

Rythu Bandhu as a Transaction-Cost Reducing Institutional Innovation: A Welfare and Market Failure Analysis of Telangana's Farm Income Support Policy

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Abstract: Agricultural markets in developing countries are often plagued by incomplete contracts, high transaction costs, and asymmetrical information, which inhibit private exchanges from being efficient and result in ongoing losses of social value. While classic welfare economic theories rationalize government intervention because of externalities and inefficiencies in the market, an alternative view identifies that inefficiencies caused by market failures may be due to the costs of organising exchange, not simply distortions in price. The Rythu Bandhu scheme in Telangana gives farmers an unconditional per acre investment subsidy, making it one of India's largest direct income transfer programs. Through an analysis of transaction cost economics, theories of asymmetrical information, and Kaldor Hicks welfare analysis, this study supports the impartial classification of the Rythu Bandhu programme as more than just a redistributive “giveaway”, but rather as an institutional innovation that decreases the cost of attaining credit, reduces the occurrence of adverse selection, requires less reliance on informal credit providers, and provides more certainty in making long-term farming decisions. Theoretical frameworks developed by Dahlman to explain the transaction costs involved in externalities, the lemons problem posited by Akerlof, and the welfare criteria for compensation are used to demonstrate the agricultural distress in relation to the Rythu Bandhu scheme. By utilising descriptive evidence, secondary data sources, and analyses based on a cost benefit approach, this paper provides evidence to demonstrate that Rythu Bandhu contributes to partially internalising risks in a market that is unable to provide the necessary insurance due to both high information costs as well as high bargaining costs.

Keywords: Transaction Costs, Externalities, Information Asymmetry, Welfare Economics, Agricultural Policy, Telangana, Rythu Bandhu, Income Support

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