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Show Them the Money: Why Giving Cash Helps Alleviate Poverty

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Abstract (summary)

New research suggests that cash grants to the poor are as good as or better than many traditional forms of aid when it comes to reducing poverty. Study after study has shown that recipients of cash grants invest the money or spend it on such basic items as food and better shelter. Poor people don't always make the best choices with their money, of course, but fears that they consistently waste it are simply not borne out in the available data. In some ways, the new research on cash transfers actually affirms the wisdom of traditional approaches to development assistance. This abundance of data suggests that people are poor not because they lack initiative but because they lack resources and opportunities -- things that, in many places, money can buy. Despite everything that cash transfers can do, their future role in poverty alleviation remains uncertain. The effectiveness of cash-transfer programs are only partly proven, and many unknowns and risks remain.

Full Text

Every year, wealthy countries spend billions of dollars to help the world's poor, paying for cows, goats, seeds, beans, text- books, business training, microloans, and much more. Such aid is designed to give poor people things they can't afford or the tools and skills to earn more. Much of this aid undoubtedly works. But even when assistance programs accomplish things, they often do so in a tremendously expensive and inefficient way. Part of this is due to overhead, but overhead costs get far more attention than they deserve. More worrisome is the actual price of procuring and giving away goats, textbooks, sacks of beans, and the like.

Most development agencies either fail to track their costs precisely or keep their accounting books confidential, but a number of candid organizations have opened themselves up to scrutiny. Their experi- ences suggest that delivering stuff to the poor is a lot more expensive than one might expect.

Take cows. Many Western organizations give poor families live- stock, along with training in how to raise and profit from the animals. Cows themselves usually cost no more than a few hundred dollars each, but delivering them--targeting recipients, administering the donations, transporting the animals--gets expensive. In West Bengal, India, for example, the nonprofit Bandhan spends \$331 to get \$166 worth of local livestock and other assets to the poor, according to a report by the rating agency Micro-Credit Ratings International. Yet even this program sounds like a bargain compared to others. In Rwanda, a study led by the economist Rosemary Rawlins found that the cost of donating a pregnant cow, with attendant training classes and support services, through the charity Heifer International can reach \$3,000.

Such programs surely reduce poverty: having a cow is undoubtedly better than not having one. But they also carry an opportunity cost, since the money spent on procuring and delivering the cows or other assets could instead go directly to the poor. Bandhan, for example, could give twice as many households cash grants equal to the local price of the livestock it now gives as it does actual livestock. And in place of each cow it provides, Heifer could give \$300--roughly half of Rwanda's per capita income--to ten poor families.

Does the benefit of an in-kind donation to one family really outweigh the value of helping twice or even ten times as many households? For a growing number of antipoverty programs, the answer to that question appears to be no. New research suggests that cash grants to the poor are as good as or better than many traditional forms of aid when it comes to reducing poverty. The process of transferring cash, moreover, is only getting cheaper, thanks to the spread of technologies such as cell phones and satellite sig- nals. And simply asking whether a given program is doing more good than it costs puts pressure on the aid sector to be more trans- parent and accountable. It's well past time, then, for donors to stop thinking of unconditional cash payments as an oddball policy and start seeing them for what they are: one of the most sensible tools of poverty alleviation.

MONEY MATTERS

When it comes to deciding how to help the poor, the stakes couldn't be higher. Each year, U.S. households donate at least \$15 billion abroad. Their government gives \$30 billion in foreign aid, and wealthy states collectively give \$150 billion in development aid. Yet the world's poorest people receive very little of that money in actual cash.

"Just give the poor cash" is an old refrain. What is new, however, is a burgeoning body of experimental evidence, produced by groups ranging from the nonprofit Innovations for Poverty Action to the World Bank, on how the effect of cash grants compares to that of in-kind donations. Recent studies have come to surprising conclusions, finding that typically lauded approaches to reducing poverty, such as educational and loan programs, are not so effective after all.

One of the best examples is microloans, small, short-term loans to poor entrepreneurs. By opening up credit to people who were too poor to borrow from banks, the logic went, microfinance would give the poor the jump-start they needed to escape their plight. Beginning in the 1990s, the microcredit movement took the development world by storm, leading to a Nobel Peace Prize for the Bangladesh-based Grameen Bank in 2006.

Yet a belated series of randomized trials has called the success of microloans into question. One example comes from the Indian non-profit Spandana. Beginning in 2005, the group made loans of about \$250 to hundreds of women in Hyderabad, India, at relatively low interest rates. The MIT economist Abhijit Banerjee and a number of collaborators worked with Spandana to evaluate the program's performance over three years; they found no effect on education, health, poverty, or women's empowerment. To be sure, people certainly benefit from access to credit; it helps them cope with crises and buy expensive things such as new roofs or farm equipment and pay for them over time. But as Banerjee concluded after reviewing an additional two decades' worth of data on such loans, "there is no evidence of large sustained consumption or income gains as a result of access to microcredit."

Another popular approach to development aid has been business and vocational training. There is little data on how much aid spending goes to training, but as an example, the International Labor Organization's Start and Improve Your Business Program claims to have trained more than 4.5 million people in over 100 countries since 1977. "Teach a man to fish and you feed him for a lifetime," the proverb goes. Yet the results of teaching anything—be it fishing or farming or word processing—have been patchy at best. In 2012, the economists David McKenzie and Christopher Woodruff reviewed more than a dozen randomized trials in developing countries and concluded that training business owners had little lasting effect on their sales or profits.

No wonder people in developing countries, when given the choice, don't necessarily choose to invest in skills training. In another recent study, one of us (Christopher Blattman) worked with the economists Nathan Fiala and Sebastian Martinez to examine a government-run training program in Uganda. Rather than simply providing classes in various trades, the initiative gave grants of around \$7,000 to over 250 groups of 15–25 young adults (roughly \$400 per group member) in return for a simple business plan describing how they would use the money to buy vocational training and tools. The groups were otherwise free to spend the money without oversight. The majority of the participants ended up using the funding to enter skilled trades such as tailoring or metalworking. But they spent most of the money acquiring the physical tools and materials they needed to start working, allocating only around ten percent of the grants to training. That turned out to be a wise investment decision: over four years, the participants' incomes rose by an average of roughly 40 percent.

None of this is to say that existing practices should be tossed aside. But they can certainly be improved. With microfinance, for example, finding ways of lending larger sums for longer periods at lower rates would surely make many businesses more sustainable and profitable. The key point, however, is that new data are challenging the conventional wisdom that has long dictated how billions in development dollars are spent. Simply having a plausible theory of change doesn't cut it anymore. These days, it's about providing evidence of change—especially change that justifies the price of bringing it

DON'T HAVE A COW, MAN

Over the past few years, it has become increasingly clear that giving away money works in a wide range of development situations. Mexican families, Ghanaian farmers, Kenyan villagers, Malawian schoolgirls, and war-affected Ugandans—all have been shown in randomized trials to benefit from cash transfers. Economists have studied money transfers with conditions and without conditions, under supervision and not under supervision, on large scales and small scales, and against comparable loans. And by testing the effects of handouts over unusually long periods of time—five years out in Sri Lanka, four years out in Uganda—scholars have had access to far more detailed data than is available for many other poverty-reduction strategies.

These findings are particularly important because many funders, including governments, aid organizations, and development professionals, still harbor significant reservations about cash transfers. They raise a variety of familiar concerns: that men drink their cash away, that the diligent but uneducated poor struggle to make sound decisions, and that handouts make people ever more dependent on aid. So far, however, the data contradict the most pessimistic of these worries.

Studies have shown that the world's poorest people do not squander cash transfers, even when there are no strings attached. An extreme example comes from a recent experiment run by one of us (Blattman), Julian Jamison, and Margaret Sheridan. In 2010–13, we gave unconditional grants of \$200 to some of the least disciplined men to be found: drug addicts and petty criminals in the slums of Liberia. Bucking expectations, these recipients did not waste the money, instead spending the majority of the funds on basic necessities or starting their own businesses. If these men didn't throw away free money, who would?

That finding echoes similar results elsewhere. Study after study has shown that recipients of cash grants invest the money or spend it on such basic items as food and better shelter. Poor people don't always make the best choices with their money, of course, but fears that they consistently waste it are simply not borne out in the available data.

Nor is there evidence that unconditional cash transfers make recipients lazy. Especially for poor people who have not fulfilled their potential, such as small-business owners or underemployed youth with little access to hard capital, cash grants have frequently created wealth. Using such donations, entrepreneurs in Ghana and Sri Lanka have expanded their businesses, displaced women in Uganda have become traders and doubled their earnings, and farmers in Kenya have made home investments with high returns. In most of these experiments, people increased their future earning potential over the long term. In some cases, they did not. But in every study, people worked at least as many hours in the labor force as they had before receiving the cash transfers, if not more.

In some ways, the new research on cash transfers actually affirms the wisdom of traditional approaches to development assistance. Poor people in developing countries often use the cash given them to buy the same things that aid organizations have traditionally provided—livestock, tools, training, and so on. No one living on less than \$2 a day says no to a free cow, even if he is not cut out to be a dairy farmer. But the advantage of cash is its flexibility. When people have cash in hand, they tend to buy a wider variety of goods and services. Not everyone, after all, wants a cow.

THE FUTURE OF GIVING

This abundance of data suggests that people are poor not because they lack initiative but because they lack resources and opportunities—things that, in many places, money can buy. Donors should thus ask themselves: With each dollar we spend, are we doing more good than the poor could do on their own with the same dollar?

In 2010–11, the Association of Volunteers in International Service, a Catholic development organization, did just that, evaluating an ongoing program in postwar northern Uganda in real time. To help 1,800 of the country's poorest women become retailers and traders, the program had been providing each woman with a grant of \$150, five days of business planning assistance and training, and follow-up visits from aid workers who offered supervision and advice. Altogether, the program cost nearly \$700 for every impoverished woman it assisted. The organization, working with a team of researchers that included one of us (Blattman), decided to measure the impact of the program without its most expensive service: the follow-up visits. We found that such visits did increase the women's profits yet cost more than twice the amount of the cash grant itself. In other words, the follow-up was far less effective per dollar than the grant and the training course.

One potential response would have been to cut the follow-up service and give out larger cash grants. But in this case, the organization plans to find a way to provide the extra services more cheaply. This will prove a high bar to meet, but either way, the end result will be that it gets more bang for its buck.

The Ugandan example illustrates another upside to cash transfers: they can serve as the index funds of international development. An index fund is a bundle of investments that is not actively managed, reducing the costs for investors. Its value simply reflects the upward and downward swings of the individual stocks that are included in the bundle. Similarly, a cash transfer is a development project stripped of any active management costs, and its performance tracks the success or failure of the individual recipient. Cash transfers thus provide a baseline for evaluating the active management performance of government officials and development professionals. Unfortunately, the sort of hard-nosed performance review seen in the Ugandan study—let alone the courage and discipline required for any organization to put its core competencies to the test—remains rare.

Still, the studies so far, plus basic economic reasoning, suggest three predictions about how cash will perform relative to traditional aid programs. First, money transfers will likely prove most valuable in places where the population has been hit hard by unexpected crises—countries or regions recovering from violent conflicts, natural disasters, or extended periods of political uncertainty. Think of Southeast Asia after a tsunami or the Middle East flooded with Syrian refugees, where the returns on capital after a recovery period are likely to be unusually high and the challenge of making smart investments without localized knowledge unusually large.

Second, cash could also excel in places such as Ghana, Kenya, or Uganda—reasonably stable, growing countries that happen to have few firms offering jobs and where most workers, by necessity, are self-employed. Here, many of the poor are working below their potential because they lack the capital, credit, or insurance products necessary to grow their businesses. In the absence of financial services, which can take decades to develop, cash can fill the gap.

Third, the forms of aid most likely to outperform cash will be those that address collective problems, or what economists term "public goods." Consider health, for example. Say you were buying a vaccine to reduce your child's risk of getting sick. A big part of the social value of this purchase would be reducing your neighbors' risk of illness, too. If you had little cash to spare, the vaccine might cost more than it was worth to you but less than it was worth to the community at large. In this case, an outside group would be better placed to tend to the greater good by subsidizing the vaccine or even providing it for free. A cash transfer wouldn't solve the social problem if the recipient had more pressing needs to spend the money on than the vaccine.

In many cases, however, Western officials and organizations are not the best judges of what poor people in developing countries need to make a better living; the poor people themselves are. One of us (Paul Niehaus), working with fellow economists Karthik Muralidharan and Sandip Sukhtankar, is currently conducting an unusual poll in rural Bihar, India. We are giving poor citizens a choice between two types of aid: the assistance provided by the government's Public Distribution System, a venerable program of subsidized food delivery that consumes nearly one percent of India's GDP, or cash transfers, calibrated to cost the government the same amount per family. Both forms of welfare have their advantages. Direct cash transfers bypass corrupt officials and crafty middlemen, whereas food transfers provide a more reliable form of insurance against rising food prices. The results are not yet in, but the experiment should provide a promising model for determining how to spend aid dollars in the future.

Such exercises have their limitations, of course, but they also have the advantage of linking smart policy with smart politics. Offering citizens their choice of programs gives elected officials the kind of insight they crave: raw data that describe what voters want and whether or not the civil service is delivering it. Like cash transfers themselves, such mechanisms can help make aid delivery more accountable to the people the aid is intended to serve.

CASHING IN

Despite everything that cash transfers can do, their future role in poverty alleviation remains uncertain. The findings of small-scale experiments, involving just a few thousand recipients, cannot reliably tell what might happen when the same policies are rolled out to millions. One looming question is whether money transfers are more or less feasible on a large scale than traditional programs—whether, for example, corrupt officials and armed groups could exploit such programs more easily.

But the evidence from countries that already use cash transfers on a massive scale is promising. According to the United Kingdom's Department for International Development, governments in the developing world already run cash-transfer programs that reach between 750 million and one billion people, whether by way of employment programs in India, pension funds in South Africa, or welfare schemes in Brazil. Many of these programs involve some kind of condition that must be met before recipients get paid, such as getting a checkup or a vaccine at a health clinic. But they all end in cash transfers. The worst fears surrounding them—of fraud, corruption, and plain ineffectiveness—have thus far not been realized.

New technologies have also made such programs easier to implement. In India, one of us (Niehaus), along with Muralidharan and Sukhtankar, recently worked with the government of the state of Andhra Pradesh to measure the effects of replacing paper money delivered through the mail to pensioners and workfare participants with digital payments using biometric authentication. We found that the new system both reduced theft and improved the speed and reliability of the payments. Taking this approach further, the non-profit GiveDirectly (of which Niehaus is president) now delivers unconditional cash payments to thousands of extremely poor households in East Africa through accounts on their cell phones, all at a cost of less than ten cents per dollar donated.

Another concern about rolling out cash transfers on a large scale in developing economies is that an influx of money could lead to disruptive inflation. Whether that fear will materialize remains unclear. It will depend in large part on what the macroeconomic effects of cash transfers are compared to—whether food aid, universal education, or other goods and services. Any large-scale influx of goods or currency has the potential to be disruptive, and so the real question is whether giving cash is worse than giving something else.

Economic theory and experience provide some reassurance. Consider the hundreds of thousands of Syrian refugees now living in Lebanon, where the United Nations and humanitarian agencies are dispensing cash via ATM cards as the main form of relief. In such open economies, cash should have little effect on food prices or supplies, and it could even stimulate local production. But when it comes to goods that are slow to keep up with demand—electricity or rental housing, for example—prices are rising and supplies are dwindling. However troublesome the shortages, though, there are few better or more efficient options for helping the refugees buy basic necessities.

To be sure, cash is no panacea. Not every person will grow his or her income or business with a grant; some recipients will use all the money to pay for immediate needs. The effectiveness of cash-transfer programs are only partly proven, and many unknowns and risks remain. But the evidence is stacking up faster in favor of cash than it is for a lot of the alternatives, and direct cash transfers deserve to shed their reputation of being eccentric. Just as important, donors and the public must hold charitable organizations accountable for the wasteful expenses they regularly incur. The expansion of cash-transfer programs themselves could do the most to bring such costs into clearer focus. And when that happens, the global effort to end poverty will have entered a new and better era. ²

Sidebar

Cash grants to the poor are as good as many traditional forms of aid when it comes to reducing poverty.

Fears that poor people waste cash are simply not borne out by the available data.

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