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Free money

Here's an idea for foreign aid: Just hand over the cash

By Drake Bennett | July 18, 2010

There are all sorts of things very poor people living in poor countries don't have. They lack secondary-school educations, usually, and good medical care. They lack steady work and life insurance, bank accounts and competent legal representation, adequate fertilizer for their crops, adequate protein in their diets, reliable electricity, clean water, indoor plumbing, low-interest loans, incubators for their premature babies, vaccinations and good schools for their children.

But the central thing they lack is money. That is what makes them, by definition, poor: International aid organizations define the "very poor" as those who live on less than a dollar a day. Despite this, the global fight that governments and nongovernmental organizations have waged against poverty in the developing world has focused almost entirely on changing the conditions in which the poor live, through dams and bridges and other massive infrastructure projects to bring commerce and electricity to the countryside, or the construction and staffing of schools and clinics, or subsidizing fertilizer and medicine, or giving away mosquito nets or cheap portable water filters.

In the last decade, however, the governments of the nations where most of the world's poorest actually live have begun to turn to an idea that seems radical in its simplicity: Solve poverty and spur development by simply giving out money. In Brazil and Mexico, India, China, South Africa, and dozens of other nations, hundreds of millions of poor people are now receiving billions of dollars in cash grants. The programs vary widely, but typically the money — disbursed through banks, post offices, state lottery offices, and even, in rural Africa, ranging armored cars with ATMs on them — goes directly to the poor, rather than being spent on particular projects by government or international aid officials.

The regular infusions of cash augment the paltry budgets of poor households, alleviating the pinch of deprivation, but proponents also see them as a long-term path out of poverty, and even a catalyst for economic growth. Research has credited cash transfers with improving the health and education of poor children, and there is also evidence that cash transfers nurture microenterprises, improve crop yields, and allow the poor to begin to save and invest. On a broader scale, some development experts argue that giving the poor more money to spend expands consumption and markets, and can boost local and national economies. Cash transfers don't just lift people out of poverty, in other words, they lift entire countries as well. In the process, they may render superfluous large swaths of today's aid industry.

"Cash transfers are a major success story in development in the last 10 to 15 years," says Francisco Ferreira, a World Bank economist who helped design Brazil's transfer program, Bolsa Familia. "They've spread incredibly fast from relatively modest beginnings in Bangladesh and Brazil."

Still, many economists and development experts emphasize that cash transfers are only a limited part of what developing nations need to do to actually develop — giving a family money it can spend on fertilizer or school books or medication can only do so much if the schools and clinics are understaffed and the roads to get crops to markets are impassable.

More fundamentally, cash transfers have triggered a discussion about the extent to which the poor can be relied upon to wisely spend money — theirs and the government's. The oldest and most closely studied of the cash-transfer programs, in Mexico and Brazil, attach requirements to the money: Eligibility is conditioned on family members going for regular preventive health checkups, or enrolling their children in school. Other programs, however, like South Africa and Bolivia's pension and child-support grants, simply give out the money with no strings attached.

The debate over whether to attach conditions, or whether to give the money at all, is taking place even as images of the devastation in Haiti — and the chronic and extreme poverty that exacerbated it — are still fresh in the minds of the American public. At the same time, economists and other development experts are beginning to examine just how the world's poorest people actually spend their money. What they're finding is that, because the stakes are so high, the very poor are often quite financially savvy. For the staunchest supporters of cash transfers, it's more evidence that just giving the poor money is, dollar for dollar, among the best uses for aid.

“We’re arguing, basically, that poor people are poor because they don’t have money. It’s not that they’re stupid or need education. They actually know what to do with the money,” says Joseph Hanlon, a development expert at England’s Open University and coauthor of a new book on cash transfers entitled “Just Give Money to the Poor.” “You can’t pull yourself up by your bootstraps if you don’t have boots, and cash transfers are providing boots.”

Cash transfers are new in the context of international aid, but in certain forms they are as old as the modern state. Pensions, after all, are a cash transfer. And while we’re accustomed to thinking of pensions as relative luxuries that wealthy nations can provide for their citizens, economic historians argue that, in many cases, they have served as precursors of economic growth and development. The sociologist Samuel Valenzuela, in work Hanlon and his coauthors cite in their book, compares Chile and Sweden, two countries that at the beginning of the 20th century were identical in terms of population, natural resources, and development. Sweden instituted pensions and universal health care, Chile did not, and as a result, Valenzuela argues, the growth in Sweden’s gross domestic product per capita since then has far outpaced Chile’s.

One of the most prominent proponents of direct cash transfers as a poverty-fighting measure was none other than Milton Friedman, father of the neoclassical Chicago school of economics. In 1962, Friedman proposed replacing all government welfare programs in the United States with what he called a “negative income tax,” a cash handout indexed to income. (Today’s earned income tax credit grows out of the idea, though it is conditional, only going to people with jobs.)

The turn toward cash transfer programs in poorer nations builds off this history, but it also grows out of frustration at decades’ worth of failed development strategies. In the 1980s and 1990s, for example, organizations like the World Bank pressured developing countries to trim social benefits to help balance their budgets. Whether these policies brought growth and stability remains a deeply contested question, but they certainly did little to improve the lot of those nations’ poorest. At the same time, economists were finding that the billions of dollars being spent on aid — whether it was to build clinics or fly in food — were having little appreciable effect on poverty, even when the money wasn’t pocketed by corrupt government officials.

“There was a real discouragement with many of the things we had tried that didn’t seem to work, and a real appetite for experimentation,” says Norbert Schady, an economist at the Inter-American Development Bank and coauthor of a recent World Bank book on cash transfers.

The cash transfer programs spawned by that frustration were instituted not by first-world development agencies but by developing nation governments themselves. Brazil and Mexico started their programs in the late 1990s. Mexico’s, called Progresa, initially targeted 300,000 families; renamed Oportunidades by President Vicente Fox in 2002, it now reaches nearly a quarter of the country’s population. The average cash grant is $38 per household per month, more than a quarter of the average household income of the rural poor, and the total cost of the program runs to 0.3 percent of gross domestic product. There are no restrictions on how the money can be spent, but eligibility is contingent on a set of conditions: children’s enrollment in school, mothers’ regular visits to health clinics with their children, attending talks on health and nutrition, and participating in communal labor projects.

Bolsa Familia in Brazil also reaches roughly a quarter of the country’s population, some 50 million people. Eligibility is linked to income, with poor households receiving a family grant of just over $30 a month, with additional grants for each child. As in Mexico, families are required to take their children to health clinics and enroll them in school, though failing to do so doesn’t result in disqualification as it does in Mexico, but instead triggers a visit from a social worker.

In countries like South Africa and Bolivia, the grant takes a different form: a noncontributory pension, given with no strings attached (South Africa also has an unconditional child support grant). The pensions bring a measure of security to the lives of the nations’ elderly citizens, and in countries where three or even four generations often live under one roof, it also gives a significant boost to a household’s pot of money. Pensions have been found, for example, to lead to an increase in school attendance — with more money, households can forgo the income of a working child and instead send him or her to school. In Bolivia, farmers using their pension to buy fertilizer were able to increase household consumption by an amount double that of the pension.

There is a growing consensus that cash transfer programs can effect dramatic short-term changes at the level of the household. Progresa/Oportunidades and Bolsa Familia in particular have been carefully studied: The households receiving the grants were compared with otherwise identical households without them as the programs were rolled out. In both cases, the findings have been dramatic: Children in households receiving the grants were better fed, healthier, even taller (a sign of better nutrition). They were more likely to attend school and more likely to stay in school up through high school. Studies of cash grants in Ecuador and Nicaragua that Schady of the Inter-American Development Bank did with other economists found that the grants modestly boosted children’s cognitive development as well. Kids in grant households had a larger vocabulary, better short- and long-term memory, and were better behaved.

The grants also seem to bring a measure of gender equality to previously male-dominated households. In most countries, the grants are given to women — they are the primary guardians of the children, and grant officials see them as more likely to spend the money on household necessities — giving them control of a family's purse strings.

The broader question, though, is whether the programs can truly break intergenerational cycles of poverty, not only mitigating the lives of the poor, but lifting them out of poverty altogether. The focus on children in many transfer programs is an attempt to do this, by narrowing the gaps in health and education that make climbing into the middle class so much harder for poor children.

There is evidence that the grant money is being put to long-term use. Studies have found that, while the grants are mostly spent on better food and child-related expenses, many households do manage to set aside a portion to save or invest or seed a micro-enterprise. Researchers looking at Oportunidades found that recipients tended to regularly put some of the cash into assets like working animals to improve the productivity of their farms, fabric to make textiles to sell, or tools or machinery for carpentry or repair businesses. Having a reliable, regular source of extra income unleashed the inner entrepreneur in many of the recipients.

Proponents like Hanlon, and his coauthors Armando Barrientos and David Hulme of England's University of Manchester, argue that cash transfers can also grow economies. They point to a 2009 study of Bolsa Familia that found that the program stimulated the national economy. By putting money in the pockets of millions of the poor, it juiced the demand for goods and services and created jobs nationwide.

Simone Cecchini, an economist at the United Nations Economic Commission for Latin America and the Caribbean, makes a similar point. "In some rural areas, where there was not much circulation of cash, we see a sort of multiplier effect, with small businesses benefiting from the money and generating more income."

But even among the architects of cash transfer programs, there is caution about claiming too much for the programs. A pilot program in New York City modeled on Oportunidades was shut down earlier this year when the results were disappointing. Even the oldest of the programs are barely more than a dozen years old, not enough time to see whether they can effect intergenerational change. And some of the research on longer-term effects has been inconclusive: More children are in school thanks to cash transfer programs, but it's been hard to show that the students are benefiting from the additional schooling.

"There's less evidence of impact on the final objectives: Do [the children] learn more in schools, is their health care really better over time, that sort of thing," says Ferreira.

And while a great part of the appeal of cash transfer programs is their simplicity and resulting lack of bureaucracy — simply handing out money is much easier than allocating the right medications to the ill or targeting subsidies to the particular farmers who need them — it's also true that significantly supplementing the income of a nation's poor can get expensive. Dean Karlan, a Yale University development economist, suggests that there may be even simpler, cheaper ways to achieve some of the individual ends of cash transfer programs. For example, work by the economists Michael Kremer and Edward Miguel suggests that, in rural areas in poor countries, deworming children is the most cost-effective way to improve school attendance — the children miss fewer days out sick.

Regardless of the final verdict on these macro claims, however, the success of these programs has shown development economists something they didn't necessarily expect: that very poor people are, by and large, careful shepherds of money, and giving them more of it is not a recipe for indolence, debauchery, and waste. And though the biggest cash transfer programs are conditional ones, among development experts today there is widespread agreement that the conditions themselves are not the key to the programs' success.

Poor people, like rich people, do fall victim to biases, both inborn (like privileging today's spending over tomorrow's) and cultural (undervaluing, in some parts of the world, the future payoff of educating daughters). Cash-transfer programs have shown, however, that most of the time poor people freely choose to do the very things with their money that the architects of conditional cash transfer programs are trying to pressure them to do. Hanlon points to the fact that school attendance among poor households went up more in South Africa, where the cash transfer was unconditional, than in Mexico, where school attendance was a condition of the grant.

Jonathan Morduch, an economist at New York University, is coauthor of the book "Portfolios of the Poor," an in-depth look at how the world's poorest actually manage their financial lives. "By and large they're doing smart things with their money, they're thinking hard about how to best spend it, whether, for example, to keep a kid in school or put the money into their business, that sort of thing," he says.

These are very difficult decisions, of course, where small sums can have life-altering ramifications. That difficulty helps explain the care with which those choices are usually made — and the dramatic effects that providing a little financial breathing room can provide.

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