Replacing Welfare Provisioning with Cash Transfer

Evaluation from the Perspective of Redistribution

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The proposition that direct cash transfer should replace the welfare model of subsidized goods and services because it is a more effective social protection strategy lacks merit. This paper argues that by switching to cash transfer, a section of the beneficiaries of the current system, especially those who depend on it the most, would be the worse-off. It is, the authors argue, a less-efficient system of redistribution compared to a need- based welfare regime of subsidised goods and services. Further, in a country that has a high level of absolute impoverishment, subsidised goods and services, which provide need-based social protection have to be further promoted.

Keywords: cash transfer, universal transfer, public provision, goods and services, welfare schemes

In recent times, a section of the academia and activists has been arguing that cash transfer is a more effective strategy to fight poverty and should replace the existing welfare model of subsidized goods and services. The proposition is apparently simple, which makes this all the more attractive: equally distribute the amount of money that is currently spent on welfare programmes and subsidies to everybody directly. The main benefits counted in its favour are (a) it would reduce the leakages that welfare programmes currently suffer from that prevent the benefits from reaching the needy, and (b) the recipient will have the choice to use the money according to their priorities rather than the state dictating their choice (Svedberg, 2012; Jhavbala, 2016). Such benefits are supplemented to other macro-economic effects of cash transfers – that cash would have a 'multiplier effect' boosting economic growth, it would reduce social in-equalities, etc. (Standing, 2012).

Even the *Economic Survey (ES)* joined the debate with a dedicated chapter on the subject, calling such cash transfers as a 'basic income' which a government pays to all its citizens without any conditions attached (GoI, 2017a). The *ES* sees it as a basic right of citizens, a "minimum income which they can count on, and which provides the necessary material foundation for a life with access to basic goods and a life of dignity" (GoI, pp. 173). But is this a new idea, which is a "compelling paradigm shift in thinking about both social justice and a productive economy"as the advocates of cash transfer claim it to be?

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Cash Transfers: A Diverse Concept

We find that the idea of the state providing an unconditional income to all its citizens dates way back to the 18th century, elaborated in Thomas Paine's *Agrarian Justice* (Paine, 1795). In this seminal work he argues that "condition of every person born into the world, after a state of civilization commences, ought not to be worse than if he had been born before that period" (Paine, 1795). As landed property had dispossessed many of the proprietors of land in its natural state, he proposed that the land owners should pay a fraction of their value of land[3] to the state to be distributed equally to every citizen. More than two centuries later, we hear an echo of Paine's proposal in leftist economist Yanis Varoufakis'(2016) suggestion that a percentage of capital stock (shares) should be put into a Commons Capital Depository and the dividends from it should be universally distributed. These models of cash transfers do not advocate any concomitant cuts in government's existing social protection/welfare expenditures funded by general taxation that act as a corrective for the iniquitous income *flow*. Rather, they try to address a deeper structural inequality, i.e. inequality of ownership of productive assets/capital stock which they want to 'tax'. In this sense, these models of cash transfers transcends the welfare state, it does not replace it. We will term these as 'cash transfers in addition' models.

In contrast, there is another set of ideas where cash transfers necessarily replace state welfare provisions reducing government expenditures. Milton Friedman, one of earliest advocates of this model, envisions it as a negative income tax replacing all welfare programmes which he thought are inefficient and wasteful (Friedman, 1968). Murray's advocacy of cash transfer comes from a conservative political point of view. In his perception, in addition to reducing what he considers social 'problems' induced by the welfare state, such as deteriorating traditions of work,[4] weakening neighbourliness,[5] etc., cash transfer would give state less power to control people's lives than the welfare regime (Murray, n.d.). We can call this as the 'replacement model' – one that replaces welfare provisions – of cash transfer.

It is amply clear from this account that these are two vastly dissimilar perspectives on cash transfers. Implementation of one variety would draw flak from the advocates of the other. In India today, the 'replacement model' has attracted support from certain official policymakers as well as non-governmental advocates, with very few talking about the 'cash transfers in addition' alternative.

While there can be no argument against a progressive redistribution (i.e. from the rich to the poor) through cash transfer in general, a *shift* in redistributive strategy to replace public provisioning by cash transfers (or call it a basic income) is a different matter altogether that requires a thorough debate. In the following sections, we will critically examine the existing arguments and evidence to understand whether a system of cash transfer that replaces public provisioning is a better strategy for 'welfarist' interventions.

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[3] Paine considered the total value of land as the sum total of its value in its natural state and the improvements that the land owner makes onto it. In his view land holders can't have ownership rights on that fraction of the value which is accrued from its natural state. This he suggested to be distributed universally.

[4] Contemporary and historical review of literature both from US and Britain that traces the patterns of labour productivity in different sectors finds it closely associated with work conditions, inadequate wage increases or otherwise, low levels of human capital more due to state failures rather than traditions of work (Tomlinson, 2007).

[5] The critiques of this view consider deteriorating 'neighbourliness' or 'communitarianism' as a result of competitiveness that capitalism enforces upon individuals for their basic needs and livelihood, which under 'free-market' are individuals' responsibility rather than a social guarantee (Navarro, 2002). Murray's advocacy for less welfare measures is actually contradictory to his wish for greater 'neighbourliness' or 'communitarianism'.

Redistributive justice requires that we talk not only of fairness and equity in access and availability of goods and services but also of objective reality. The existing inequality demands that, those whose needs are greatest, are given priority. So, there is an important question that needs to be answered: how efficient is cash transfer, i.e. can a given public outlay through cash transfers achieve the same level of access to goods and services through welfare interventions and avoid wastage? We will examine this through empirical experiences of public health care services and public distribution system (PDS) in India.

Health Care Provisions

Let us consider health expenditures of the households where members had to be hospitalized and were treated in public health facilities. We assume that in absence of subsidized public health facilities, the rural-urban and state-specific median expenditure of treatment for a particular type of ailment in private hospitals incurred by individuals to be the probable expenditure.[6] Keeping in mind that mean values might be influenced by outliers, we used the median. This method is used by others as well (Dreze and Khera, 2013). We have calculated the household's 'potential extra expenditure' (PEE) for the last year from NSS 2014 data, as the difference between probable expenditure if they were to go to private health care and the expenditure they actually incurred for treatment in a public facility. This is adjusted for a standard five-member household size. Our objective is to find out whether cash transfers made out of government health expenditures will be sufficient to compensate the PEE. In Graph 1, we have plotted distribution (density) of households by their PEE (at 2014 current price). PEE varies for different households. The distribution is so skewed that the 25th percentile household has a PEE of Rs. 5,300 annually while for the 90th percentile it's as high as Rs. 30,300.

If a universal transfer were to be made from the total health budget of 2013-14 (centre and states combined), it would have been no more than Rs. 4500 per household which is pretty little to adequately compensate every households (for their PEE on hospitalisations) which is clear from Graph 1. In such a scenario, more than 75 per cent of households – whose PEE is more than Rs. 4,500 – will go under- compensated. This is while considering only the households' hospitalization expenditures; adding to it the costs for out-patient services would further inflate the estimates of PEE. Under-compensation in this manner will harm the poor more (since they use the public health care services more) than the richer households (Table 1), and their health care expenditures are higher relative to their incomes.

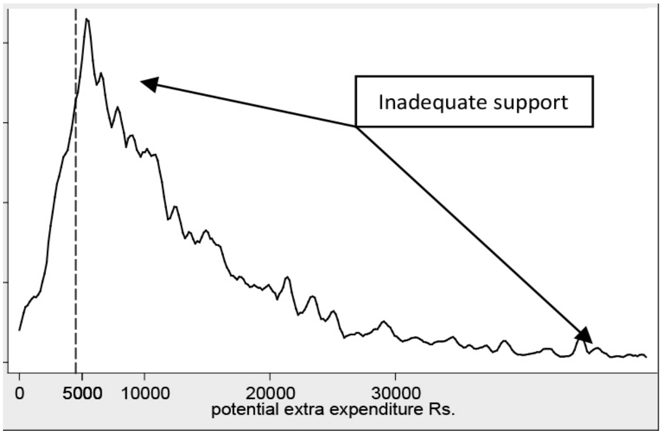
Table 1: Percentage of households with hospitalisation cases using public health care services by MPCE - 2014

MPCE Quintiles	Percent
Poorest quintile	65.52
2nd poorest	60.07
Middle	54.11
2nd richest	44.05
Richest quintile	36.58
Total	49.38

Source: NSSO 2014

[6] We are not considering the strong possibility that dismantling public healthcare services might increase private healthcare charges from their existing levels.

Graph1 : Distribution of household with hospitalisation by prtential extra expenditure (adjusted)



Source: NSSO 2014

Public Distribution System

Similarly by dismantling PDS, the (annual) maximum amount of money that could be disbursed universally from the Central Food Subsidy of 2011-12 (Rs. 72822 crore) was roughly Rs. 600 per capita. Instead of universal disbursal, when calculated only for food grains purchasers from PDS (number of food grain purchasers from PDS estimated by authors from NSS Consumer Expenditure Survey, 2011-12), the transfer amounts to Rs. 1300 per capita. In Graph 2, we have plotted the cumulative distribution of households who buy food grains from PDS by their annual per capita PEE[7] (at 2011-12 current prices). It shows that roughly 22 per cent households would incur per capita PEE of more than Rs. 1300 and they will be under compensated by transfers of such magnitude. For that year, to adequately compensate nearly all households (more than 95 per cent) required transfer of around Rs. 2200 per capita.

Moreover, the data also show a great deal of variation in the percentage of under-compensated households (i.e. PEE >Rs. 1300) among *total* households – which indicates the adverse impact of such cash transfers for overall population – across states. Among the major states, it is quite high for Jammu & Kashmir (31 per cent), Tamil Nadu (25 per cent), Chhattisgarh (23 per cent) and Orissa (21 per cent), followed by Himachal Pradesh and Kerala (over 15 per cent in both) where impact is substantial (Graph 3). This indicates that for states where PDS is functioning better or has improved over the years (see Khera, 2011), the adverse impact of cash transfer will be relatively higher. Those who are adversely affected will be more likely to be from the poorer households as their quantity of food grain purchase from PDS as well as food budget share[8] in it is higher compared to their richer counterparts (Graph 4).

There are five addtional caveats that we should bear in mind while we compare the available money for cash transfer with PEE. Firstly, there will be administrative and other overahead costs of cash transfers. So the full government allocation that goes into a welfare scheme will not be available for transfers upon the scheme's abolition. Secondly, any leakages in cash transfers will further reduce

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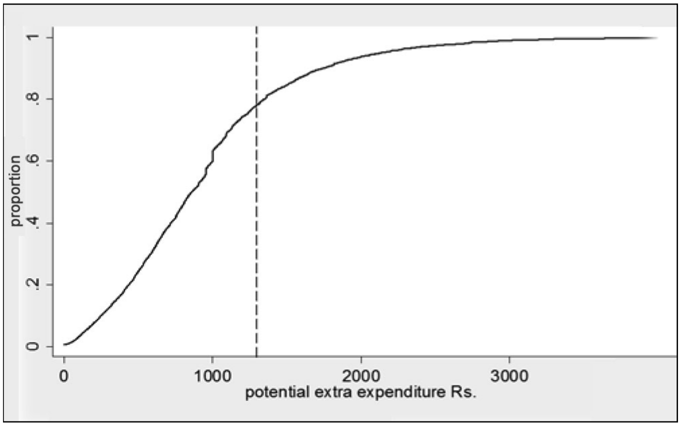
7 The cumulative distribution plots the proportion of households at or below a certain level of PEE for all values of PEE.

8 More than absolute quantities, the relative importance of PDS on food is actually much higher in poorer households.

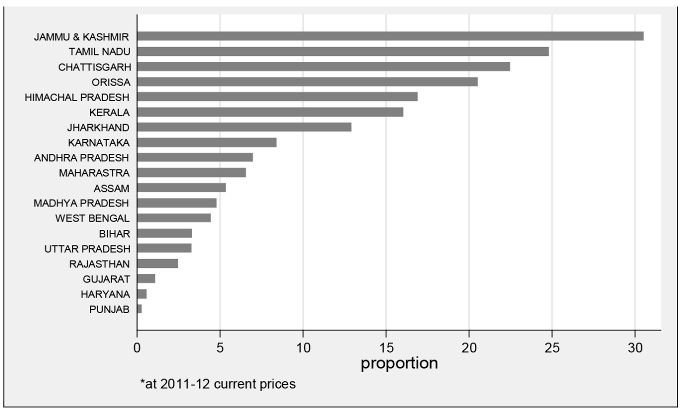
the actual transfered amount. Thirdly, if a targetted scheme is replaced by a targetted cash transfer, then the very problems of targetting itself will persist. On the other hand, universalising the transfer will spread the resources too thin. Fourthly, dismantling a scheme might affect market prices and hence, will change the estimates of the PEE.[9] Fifthly, PEE sould not be viewed as the full measure of benefit of a welfare scheme. It only measures consumer benefit whereas there are provider/producer benefits as well (eg. public health care personnels' salary, farmers' income from sale to PDS, etc.).

Graph 2: Cumulative distribution of PDS households by Potential Extra Expenditure* (Rs.)



Source: Author's calculation using NSS 68th round unit data

Graph 3 : Under-compensated households by states (2011-12) as percentage of total households



Source: Author's calculation using NSS 68th round unit data

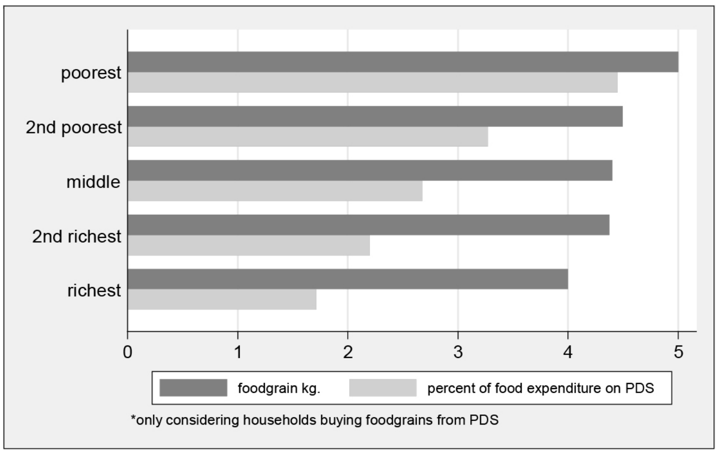
Advantage of Provisioning

The distinct advantage of public provision of goods and services over universal cash transfer is its priority for the needy. Public health care is availed by those who require affordable health services; those who cannot afford higher priced foodgrains from the market buy from PDS shops despite the

[9] There is a debate over the effect of PDS on food prices, some theoretically arguing that it drives up market prices (Basu, 2011). Empirical evidence on the other hand shows that reduction in food subsidy increases market prices of food (Ramaswami and Balakrishnan, 2002).

poor quality of goods and the difficulty in accessing them, the unemployed opt for MGNREGS wage for hard manual labour, and so on. In effect, public provisioning of goods and services, financed by pooling resources through progressive direct taxation, mitigates individual risks during a private crisis (illness, job-loss, etc.). In the presence of high economic inequality, welfare measures should not be based only on equal entitlement but be amenable to positive discrimination as well. Experiences from around the world have shown that the poor utilise universal public welfare measures relatively more than the not so poor, because their need for these services is higher, as for instance, in the National Health Services of UK (Collins and Klein, 1980 and O'Donnell and Propper, 1991). Table 1, shows that for hospitalisation services in India, the relative use of public health care facilities by the poorest quintile is almost double that of the richest quintile. If cash replaces subsidised goods and services, the only way to ensure that the neediest do not end up under-supported is to fix the per-household cash transfer amount at the level of households with the highest PEE. This would require a massive expansion of public outlay; otherwise such a cash transfer system will only worsen the situation of those with the highest PEE compared to the subsidized goods and services regime. According to Rawls' 'difference principle' of justice, any redistribution is less just if it worsens the condition of the least advantaged (Altham, 1973). In our scenario, those with the highest PEE (the least advantaged in this case) are left with a worse outcome if cash transfers are insufficient, and hence it is less just. Friedman even in his defence of cash transfers as replacement of welfare programmes, airs a similar concern:

Graph 4 : Foodgrain from PDS - quantity and expenditure median monthly per capita values by MPCE quintiles*



Source: Author's calculation using NSS 68th round unit data

> (T)hese [welfare] programs…more or less incidentally…do help some people who are disadvantaged. Can we in good conscience mount a political attack on them unless we can provide an alternative way to achieve their good results? (Friedman, 1968)

We believe his conscience would have been troubled had he seen the good results of public health care system or PDS for the least advantaged getting threatened by cash transfers of this nature.

Does Cash Transfer Have Corrective Mechanism?

As we see above, the degree of justice in a system of cash transfer that replaces subsidized goods and services would inherently depend upon the amount of money transferred. Therefore, a related question that arises is whether the ‘unjust’ situation created by the replacement of welfare provisioning by cash transfers (‘replacement model’) will have mechanisms to rectify itself to a more just situation (i.e. increase in cash entitlement)? When a system to provide subsidized goods and services deviates from its pledge, it ignites public protest, academic criticisms and causes potential electoral reverses. It does impact in improving public provisioning, even if in limited ways, as seen in the case of PDS. Such rectification is possible as the existing entitlements for provisioning of goods and services have been clearly spelt out. A cash transfer system that starts from inadequate cash entitlement (PEE greater than household’s cash entitlement) has less possibility of rectification as entitlements of material goods and services are not defined at all in this monetized (cash transfer) system. In addition, the state’s responsibility to ensure a minimum level of food, health care, education, or wage-for-work is shifted to the people in the name of giving them greater choice. In reality, all that people will have in terms of choice is managing their needs the best they can from a meagre state grant. To draw from our case in Graph 1, we would not understand the need to push up the amount of cash transfer without defining the underlying material (health) entitlement, which remains unmet for many households at Rs. 4,500 level. Or the predicament of those households who need more than Rs. 1300 per capita to compensate for food grains that they presently purchase through the PDS (Graph 2). Such inadequate amounts of cash will not fulfil food or health requirements, but without a defined material entitlement have little chance of correction. This is perhaps the reason why some of the cash transfer schemes in India failed to translate into material entities as desired, as for example, the partial cash support to targeted rural households to construct houses under Indira Awas Yojana, as for many households, the cash amount they received was insufficient for the stated purpose (Shah, 2008).

Maintaining Entitlements Over Time

Another concern is that, whether cash transfers will be able to maintain the beginning levels of entitlement amid rising prices. The best way to achieve this is indexing the cash transfer to price indices regularly. But even that is fraught with many difficulties. How the alteration of subsidy disbursement by shifting to a cash transfer system affects prices, will become a critical aspect of price indexation (Kishore et al., 2013). And even price indexations are known to have considerable time lags, which in the face of volatile and rising prices erodes the real value of cash and people have to bear with reduced entitlements during the lag period (Ghosh, 2011).

But even in an ideal world scenario – one where there is reasonable price information, altering subsidies do not sky-rocket the prices and indexing has negligible time lag – use of price indices for the purpose has at least two distinct problems. The first one is that indexing through price indices does not necessarily maintain entitlements, or levels of purchase/consumption. Food consumption, or calorie intake, is the best example of it. At poverty line expenditures – which are indexed with consumer price indices – calorie intakes have declined over time (Patnaik, 2013) even for those with intakes much less than the minimum requirements (Qadeer et al., 2016) or those whose average calorie requirement has in fact increased, viz. the poorer sections in urban areas (Eli and Li, 2015) with no clear evidence of improvement in quality of diets. This is the reason why we do not stop merely at indexing by price indices while demanding yearly salary hikes or increase in budgetary allocations for welfare schemes.

The second problem is that price rise affects individuals/families even in the same economic strata in very different ways. The price indices do not capture these variations in the effect of price rise among different individuals/households but at best show average inflation, generally for specific sections of the population. But even different segments of the population, let alone individuals/households, have different expenditure priorities, represented by the variations in their share of expenditure on different items. Hence, an increased set of prices for different items will affect each one differently. For example, all other prices remaining the same, a rise in prices of healthcare services will affect those that have highest share of expenditure in health the most. Price indices based on average expenditure shares will not capture their plight fully. Simply increasing the amount of cash through indexation based on price indices will not fully cover for inflation for the most affected, which leads us to the problem of distributive justice as discussed earlier.

A proposed mechanism to bypass the problem of price indexation is to fix it as a certain percentage of the GDP (Ray, 2016; GoI, 2017a). But this still is a compromise to the long standing struggle of increasing the share of government welfare spending in GDP. India's rank in social protection expenditure as percentage of GDP is one of the lowest among its Asian counterparts (Terry and Handayani, 2013).

Cash Transfer: Experiences So Far

A cash transfer is at least as good as a subsidised goods and services welfare regime only if it provides the same quantum of protection. Our discussion till now shows that to ensure that none is under-compensated everyone has to receive a transfer that is large enough to cover the requirements of the most disadvantaged of the lot. Additionally, these transfer amounts would require frequent large up-scaling, something in the style of a Pay Commission, to ensure that the most disadvantaged do not fall outside the protective umbrella due to inflation. These are the conditions that determined the outcomes of micro-experiments on cash transfers on ground. The experiments were successful where:

(a) The transfers were fairly large: as in a 2011 UNDP-Government of Delhi experiment where BPL households barred from PDS were compensated with Rs. 1000 monthly in cash (SEWA Bharat, 2012) which, for a five-member family comes to Rs. 2400 per head annually. This is quite close to our estimate (Rs. 2200) of what should be the adequate compensation for dismantling PDS which we presented earlier from 2011-12 data. This compensation amount given in the experiment is 85 per cent higher than the amount that can be distributed per head to PDS households from central food subsidy of 2011-12.

(b) Cash did not replace any existing social welfare programme as in the 2011-12 UNICEF-SEWA experiment conducted in Madhya Pradesh (SEWA Bharat and UNICEF, 2014). This particular experiment also increased the cash transfer amount after a year by 50 per cent to compensate for inflation, which clearly shows necessity of frequent large upward revision of cash transfers. On the other hand, two prominent experiments to replace PDS with cash transfer that did not have these characteristics – the Delhi Annashree Yojana and a similar one in Puducherry – faced many obstacles and were discontinued. In the international scenario as well, successful cash transfer schemes echo this feature. The succesful (conditional) cash transfer programme Bolsa Familia (or 'Family Grant') of Brazil was introduced as an addition to a well funded public education and healthcare system (Ghosh, 2011; pp.68). The contrast to this is the experience of Iran, where the system of subsidised provisioning of food, health and other utilities which existed since 1980, was replaced with cash trasfer in 2010 against popular will,in the government's bid to reducewelfare expenditures (Nikou and Glenn, 2010). It resulted in accelerating inflation and the rapid erosion of the real value of the cash transfers (Tabatabai, 2012).

'Basic Income' of the Economic Survey

In the light of the above discussion, the ES's proposal of replacing welfare schemes with cash transfer appears to be quite alarming as far as the interest of the poor is concerned. The biggest problem lies in the determination of the quantum of 'basic income' and the proposed mode of financing it. The determination of cash amount is done in two stages. First it defines 'basic income' as one that takes even the poorest person above the official poverty line of 2011-12, which was consumption expenditure of Rs. 30 per capita per day. There is enormous debate on whether this paltry amount is indeed sufficient for "necessary material foundation for a life with access to basic goods and a life of dignity" (ibid). In the second step, the 'basic income' calculated for 2011-12 is upscaled for 2016-17 using price indices and adjusting for real GDP growth rate assuming real income growth equals to that of real per capita GDP, which came to just Rs. 18 per person per day for 2016-17.

By this methodology, an individual's 'basic income' would not increase even at the rate of inflation which will erode its real value over time. It would also mean that, other things remaining the same, the higher the real GDP growth the lower would be an individual's 'basic income'. Hence, an individual's 'basic income' share in GDP would fall over time, as the rate of growth of her basic income (which is even less than the inflation rate) is less than the rate of growth of nominal GDP (which is inflation plus real GDP growth rate). The government's total expenditure on 'basic income' for the entire population (or for a certain percentage of the population) would then fall as a share of GDP, given that the per person fall is not offset by very high population growth.

What is even more problematic is its proposal to finance this 'basic income' by dismantling major welfare schemes such as the PDS, MGNREGS and various other subsidies.This has threemajor issues. Firstly, the ES doesn't even stick to its own meagre standard of 'basic income' whose calculation is based on the current economy that has these welfare schemes/subsidies in place. Dismantling these would increase the cost of living of the poor and accordingly the 'basic income' level, even by ES's standard, would require a raise. Secondly, as we had discussed earlier, for many poor families the cash in return of dismatling existing welfare schemes will not be even compensatory (adequately compensating PEE), let alone provide additional gains.The decision to give Rs. 18 in cash per day to a poor person while taking away all other major welfare provisions will be grossly inadequate for "necessary material foundation for a life with access to basic goods and a life of dignity" (ibid). The meagre transfer would not give much choice to the recipients; from such fixed small amount of cash, it will be impossible for the poor to manage their economic crises such as, unemployment, catastrophic health expenditure of private care, food crisis etc. which only a need based welfare system can handle - much more efficiently and within limited resources.Thirdly, since ES proposes to replace all welfare expenditures by such cash transfer, this proposed methodology would result in ever-reducing government expenditures (as a percentage of GDP) which undermines the progressive redistributive role of the state.

Concluding Remarks

From macro-economic perspective, crucial for the success of a cash transfer programme is its ability to have a positive ‘multiplier effect’. This in fact is often pointed out as one of its strengths to garner support for it. It can even strengthen public welfare services through increased demand for the same (Standing, 2012). However, these economically expansionary characteristics have little common ground with the version of cash transfer that calls for concomitant withdrawal of other welfare programmes.In a country like ours which not only have high economic inequality but also high level of absolute impoverishment, positive discrimination is a necessity; we need a welfare system that universally provides social protection, benefitting different segments of the population according to their need; because granting everybody a uniform cash transfer that covers the neediest would be too high an amount and an inefficient way of using public resources.Instead of strengthening the institutions and systems to efficiently allocate public resources, the proponents of cash transfer unfortunately seek an escape route in a system which as a stand alone methodof redistribution is evidently less efficient.

Our analysis uncovers the fact that cash transfer replacing welfare provisioning is yet another onslaught on public social protection by stifling state’s spending. The need of the hour is to provide more resources to public welfare programmes; this could be done through increasing direct taxes of the rich, pooling contributory funds for public services that people anyway pay to costlier private providers (like Canada’s income- contributory fund for universal social health insurance). In India, it is the proportion of indirect taxes (which the rich and the poor pay alike) that is increasing while that of direct taxes (which are proportionately higher for individuals with higher earnings) is going down. At the same time huge concessions are being provided to the corporate sector at the expense of tax revenue, estimated to be around Rs 83,492crore for the year 2016-17 (GoI, 2017b). Additional resources can even be raised from a ‘tax’ on capital stock, if we agree in principle that common people have equal rights on productive assets (as argued by Paine (1795) and Varoufakis (2016)). It is, however, important to recognise that the redistributive welfare interventions’ ability to correct economic inequality is only partial. Poverty is not just the lack of money/cash, as the proponents of cash transfers in India simplistically view it to be. The most important causes of poverty are structural such as un-remunerative incomes, volatile prices, lack of employment, unequal ownership of productive assets. etc. Recognising these is vital to uplift the marginalised.

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