From conditional cash transfers to unconditional basic income ?

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Executive Summary

Along with many other middle-income countries in the world, Egypt seems to be moving in the direction of an income distribution system in which conditional cash transfers play a significant role. At the same time, from California to Kenya, the more radical idea of an unconditional basic income is gaining unprecedented popularity across the world. There are important differences between the two ideas. But it is not inconsistent to defend both. Conditional cash transfers may be politically and fiscally possible under conditions in which an unconditional basic income is not. And the latter does not only provide a structural solution to the former's intrinsic defects. It also constitutes a central feature of a free society and a sane economy, by reference to which the expansion of conditional cash transfers can be regarded as an important step forward.

Basic income, guaranteed minimum income and conditional cash transfers

A *basic income*, or unconditional basic income, is an individual, universal and obligation-free cash income paid at regular intervals by a political community to each of its members. (1) Its being individual means that it is paid to every individual at a level that is not affected by the composition of the household. (2) Its being universal means that it is not subjected to the satisfaction of a means test and is therefore not restricted to the poor. An (3) its being obligation-free here means that it is not subjected to the satisfaction of a work test and is therefore not restricted to the employed and the involuntarily unemployed.

Consequently, a basic income differs in three ways from the *guaranteed minimum income* schemes that exist in many developed countries as part of the social assistance component of their welfare states. These existing minimum income schemes also take the form of regular cash transfers, but these are typically conditional in the sense that (1) entitlement to them and their level depend on the household situation; (2) they are restricted to households that qualify as poor; and (3) they require availability for employment.

The so-called *conditional cash transfers* implemented or envisaged in many developing countries possess at least the first two of these features, usually not the third one both because of the low level of the benefits involved and because of the prevalence of informal employment. They also often add restrictions to households with children and conditions of health monitoring and school attendance. Such schemes now exist in over sixty countries. The most notorious is Brazil's *bolsa familia* developed from 2004 onwards under President Lula on foundations laid under his predecessor Fernando-Henrique Cardoso. The Takaful scheme in the process of being expanded in Egypt is also such a scheme.

Conditional cash transfers: the main challenges

There is no doubt that conditional cash transfer schemes can produce a significant decrease in the levels of poverty, and especially of extreme poverty, with positive side effects on health and education. Yet, they are not uncontroversial. Firstly, it is sometimes argued that in-kind transfers would be better than cash, because they ensure that the resources made available for the poor would be spent on necessities. If only because of the strong associated positive externalities, there is certainly a strong case for the free or generously subsidized provision of education and health care, public spaces and public transport. But beyond that, the case for in-kind provision is generally much weaker. To an extent that depends on the good concerned (food or energy, for example) and on the method used (direct distribution, vouchers, or subsidies), in-kind transfers often suffer from serious disadvantages compared to cash transfers: heavier administrative burdens, higher risks of mismanagement, clientelism and corruption, discouragement of local production (especially in the case of food distribution), unwelcome price distortion and perverse redistribution to the better off (especially in the case of energy subsidies). At least as long as benefits do not reach the poverty threshold and particularly if they reach women as much or more than men, there is therefore often a strong presumption in favor of cash transfers: in the overwhelming majority of cases, poor households can and must be trusted to make the best use of the cash they are given. In some regions of the world, the lack of personal identification and personal bank accounts still makes the efficient delivery of cash benefits tricky. But as the decennia-long functioning of South Africa's noncontributory old-age pension scheme has shown, modern technology has made the running of cash transfer schemes possible at a manageable administrative and security cost even in remote rural areas.

Secondly, there is the question of whether it makes sense to impose conditions of health monitoring and school attendance. At the time of the introduction of Brazil's *bolsa familia*, for example, the imposition of such conditions was politically important because it signaled clearly that the program was meant as an investment in the country's human capital. It is controversial, however, because of the adverse way it may affect some of the households most in need of financial assistance. Failure to show up for the health tests or to secure one's children's continued presence at school may be due to geographical distance, climatic conditions, lack of information, domestic conflict, family dislocation, mental health problems and other circumstances more or less directly associated with material deprivation. Like the linking of entitlement to child benefits to school attendance in countries with a highly developed welfare state, the imposition of such conditions can still play a positive role, but only if they are implemented in a sufficiently flexible, sensitive way. They must work as instruments for strengthening the human capital of some of the worst off, not as exclusion mechanisms that will make them even worse off.

Thirdly and most crucially, there are three important difficulties related to the fact that conditional cash transfers are means-tested, i.e. restricted to a subset of the population qualifying as poor.

To start with, in countries in which the informal economy plays a major role, especially among the poorer parts of the population, it is very difficult, indeed impossible without a prohibitively expensive and intrusive bureaucracy, to make a precise assessment of a household's current income in order to determine whether it qualifies as poor. In some countries such as Brazil, a rough income assessment based on self declaration is made, say, once every six years and determines the entitlement for the following period, save for changes in the household composition. Checking reliably a household's annual informal income is obviously beyond the capacity of even the best administration. In many other countries, therefore, the assessment is based on proxies, such as the number of rooms in the household's home, the number of light bulbs, the possession of a fridge, a television or a vehicle, etc. It is such an approach that is being envisaged, it seems, for Egypt's expanded Takaful program. In the most sophisticated versions of it, such as the one used in Mexico, one first selects a large number of variables such as those listed above, more easily observable than household annual income and likely to be correlated with it. Using a household survey of a representative sample of the relevant population, one subsequently identifies a weighted combination of these variables as the best predictor of a household's income level. This defines an index that can serve as a proxy for income poverty and makes it possible to ascribe a score to each household using the observable variables. Households that score below some cut-off value are entitled to a benefit. Households that score above it are not. The higher the chosen cut-off point, the higher the occurrence of "false positives", i.e. of households entitled to benefits despite their income exceeding the income poverty threshold. The lower the cut-off point, the higher the occurrence of "false negatives", i.e. of income-poor households not entitled to benefits. Even with the best method of this sort, one faces the obvious problem that, once the variables entering the proxy index are known, households will understandably adjust their visible consumption choices so as to increase their chance of qualifying for the transfer. Anticipating this, the authorities in charge therefore endeavor to keep the proxy formula secret and thereby prevent potential recipients from checking whether they were treated fairly and open the door for opaque arbitrary decisions by local administrators. Consequently, whether one opts for direct income assessment or for the proxy method, the degree of discretion is unavoidably high, and the risk of clientelism and corruption among those in charge of determining who is entitled and who is not is considerable in the context of a largely informal economy.

A second difficulty linked to the means-tested nature of conditional transfers arises whether or not the economy is largely informal. It relates to the so-called rate of take up. What is the proportion of the poor who will actually receive the transfer meant to alleviate their poverty? Even in countries with a relatively mature and efficient welfare state, the proportion of poor people entitled to means-tested benefits who never receive them, or receive them too late, is very high. It is in the order of 50% in France, for example. There are two main reasons for this. One is the lack of information. It is a challenge to make intelligible information available at the appropriate time to people living in hardship, often with a limited degree of administrative literacy. And as it is not in the financial interest of the public authorities in charge to identify as many as possible of the households entitled to the benefits, one cannot expect them to devote huge efforts to public information campaigns and the detection of individual cases. A policy can then sound very generous, while remaining surprisingly inexpensive. The second reason is the stigmatization unavoidably attached to the status of beneficiary of a means-tested transfer: claiming it amounts to recognizing that one is destitute, incapable of providing for oneself and one's family. Even with the most humane staff in the local welfare offices, this can be experienced as such an humiliation, such a blow to one's self-esteem, that some poor people prefer not to claim benefits they are entitled to. A low rate of take up obviously weakens the effectiveness of means-tested schemes as poverty alleviation policies — over and above the inefficiency induced by the occurrence of "false negatives", i.e. by the use of entitlement criteria that wrongly exclude households that are below the level of income the scheme aims to secure.

The third important difficulty that arises from the means-tested nature of conditional cash transfers relates to the so-called poverty trap. However well meant, a scheme that targets the poor has the unavoidable implication of punishing those who manage to get out of poverty. As soon as earning some money or possessing some goods lifts a household, however modestly, above the cut-off point stipulated by the scheme, it is "rewarded" by the loss of the benefit it was entitled to. Understandably, this reduces the incentive for poor people to improve their material situation. The net pay may hardly exceed, sometimes even fall short of what they get in benefits, especially if account is taken of the work-related costs in transportation, clothing or childcare. Moreover, taking the job may create an uncertainty that poor people can ill afford: they may not be able to put up with the job or be sacked, and then have difficulty recovering the entitlement to the benefit. Ant the additional uncertainty generated by the opaque working of a proxy method further invites the poor to being cautious. The result is that many of the poor get stuck in a situation of benefit dependency. This process is further reinforced by the fact that they have to adjust psychologically by giving up the ambition of becoming "self-supporting" — at least in a sense that can be detected by the officials in charge of enforcing the means test. This is the poverty trap, also sometimes called the unemployment trap. In order to reduce it, some means-tested schemes have introduced the possibility of combining the benefit with earnings for a limited period of time or up to some modest level of earnings. Such amendments go some way towards addressing the first aspect (income differential) but do little for the second, are often difficult to grasp by the beneficiaries and come at a considerable administrative cost, especially when the economy is largely informal.

The unconditional basic income: a hopeful horizon

Given these difficulties intrinsic to the means test, many have been driven into taking seriously, and sometimes advocating, universal schemes, i.e. schemes that are not targeting the poor but distribute benefits to the rich and the poor alike. This is where the reflection on the experience of conditional cash transfers meets the contemporary discussion on the idea of an unconditional basic income, i.e. an income that is strictly individual (i.e. not household-tested), universal (i.e. not means-tested) and obligation-free (i.e. not work-tested). Obviously, the management of a universal basic income does not face the unsolvable problem of implementing a reliable yet affordable income test in an informal economy. At least in circumstances in which everyone has access to a bank account, it can easily attain a very high rate of take up among the poor because of automatic payments that demand little information on the part of the beneficiaries and involve no stigmatization. And it gets rid of the poverty trap, since a basic income is combinable with earnings without any limit in terms of either duration or amount.

Introducing such a basic income would amount to a major innovation in the domain of social protection or basic economic security, a third model irreducible to public assistance to the poor (born at the beginning of the 16th century) and to social insurance between workers (born at the end of the 19th century): a social dividend distributed equally among all citizens. But it would be compatible, even in the long term with top-ups belonging to these other two models: social assistance to people with special needs — like Egypt's Karama scheme — and earnings-related unemployment benefits, work injury or old age social insurance, whether compulsory or voluntary, paid for by payroll taxes, of a sort that also exists in Egypt. And it can easily be understood as a logical cash complement to free universal primary and secondary education and to a universal health care system of the sort that Egypt intends to expand and improve.

A frequent but superficial objection to a universal basic income is that it is absurd to make the rich richer by paying them the same benefits as the poor. The obvious answer is that the scheme needs to be financed, and that the rich will pay for their own basic income. In countries with a developed income tax system, the simplest way of conceiving the funding of a universal basic income is by coupling its introduction with a reduction of all existing benefits by the amount of the basic income (and the scrapping of any lower benefit), the suppression of the tax exemptions on the lower tranches of every taxpayer's income (which would henceforth be taxed from the first unit earned at the a marginal rate of 30 or 40% that currently applies to workers at the minimum wage or slightly above), and some adjustment of the tax rates on higher incomes so as to cover the net cost. However, there are other possible sources of funding. In Alaska, where a very modest basic income (on US standards) has been in place since 1982, the scheme is funded by part of the return on a fund created out of the revenues from oil. Of more general relevance — and actually advocated from Switzerland to South Africa — is the idea of funding the basic income by a consumption tax, in particular the Value Added Tax commonly used in European countries. And there are a number of more speculative ideas floating around, such as a micro-tax on all electronic payments. Whatever form of taxation is used, a universal basic income, though paid also to the rich, will operate, like means-tested schemes, as a redistribution from the rich to the poor.

Of course, the funding of a significant basic income is more easily achievable when the country's fiscal system is able to capture, whether at the point at which it is earned or at the point at which it is spent, the bulk of a country's national income. This is not the case in countries, such as Egypt, in which there is a large informal economy. But even in these countries, some very modest basic income could be funded thanks to the scrapping or phasing out of in-kind benefits or subsidies that involve a lot of waste and/or create perverse economic incentives and/or benefit more than proportionally the richer households. This option is actively discussed in India. It is also relevant to Egypt. With a low level of benefit, however, there is a risk that the administrative cost of channeling the benefits to the beneficiaries would absorb an unreasonably large share of the budget. Universal access to a bank account is a necessary but not a sufficient condition. The ongoing experience with means-tested cash transfers should both help identify what other conditions need to be satisfied and contribute to their satisfaction.

With this qualification in mind, it remains true to say that the anti-poverty policies of countries with a large informal economy face a dilemma between means-tested schemes that have difficulty tracking accurately the households with an income below the stipulated threshold and universal schemes that have difficulty catching the broad tax base they need in order to be sustainable. An unconditional basic income would have the advantage of addressing head on both of the intrinsic defects of means-tested schemes, it could attain with far less effort a very high rate of take up among poor households and it would reduce or even abolish the poverty trap. Except under conditions under which it could be funded from an exogenous source — such as the oil resources of the gulf states —, a sufficiently extensive formalization of the economy is a precondition for its viability. In the meanwhile, the advantages it enjoys over means-tested schemes are out of reach. But it can remain a useful horizon that helps make sense of any step taken in the direction of relatively generous and inclusive conditional cash transfer schemes. It must be possible to entertain the realistic dream of a society that does more than attempt to provide stigmatizing aid to those its economy does not manage to feed. Basic income is a core component of that dream. It is far more than a more efficient way of tackling poverty.

To understand this, it is important to bring in the other two unconditionalities — next to universality or the absence of a means test — that distinguish a basic income from existing conditional minimum income schemes. One is its strictly individual character: it is not the head of the household who receives it, but each of its adult members, and its level is not lower if one lives as a member of a multi-adult household than if one lives alone. The other is the absence of a work test: the basic income is not restricted to people willing to take paid employment. These two features are essential for making basic income a tool for the redistribution of bargaining power, not only for the redistribution of purchasing power. In particular, if the obligation to accept any job and to stick to it, however lousy, was imposed as a condition for the entitlement to a universal benefit, the latter would de facto function as a subsidy to employers. Employers could get away with paying lower wages to the working poor because a subsistence income would be paid to them by the state. But a basic income is not only meant to make it easier to say "yes" to some jobs or to start one's own business, owing to its being universal, i.e. its being combinable with earnings. It is also meant to make it easier to say "no" to other jobs or to reduce one's working time, owing to its being "obligation-free, i.e. its involving no restriction to those willing to work, let alone to those willing to work full time. In other words, it aims at abolishing, or at least at reducing dramatically, both the (involuntary) unemployment trap and the (lousy) employment trap.

This is what makes a basic income not only, like conditional cash transfers, an important instrument for the alleviation of poverty, but also a key institution for a free society and a sane economy. To Egypt like to any country in the world, it offers the prospect of helping to tame the dynamics of capitalism in such a way that the real freedom of those with least of it is boosted, without destroying our planet in the process.

Further reading:

Hanna, Rema & Benjamin A. Olken. "Universal basic incomes versus targeted transfers. Anti-poverty Programs in developing countries", Cambrige (Mass.): National Bureau of Economic Research, Working Paper 24939, August 2018, 33p.

Van Parijs, Philippe & Yannick Vanderborght. *Basic Income. A radical proposal for a free society and a sane economy*. Cambridge (Mass.): Harvard University Press, 2017, 384p. (Has been translated into Chinese, French, Italian, Korean, Portuguese and Spanish.)

Both items contain extensive bibliographies