

Available resources, affordability and sustainability

The objective of this chapter is to examine the spending decisions made by middle- and low-income countries in relation to social protection. Such decisions are impacted by numerous factors including political will and affordability. How much a government will allocate to social protection and where they will get the funds to sustain their programmes are two important questions which must be answered when establishing a social protection framework.

Introduction

Social protection spending (including both social transfers and social insurance¹) ranges between zero and twenty percent of national income in most low- and middle-income countries, but spending in half the countries (for which data is available) ranges between three and nine percent. Social insurance spending (which often does not reach the poor) constitutes most of the social protection spending in many countries: the average (mean) spending on social insurance is 5% of national income (median is 3.5%), compared to an average (mean) spending for social assistance of 1.9% (median is 1.5%). Figure 11.2 illustrates the wide range of expenditure choices across countries for both social assistance and social insurance. (The inserted graph includes countries for which only social assistance spending is available.) Effective social assistance programmes in Latin America (*Oportunidades* in Mexico and *Bolsa Familia* in Brazil) cost a fraction of one percent of national income, while programmes in Africa often cost several times that amount (South Africa spends more than three percent of national income on its social transfer programmes).

The variability of social protection spending decisions by low- and middle-income countries reflects differences in both perceptions of affordability and political will. Effective interventions require a sizable commitment of financial resources – social assistance programmes in developing countries

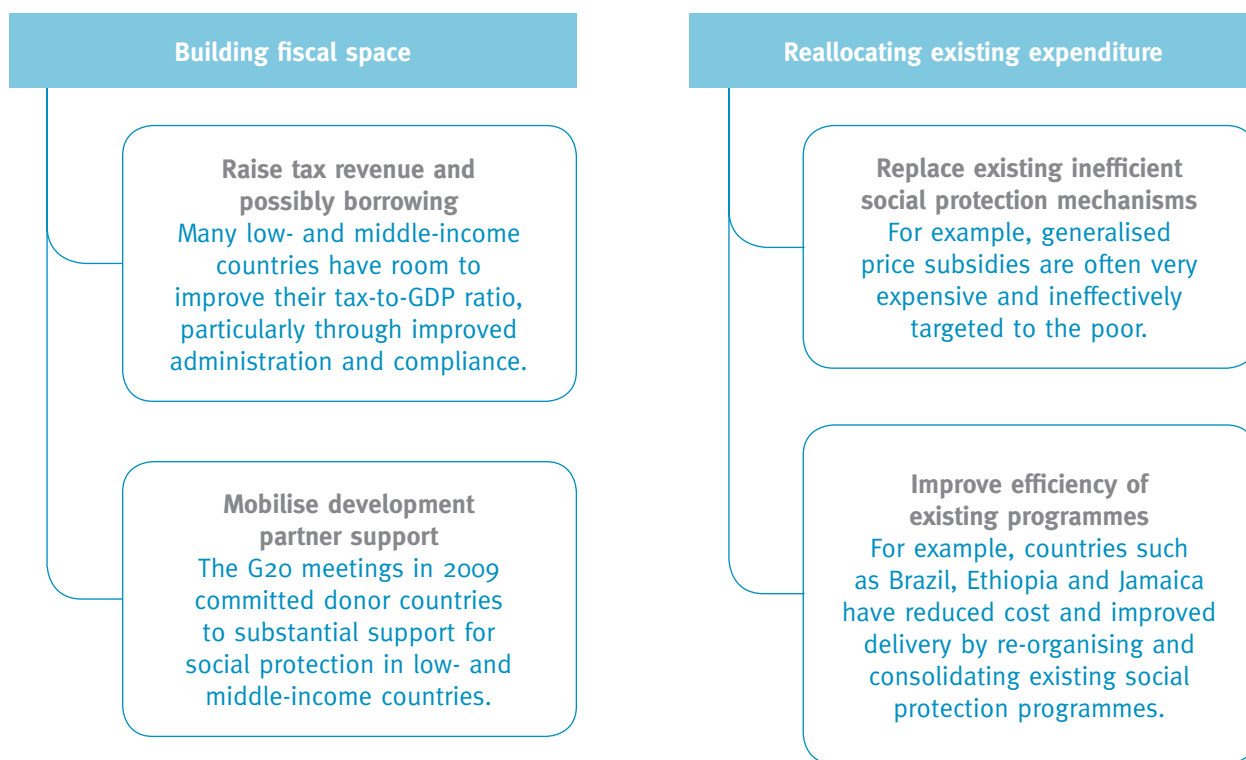


Figure 11.1 Options for financing social protection interventions

usually require 1-2% of national income. Governments generally finance this significant commitment over the longer term from tax revenue, although development partner support can play an important interim role or cover up-front development costs. Increasingly, development partners are developing longer term instruments – up to ten years in some cases – to support the permanent commitments governments must make to their people in building social protection systems.

Depending on the social protection context within the country, some resources may be mobilised by reallocating existing government expenditure. For example, Indonesia has substantially reduced spending on generalised food subsidies with few social protection benefits by implementing more efficient unconditional cash transfer programmes. Senegal is currently considering cash transfer initiatives as a substitute for similarly expensive general price subsidy programmes for food.

It may also be possible to increase the efficiency of existing interventions through appropriate reorganisations and programme consolidations. Brazil has realised substantial cost savings and implementation efficiencies by consolidating four cash transfer programmes under the umbrella of *Bolsa Familia*. Jamaica likewise consolidated multiple programmes into the more

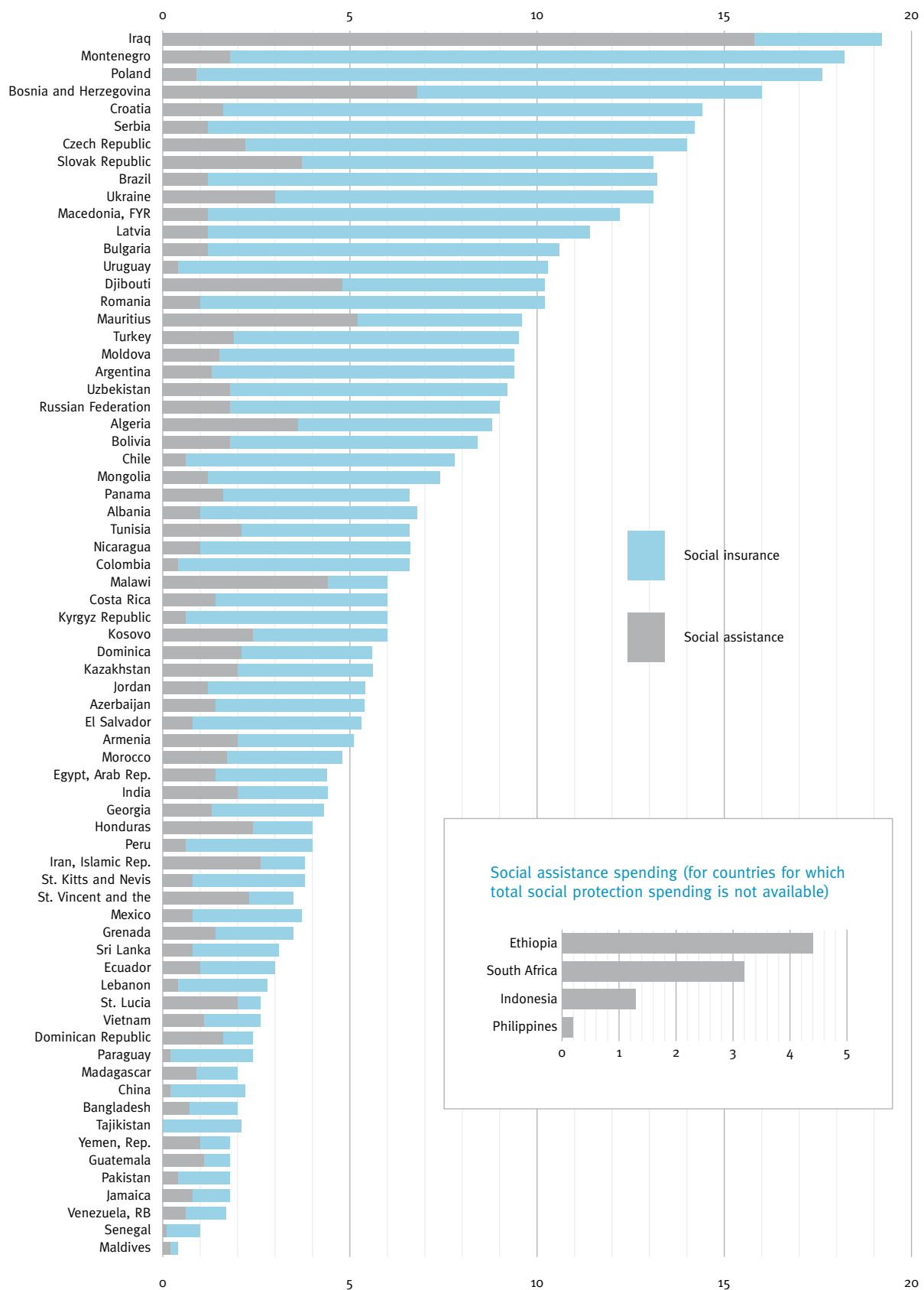


Figure 11.2 Social assistance and social insurance spending for low- and middle-income countries, as % of GDP.

SOURCE: World Bank (2008b). Data from different regions are drawn from various years between 1998 and 2006.

comprehensive PATH initiative. South Africa reorganised provincial delivery mechanisms into a more comprehensive national system operated by the South Africa Social Security Agency, which streamlined operations and realised substantial economies of scale while increasing bargaining power vis-à-vis private sector service providers. Figure 11.1 illustrates these financing choices.

National and donor financial resources

Affordability is multi-dimensional. At one level, it is largely a matter of political will: South African politicians have expressed concern about the sustainability of social security spending even while surprisingly collecting tax revenue exceeding the budget by 3% of national income. Meanwhile, neighbouring Lesotho has implemented a universal pension programme for its elderly despite more pressing fiscal constraints. Economists' attempts to scientifically measure fiscal capacity have generally found that most of the differences across countries are explained by non-economic and largely political factors.²

Social transfer programmes are affordable in a broad range of low-income countries. Zambia's Kalomo pilot, which provides the equivalent of \$15 per month to a thousand poor households, could be scaled up to the poorest ten percent of the population for less than \$20 million – 0.3% of national income and less than one percent of current government spending. Similar programmes could be provided in other African countries for usually less than half a percent of national income and less than 3% of current spending. Figure 11.3 compares the fiscal simulations from a study by the International Labour Organisation for seven low-income African countries. In most of these countries, the programmes could be funded for less than five percent of existing aid flows.³

At an economic level, however, many countries face real fiscal constraints in financing social transfers. Understanding affordability requires information about both the static and dynamic conditions of the national treasury, as well as the availability of international assistance and credit. Affordability is both a short run and long run question. Between domestic and international sources, a country may be able to fund an ambitious social transfer programme. Is this sustainable in the long run? The answer depends on the dynamic impact of the programme on the economy. Effective social protection is often economically productive through a number of transmission mechanisms, thus increasing the resource base available to a country.⁴ "Putting money in the hands of the poor can yield very high rates of return, partly because they use their assets so intensively and partly because the cost of falling below a critical consumption level is so great, small amounts can yield a high effective return".⁵ Increasingly, the World Bank and the Inter-American Development Bank are making loans to finance social transfer strategies.⁶

In addition, the returns to productive social protection expenditure will affect long-run affordability. Increasing evidence documents how social transfers promote economic growth (see Box 11.1). Productive returns from

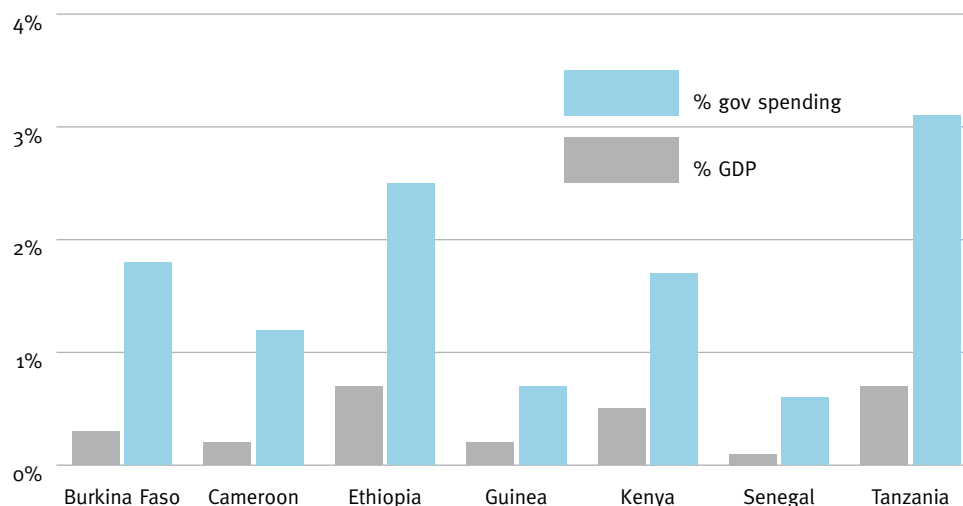


Figure 11.3 Fiscal simulations comparison

SOURCE: Pal et al., (2005).

investing in social protection increase the longer-term affordability of social transfers and promote sustainability.

Importantly, the political and economic decisions determining the amount of available resources may depend on the type of social protection system selected. A programme very effectively targeted to the poor may lack the broad political appeal required to mobilise adequate resources. A universal old age pension or child benefit, for example, may be less progressive but generate sufficiently greater financial support that the poorest benefit more. In this sense, the resource cost of a targeted scheme is not simply comparable with that of a universal programme – some of the direct transfer costs of a universal programme almost pay for themselves. (The political economy dimensions of targeting are discussed further in chapter 8.)

Decentralised financing mechanisms may create spatial differences in affordability within a country. For example, a country with a provincial or state tax-collection system and significant regional income disparities will find it more difficult to finance social protection for the poorest. The provinces or states with the greatest poverty will also have access to the most limited tax resources, unless the national government provides federal grants.

The role of international donors will vary from country to country, and often depends on the type of programme being financed. In very low-income countries and fragile states, the role of donors may be particularly important, particularly in terms of predictability and coordination. In some countries, donor programmes lack the permanence, predictability and

Box 11.1: Social protection and economic growth

An increasing body of evidence documents how social protection programmes contribute to economic growth – and increase the pool of resources available for financing social transfers. Policymakers do not face a trade-off pitting social protection against growth objectives; rather, they have the opportunity to engineer a virtuous circle of increased equity, which promotes growth, supporting further improvements in equity. There are at least seven paths through which social transfers promote growth:

1. Social protection promotes human capital development, improving worker health and education and raising labour productivity. Studies in South Africa and Latin America repeatedly document significant responses

- of health and education outcomes to both conditional and unconditional programmes.
2. Social protection enables the poor to protect themselves and their assets against shocks, enabling them to defend their long term income-generating potential. Droughts in Ethiopia have significantly reduced household earning power as long as 15 years later. Social transfers enable households to resist desperate measures and reduce future vulnerability.
3. Social protection mitigates risk and encourages investment. The downside of the most productive investments is that they are the most risky, and can threaten the poor with destitution. Social transfers enable people to face these risks. For example, farmers protected by the Employment Guarantee

reliability necessary for effective social protection support. Frequent changes in aid programmes tax a country's administrative capacity, undermining the development of effective management systems. "Part of the solution is for donors to commit to long-term support for programmes and to maintain basic programme design – even if imperfect – unless there is an absolutely compelling reason to change it." ⁷

Donor coordination can also increase the efficiency of a given level of aid resources.⁸ For example, both the World Food Programme's Food-for-Work and Malawi's Social Action Fund's Cash-for-Work initiatives included concentrations of activity in the same geographically targeted rural areas, enabling some communities to enjoy access to both projects while equally poor neighbouring areas were unsupported.⁹ At one time in Malawi, different donors operated fifteen various social protection projects – public works, feeding schemes and social transfer programmes.¹⁰ Integration of aid initiatives can foster more comprehensive coverage, reduce duplication and lower administration costs.

What size of social transfer is provided?

Once the intended group of beneficiaries is identified, the second decision is to identify the size of the grant. This involves weighing the available resources against the range of possible benefits, from the minimum to the optimal level. When the programme includes multiple targeted beneficiaries – for example, the children and the elderly, or primary and secondary school students – the size of the benefits for each may vary.

Determining the appropriate level of benefits similarly requires an

Scheme in Maharashtra, India invest in higher-yielding varieties than farmers in neighbouring states.

4. Social protection programmes combat discrimination, unlocking economic potential. In Bangladesh, Brazil and South Africa, transfers provided to women have a greater positive impact on school attendance by girls compared to boys.
5. Social protection supports the participation of the poor in labour markets. Job search is often expensive and risky. In South Africa workers receiving social transfers look harder for work than those in comparable households not receiving grants – and they are more successful in finding employment.
6. Social protection stimulates demand for local

goods and services. In Zambia 70, per cent of social transfers is being spent on locally-produced goods, stimulating enterprise in rural areas. In South Africa, social grants shift the composition of national expenditure from imports to local goods, increasing savings and economic growth.

7. Social protection helps create an effective and secure state. It builds social cohesion and a sense of citizenship, and reduces conflict. A safe and predictable environment is essential to encourage individuals, including foreign investors, to work and invest.

SOURCE: DFID (2006b).

understanding of the politics, the social profile of poverty, the socio-economic status of beneficiaries and their livelihood strategies, the capacity of government and the fiscal position of the country. The determination of the appropriate benefits level requires significant economic and political trade-offs, reflecting the priorities of policymakers and their political economy constraints.¹¹

The minimum benefit level provides a floor beneath which social transfer programmes are unlikely to be effective. At the other end of the range, the optimal benefit level could be greater than the poverty gap because of targeting uncertainty, the expectation that the grant will in turn be redistributed within the household (or across households), or the desire to move further than just eliminating poverty. For example, South Africa's State Old Age Pension – at R1010 (US\$140) per month – is about twice the level of the most commonly used poverty lines.

Hypothetically, given the fundamental objective of eradicating poverty, a government with no constraints would set the minimum benefit level equal to each household's gap between their income and the level required for them to escape poverty. In practice, however, governments often face severe constraints: mobilising the resources necessary to finance the grant, identifying and reaching the poor, and accurately calculating the poverty gap for each household.

When financial and information resources are scarce, the minimum benefit may fall below what is required to raise the incomes of the poorest to the poverty line, and a flat per capita transfer to the poor (or universally distributed) may be most feasible.

While fiscal constraints may prevent the implementation of an ideal social protection system, increasing evidence documents the affordability of basic social protection in most countries. The position that “even a small amount of cash in the hands of a poor mother can do wonders” sets a minimum baseline

of the unconditional transfer of the smallest affordable amount.¹² The very poorest, even in middle-income countries may be subsisting on a fraction of a dollar per day – and the poorest in some low income countries, are not even subsisting. The minimum benefit may be constrained by what can be cost-effectively transferred; however, technology holds the potential to significantly reduce transaction costs, even in countries severely scarce on infrastructure.

A smaller transfer more broadly distributed may help children more than a larger grant with stricter targeting conditions. Evidence for South Africa documents that adults in poor households are more likely to face hunger than are children – and grants are more likely to reduce child hunger than adult hunger.¹³

Minimum benefits set at very low levels may create political difficulties. While many countries have shown that very small benefits can nonetheless produce very significant results, the idea of a minimum level influences policymakers. Key policymakers in South Africa have expressed doubts about a universal income transfer proposal because of concerns the small amount (US\$20) would not make a sufficient impact on poverty.¹⁴ In South Africa's case, this “minimum” benefit would more than double the average consumption of the poorest 20% of the population. The recognition of the intensity of poverty implicit in these minimum benefit determinations can intimidate policymakers.

Nevertheless, the social, economic and political impact of even minimum benefits can be significant. For instance, Kyrgyzstan's Unified Monthly Benefit delivers an average transfer equal to only about one-quarter the extreme poverty line. While small, the resulting 15% increase in the average recipient's income makes a material contribution to living standards.¹⁵

Benefit levels set in a decentralised arrangement involve greater complexities, particularly when resources cannot be pooled nationally. Brazil's *Bolsa Escola* programme was implemented and funded at a municipal level. In poorer regions like Salvador, Fortaleza, Belém and Recife, demand for benefits was greater and fiscal receipts weaker than in cities like Brasilia and São Paulo. A lower but locally more affordable benefit level would jeopardise the poverty reduction objective.¹⁶ Bolsa Familia's incorporation of Bolsa Escola at a national level addressed this problem and enabled benefit levels to rise significantly.

Benefit levels are not static; most countries adjust them for inflation on a regular basis, and sometimes other adjustments are made reflecting country circumstances.

When programmes impose labour supply or human capital investment conditionalities, the value of the benefit must be relatively greater, both to offset the cost of complying and to provide social protection. A programme that requires a child to attend school must take into account the age-specific direct and indirect costs of attendance – transportation, uniforms, supplies, school fees and any foregone labour income. A similar calculation applies to conditionalities involving health care.¹⁷

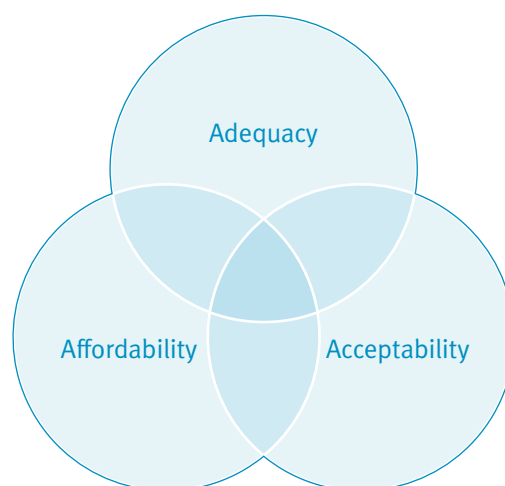


Figure 11.4 Balancing imperatives in designing a social protection programme

The existence of multiple objectives complicates the determination of the appropriate benefit level. Programmes aimed at poverty reduction require benefits that bring households up to the poverty line, while conditional transfers aimed at changing behaviour must focus on the opportunity cost of compliance, adjusted for the household's own preference for the imposed conditions.¹⁸ For example, the cost of sending a child to school (including foregone labour opportunities) might be the equivalent of US\$30. If the household is willing and able to allocate US\$10 to the child's education, a transfer of US\$20 should be sufficient to sway the balance and achieve the educational outcome.

There is no necessary conflict between poverty reduction and human capital development. An acceptable level for the poverty line should provide households with adequate resources to meet the conditions imposed by a reasonable social protection strategy. Transfers that raise household income to this level eradicate poverty and support human capital development.

In practice, countries demonstrate a broad range of methodologies and very different outcomes in setting benefit levels. The questions of "Who benefits?" and "What size of transfer is provided?" depend critically on each other – particularly when resources are limited. While social policy analysts pose rigorous methodologies for assessing basic needs, fiscal constraints and political considerations often render the analysis moot. Rarely are benefit levels sufficient to raise households to the poverty line – and when transfer amounts are substantial, they often attract new members to the household, exacerbating the problem of benefit dilution.

Given the beneficiary group and the size of the transfer, it is possible to

Box 11.2: Examples of answers to “What size of social transfer is provided?”

Programme	Benefits size (monthly)	How was the size determined?
Zambia’s Kalomo Pilot	ZMK 30,000 (US\$6), but ZMK 40,000 (US\$8) for households with children	Originally estimated to cover the cost of a meal a day. ZMK 30,000 was sufficient to purchase one 50 kilogram bag of maize (the main cereal). Raised to ZMK 40,000 for households with children based on participant feedback.
Brazil’s Old Age Pension	200 Reais in 2002 (US\$80)	Set equal to the Brazilian minimum wage. Brazil’s 1988 Constitution guaranteed rural workers the right to social security – and the social pension was increased from 50% of the minimum wage to 100%.
Lesotho’s Old Age Pension	M150 (US\$25)	The benefit was set equal to the official national poverty line for a single person. The amount is relatively low by the standards of non-contributory pensions in Southern African countries, but constrained by Lesotho’s limited fiscal resources.
Nepal’s Old Age Pension	150 Rupees (US\$2)	150 Rupees can buy approximately 10 kg of wheat or rice in Nepal. 150 Rupees is equivalent to 11% of the average citizen’s monthly income, or the wage for a little more than two days of agricultural labour. Adjustments are irregular and ad hoc.
South Africa’s Child Support Grant	R240 (US\$34)	A government-appointed commission recommended R75 per child per month – citing severe budget constraints. The Parliamentary committee responsible for social security overruled the recommendation and raised the initial amount to R100 (but the National Treasury did not increase the overall budget allocation). The grant was increased substantially in 2002 due to substantial food price inflation, and has been adjusted for inflation annually since then.

estimate the maximum amount the programme will cost by assuming (for analytical simplicity) the universal provision of benefits to the intended group.

Costing social transfer programmes

The cost of social transfer programmes depends on three key determinants:

- Coverage
- Benefit size
- Administration

The first of these two determinants are explicitly policy choices – the government determines the coverage of the programme by its decisions in terms of who will benefit from the programme, and the pace at which the implementing institution scales up delivery. The benefit size likewise is primarily determined at the policy level. Administration costs are not directly policy variables, but they are heavily influenced by policy choices in terms of targeting, conditionalities, payments mechanisms and other design features.

Box 11.3: Setting the size of the social transfer for public works projects in Malawi

A study commissioned by the Government of Malawi's National Safety Nets Unit together with the Malawi Social Action Fund (MASAF) analysed the wage-setting process for public works projects in the country. The study found that even very low wages were ineffective in rationing the limited number of public works jobs to the very poorest – and these low levels of transfers compromised the social protection offered by

the programme. Instead, the report recommends setting the size of the transfer to reflect the cost of living – approximately MK54 in 2004 compared to the revised public works wage rate of MK37. Because the higher wage rate would increase the attractiveness of public works employment, improved community targeting would be required.

SOURCE: McCord (2004).

The formula below illustrates a generalised method for estimating the cost of the proposed social transfer programme (Formula 11.1).

Formula 11.1: A generalised approach to estimating the cost of social transfers

$$\text{Cost} = (\text{Coverage} \times \text{Benefit size}) + \text{Administration}$$

For example, the annual cost will equal the number of people or households receiving the benefit (“coverage”) multiplied by the annual size of the social transfer (in money terms), plus the costs of administering the programme.

However, by specifying certain forms for the cost components, one can fairly easily estimate the cost of a proposed social transfer programme in terms of its required share of national income, as measured by Gross Domestic Product (Formula 11.2).

Formula 11.2: A simplified approach to estimating the cost of social transfers

$$\text{Cost (\% of GDP)} = \text{Coverage (\% of population)} \times \\ \text{Benefit size as a \% of per capita income} \times \\ \text{Administrative cost factor}$$

Most cross-country comparisons of social transfer programmes are expressed as a percentage of national income (GDP). For example, the cross-country comparisons in the preceding sections use this approach to present costs. This is useful because it expresses the cost in terms of its burden on the

Box 11.4: Financing national scale programmes: the example of universal categorical transfers

Person	Income	Benefit	Tax (25%)	Consumption
Themba	2400	6000	600	7800
Tholi	4000	6000	1000	9000
Thami	9600	6000	2400	13200
Zioni	80000	6000	20000	66000
Total		24000	24000	
Poverty	50%			0%
Inequality	33			8

NOTE: Inequality is measured as the ratio of the top quartile's welfare (income or consumption) to the bottom quartile's welfare. The poverty line is 5000.

overall national economy, which usually must finance the programme at scale in a sustainable manner.

The constituent components of cost are likewise intuitive and usually easy to estimate. The first is coverage, which is expressed as a percentage of the national population. For example, a benefit universally provided to all children under the age of five years might reach 7 per cent of the country's population. The second component is the benefit size, which in this approach is expressed as a percentage of *per capita* national income (GDP). For example, a child grant might be set equal to 10 per cent of *per capita* income. Finally, the administrative cost factor is set as a multiple of the total benefit cost. For example, the factor for a programme whose administrative costs are 15 per cent of the total benefits would be 1.15. In this case, the cost of the programme as a percentage of national income can be calculated as $0.07 \times 0.10 \times 1.15$, which is equal to 0.8 per cent of national income.

Financing universal transfers

Box 11.4 above illustrates the special case of a universal social transfer. A fixed benefit provided to each person regardless of socio-economic or poverty status will generally reduce both poverty and inequality as long as the financing of the programme is not too regressive. For example, the simple example in Box 11.4 shows that a fixed benefit financed with a proportional income tax can eliminate poverty and reduce inequality significantly. Such an instrument essentially shifts the "targeting" function from the social ministries to the government's tax revenue function. As long as the fiscal system can generate the required tax revenue, the combination of taxes and social transfers reduce poverty and inequality.

Endnotes

- 1 Social assistance includes non-contributory transfers to those deemed vulnerable or poor, while social insurance includes instruments that enable individuals to pool resources to provide support in the case of a shock to their livelihoods. For further discussion on these instruments and their role within social protection frameworks, see chapter 1.
- 2 Tanzi (1992).
- 3 Pal et al. (2005), DFID (2006a).
- 4 DFID (2005), Devereux et al. (2005), Samson et al. (2004).
- 5 Subbarao (2003), page 28.
- 6 For example, see World Bank (2005b).
- 7 Subbarao (2003), page 28.
- 8 The need for greater donor co-ordination was a major theme of discussion at the UNICEF/Wilton Park conference, November 2005. See UNICEF (2005) for greater details.
- 9 Devereux (2002b), page 4.
- 10 Subbarao (2003), page 28.
- 11 Barrientos and DeJong (2004), page 14.
- 12 De Janvry and Sadoulet (2005), page 2.
- 13 Samson et al. (2004). Research for the United Kingdom documents a similar effect. Banks and Brewer (2002) report that caregivers appear to target a minimum consumption level – so children in low-income households and those in slightly higher-income households receive similar levels of resources, even if parents in the lower-income households must go without essentials, even regularly skipping meals. Money spent on extremely poor households will tend to go disproportionately to children – but once that minimum threshold is met, resources are more broadly shared.
- 14 McCord (2004) demonstrates that a public works transfer amount that was less than the proposed Basic Income Grant amount provided a substantial positive impact on household well-being, challenging the assertion that a transfer of R100 would not be significant.
- 15 Foundation for Assistance International and CASE Kyrgyzstan (2003), pages 9–10; Barrientos and DeJong (2004), page 13.
- 16 Sedlacek et al. (2000), pages 18–19.
- 17 Barrientos and DeJong (2004), page 29.
- 18 Sedlacek et al. (2000), page 18.

