The Failure of Subsidy Policies In Conditions of Information Asymmetry : Theoretical and Empirical Analysis

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ABSTRACT

Subsidy policy is an instrument of state intervention aimed at improving welfare distribution and correcting market failures. However, its effectiveness often does not align with its formulated normative objectives. This study aims to analyze the failure of subsidy policy by positioning information asymmetry as a key structural determinant influencing policy design, implementation, and outcomes. The research approach uses a theoretical-analytical qualitative method, combining studies of public economic theory, information asymmetry theory, and institutional perspectives, as well as a critical analysis of empirical findings from various policy documents and previous studies. The analysis shows that information asymmetry between the government, subsidy recipients, and intermediary actors results in inaccurate targeting, incentive distortion, and systemic opportunistic behavior. The gap between the normative design of the policy and the reality of empirical implementation is exacerbated by limited administrative capacity, institutional fragmentation, and weak public information systems. These conditions not only reduce the effectiveness of subsidy policy but also create a significant fiscal burden and hamper the sustainability of public policy. This study emphasizes the importance of reformulating subsidy policy through strengthening governance, integrating information systems, and shifting the paradigm towards recipient-based subsidies. The integration of theoretical and empirical analysis provides a more realistic conceptual basis for the formulation of adaptive, accountable, and sustainable subsidy policies.
Keywords: Subsidy Policy, Information Asymmetry, Public Policy Failure

INTRODUCTION

Subsidy policy is an instrument of state intervention aimed at improving welfare distribution and correcting market failures that cannot be addressed by the price mechanism. The design of these policies is generally based on the assumption that the government has adequate information regarding economic conditions, needs, and characteristics of target groups. Empirical reality shows that this assumption is often not fully met. Differences in information levels between policymakers and beneficiaries create structural information asymmetries (Liu & Wang, 2022). This condition affects the quality of decision-making from the policy formulation stage. Inaccurate initial information has the potential to result in subsidy designs that are unresponsive to socioeconomic realities. Consequently, the desired goals of equity and efficiency are difficult to achieve. This situation is the starting point for various forms of subsidy policy failure.

Information asymmetry makes it difficult for the government to identify groups truly deserving of subsidies. Administrative data often does not reflect the actual conditions of society due to dynamic economic changes. Subsidy recipients have incentives to conceal or manipulate information to obtain economic benefits. This information asymmetry weakens the selection and verification functions of public policies (Song & Wang, 2022). Weak

targeting mechanisms create room for systematic mistargeting. Subsidies that should be compensatory are instead enjoyed by groups who do not need them. The unequal distribution of benefits reduces the legitimacy of policies in the public eye. This situation demonstrates that information issues are not merely technical but fundamental.

Information problems not only impact targeting accuracy but also influence the economic behavior of the actors involved. Subsidies create incentives that can be exploited opportunistically by certain individuals or groups. When oversight fails to keep pace with information complexity, the potential for moral hazard increases. Subsidy recipients can potentially adjust their behavior to meet administrative criteria without reflecting real needs. Intermediaries can exploit information gaps for personal gain. These behavioral distortions disrupt market mechanisms and economic efficiency. Public resource allocation becomes suboptimal due to unanticipated behavioral responses. This pattern reinforces the argument that information asymmetry deepens the failure of subsidy policies (Chen et al., 2020; Kauppi et al., 2024).

The theoretical perspective of public economics views subsidies as a corrective tool for specific market failures. Theoretical models generally assume actor rationality and relatively symmetric information availability. Mismatches between theoretical assumptions and empirical conditions create analytical gaps. Information asymmetry distorts policy outcomes from those predicted by standard theory. Policy outcomes no longer reflect the optimal equilibrium as normatively formulated. The effectiveness of subsidies becomes highly dependent on the institutional capacity of the state. Institutional limitations magnify the negative impact of information asymmetry (Ugur & Trushin, 2023; Song & Wen, 2023). The theoretical framework needs to be retested through relevant empirical evidence.

Empirical findings across various sectors indicate that subsidies often fail to achieve distribution and efficiency goals. Field data reveals significant levels of budget leakage in subsidy implementation (Jiang et al., 2022). Mistargeting is a recurring pattern across regions and programs, and policy evaluations often show a smaller impact than the fiscal costs incurred (Meunier & Ponssard, 2024). The discrepancy between policy plans and implementation on the ground highlights the dominant role of information. Monitoring and evaluation capacities have not been able to close this information gap. Empirical evidence reinforces criticism of the effectiveness of conventional subsidies. Analyses that integrate theory and data are becoming increasingly relevant.

The impact of subsidy failure is not limited to microeconomic aspects but also affects the country's fiscal stability. The subsidy budget absorbs a significant portion of public spending each year. Inefficient fund allocation narrows the fiscal space for productive development programs (Li et al., 2019). Long-term budget burdens increase the risk of unsustainable public policies. Fiscal pressure can reduce the country's ability to respond to economic shocks. Decisions to maintain subsidies are often influenced by less-than-rational political considerations. Information asymmetry reinforces policy biases that are difficult to correct. These fiscal consequences underscore the importance of evidence-based policy evaluation.

Institutional dimensions play a crucial role in exacerbating or mitigating the impact of information asymmetry. The quality of governance determines a country's ability to manage information accurately. A weak administrative system increases the opportunity for data manipulation. Policy transparency impacts the level of accountability for subsidy implementation. Inter-institutional coordination is a crucial factor in information exchange. Data asymmetry across institutions creates policy fragmentation. Human resource capacity also impacts the effectiveness of oversight. Institutional strengthening is a prerequisite for improving the performance of subsidy policies.

Analyzing subsidy policy failures requires an approach that comprehensively combines theoretical frameworks and empirical evidence. Theoretical approaches help identify the causal mechanisms underlying policy failures. Empirical analysis provides a

clear picture of implementation patterns and their impacts. Integrating both approaches allows for more objective and in-depth policy evaluation. Understanding the role of information asymmetry is key to improving policy design. Subsidy reformulation needs to consider the country's information and institutional capacity. Data-driven policy innovation has the potential to reduce existing distortions. This study provides an academic foundation for formulating more effective and sustainable subsidy policies.

RESEARCH METHOD

This study uses a qualitative approach with theoretical-analytical methods to examine the failure of subsidy policies under conditions of information asymmetry. This approach was chosen because the research problem is structural, conceptual, and institutional in nature, and therefore cannot be adequately explained through quantitative measurements alone. The primary focus of the study is to explore the causal relationship between information inequality, actor behavior, policy design, and subsidy implementation outcomes. The analysis is conducted by integrating public economic theory, information asymmetry theory, and institutional theory as the primary conceptual framework.

The research data sources consisted of secondary data obtained from policy documents, subsidy evaluation reports, academic publications, and relevant previous empirical research. Data selection was conducted purposively, considering theoretical relevance and analytical depth regarding the issues of information asymmetry and subsidies. Data collection techniques used documentation studies and systematic literature reviews to identify patterns and inconsistencies.

RESULTS AND DISCUSSION
Information Asymmetry as a Structural Determinant of Subsidy Policy Failure

Information asymmetry plays a central role as a structural determinant in explaining the failure of subsidy policies. The information gap between the government, as policy designer, and the public, as beneficiaries, creates a basis for decisions that does not fully reflect actual socioeconomic conditions. The information used in policy formulation is often aggregated and static, while the economic reality of society is heterogeneous and dynamic. These differences in characteristics lead to subsidy policies being designed based on simplified representations. Information simplification increases the risk of inaccurate targeting from the initial stages of the policy. The process of establishing recipient criteria becomes insensitive to variations in real needs. The lack of synchronization between data and reality weakens the corrective power of subsidies against market failures (Pambudi, 2025). Policy structures built on unequal information tend to result in systemic failure.

Information asymmetry also impacts the relationship between the state and subsidy recipients within a principal-agent framework. The government acts as the principal, setting policy objectives, while subsidy recipients act as agents with superior information about their economic conditions. This information asymmetry creates room for adverse selection behavior. Individuals or groups that do not fully meet the criteria may adjust their representation of their situation to access subsidies. Administrative selection mechanisms are often unable to detect such information distortions. Limited verification processes reinforce the state's reliance on data provided by recipients. When economic incentives are substantial, information manipulation becomes individually rational. The accumulation of such behavior reduces the collective efficiency of subsidy policies (Sudiyarti et al., 2025).

Information asymmetry contributes to the emergence of moral hazard after subsidies are received. Beneficiaries tend to change their economic behavior because the consequences of the policy are not fully internalized. Subsidies intended to improve welfare can reduce productivity incentives. Dependence on state aid grows when oversight cannot keep up with the complexity of information. These behavioral changes are rarely captured in policy design assumptions. Subsidy instruments are often designed as if recipient behavior

is incentive-neutral. Inconsistent behavioral assumptions weaken the long-term effectiveness of policies. The impact of policies shifts from correcting market failures to creating new distortions. This pattern suggests that subsidy failure stems from uncontrolled incentive mechanisms.

The involvement of intermediary actors complicates the information structure of subsidy policies. Technical implementers, distributors, and lower-level bureaucrats act as information nodes that determine the flow of subsidy benefits (Nabilah & Addainuri, 2025; Assagaf & Ali, 2017). Each layer of actors has different interests and information limitations. Information fragmentation between actors creates opportunities for implementation deviations. Weak coordination widens the gap between written policies and field practices. Distorted information at one point has a ripple effect throughout the system. Accountability becomes difficult to enforce when information flows are opaque. Dependence on complex bureaucratic structures increases the risk of policy failure. Information asymmetry develops as an institutional phenomenon, not simply a technical issue.

Accumulated information asymmetry leads to recurring and persistent failures in subsidy policies. Administrative-only improvement efforts tend to miss the root of the problem. Policy reforms often focus on adjusting budgets or criteria without improving information structures. The inability to manage information comprehensively weakens policy adaptation capacity. Policy evaluations become biased due to reliance on incomplete data. The cycle of failure repeats itself because policy learning is suboptimal. Information asymmetry persists as a structural characteristic of public policy. A thorough understanding of the role of information is a prerequisite for improving subsidy policies. Without structural transformation, subsidy failures will continue to be reproduced.

The Gap between Normative Policy Design and Empirical Implementation Reality

The normative design of subsidy policy is built on theoretical assumptions that emphasize rationality and actor compliance. The public economic model positions subsidies as corrective instruments that work linearly towards policy objectives. This assumption assumes that information is relatively symmetrically available. The reality of implementation reveals far more complex conditions. Limited data and administrative capacity hinder the translation of normative objectives into practice. A theoretically optimally designed policy loses effectiveness when its underlying assumptions are not met. This discrepancy between design and implementation creates a gap in policy outcomes, which undermines the credibility of state interventions (Widia, 2025). This mismatch is a major source of empirical failure of subsidy policy.

Subsidy policy structures are often centralized and uniform, an approach intended to simplify budget management and control (Jamil, 2024). Variations in community socioeconomic conditions are not fully accommodated in policy design. Implementation at the local level faces realities that differ from central government assumptions. Implementing officials are forced to informally adapt policies to field conditions. This informal adaptation creates deviations from the initial design. Inconsistent implementation weakens policy integrity. The gap between norms and practices widens with increasing social complexity. Policy loses its prescriptive power at the operational level.

Evaluations of subsidy policies often show results that do not justify the fiscal costs. Indicators of success tend to be output-oriented. Long-term impacts on welfare and market efficiency are difficult to accurately measure. Limited evaluation data reinforce biases in policy assessments (Mozin et al., 2025). Empirical findings often reveal leakage and inaccurate targeting. Interpretation of evaluation results is influenced by political and bureaucratic interests (Blom-Hansen et al., 2021). Misalignments between objectives and outcomes are increasingly difficult to correct. The policy learning process is not reflective. The design-implementation gap persists without fundamental correction.

Institutional aspects deepen the gap between normative policies and empirical

reality. Coordination between institutions is often hampered by fragmented authority. Unintegrated information systems exacerbate implementation distortions. Each institution manages data based on sectoral interests. Policy consistency is compromised by differing administrative interpretations. Human resource capacity impacts the quality of implementation on the ground. Bureaucratic training and incentives are not fully aligned with policy objectives. Institutional disharmony hampers the effectiveness of subsidies. The gap between design and practice is becoming increasingly evident as a structural pattern.

The discrepancy between normative policy and empirical implementation underscores the need for a more critical evaluative approach. Policies cannot be judged solely on the internal consistency of their design. Implementation conditions are a determining factor in the success of public policies. Empirical analysis is necessary to test the validity of normative assumptions. Policy reformulation must consider administrative and information capacity. Adaptive policy design is more relevant than a uniform approach. Implementation gaps are not anomalies, but rather structural consequences. This understanding opens up space for more realistic policy improvements. Integrating theory and empirics is a methodological necessity.

Institutional Implications and Information-Based Subsidy Policy Reformulation

The institutional implications of failed subsidy policies place governance as a crucial factor. The quality of institutions determines a country's ability to manage information effectively. Weak administrative systems increase the risk of policy distortion. Data transparency is a prerequisite for public accountability. Information secrecy weakens public oversight. Unresponsive institutions struggle to adapt policies to social dynamics. Subsidies managed without robust information systems tend to be poorly targeted. The role of institutions is a key determinant of policy effectiveness. Institutional reform is an urgent need.

Subsidy policy information systems play a strategic role in reducing information asymmetry. Database integration between institutions allows for more accurate verification. Information technology opens up opportunities for real-time policy monitoring. The availability of up-to-date data improves the quality of decision-making. Data fragmentation increases the opportunity for manipulation and leakage. Policy reforms without updated information systems tend to be ineffective. Investment in data infrastructure is an integral part of subsidy policy (Rahayu et al., 2025). A country's analytical capacity determines the quality of public intervention. A data-driven approach enhances policy precision.

Institutional accountability plays a crucial role in maintaining the integrity of subsidy policies. Internal oversight mechanisms need to be strengthened to mitigate irregularities. External oversight by the public and independent institutions enhances policy legitimacy. Budget transparency allows for more objective evaluations (Wea & Rahmadhani, 2025). When information is openly available, opportunistic behavior can be suppressed. Bureaucratic incentives need to be aligned with policy objectives. Incentive misalignments weaken policy implementation. Institutional reforms must address both structural and cultural aspects. Accountability is the foundation of policy sustainability.

The commodity-based subsidy paradigm demonstrates limitations in conditions of unequal information. This approach assumes homogeneity in recipient needs. Socioeconomic realities demonstrate high heterogeneity. Subsidies based on recipient characteristics offer a more adaptive alternative. This approach demands stronger information capacity. Policy reform requires a paradigm shift in state intervention. Subsidies are positioned as selective, not universal, instruments. Fiscal efficiency is increased through more precise targeting. The new paradigm emphasizes information quality as a key policy driver.

Information-based subsidy policy reformulation opens up opportunities for increased effectiveness and legitimacy. Adaptive policies are able to respond to

socioeconomic changes. The integration of theoretical analysis and empirical evidence strengthens the policy foundation. Strong institutions support consistent implementation. Policy transformation requires political and administrative commitment. Information system improvements are a long-term investment. Effective subsidy policies contribute to fiscal sustainability. An information-based approach reduces distortions and leakages. This study emphasizes the importance of structural reform of subsidy policies.

CONCLUSION

The conclusion of this study confirms that the failure of subsidy policies cannot be understood as a purely technical issue, but rather as a structural consequence of information asymmetry inherent in the design and implementation of public policies. Information asymmetries between the state, beneficiaries, and intermediary actors form the basis for decisions that do not fully reflect socioeconomic realities. This condition leads to inaccurate targeting, distorted incentives, and the emergence of opportunistic behavior that undermines the effectiveness of subsidy policies. Theoretical analysis shows that normative assumptions about rationality and information symmetry are inconsistent with the empirical conditions of policy implementation. Empirical findings reveal a persistent gap between policy objectives and results achieved on the ground. Limited institutional capacity and fragmented information systems exacerbate this gap. The fiscal burden imposed by inefficient subsidies reduces policy space for more productive development programs. Policy evaluations that rely on distorted data weaken the public policy learning process. Subsidy policy reform requires an approach that places information management at the center. Institutional strengthening, data system integration, and increased transparency are key prerequisites for policy improvement. A paradigm shift toward recipient-based subsidies offers a more adaptive and precise alternative. Overall, the integration of theoretical and empirical analysis provides a strong basis for the formulation of more effective, accountable, and sustainable subsidy policies.

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