



## Cash Transfers as a Strategy for Poverty Reduction: A critical assessment

In the past decade, cash transfers have been gaining in popularity as a preferred strategy for poverty reduction in different parts of the world. Some have even argued that it can become *the* solution to the problem of poverty. Some analysts have described cash transfers as not only “the most necessary, obvious and imperative strategy for poverty alleviation” but even suggested “that these should replace a great deal of other government activity”.<sup>1</sup>

This policy brief discusses some of the pros and cons of using cash transfers as a strategy for poverty reduction. It also discusses the need for seeing cash transfers as supplements, rather than as substitutes of public provisioning of goods and services.

**Cash transfers**, as the term suggests, are direct transfer of money to people by government. Although some proponents tend to see cash transfers, in vogue since the mid-1990s in several Latin American countries, as a radically new idea, “an elegant southern alternative” in reality historical records suggest that they were employed by governments in different parts of the world in antiquity as well as in the Middle Ages.

In recent times, cash transfers made by developing country governments have been either

- **Conditional** (i.e. subject to the beneficiaries meeting certain pre-specified conditions such as children attending school, families visiting health clinics for check-ups, or immunizing children as per the prescribed schedule and the like); or
- **Unconditional, often to certain categories** (such as pensions for older people or child support grants).

While there are examples of **universal cash transfers**, they are usually **targeted** to a certain section of the population meeting particular criteria, typically those described as poor. The cash transfers provide resources needed to meet basic needs of the poorer sections of the population as well as help them to access various services such as health, education.

In Latin American countries, cash transfers have had a measure of success in fighting poverty and in most cases the beneficiaries are required to meet a set of conditions to get the transfer. The conditions can range from being light (as in Brazil’s *Bolsa Familia*) to being extremely time-intensive, especially for mothers (as in the *Oportunidades* programme in Mexico).

Because of the perceived success of these transfers in Latin America, cash transfers, both conditional and unconditional, have proliferated in countries of other developing regions, although even here they are not really a novelty. In Sub-Saharan Africa, for example, several such programmes are donor funded and implemented on pilot basis, usually covering a small segment of the intended beneficiaries. Further, in several cases, especially in countries afflicted by HIV/AIDS, cash transfer programmes are unconditional, provided as pensions to old-age people and/or in some cases as child grants for overall development of children.

### Cash transfers as supplements to public provisioning of goods and services

The need for progressive redistributive transfers, including cash transfers, is well known and indeed they are essential in any civilized society, however poor. The Latin American experience makes a strong case for cash transfers (conditional and unconditional), but it is critical to understand the specific context of and reasons for their success. Two significant aspects of the well-known success stories of cash transfers in Latin America are:

- These have typically complemented public provision of essential social services. In most programmes of conditional cash transfers in Latin America, the conditionalities often mandated the use of government-managed facilities such as schools and clinics.
- Typically, extensive efforts were simultaneously made to expand and improve the public delivery of such services and facilities. So the success of cash transfer schemes has been associated with continued and enlarged investment in public services.

Clearly, it is important to combine different strategies to ensure social protection, and emphasis on any one instrument (such as cash transfers) should not lead to the exclusion or even diminution of other redistributive measures and social policies.

This approach is validated by some recent schemes. For example, Zimbabwe's National Action Plan for Orphans and Vulnerable Children, which is to provide cash transfer to the poorest families, emphasises that "these critical social protection measures to benefit vulnerable children include making sure that cash is complemented by access to basic social services including health and education, as well as social welfare services and access to justice."

### **Problems of posing cash transfers as an alternative**

Despite this, in some countries there is a tendency to see cash transfers as a *substitute* for publicly provided goods and services. For example, in India, there is an argument for encouraging the government to give the poor cash transfers that will allow them to access whatever goods and services they want that are generated by private markets, rather than struggling to ensure public provision.

There are several reasons why such a move may not be desirable and may fail to deliver on its stated objective.

- ***Rising prices in deregulated markets***

The most immediate threat of direct public provision of some essential goods (like food and fuel) being substituted by cash transfers to consumers, is that of rising prices in these deregulated markets. Rise in prices would render such goods unaffordable for the lower-income segments, i.e. those who need them most. Typically, in situations of volatile and rising prices, the real value of cash transfers can get quickly eroded. While it can be argued that cash transfer systems can be indexed to price indices (for example in the case of food items, to the price index for the foods in question) to get around this problem, it is well known that in most developing countries the systems of price indexation of such transfers are typically slow and inadequate to cover the price increases. Given the lags in public response to price changes, depending on price indexation to take care of the problem of rising prices is unlikely to prevent erosion of the entitlements of the poor.

- ***Quality of services in deregulated markets***

There is also the problem of ensuring the quality of private provision, especially in services like health and education where there are many problems of inadequate information. This is why public provision is important, though of course it is critical to ensure the quality of such provision as well. But in the case of say, health services, the absence of a reasonably well-funded public health system that provides access to preventive and curative services cannot be compensated for by providing small amounts of cash that allows people to visit local private quacks! In education, sub-standard private educational institutes that operate mainly as money-making machines, will not be effective substitutes for adequately funded public educational institutes and policies designed to ensure improvements in the performance of children in schools. Case studies show that building more schools and improving the quality of teaching have greater impacts on primary school attendance than measures that increase household income.<sup>2</sup>

- ***Ensuring that the cash transfer actually goes to the intended beneficiaries***

The possibility of cash transfers being diverted for expenditure that do not meet the intended purpose is another issue that can pose serious problems. Even when the poor household is correctly identified, structures of power *within* households as well as social constructions of gender behaviour can affect decisions about how the money is spent, in ways that are not always expected or desired. The argument that handing over the cash payments directly to women will solve this problem is not necessarily correct. Especially with respect to food, it has been found (particularly in south Asia) that women and girls are guilty of voluntary self-denial rather than being forced into choices that reduce their own consumption.

These problems perhaps explain why poor people in general prefer public provision of the good or service in question at a defined price, when it is of reasonable quality. In fact, several studies show it is the relatively better off who prefer cash, while the poor are more likely to prefer provision in kind.<sup>3</sup>

In any case it is better to view cash transfers as complements that will enhance the effectiveness of public provision, rather than as alternatives. Poor families are better able to get the benefits of cash

transfers when there are public services and other provision of goods that they can access with those payments.

### Targeting versus Universalism

Public provisioning of goods and services often involves choices about whether these are to be provided universally or should be targeted to a particular section of the population. Under universalism (which can also pertain to categories such as “all old people” or “all young people” or “all infants” etc.), the entire population is entitled to social benefits, while under targeting, only those deemed eligible are entitled to get the benefits.

In recent years, provision of social protection in many developing countries has been considerably reduced under the influence of more market-friendly development policies. The practice of targeting benefits to only those considered as poor and “needy” has been used extensively to cut down public expenditure on direct provision of services by the government in many countries.

However, targeting is often replete with problems that substantially reduce the scope of such policies as an instrument of poverty reduction. This is because targeting always involves direct and indirect costs, but these are often not taken into consideration when deciding whether and how to target. Some of these problems include:

- **Exclusion and inclusion errors**

Targeting often leads to the actual poor not getting the benefits (exclusion error), and leakage to better-off or to those who do not ‘need’ the benefit (inclusion error). Evidence shows that even the most ‘successful’ targeted programmes in Latin America fail to reach a large proportion of the poor. For instance, in Brazil’s *Bolsa Familia*, 59% of the poor were not reached. Similarly, Mexico’s geographically targeted *PROGRESA/Oportunidades* programme did not reach 70% of the poor.<sup>4</sup>

- **Regressive**

Because of problems such as wrong identification of the poor, class interests that influence the distribution of resources, leakages and so on, targeted programmes could also turn out to be regressive, i.e. transfer less resources to the poor than a universal scheme would have done. A World Bank study, evaluating 122 antipoverty targeting interventions in 48 countries in various parts of the world, shows that one out of four targeted programmes turn out to be regressive.<sup>5</sup>

- **High administrative costs**

For the identification of beneficiaries and reaching benefits to them, targeting often requires complex methods and advanced institutional capacity. These, in turn, translate into high administrative costs, which often consume a large chunk of allocated funds. Studies based on simulations of transfer programmes in low-income countries show that total administrative costs for targeted programmes can be as high as 30 per cent, compared to 15 per cent for universal programmes.<sup>6</sup>

Besides the problems associated with targeting in general, there are some that characterise cash transfer-based schemes in particular. For example, in the case of cash transfers, it is difficult to employ certain targeting methods that are relatively less costly and more effective. Thus, targeting methods such as self-selection (i.e. schemes that only those truly in ‘need’ would accept and the better off will not be interested in such as employment programmes) cannot be used in the case of cash transfers as there is little incentive for self-selection in such programmes.

Targeting is a more effective method of reaching benefits to the poor where they form a small percentage of the population. In countries where poverty is widespread and poor face different kinds of discrimination, there is little justification for targeting, as the problems associated with identifying beneficiaries and monitoring programmes tend to far outweigh the benefits.

#### Universal provision, on the other hand, has several benefits:

- Historical evidence shows that countries (even those starting from low levels of development) that adopted relatively less targeted approach in their social systems, have been more successful in reducing poverty as well as inequality.<sup>7</sup>
- As Mkandawire (2005) notes, universal access is most effective in ensuring “political support by the middle class of taxes to finance welfare programmes”.
- Universal schemes are easier and less costly to administer.

In sum, cash transfers can play important positive and redistributive roles, when they are additional to public provision and not seen as alternatives. At the same time, they can play only a limited role in transforming economies and ensuring that structural

transformation reduces poverty. Poverty is not just about lack of adequate income: it is caused by a host of factors such as lack of assets, lack of access to productive employment or to 'decent' work, and so on. Since cash transfers do not address the basic causes of poverty, they cannot be a solution to the problem of persistent poverty. Therefore, it is better to treat cash transfers as (welcome) temporary palliatives, rather than as a development panacea.

- <sup>1</sup> Ghosh, J (2011), 'Cash Transfers as the Silver Bullet for Poverty Reduction: A Sceptical Note', *Economic and Political Weekly*, Vol xlvi, No. 21.
- <sup>2</sup> Handa, S (2001), 'Raising Primary School Enrolment in Developing Countries: The Relative Importance of Supply and Demand', *Journal of Development Economics*, 69, 103–128.
- <sup>3</sup> Ahmed, Akhter U, Agnes R Quisumbing, Mahbuba Nasreen, John F Hoddinott and Elizabeth Bryan (2009), 'Comparing Food and Cash Transfers to the Ultra Poor in Bangladesh', *IFPRI Research Monograph*, No. 163 (Washington DC: IFPRI).
- <sup>4</sup> Soares, Fábio Veras, Rafael Perez Ribas, Fábio Veras and Rafael Guerreiro Osório (2007), 'Evaluating the Impact of Brazil's *Bolsa Família*: Cash Transfer Programmes in Comparative Perspective', *IPC Evaluation Note*, No. 1, December (Brasilia: International Poverty Centre).
- <sup>5</sup> Coady et al, (2004), 'Targeting of Transfers in Developing Countries: Review of Lessons and Experience', World Bank, IFPRI.
- <sup>6</sup> Cited in Dutrey, Alexander Peyre (2007), 'Successful Targeting? Reporting Efficiency and Costs in Targeted Poverty Alleviation Programmes', *Social Policy and Development Programme Paper*, Number 35, November, UNRISD.
- <sup>7</sup> Mkandawire, T (2005), 'Targeting and Universalism in Poverty Reduction', *Social Policy and Development Programme Paper*, Number 23, December, UNRISD.