2 WHY SOCIAL TRANSFERS: THE ECONOMIC CASE

Introduction

This brief puts forward the socio-economic case for investing in social transfers. It highlights the benefits of predictable social transfers as a policy instrument to deal with poverty, risk, vulnerability and food insecurity.

Southern African countries are characterised by pervasive poverty, low life expectancy, weak economic growth and highly skewed wealth distribution (see table). There is increasing evidence that predictable cash transfers not only reduce poverty amongst direct beneficiaries and their households, and improve wealth distribution, but also that they generate economic growth within local communities and beyond. This makes them an attractive policy instrument, not only to Ministries of Social Welfare but also to traditionally sceptical Ministries of Finance and Economic Development.

There are four main socio-economic impacts of predictable social transfers:

- **Reducing poverty**
- **Promoting equity**
- **Stimulating growth**
- **Conserving fiscal resources**

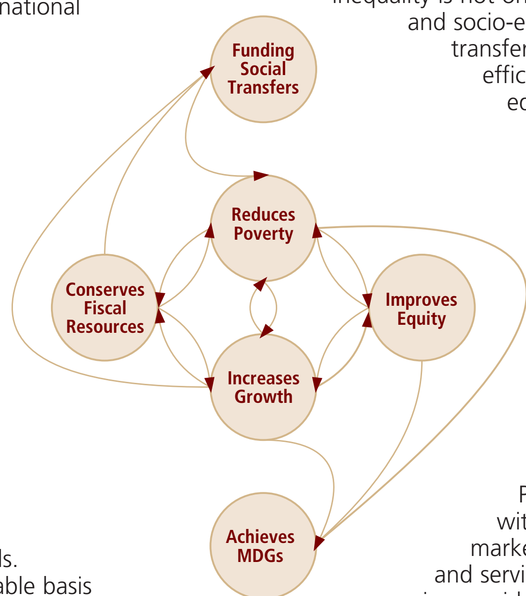
Taken together, these impacts can translate into substantial improvements in the living standards of the poor and most vulnerable, at the same time as generating national economic growth.

Reducing poverty

The direct aim of social transfers is to reduce poverty through the provision of social assistance to the poor. Bearing in mind the pervasiveness and severity of poverty, a comprehensive programme which distributes even a relatively small transfer can have a significant impact on the well being of the beneficiaries and the prevalence of poverty within the country.

But predictable social transfers provide more than simple welfare to the poor. Evidence shows that beneficiaries use social transfers for a range of purposes beyond meeting their immediate consumption needs. Transfers provided on a regular and predictable basis allow beneficiaries to manage risk better. They reduce beneficiaries' vulnerability to shocks and their need to resort to the sale of assets. They also enable them to make investments, however small, that can improve their livelihoods and extricate them from the cycle of poverty.

In **South Africa**, social transfers have reduced the poverty gap (i.e. the extent to which poor people fall below the national poverty line) by 47 percent. In **Mauritius**, the old age pension has reduced the proportion of households living below the poverty line from thirty percent to six percent. In **Tanzania**, the International Labour Organisation estimates that a universal benefit for school age children (between seven and fourteen years) would reduce the number of people living below the poverty line by one third. In **Swaziland**, the elderly are major carers for orphans and vulnerable children: apart from helping to feed the household, the universal, non-contributory old age grant is used for a range of other purposes including helping children to access health and education services.



Human Development Indicators (source: HDI2006, UNDP)

Country	% of population living <$1/day	Gini coefficient	Life expectancy at birth (years)	HIV prevalence (% 15 to 49 yrs)	<5 mortality (per 1000 live births)	Per capita GDP annual growth (%)
Lesotho	36.4	63.2	35.2	23.2	82	4.5
Malawi	41.7	50.3	39.6	14.1	175	0.9
Mozambique	37.8	39.6	41.6	16.1	152	4.2
Swaziland	--	60.9	31.3	33.4	156	2.1
Zambia	75.8	42.1	37.7	17.0	182	-1.1
Zimbabwe	56.1	50.1	36.6	20.1	129	-1.9

Promoting equity

Data from the **South African** 2000 Income and Expenditure Survey indicate that a full uptake of the state old age pension, disability grant, and child support grant would reduce the Gini coefficient (an indicator of the severity of income inequality in a country) from 63% to 60%.

Most southern African states rank high in the global league table of countries having the worst income distributions. Income inequality is not only socially unjust but it also leads to political and socio-economic instability. Properly designed social transfer programmes redistribute wealth in a highly efficient manner, thus promoting a more equitable distribution of income, especially when they are linked to progressive taxation policies.

Stimulating growth

Poor economic growth is one of the main underlying causes of poverty and hunger. Predictable social transfers can provide a stimulus for economic growth which creates employment, raises incomes and thus creates a virtuous cycle of poverty reduction.

Predictable cash transfers enable households with low purchasing power to engage in local market activity. Increased local demand for goods and services in turn stimulates local producers and service providers to increase production and employ more people. Furthermore, the greater purchasing power in remote rural areas holds the potential to revitalise local economies. This local market 'multiplier' effect can revitalise local economies even in remote rural areas. Replicated across the country, it can become an engine for wider economic growth.

The relatively small value of individual benefits and the fact that social transfers are disbursed on a regular basis (usually monthly) helps to ensure that such instruments do not generate inflation (although this may be a risk where there are severe market supply problems). After all, developed countries disburse far more substantial sums in social benefits without stimulating inflation.

Predictable social transfers shift spending power from upper income groups to the poor. If the poor spend more on labour intensive goods, this redistributive effect may increase the demand for labour, promoting job creation. Further benefits to local economies arise because the poor are more likely to spend on domestically-produced rather than imported goods.

A study of the local market impact of Concern Worldwide's **Dowa Emergency Cash Transfer** (DECT) programme in **Malawi** in January 2007 used a social accounting matrix method to track the knock-on effects of increased expenditure by DECT's direct beneficiaries. The study estimated a regional multiplier effect of between 2.00 and 2.79 – in other words DECT resulted in a total increase in income in the local economy of at least twice the value of the cash transferred by the programme. Apart from direct beneficiaries themselves, the main groups benefiting from this increased income were local traders, other households which received gifts from beneficiaries or benefited from a rise in local casual wage rates, and local clinics and schools since part of the money was spent on health and education. Schools in the area reported improvements in enrolment and drop-out rates which they attributed to DECT.

Conserving fiscal resources

Predictable social transfers also conserve fiscal resources in important ways: the infant whose nutrition was funded by a social transfer will grow into a school-age child better able to learn and more likely to succeed in school. Fewer fiscal resources will be wasted on children who have to repeat grades they otherwise would have passed. The child will grow into an adult more likely to find work and pay taxes. The worker will grow older with a lower chance of contracting a chronic debilitating disease (such as diabetes which is a severe problem in southern Africa), and so will be less likely to burden unnecessarily the public health care system.

In **South Africa**, households including women eligible for the old age pension reported significantly better weight-for-height indicators for girls. In **Lesotho**, fifty percent of pension recipients spend more on health services since the implementation of the pension. Sixty percent of the pensioners live in households containing young people attending school or college. A significant number of these dependent children have been orphaned by HIV/AIDS. Pensioners are buying uniforms, books and stationery. Approximately 10 000 school children nationally are getting some educational support from the pension money.

Promotion of the Millennium Development Goals

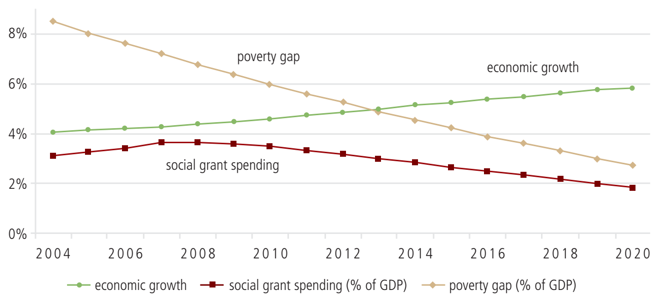
The Millennium Development Goals (MDGs) provide measurable goals for the improvement of living standards for hundreds of millions of people in the developing world by 2015. Conventional socio-economic policies have failed to put Africa on the path towards achieving the MDGs. To date Africa has registered the least progress and has even suffered reversals in some crucial areas. In sub-Saharan Africa (SSA), the number of people living in extreme poverty (on US$1 a day or less) rose from 217 million in 1990 to 290 million in 2000, with the majority of these being women. Evidence suggests that adult life expectancy has declined from over 50 years to 46 years.

Social transfers are an effective weapon in the armoury of policy–makers in their attempts to attain the MDGs. In addition to improving the incomes of the poorest households, evidence shows that social transfers have other broader impacts on the quality of life of these households, and thereby contribute to the achievement of a broader spectrum of MDGs in areas such as health, education and gender equality.

MDG 3 is the promotion of gender equality in primary and secondary school enrolment. Social transfers can help achieve this objective directly and indirectly. They do so directly by increasing household income available for education. Traditionally, in a low income household, resources available for schooling will be spent preferentially on boys. Social transfers increase household income, improving the chances of girls receiving education. The indirect effect works through the nutrition outcomes of social transfers. Healthier girls will be better able to cope with school and to complete their primary and secondary education.

Modelling the economic and poverty impact of social transfers

The impact at national level of investing in predictable social transfers can be assessed using a macro-simulation model. This model analyses the inter-relationships between spending on social transfers, economic growth and the poverty gap, as well as other variables. The graph below shows the outcome of such a model based on expected levels of social transfer spending in South Africa up to 2020. Social transfers produce long-term developmental effects by improving nutrition, health, education, labour productivity and social stability. The long-term effect is cumulative - an investment this year generates benefits over a multi-year horizon. The scenario depicted in the graph shows the impact of social transfer spending and economic growth on the size of the poverty gap and how the required level of social transfer spending can be reduced as the size of the poverty gap decreases.



Source: Economic Policy Research Institute (EPRI)

In conclusion

At the **household** level, predictable social transfers provide more than just welfare and can positively improve the livelihoods of the poor. They can also increase access of household members to education and health facilities, which have long term benefits. At **community** level, predictable social transfers generate demand for goods and services, stimulate markets, create employment and foster growth. At **national** level, broad-based, comprehensive social transfers reduce poverty and inequality, create growth, support social and political stability, and directly promote the achievement of a range of MDG indicators. Their fiscal impact, in generating economic growth, means that they are ultimately more affordable than a continuous series of short term ad hoc transfers.

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