Annex 1: Targeted Income, Safety Nets, and Other Support for Vulnerable Groups[40]

Broadly speaking, social safety nets comprise policies and programs that provide short-term income support and access to basic social services to the poor during economic crises and adjustment programs (IDB, IMF, WB, and ADB, 2001). These programs may not be different from those that address chronic poverty and long-term unemployment. The goal is to recognize, in the design of these policies and programs, that the causes and duration of poverty and unemployment during economic crises and adjustment programs (including those in response to exogenous shocks such as droughts, and fall in commodity prices) may differ from what prevails in more normal periods. As a result, social safety nets focus on immediate relief from the effects of crisis and adjustment programs, as opposed to protecting households against lifecycle contingencies, such as sickness and old-age.

Temporary crises may have adverse long-term consequences to the extent that they erode human capital and labor productivity as well as financial capital of households. This risk is particularly high for the poor in that they may be forced to take their children out of school or reduce their intake of food (Easterly and Fisher, 2001; Guitián, 1998). Transitory social safety nets thus play an important role in mitigating these costs for the individual and for society as a whole.
Countries have employed a number of different instruments as social safety nets. The choice of instruments depends on the existing social protection system, the availability of information on the vulnerability of different groups, administrative capacity, and the availability of budgetary resources in the context of a sustainable macroeconomic framework.

Existing social protection systems. Although some countries—particularly transition economies—have a variety of such instruments, others—notably in Africa—may lack them. Since social insurance programs do not have poverty reduction as their principal objective, they may need adaptation—a process that may generate political resistance, as found in transition economies. In cases where speed is of the essence, the administrative structure of existing instruments can be used to transfer benefits quickly to population groups affected by crises and reforms.

The availability of information. Data describing who the poor are and where they reside may not be available. Even when data are available, they may not reflect recent changes in incomes of households. For example, there are significant changes in household incomes during crises. Therefore, relying on pre-crisis assessments of poverty can fail to capture segments of the population in need of assistance, such as the new poor. Information on the characteristics of the poor is needed for targeting. While means testing may be a preferred targeting method, many countries lack the capacity to implement it effectively, due to the lack of accurate information on individuals and households, or because the poor derive incomes from the informal sector that are difficult to verify. Thus determining eligibility on the basis of income may lead to mistargeting, particularly when administrative capacity is weak. As a result, many programs must rely on indirect targeting mechanisms (for a discussion of targeting methods see Grosh, 1994).

Administrative capacity. In many countries, weak governance and administrative capacity hamper the targeting and delivery of benefits. Weak governance can divert and waste resources; weak administrative capacity results in a lack of cost-effective mechanisms to channel transfers to the designated population groups, insufficient

[40] Contributed by IMF Fiscal Affairs Department

information on the poor, and insufficient computerization of available data (Gupta and others, 2000). Even where administrative capacity exists, targeting and delivery can be difficult as incomes change over time and frequent updates of data are costly (van de Walle, 1998). The problems of weak administrative capacity are compounded by overlapping responsibilities for social safety net programs across various ministries and departments (Grosh, 1993). Finally, administrative structures may be especially weak at the local level, where benefits are typically disbursed.

Budgetary constraints. A common response to economic crises are fiscal adjustment programs. For emerging market countries, fiscal restraint may be essential for regaining access to financial markets; for others, it is needed to create the conditions for sustainable growth. This suggests that the amount of financing allocated for social safety nets must be consistent with broad macroeconomic goals. Spending on these programs should be fully costed and integrated into the budgets. Channeling more resources to social safety nets may require shifting resources away from other, less critical purposes. Foreign financing—when available and absorbed quickly and productively—can alleviate this pressure on the budget.

Desirable characteristics of social safety nets

To be effective, safety nets should:

1. Strike a balance between the need to provide protection to the poor and maintain appropriate incentives to work. That is, safety nets should not create a culture of dependency among beneficiaries (Atkinson, 1995; Kanbur and others, 1995);

2. Avoid displacing informal mechanisms of income transfer. Private transfers can be large, constituting between 10 and 46 percent of recipient households' incomes, and are typically directed towards vulnerable groups, including the elderly, the disabled, and the unemployed (Cox and Jimenez, 1989). Government support could displace private transfers, with no net gain on the part of beneficiaries, but an increase in public spending;[41]

3. Be in place *before* crises occur. Precrisis planning can contribute to the design of effective safety nets. Such planning typically includes an assessment of population groups at risk, the identification of relevant social safety net programs, a sustainable level of financing, and a strategy for expanding or contracting programs during and after the crisis (Ferreira and others, 1999; IADB, IMF, WB, ADB, 2001); and

4. Be transparent and open to public accountability. Mass publicity campaigns should inform the public about the nature and scope of different programs, as well as their eligibility criteria. Periodic, independent evaluations of social safety net programs should be made available to the public.

In what follows, the most common social safety net instruments are reviewed, along with an assessment of their strengths and weaknesses (Gupta and others, 2003).

[41] For a description of public safety nets which complement and extend informal ones, see Morduch and Sharma (2002).

Cash transfers, as opposed to in-kind (often food) transfers, confer the maximum welfare upon recipients, owing to their fungibility. Compared to price subsidies, they have the advantage of not distorting prices, but may create disincentives for labor market participation. Their targeting through means-testing is information-intensive and often proxy-means testing is required by restricting benefits to single mothers, the disabled, elderly, or unemployed.

Price subsidies have low administrative costs and can be implemented very quickly. A drawback is that they are often biased towards the urban poor and difficult to remove (e.g., after a crisis has subsided); they may also entail substantial leakages in that they benefit the population as a whole (Gupta and others, 2000; Cornia and Steward, 1995). One solution is self-targeting by subsidizing goods consumed disproportionately by the poor. In Indonesia, for example, food subsidies were confined during the 1997/98 crisis to rice of lower quality (IMF, 2000b).

Public works programs are a common response to macroeconomic crises, as they can be implemented and removed quickly and, in addition, help create or maintain public infrastructure. Indonesia and Korea implemented public works programs during the Asian crisis, as did Mexico following the 1994 crisis, while Argentina extended an existing program in 2002. Mechanisms of self-targeting are easily incorporated by offering a wage below the market wage for unskilled labor (Subbarao and others, 1997). Should this wage be too low to support a household, the government may offer food as a benefit, possibly of lower quality to encourage self-targeting. Despite their apparent strengths, public works programs have at times proved difficult to administer. A large number of small projects created enormous logistical problems in Indonesia (IMF, 2000b), while in Korea, infrastructure projects tended to be executed in an ad hoc manner and wages were reduced several times because workers were leaving their regular employment.

Extension of existing social protection systems may be an option in some countries. By using administrative structures already in place, this is a speedy way of conferring benefits to the most needy. However, often the schemes intended to alleviate life-cycle contingencies need to be adapted to the crisis situation. Korea, for example, expanded its unemployment insurance programs from firms with more than 30 employees to all firms. Eligibility was also expanded to cover temporary and daily workers. In addition, the required contribution period for benefit eligibility was shortened and the duration of benefits extended. As a result, the number of beneficiaries increased tenfold between January 1998 and March 1999.

Expanding targeted assistance to foster human development can take the form of waivers for fees for health and education services, as well as cash and food transfers in exchange for school attendance or utilization of preventive health care. Initiating or expanding such programs during economic crises may prevent large numbers of people entering the vicious circle of malnutrition, low productivity, and poverty. In Argentina, budgetary allocations for emergency education programs were almost doubled in the wake of the crisis, including (i) school lunches and scholarships for secondary students to encourage attendance and (ii) the provision of learning materials, which may otherwise have been out of reach of poor families. Also, the coverage of emergency health programs was significantly expanded, in particular those focusing on financing immunization, disease control (including AIDS), drugs for primary health centers, and basic maternal and health care. However, these programs tend to be information-intensive. In Indonesia, beneficiaries of a national scholarship program for the poor were chosen by administrative criteria, combined with recommendations by the school principal, the head teacher, and a representative of the community (IMF, 2000b). Their effectiveness also depends crucially on existing school and health infrastructure, as well as on the opportunity costs of school attendance.

Food stamps and other targeted food-based safety nets have the principal aim of alleviating and preventing malnutrition. In this respect they are superior to cash benefits, in that they are conducive to self-targeting, especially when restricting stamps to inferior foods (albeit enriched with nutrients). They are also believed to have a greater impact on children's health and nutrition, as they often fall under the control of women (Pinstrup-Andersen, 1988; Sanghvi and others, 1995). Still, additionality may be an issue, in that the household head could reduce own expenses for food when allocated food stamps. However, there is some evidence that food stamps have a larger effect on food consumption than cash transfers (Fraker, 1990; Fraker and others, 1995). In addition, some countries may lack the capacity to produce forgery-proof stamps.

The main lessons in effectively implementing social safety nets can be summarized as follows. First, safety net instruments should be in place before a crisis occurs. If adequate information and administrative capacity exist, programs can be better targeted. Second, safety nets should provide adequate protection to the poor, avoid creating a culture of dependency among beneficiaries, minimize disincentives to work, and be consistent with prudent fiscal policy. Third, transparency and accountability in the design and implementation of programs and in the use of resources are critical for the effectiveness of social safety net programs. Fourth, social safety net programs should be coordinated across implementing ministries and departments, as well as different government levels, to avoid inefficient overlap and administrative waste. Finally, during crises, proportional cuts in social spending in general and safety nets in particular should be avoided. If possible, spending should be maintained or increased and key programs should be protected.

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