that of total government spending, was larger in periods of severe downturns. Unsurprisingly, such spending positively affected private consumption. While it was found to have negligible effects on investment, it is likely that such effects could operate over a longer period because of the impact on consumption, and, therefore, expansion of the domestic market. Among the main social spending

Figure 2.1: Economic effects of public social spending on inequality and development



subcategories (education, healthcare including sanitation, social security and housing/community amenities), spending on health and unemployment benefits were found to have the greatest effects.

Another study analysing trends in developing countries over the period 1990–2013 (Ahuja and Pandit 2022) found that all categories of social spending produced a significant reduction in income inequality. Further, the impact of health and education spending on economic growth was significant. According to them, this indicates that ‘both health and education spending can break the trade-off between equity and efficiency; that is, it can lead to both growth and progressive distributional change.’ A study for Latin American countries (Quinonez 2024) found that increased levels of overall social spending were strongly associated with reduced levels of income inequality in the region. However, each of the four main areas of social spending was observed to have different effects on income inequality and these varied across countries.

Aggregate public investments in education, particularly during formative years, consistently predict higher social mobility (Iversen, Krishna and Sen 2021). A 25-country OECD panel (2000–09) showed that a 1 per cent increase in health spending is associated with a 14 per cent reduction in intergenerational inequality (Aizer 2014). Similarly, stunting due to malnutrition in poor children—which can be reduced through public interventions to provide nutritious food—has been directly linked to adult earnings and economic productivity because of its impact on cognition and educational achievement (De Sanctis et al. 2021; McGovern et al. 2017).

Haile and Niño-Zarazúa (2018) examined the causal effect of government spending on the social sectors (health, education and social protection) on three measures of aggregate welfare: the Human Development Index, the inequality-adjusted Human Development Index, and child mortality rates, using longitudinal data from 55 low and middle-income countries from 1990 to 2009. They found that strong government social spending has played a significant role in improving aggregate welfare in the developing world.

Another recent study by *Development Pathways* (2022) considered the potential impact of social protection policies on the economies of eight countries across four continents (Bangladesh, Colombia, Costa Rica, Georgia, Ghana, India, Rwanda, and Serbia). This study simulated the impact of investing the equivalent of just 1 per cent of GDP in each of these countries on domestic indicators such as GDP growth, employment and tax revenues, as well as on households' income by wealth quantiles, poverty and inequality. This research confirmed many of the analytical arguments made in favour of the positive impact of social protection: positive returns on the economy and GDP growth, increased tax revenues, lower poverty, and reduced barriers for women entering or returning to paid work. Social protection plays an important part in consumption smoothing, which is particularly helpful in enabling lower-income households to cope with adverse shocks. Households are thereby better able to avoid being forced into negative coping strategies, such as selling household assets or taking children out of school. The simulations also reinforce the expectation of higher multiplier effects of social protection investments, by showing that they induce an increase in labour demand.

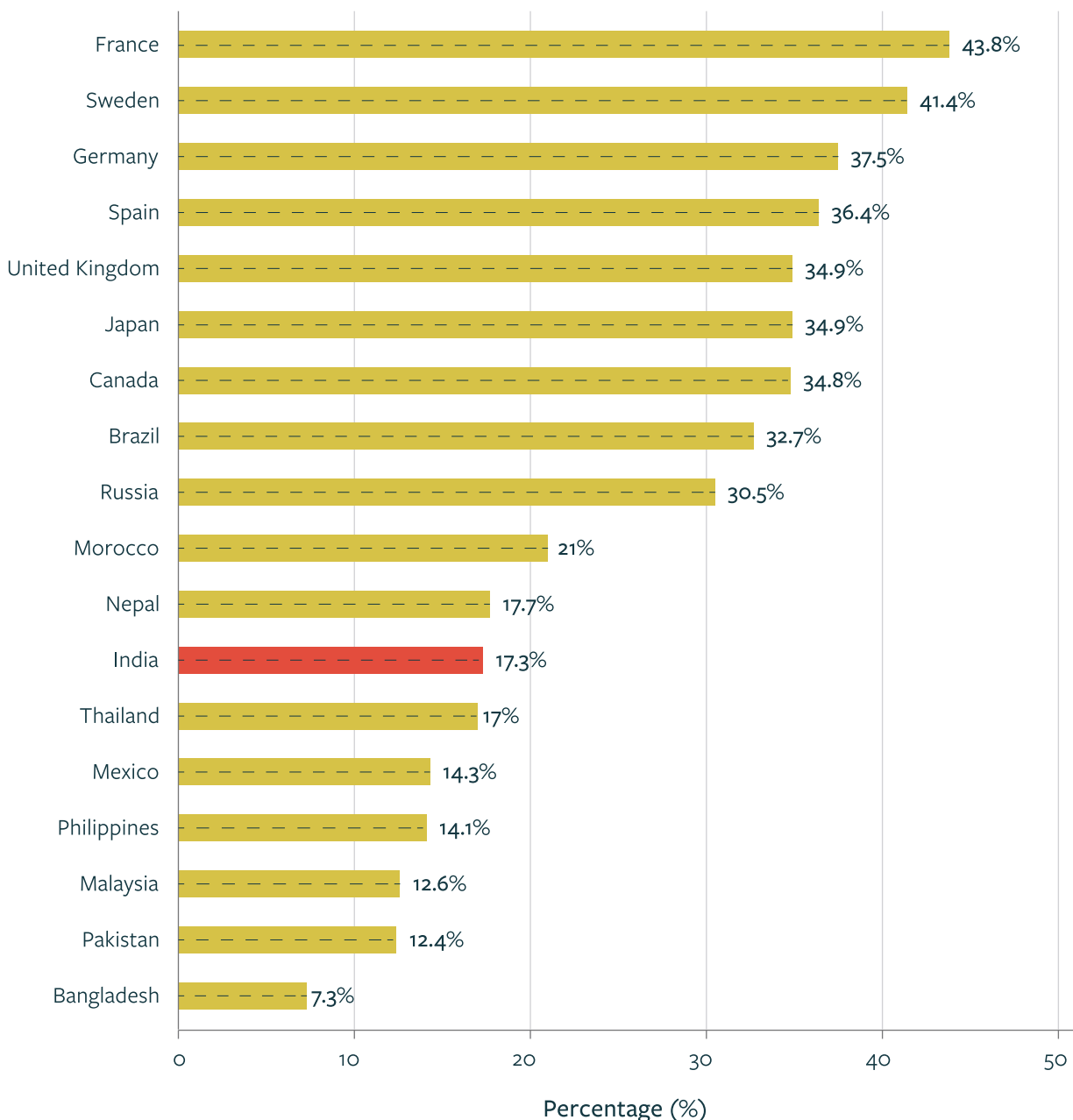
Significantly, the analysis also suggests that total tax revenues increase with public spending on social protection. Increasing such spending by 1 per cent of GDP leads to an increase in total government tax revenues of between 0.6 per cent and 3.5 per cent in the eight countries considered. This works through the mechanism of increased economic activity, which means that, in effect, the 'cost' to the government is significantly lower than the initial budgetary outlay. The macroeconomic cushioning effect is evident, particularly in cases of economic shocks and business cycle downswings. The simulations also confirm the important role of social protection in reducing poverty and inequality, including gender inequality.

It is important to note that increased social welfare spending, including social protection, can occur at many different levels of per capita income. Countries in Latin America provide good examples of how this has worked, especially in recent years. Three main types of social protection institutions are at the core of social protection in the region: occupational insurance, personal pensions and social assistance. Social assistance consists mainly of family transfers or conditional income transfers and old-age transfers. It has been argued that the emergence and evolution of social protection institutions in Latin America have been associated with significant political realignments (Barrientos 2025).

Left parties, trade unions and other labour-based organisations in Latin America traditionally favoured occupational insurance as the social protection institution of choice. However, from the early 1990s, conditional income transfer programmes spread through the region during the ‘Pink Tide’, when many left-leaning governments took power (Borges 2023). In Brazil in the early 1990s, there was a programme to support children’s schooling by providing cash transfers to economically vulnerable families, which was scaled up to Bolsa Escola in 2001. This, along with other schemes, was consolidated into the *Bolsa Família* system of cash transfers in 2003 by the Lula government, which also committed to ‘Zero Hunger’, implemented through food assistance in kind.

In Mexico, the social impact of the agricultural trade liberalisation associated with the North American Free Trade Agreement (NAFTA), which affected peasant livelihoods and employment, led to PROGRESA. This was designed as a rules-based conditional family cash transfer programme that linked income transfers with schooling and health. These social assistance transfers in Latin America were decoupled from employment. Since conditional transfers typically provided only around 20 per cent of household income, it was expected that recipients would receive other income through employment. Old-age and disability transfers have also expanded in the region. Universal pensions—transfers offered to all above a certain age—were introduced in Bolivia; transfers were paid to all older people without formal pensions in Chile; while in Guatemala, such pensions were provided only to older people living in poverty. In all of these examples, the impact on poverty reduction was notable. In countries like Argentina, where social protection measures were combined with increases in minimum wages, there were also positive effects in terms of a more rapid recovery from the economic and financial crisis.

Figure 2.2: Share of Tax Revenue to GDP, Selected Countries, 2023



Sources and notes: UNU-WIDER Government Revenue Dataset (2025)

2.2 Financing social welfare spending

Notwithstanding the many positive economic effects of social welfare spending, it will require additional public spending if it is to be effective. Significantly enhanced public expenditure will be required both directly, to ensure basic needs for all and social protection (along with transformative green investments); and indirectly, to enable private investments in areas where commercial profitability can be assured without denying access or reducing quality, by underwriting them.

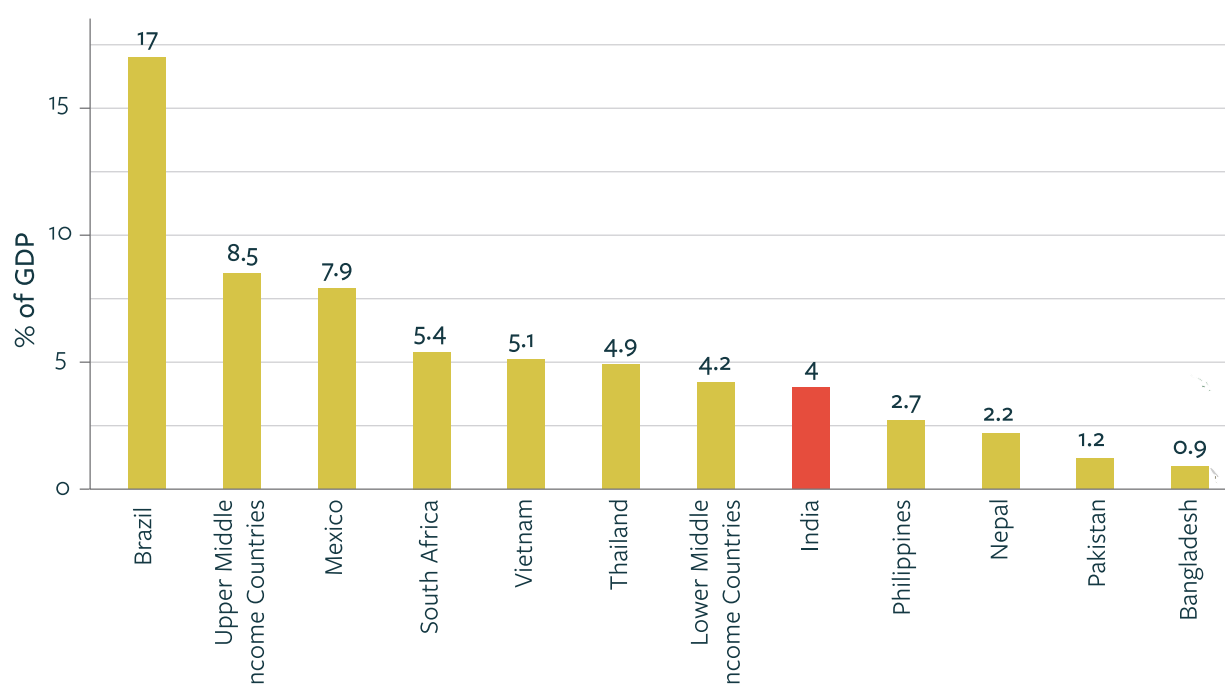
This typically brings forth the question of how such spending is to be financed. Using borrowing from the central bank (deficit financing of budgets through money creation) is possible, but can also run up against macroeconomic

constraints such as inflationary pressures. Relying on external finances, such as Official Development Assistance (ODA), is increasingly problematic, fraught with other dangers, and, in any case, less likely because of the global decline in aid spending by donor governments and multilateral institutions. Therefore, domestic public finance is key: sustaining prolonged higher levels of public expenditure directed to social welfare necessarily requires significantly more tax revenues.

This, in turn, requires a major shift in the central government's approach towards a more progressive fiscal policy. Tax-to-GDP ratios in India are relatively low, even when compared to other middle-income countries, and among the lowest in the G20 countries. And the tax system is also regressive, relying on taxes that fall disproportionately on the poor and middle classes (indirect taxes) rather than on the rich, who have been the main beneficiaries of recent growth.

There is obviously a political economy of domestic resource mobilisation, which must be recognised as determining the ability of governments to tax, and the nature of taxation (whether progressive or regressive) in different socio-political contexts. There are also significant constraints on states' ability to tax, posed by the international economic architecture, and in particular by globally accepted systems of taxation with regard to entities with a cross-border presence. The tax systems in operation around the world today are both outdated and regressive. They simply cannot deliver the public revenues required or ensure that the rich pay more than the poor relative to income. They fail to recognise the massive changes in the ability of multinational companies and rich individuals to avoid taxes that have been

Figure 2.3: Expenditure on Social Protection as a % of GDP (excluding health), Selected Countries (2023 or latest available year)



Sources and notes: World Social Protection Data Dashboards, ILO

generated by globalisation and financial flows. They also do not take into account how companies shift profits and wealthy individuals shift assets into low-tax jurisdictions.

Moreover, these systems rely far too heavily on indirect taxes such as value added tax (VAT), which fall more severely on the poor. Over the past few decades, this has been associated with a marked decline in public wealth alongside a rise in highly concentrated private wealth, as shown in the World Inequality Report 2022 ([World Inequality Lab 2022](#)). As a result, current tax systems in most countries—and particularly in lower-income countries that are victims of large illicit financial flows—cannot raise the required public resources and may even add to ballooning inequality.

However, there are ways to address this, if there is the political will to do so. It is possible, for example, to tax multinational companies to ensure that they pay the same effective rate as purely domestic companies; to tax windfall profits in all sectors, especially profits made during periods of scarcity and speculation when the rest of the world is worse off; to tax individually held wealth, especially the assets of the extremely wealthy taxpayers, wherever they are held; and to tax incomes from capital more progressively.

At least some of these measures depend on international coordination, because of the enhanced ability of rich corporations and individuals to shift resources across borders. The current system came into place around a century ago, when multinational corporations were rare, and when the rich in each country could not easily park their wealth in tax havens. As a result, this system barely acknowledges the possibility of companies and wealthy individuals moving their profits, incomes and assets to low-tax jurisdictions to avoid being taxed where they reside. Yet such practices are now so common that the largest global corporations and the richest individuals in the world pay barely any taxes on their incomes or assets.

A major weakness in the global tax system is the ability of multinational companies (MNCs) to manipulate their profits by shifting them to other countries. This is possible because the system treats each subsidiary of a corporation as an individual, separate entity. By shifting profits to low-tax jurisdictions, MNCs typically pay only a fraction of what domestic companies have to pay. Analysis of country-by-country reporting of profits by MNCs shows that about 35 per cent of foreign profits, amounting to \$1 trillion, were shifted to tax havens in 2022 ([EU Tax Observatory 2024](#)). This can be prevented if multinational corporations are treated as single entities and taxed accordingly, based on their sales and employment in each country to determine their share of global profits. This would need to be combined with a global minimum tax floor to fight tax competition and the race to the bottom in tax rates.

In fact, the international initiative to address this – the OECD Base Erosion and Profit Shifting (BEPS) ‘inclusive process’ – has had only limited success and has now effectively collapsed. One major outcome of negotiations that stretched over seven years was the 2021 agreement to enforce a minimum corporate tax rate. While the principle was important, the agreed rate of 15 per cent was far below 25 per cent – the median of global corporate tax rates and close to rates in some tax havens. This would generate at most around \$200 billion in additional revenue globally, whereas a 25 per cent minimum rate could generate as much as \$500 billion annually. Indeed, a low global minimum tax rate could trigger another race to the bottom in corporate income tax rates.

However, even this low minimum rate had little effect because of carve-outs introduced subsequently. One major carveout allows firms to demonstrate ‘economic substance’, enabling MNCs to benefit from reporting profits in tax havens by investing capital and hiring workers there. As a result, revenue gains from this measure have been very limited: only 3 per cent of global corporate income tax revenue, rather than the projected 9 per cent; meanwhile, profit shifting has continued unabated. More recently, the US administration demanded that G7 countries exempt US MNCs from this, a demand that was tamely accepted in a rushed meeting of the OECD Inclusive Process in January 2026. This is a clear example of coercive power in action, effectively undermining the entire effort.

The other ‘pillar’ of the OECD–BEPS negotiations was unitary taxation, which involves treating MNCs as a single entity, as they effectively are, rather than as separate entities in each country operating at ‘arm’s-length’ from one another. The basic idea is to apportion taxable profits across all countries in which MNCs have an economic presence, using a formula based on factors such as sales and employment, and allowing each country to tax its share of the total profits at its own corporate tax rate. Yet the OECD compromise was extremely narrow in scope: it included only the largest MNCs, applied only to profits above 10 per cent, and allocated just one-quarter of those profits to potential global taxation. This limited revenue potential meant that developing countries would receive negligible additional tax revenues. In return, they were required to relinquish autonomous tax measures like digital services taxes, which have been implemented successfully by several countries – and submit to problematic investor-state dispute resolution processes. In any case, even this compromise did not come into force, and the current geopolitical context makes its implementation even less likely.

Taxation of the very wealthy has long been considered difficult because extremely rich individuals can move their money across jurisdictions, both legally and illegally, to avoid taxes. As the Global Tax Evasion Report 2024 shows (EU Tax Observatory 2024), this occurs through a range of mechanisms: clearly illegal practices such as concealing income in offshore bank accounts, as well as grey-

zone tax-saving strategies, including profit shifting to foreign shell companies and the creation of holding companies or trusts that obscure beneficial ownership to manage personal wealth, and avoid individual income taxes. Global billionaires have effective tax rates as low as 0 to 0.5 per cent of their wealth, largely because they rely on shell companies to avoid income taxation.

There have been some positive steps in recent years to address this. To enable the taxation of extreme wealth, even the simple sharing of banking information across countries has been a breakthrough. The US Foreign Account Tax Compliance Act (FATCA), implemented in 2014, required banks worldwide to report the account holdings of US taxpayers, under threat of penalties. From 2017, the automatic exchange of banking information through the OECD's Common Reporting Standard (CRS) expanded to cover more than 110 jurisdictions (though notably excluding the US). These measures have made it more difficult for very wealthy individuals to conceal offshore financial wealth. In 2022 alone, around \$12.6 trillion in offshore wealth was reported to foreign tax authorities through these mechanisms.

Even so, this does not mean that such assets and incomes are subsequently taxed. Many governments have been reluctant to do so, fearing resistance and capital flight, and often responding to pressure from powerful lobbies representing the wealthy and large corporations. Offshore tax evasion has also not disappeared: it is estimated that around 25 per cent of global offshore financial wealth remains untaxed. Not all offshore financial institutions comply with reporting requirements, and the US – which itself contains several tax haven states – does not participate in the CRS. In addition, very wealthy individuals can shift into non-financial assets, such as real estate.

It is often argued that wealth taxes are difficult and cumbersome to implement because the costs of identifying and tracking wealth outweigh potential revenue gains. One way of dealing with this would be to introduce a global minimum wealth tax targeting only those with very large fortunes, say as dollar billionaires or centimillionaires, and focusing on relatively easily identifiable assets, including financial assets and land or real estate. Even a modest tax rate of 2 per cent – barely noticeable for those with such enormous wealth – could generate substantial revenues, estimated at close to \$250 billion annually from fewer than 3,000 individuals. In a recent report commissioned by the Brazilian presidency of the G20, [Gabriel Zucman \(2024\)](#) outlines a blueprint for such a tax, arguing that the primary constraint is political will. This position is increasingly reflected in government discourse: the final statement of the G20 Summit in Rio in November 2024 (endorsed by the Government of India) declared that 'With full respect to tax sovereignty, we will seek to engage cooperatively to ensure that ultra-high-net-worth individuals are effectively taxed.'

This is why the ongoing intergovernmental negotiations at the United Nations towards a framework tax convention on international tax cooperation are so significant. They offer an opportunity to rework the current international tax architecture towards more comprehensive and equitable solutions. The UN remains a body with a rules-based decision-making process, universal membership, and participation from all member countries, providing the basis for a more democratic and genuinely inclusive system than the OECD-led process. The absence of the US from these negotiations is clearly a concern; however, coordination among other countries, or even among a subset of them, could still become the basis for initiating a process of fair taxation of both MNCs and extreme wealth. In addition, the UN negotiations are also considering protocols on taxation of digital services and on dispute settlement, both of which could have significant positive effects on revenue collection.

These developments are of direct relevance for India, where major opportunities for progressive taxation continue to be overlooked. According to researchers at the World Inequality Lab, India has become one of the most unequal countries in the world in terms of both wealth and income distribution. A substantial share of GDP growth in recent decades has accrued to the top 10 per cent of the population, particularly to the very wealthy. Such extreme inequality has not translated into higher investment rates, productivity, or economic dynamism. Instead, it has contributed to the stagnation of mass consumption demand, which in turn acts as a deterrent to private investment. It has also deepened social divisions and increased political tensions. From the perspective of expanding social spending, it is therefore critical to pursue more progressive taxation strategies, both domestically and through international cooperation.

2.3 The Indian experience

While the preceding discussion has been general, its relevance to India is apparent. The Indian economy has developed several strengths over three decades of relatively rapid expansion, including a degree of economic diversification, sectoral sophistication, and a young population with rising levels of education that could support future growth. But these strengths are also accompanied by structural weaknesses: the absence of dynamic inter-sectoral linkages, stagnation in manufacturing output and employment, the dominance of informal employment, and the inadequate expansion of livelihood opportunities for the majority of the population – all of which are associated with rising inequality (Bharti et al. 2024).

The growing disconnect between output growth and employment expansion is of particular concern, especially given India's demographic structure of a predominantly young population. Indeed, the Indian economy reflects the limitations of a prolonged period of rapid economic growth that has not been matched by sus-

tained social policy interventions capable of distributing its benefits more widely or improving human development outcomes for the majority alongside aggregate income growth. This failure is closely linked to insufficient structural transformation: a large share of the workforce remains trapped in low-productivity activities in agriculture and services, which in turn contributes further to the lack of this structural change.

Some public interventions – particularly the rights-based policies introduced in the latter half of the 2000s – have been important and, if expanded and implemented more effectively, could have helped reverse these trends. Even today, a stronger emphasis on social policy, including welfare programmes, would not only improve the conditions of the vast majority but also support a more inclusive pattern of development. Such an approach could stimulate growth from below, as rising domestic demand would enable and incentivise small and medium enterprises across sectors to flourish, thereby increasing wages and improving the livelihoods of the self-employed.

Despite the clear economic rationale of such a strategy, public social spending in India remains extremely low, even as per capita incomes have risen. Data inadequacies – particularly the lack of comparable cross-country data for India – make precise comparisons difficult. Moreover, the ILO’s standard measures of social protection, such as the proportion of the population covered, can be misleading because they do not capture the adequacy of the social security benefits that are received. For instance, the International Labour Organisation (ILO) estimates that more than half of the population in Asia and the Pacific received at least one form of social protection benefit (ILO 2025), but this figure is heavily influenced by East and Southeast Asia. South Asia continues to be among the lowest-spending regions on social protection, including healthcare, at just 5.1 per cent of GDP in 2023, compared to 9.4 per cent in Southeast Asia and the Pacific and 13.7 per cent in East Asia. High-income countries, including those in North America, Europe and East Asia, spend, on average, around one-quarter of GDP on social protection.

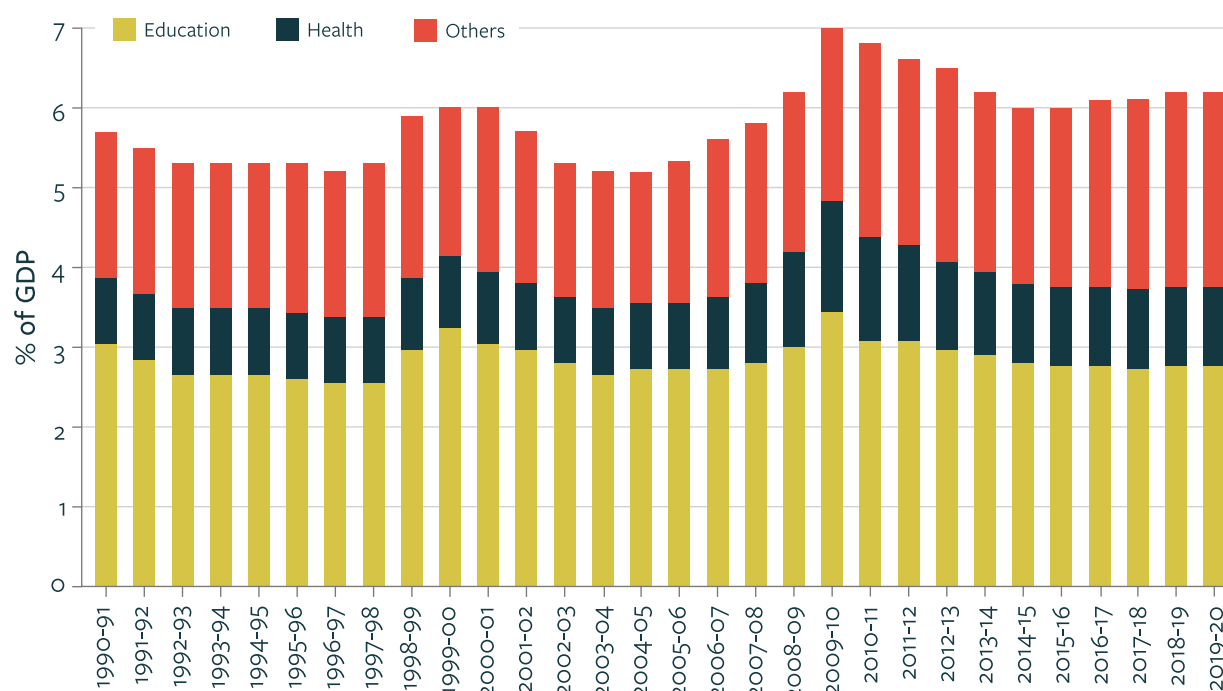
In the decade beginning in 2004, there was a shift in the government’s approach to social welfare, towards a ‘rights-based approach’ in which basic socio-economic rights were formally recognised and legislated. The rights to work, food, education and information were established through laws that made it the state’s obligation to ensure a minimum level of provision accessible to all (Ghosh 2006; Ruparelia et al. 2009). The rights to health and adequate housing were proposed but not legislated. The right to work was operationalised in a limited form, restricted to rural areas, through the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA), which promised 100 days of work for every rural household. In practice, however, only around 40–50 days of work per year were

provided on average, and fewer than 10 per cent of households received the full 100 days of work in any given year.

The right to food was formalised through the National Food Security Act (NFSA) 2013, which built on the existing foodgrain procurement and distribution system. Eligible households were provided subsidised food (₹2 per kg for wheat and ₹3 per kg for rice), with eligibility determined by lists of households classified as ‘below poverty line (BPL) based on the socio-economic census of 2011–12. Since this list has not been updated despite significant demographic change, both Type I (unjustified exclusion) and Type II (unwarranted inclusion) errors are widespread, with at least 100 million people estimated to have been excluded (Khera and Somanchi 2020). Nevertheless, framing of such public provisioning in terms of enforceable rights represented an important institutional shift.

However, in the decade since 2014, the Union government has made significant adjustments – in most cases amounting to reversals – of this approach. Social spending is no longer framed as a means of realising basic socio-economic rights; instead, it is presented as a discretionary provision by the state. Bose and Banerjee (2025) note that trends over the past thirty years indicate stagnation in the ratio of public spending on human development to GDP in India, pointing to ‘underperformance in social spending in India and the need for greater investments’. Figure 2.4 illustrates this. The evidence further suggests that since 2014, the Union government has not increased such spending either in real per capita terms or as a share of GDP; if anything, it has reduced it.

Figure 2.4: Social expenditure as a percentage of GDP in India

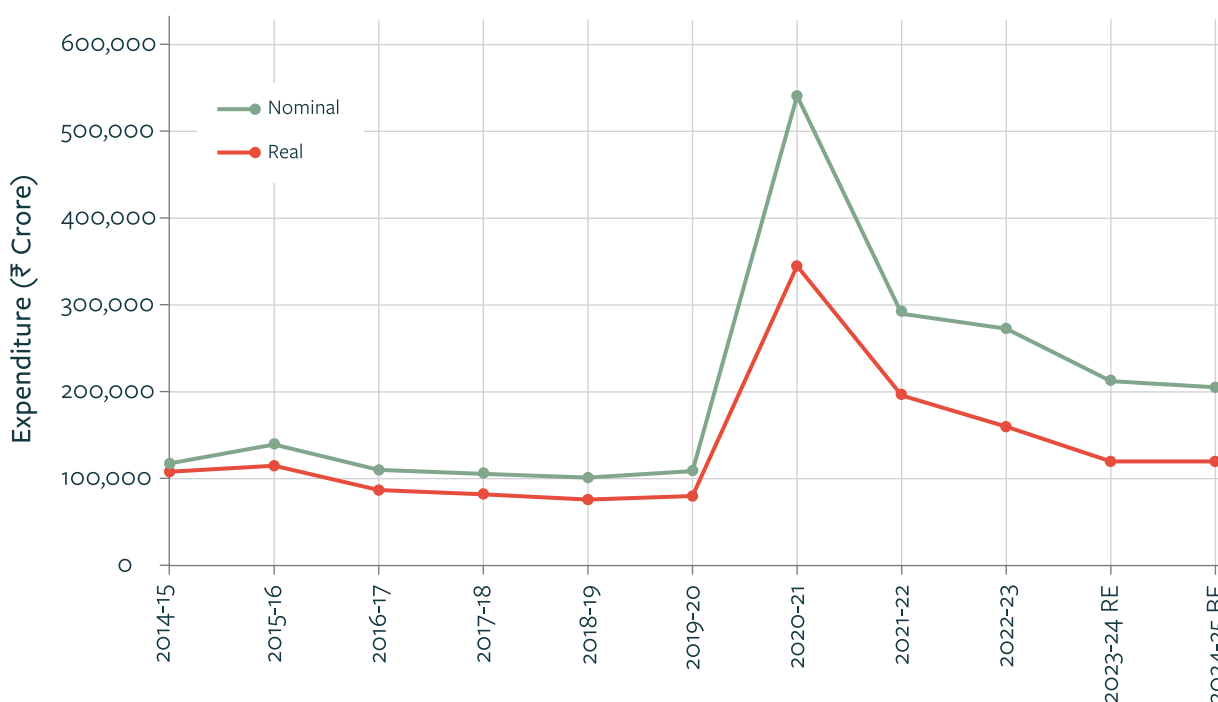


Sources and notes: Bose, Sukanya, and Saikat Banerjee. 2025. “Social Spending and Fiscal Policy in India: Towards an Alternate Macro-Fiscal Framework Integrating Human Development”. Working Paper 25/422. National Institute of Public Finance and Policy.

Khera and Asjad (2024) note that because many of the schemes introduced by the United Progressive Alliance (UPA) government were enshrined in law, it was difficult to defund them entirely. However, allocations to several schemes were substantially reduced, and some were renamed. The new welfare measures introduced by the National Democratic Alliance (NDA) government, largely in the form of cash transfers targeted at specific groups, broadly offset these reductions, but differed in approach, shifting from a rights-based framework to a more paternalistic model.

A further issue concerns the impact of inflation on the real value of benefits available to households. The provision of free food to NFSA beneficiaries since the peak of the COVID-19 pandemic has received considerable attention. However, it is important to note that the NFSA already provides highly subsidised food. The difference for 5 kg per month – ₹10 or ₹15, as opposed to no payment – was therefore marginal for the rights holders. As Figure 2.5 shows, the total expenditure on the food subsidy increased only modestly beyond the pandemic years. In nominal terms, the food subsidy rose by around 78 per cent between 2014–15 and 2024–25, but the increase in real terms over the same period was less than 14 per cent. While the pandemic years were exceptional in terms of food subsidy expenditure, this was not accompanied by comparable increases in other essential forms of social protection, whether in healthcare or livelihoods support.

Figure 2.5: Expenditure on food subsidies in real and nominal terms



Sources and notes: Accountability Initiative. 2024. “BUDGET FY 2024-25 (Interim) the Last Decade of Social Spending Where Have Government Revenues Gone?”. The spike in 2020-21 includes the additional subsidy towards covid relief as well as correction in the budgetary accounting by offsetting of past loans to Food Corporation of India from National Small Savings Fund.

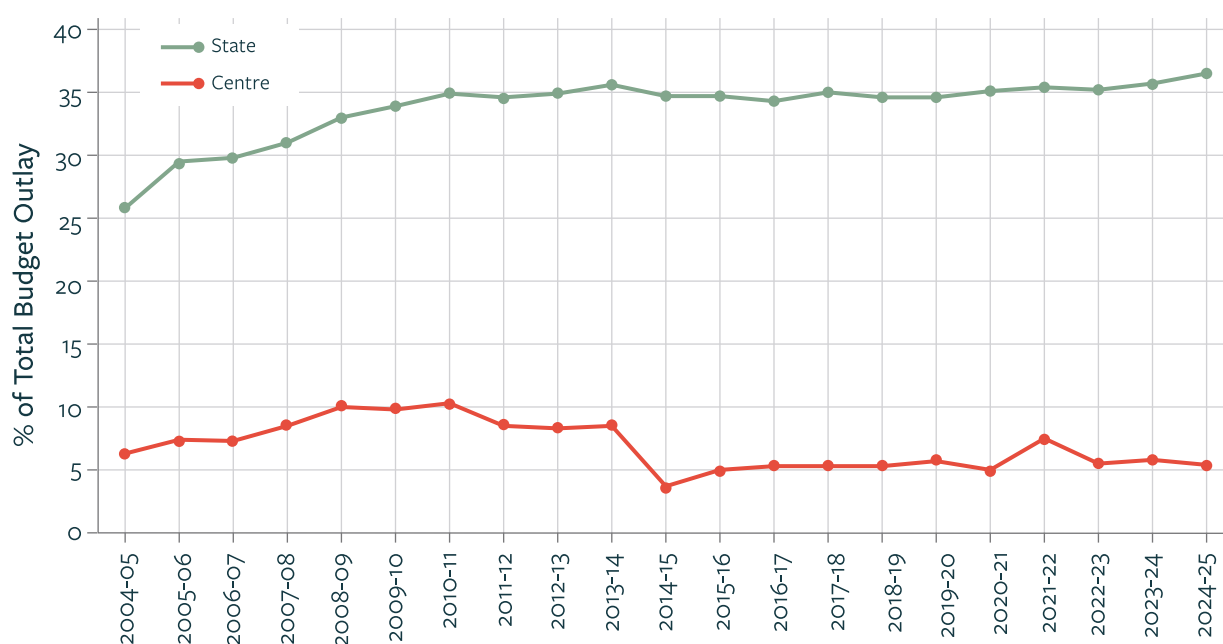
As a result, persistently low and clearly inadequate social spending by the Union government remains a major constraint on India's development. However, central spending constitutes only one component of total social spending, since state governments also bear significant responsibility. It is therefore important to assess their role, particularly over the past decade.

2.4 Fiscal federalism and social spending in India

Most of the increase in social spending in India over the past decade has been driven by the state governments, which have sharply raised their own social spending.

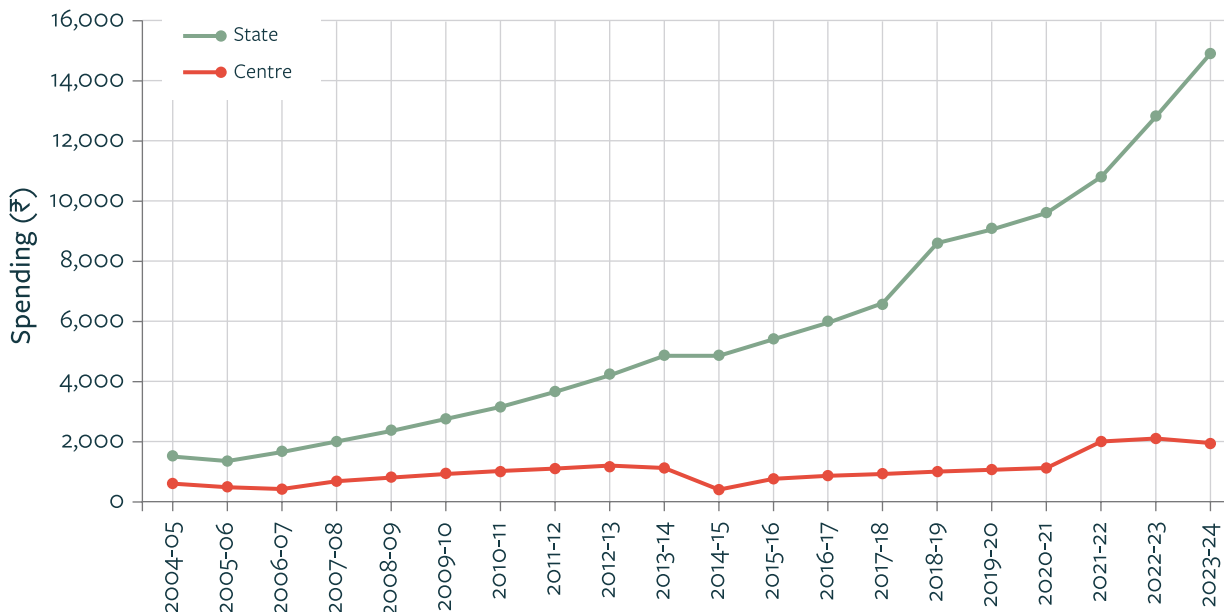
As Figure 2.6 shows, the share of social spending in the total budgetary outlays of the Union government declined from 2014–15 onwards and remained lower for most of the subsequent period, apart from the exceptional year of the COVID-19 pandemic (2021–22). This resulted in a drop in the average share of social spending in total expenditure, from 8.5 per cent during 2004–05 to 2013–14, to as low as 5.3 per cent in the period thereafter. By contrast, state governments demonstrated a much stronger and steadily increasing commitment to social sector spending over this period. Their expenditures exceeded those of the Union government by more than four times up to 2013–14 and by more than eight times thereafter. The divergence is clearly reflected in per capita social spending by Union and state governments, as shown in Figure 2.7. These figures are presented in nominal

Figure 2.6: Social services expenditure of central and state governments as a total percentage of budget outlays



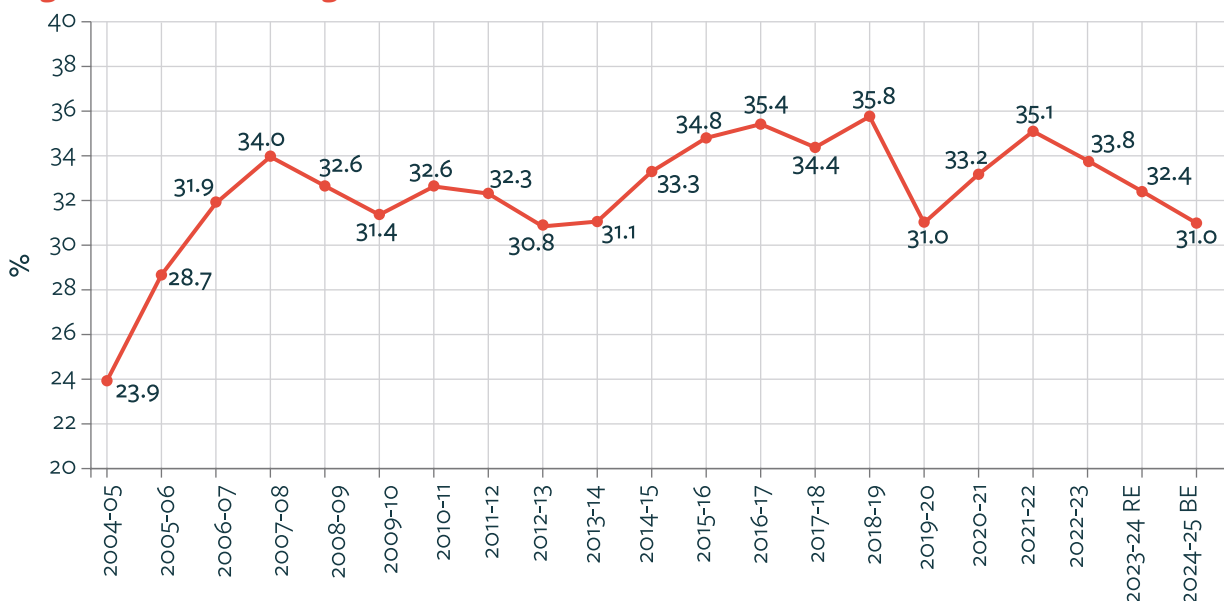
Sources and notes: Handbook of Statistics on the Indian Economy and Handbook of Statistics on Indian States, Reserve Bank of India, accessed on 8 November 2025.

Figure 2.7: Per capita social spending of central and state governments



Sources and notes: Handbook of Statistics on the Indian Economy and Handbook of Statistics on Indian States, Reserve Bank of India, accessed on 8 November 2025.

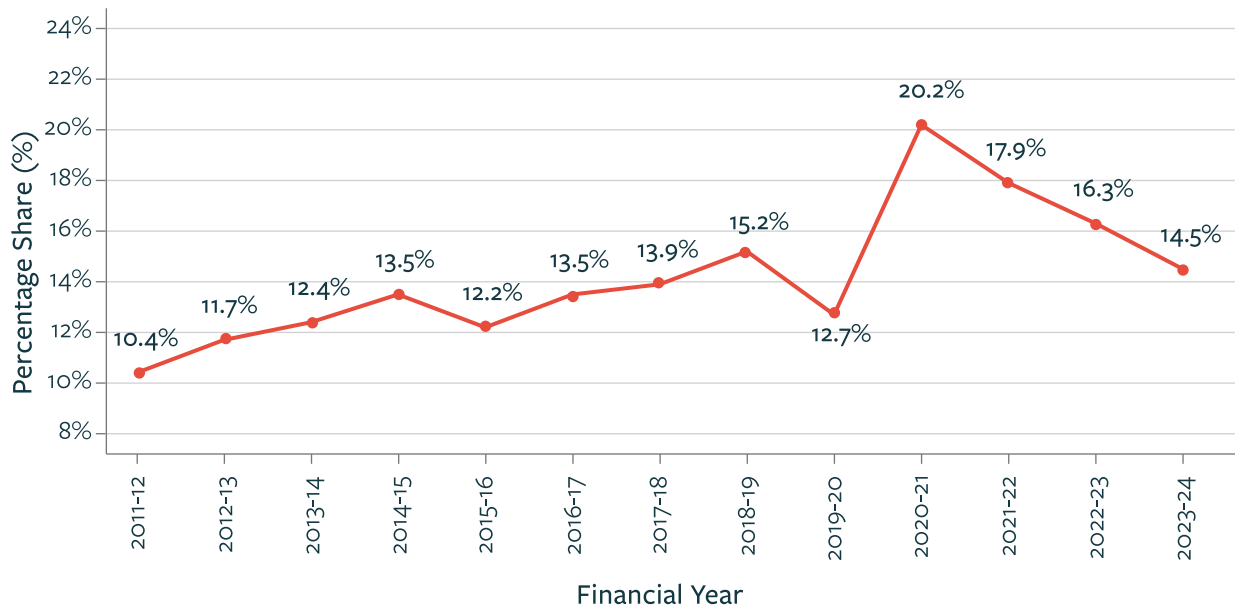
Figure 2.8: Percentage of fiscal transfers from Centre in total state revenues



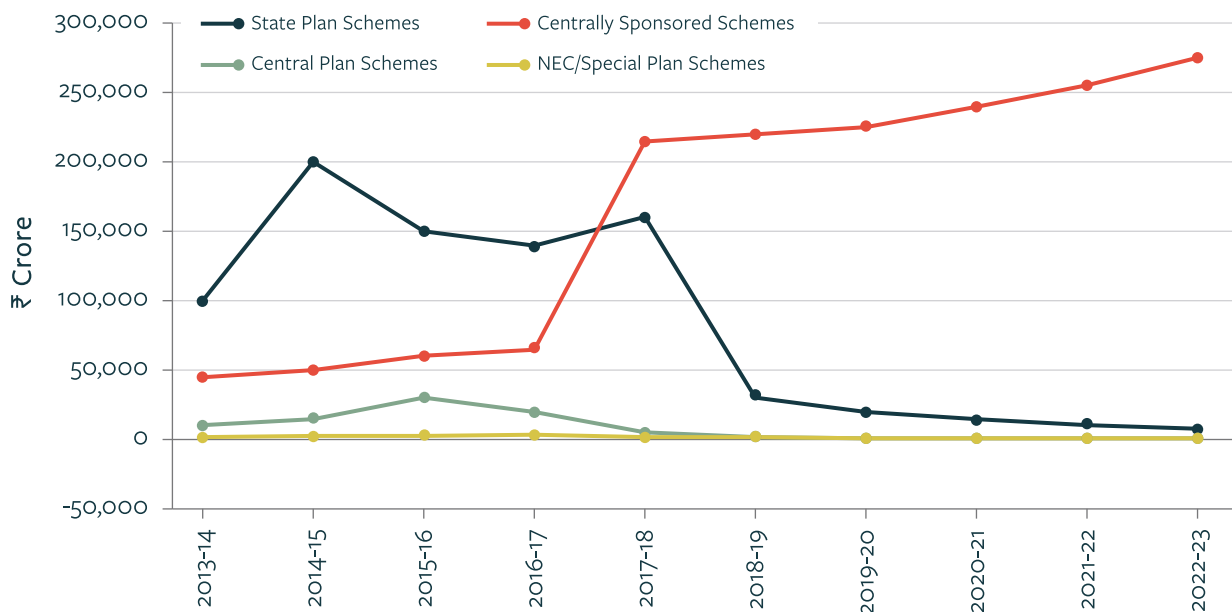
Sources and notes: Handbook of Statistics on the Indian Economy, Reserve Bank of India, accessed on 17 April 2026.

terms and therefore do not account for the effects of inflation. In addition, owing to the absence of Census data after 2011, the estimates rely on population projections that have yet to be fully validated.

The expansion of social spending by state governments is particularly notable given concurrent changes in the fiscal structure and the reduced role of transfers from the Centre. Figure 2.8 illustrates this shift. The Fourteenth Finance Commission (2014) increased the share of tax devolution to states from 32 per cent to 42 per cent, with the intention of providing greater fiscal autonomy, flexibility and enabling states to design programmes suited to their specific contexts, rather

Figure 2.9: Share of cesses and surcharges in gross tax revenue

Sources and notes: Year-wise details of Major Cesses levied and collected [Data set], Dataful. <https://dataful.in/datasets/21210>.

Figure 2.10: Centre's transfers for plan schemes

Sources and notes: Handbook of Statistics on the Indian Economy and Handbook of Statistics on Indian States, Reserve Bank of India, accessed on 8 November 2025.

than relying on centrally sponsored schemes that were not always designed for specific state contexts. While the Union government initially implemented this recommendation, as reflected in higher tax transfers, it subsequently sought to offset its effects by increasing reliance on cesses and surcharges, which are not shared with states. Figure 2.9 illustrates this shift. The share of cesses and surcharges in gross tax revenue rose from 10.4 per cent in 2011–12 to a peak of 20 per cent in 2020–21, before declining to 14.5 per cent in 2023–24.

This meant that state governments had to reduce their dependence on fiscal transfers from the Centre, with such transfers declining from a peak of 35.8 per

cent in 2018–19 to 31 per cent in 2024–25. Furthermore, as Figure 2.10 indicates, the Union government has continued to prioritise fiscal centralisation by reducing – and in some cases effectively eliminating – transfers for state plan schemes, instead concentrating non-tax transfers on centrally planned schemes that often come with conditions not always aligned with state priorities.

2.5 Conclusion

International evidence on public spending in social sectors, particularly social protection and welfare programmes, indicates that such expenditure has significant positive effects across social, economic and political domains. As noted earlier, these include reductions in poverty and inequality; stronger multiplier effects, especially in employment generation; and countercyclical impacts that mitigate the severity and duration of economic downturns. Such spending also advances the broader development process, not only through the economic gains associated with a healthier and better educated workforce, but also by helping to manage the tensions and contradictions inherent in a development process that necessarily involves change.

Social protection contributes to development through its effects on demographics, distribution and incentives, while reductions in inequality help to ease social strains that accompany processes of economic development. It is also critical for the generation of good-quality employment – an area that has remained a major weakness, and at times a failure, of India’s accumulation strategy. In this context, the trajectory of social welfare spending in India can be characterised as one of largely missed opportunities, punctuated by important positive developments (especially in certain states), that require more significant expansion and consolidation. The future trajectory of the Indian economy will depend to a considerable extent on how current and future governments respond to this challenge.

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