Over the past two decades, donors and development aid agencies alike have invested heavily in participatory development. The World Bank alone has allocated almost $85 billion to participatory projects and decentralization efforts. Other development agencies—bilateral donors and regional development banks—have probably spent at least as much. Driving this massive injection of funding has been the underlying belief that involving communities in at least some aspects of project design and implementation creates a closer connection between development aid and its intended beneficiaries. Indeed, local participation is proposed as a method to achieve a variety of goals, including sharpening poverty targeting, improving service delivery, expanding livelihood opportunities, and strengthening demand for good governance.

The purpose of participatory programs is to enhance the involvement of the poor and the marginalized in community-level decision-making bodies in order to give citizens greater say in decisions that affect their lives. In practice, little is known about how effective participatory development approaches are in promoting equity. Do these programs result in choices that are better aligned with the preferences of the poor and the socially excluded? Do they produce more resilient and inclusive local institutions? Do they reduce capture by the elites and corruption? Do participatory projects face greater challenges in some types of communities? In particular, is local inequality in wealth, status, or power a significant barrier to inclusion? These questions are at the heart of the forthcoming World Bank Policy Research Report. This article briefly summarizes the evidence on these questions that are central to the policy debate.

This article is based on “Localizing Development: Does Participation Work,” a World Bank Policy Research Report to be published in November 2012, Ghazala Mansuri and Vijayendra Rao, authors.
nicipal governments on both the demand and supply sides. On the demand side, decentralization strengthens citizens’ participation in local government by, for example, instituting regular elections, improving access to information, and fostering mechanisms for deliberative decision making. On the supply side, it enhances the ability of local governments to provide services by increasing their financial resources, strengthening the capacity of local officials, and streamlining and rationalizing their administrative functions.

This note and the report on which it is based focus on the “demand-side” aspects of participatory development. Important “supply-side” aspects of governance (fiscal decentralization, taxation policy, local government procedures, and bureaucratic inefficiency) have been dealt with extensively elsewhere and are beyond the scope of this work.

The History of Participatory Development

Participatory development and decentralization have common intellectual origins. Deliberative decision making has been a central feature of most religious and cultural traditions. In Athenian democracy, for example, important decisions were made in public deliberative settings in which all citizens (a group that excluded all women, slaves, and children) were expected to participate. Modern notions of participation arguably derive from the eighteenth and nineteenth centuries, notably from the work of Rousseau and John Stuart Mill.

In the early postcolonial period, the 1950s and 1960s, the U.S. Agency for International Development (USAID) and other donors helped drive the first wave of interest in participatory development by funding and promoting cooperative institutions, community-based development, and decentralization. By the 1970s, however, interest in participatory development had waned with the realization that cooperatives had largely failed and government reform was difficult to implement or sustain. The focus of policy shifted to large-scale investments in agricultural and industrial growth. By the mid-1980s, however, activists and scholars attacked this approach, seeing it as “top-down” and inherently disempowering and biased against the interests of the poor. Economists such as Nobel laureates Amartya Sen and Elinor Ostrom made a vigorous case for a more bottom-up and deliberative vision of development that allows the “common sense” and “social capital” of communities to play a central part in decisions that affect them. Their scholarship led to renewed interest in community-based development, decentralization, and participation by donors and governments. As the increased inequity and social costs of structural adjustment programs became evident by the early 1990s, donors began to actively fund such participatory approaches, with the aim of ensuring minimal levels of investment in public services and infrastructure and in social programs to protect the most vulnerable.

This renewed policy interest in participatory initiatives, along with the expansion in funding, has proceeded, in large part, with little systematic effort to understand the particular challenges entailed in inducing participation or to learn from the failures of past programs. As a result, the process is, arguably, still driven more by ideology and optimism than by systematic analysis, either theoretical or empirical.

Does Participatory Development Benefit the Poor and the Socially Excluded?

On balance, greater community involvement seems to modestly improve resource sustainability and infrastructure quality. But the evidence suggests that people who benefit tend to be the most literate, the least geographically isolated, and the most connected to wealthy and powerful groups. This picture may partly reflect the higher opportunity cost of participation for the poor. It also appears, however, that the poor often benefit less from participatory processes than do the better off, because resource allocation processes typically reflect the preferences of elite groups. Participation thus appears to affect the distribution of benefits in ways that suggest that “elite capture” is often not benevolent or altruistic.

Studies from a variety of countries show that communities in which inequality is high have worse outcomes, especially where political, economic, and social power are concentrated in the hands of a few. “Capture” also tends to be greater in communities that are remote from centers of power; have low literacy; are poor; or have significant disparities in caste, race, or gender.

Project design and implementation rules play a critical role in determining whether participatory programs are captured by elites and thus hinder opportunities for the poor.

For many years, willingness to contribute to programs and projects has been seen as evidence of commitment and of the sustainability of programs or of infrastructure. But this belief has little basis in evidence. What little is known suggests that cofinancing—the sine qua non of participatory projects—tends to exclude the poorest, particularly when individuals or communities self-select into a program. Evidence also suggests that cofinancing requirements for local governments can widen horizontal inequities in targeted transfer programs, because poorer municipalities or counties have an incentive to reduce the poverty threshold for transfer eligibility in order to reduce their own copayment burden. Demand-driven, competitive application processes can also place a greater burden on the weakest communities, which might self-select out of the program, exacerbating exclusion.

Policy design may also have unintended consequences on equity. A large injection of resources for a participatory development project can, for example, attract the attention of the better off, making exclusion more likely. Participatory projects also often fail to build cohesive and resilient organizations. During the course of a project, cash or other material payoffs induce people to participate and build networks—but these mechanisms tend to
dissolve when the incentives are withdrawn. Only when projects explicitly link community-based organizations with markets, or provide skills training, do they tend to improve group cohesion and collective action beyond the life of the project.

Spending decisions do seem to be better aligned with local needs under democratic decentralization, and resources are reallocated in favor of the less advantaged. But much depends on the nature of electoral incentives and the capacity of higher levels of government to provide oversight and ensure downward accountability.

Capacity also matters. The benefits of decentralization seem to be weaker in more remote, more isolated, and less literate localities. Such localities also tend to be more poorly served by mass media and other sources of information, and they are less likely to have adequate central oversight.

**Does Participation Strengthen Civil Society?**

There is little evidence that induced participation builds long-lasting cohesion, even at the community level. Group formation tends to be both parochial and unequal. Absent some kind of affirmative action program, groups that form under the aegis of interventions tend to systematically exclude disadvantaged and minority groups and women. Moreover, because similar types of people tend to form groups with one another, projects rarely promote cross-group cohesion—and may actually reinforce existing divisions.

An important question in this context is the role of facilitators who work with communities. The evidence on this issue is scant, but the few studies that have tried to measure their effects find that facilitators strongly influence the stated preferences of community members, who often tell facilitators what they think they want to hear.

Participation often tends to be driven by project-related incentives; people get together to derive benefits from project funds. It is very difficult to know whether these effects will last beyond the tenure of the project and the limited evidence indicates that it usually does not. There is some heartening evidence, though, that participation may have intrinsic value. Communities tend to express greater satisfaction with decisions in which they participate, even when participation does not change the outcome or when outcomes are not consistent with their expressed preferences.

The ballot box, though far from perfect, appears to provide a clearer mechanism for sanctioning unpopular policy choices or excessive rent seeking by traditional or political elites than more informal forums for deliberation. In decentralized settings, credible and open elections help align the decisions of politicians with the demands of their constituents. When participatory and deliberative councils exist in such settings, they can foster a significant degree of civic engagement. It is less clear how citizens can collectively sanction negligent or corrupt officials or local leaders where such venues for the exercise of voice are not available.

Repairing civic failures requires that social inequalities be addressed. One way of trying to do so is to mandate the inclusion of disadvantaged groups in the participatory process. There is virtually no evidence from evaluations of community-driven development projects on whether such mandates work. However, a growing body of evidence from village democracies in India shows impacts that are mixed but broadly positive. Quotas in village councils and presidencies for disadvantaged groups and women tend to change political incentives in favor of the interests of the group that is favored by the quota.

Mandated inclusion also appears to provide an incubator for new political leadership. Evidence indicates that women and other excluded groups are more likely to run for non-mandated seats once they have had some experience occupying a mandated seat. Quotas can also weaken prevailing stereotypes that assign low ability and poor performance to traditionally excluded groups. However, lasting change requires that the inclusion mandates remain in place long enough to change perceptions and social norms.

Democratic decentralization works because village and municipal democracies incentivize local politicians to nurture their constituencies. Because decentralized programs usually come with a constitutional mandate or other legal sanction from the center, they are relatively permanent and can therefore change social and political dynamics over the long term. In contrast, community-based projects are usually ad hoc interventions that are unable to open political opportunities for real social change and inclusion.

Participatory interventions have been used in post-conflict settings as a quick way of getting funds to the ground. The limited evidence of their effectiveness suggests that such projects have made little headway in building social cohesion or rebuilding the state. However, evidence from Africa seems to suggest that people emerging from civic conflict have a strong desire to participate in their communities and that well-designed and -implemented projects could draw on this need.

In sum, the evidence suggests that, although local actors may have an informational and locational advantage, they use it to the benefit of the disadvantaged only where institutions and mechanisms to ensure local accountability are robust. Local oversight is most effective when other, higher-level institutions of accountability function well and communities have the capacity to effectively monitor service providers and others in charge of public resources. Local participation appears to increase, rather than diminish, the need for functional and strong institutions at the center. It also implies that implementing agencies for donor-funded projects need to have the capacity to exercise adequate oversight. There is little evidence that they can substitute for a nonfunctional state as a higher-level accountability agent, however. Reforms that enhance judicial oversight, allow for independent audit agencies, and protect and promote the right to information and a free media appear to be necessary for effective local oversight.
Policy Implications for the Evidence

Three main lessons emerge from distilling the evidence and thinking about the broader challenges in inducing broad-based participation that promotes equity.

1. **Induced participatory interventions work best when they are supported by a responsive state.** The state does not necessarily have to be democratic—though being democratic helps a great deal. But in the sphere in which the intervention is being conducted—at the level of the community or the neighborhood—the state has to be responsive to community demands.

   Parachuting funds into communities without any monitoring by a supportive state can result in the capture of decision making by elites who control the local cooperative infrastructure, leading to a high risk of corruption. In the absence of a supportive state, participatory engagement might still be able to make a difference, but projects implemented in such environments face much greater challenges and higher risks of increasing inequities.

2. **Context, both local and national, is extremely important.** Outcomes from interventions are highly variable across communities; local inequality, history, geography, the nature of social interactions, networks, and political systems all have a strong influence. Local inequality is particularly important in determining the likelihood of capture. The variability of these contexts is sometimes so large, and their effect so unpredictable, that projects that function well usually do so because they have strong built-in systems of learning and great sensitivity and adaptability to variations in context.

3. **Effective civic engagement does not develop within a predictable trajectory.** Instead, it is likely to proceed along a “punctuated equilibrium,” in which long periods of seeming quietude are followed by intense, and often turbulent, change. Donor-driven participatory projects often assume a far less contentious trajectory. Conditioned by bureaucratic imperatives, they often declare that clear, measurable, and usually wildly optimistic outcomes will be delivered within a specified time frame. There is a danger that such projects set themselves up for failure that derives not from what they achieve on the ground but from their unrealistic expectations.

One important reason for this overly ambitious approach is that many donors’ institutional structure continues to derive from a focus on capital-intensive development and reconstruction. Building dams, bridges, and roads, or even schools and clinics, is a much more predictable activity than changing social and political systems. Repairing civil society and political failure requires a shift in the social equilibrium that derives from a change in the nature of social interactions and from modifying norms and local cultures. These much more difficult tasks require a fundamentally different approach to development—one that is flexible, long term, self-critical, and strongly infused with the spirit of learning by doing.

Enhancing the Redistributive Role of Fiscal Policy in Developing Economies

Francesca Bastagli, David Coady, and Sanjeev Gupta

Past contributions to *Inequality in Focus* have highlighted how income inequality has increased in many countries worldwide over recent decades. Advanced countries clearly have been able to tackle high inequality better than developing countries. A key factor in explaining this difference is the greater redistributive impact of fiscal policy in advanced countries.

In a recent paper, we reviewed evidence on the redistributive impact of fiscal policy in both advanced and developing countries (Bastagli, Coady, and Gupta, 2012). We assembled a comprehensive database on trends in disposable (i.e., post-tax-and-transfer) income inequality in 150 advanced and developing countries. These data confirm that inequality of disposable income has indeed increased in most advanced and many developing countries over recent decades. They also show that there is greater inequality in developing countries than in advanced economies.

Inequality trends between 1990 and 2005 are especially enlightening because data are available for a large sample of advanced and developing countries. Our analysis uses the Gini coefficient, a commonly used inequality measure, which runs from 0 (where everyone in the economy has the same income) to 1 (where one person has all the income). In most countries, the Gini is between 0.25 and 0.6. The data, shown in
Table 1: Changes in Disposable Income Inequality Across Regions, 1990–2005

(Percentage-point change in Gini coefficient)

<table>
<thead>
<tr>
<th>Region</th>
<th>Change</th>
<th>Large Increase (Change ≥ 5)</th>
<th>Medium Increase (3 ≤ Change &lt; 5)</th>
<th>Small Increase (0 &lt; Change &lt; 3)</th>
<th>Small Decrease (-3 &lt; Change &lt; -5)</th>
<th>Medium Decrease (-5 &lt; Change ≤ -3)</th>
<th>Large Decrease (Change ≤ -5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Latin America and Caribbean</td>
<td>1990-2005</td>
<td>Colombia, Honduras, Paraguay, Venezuela</td>
<td>Bolivia, Costa Rica, Uruguay</td>
<td>Argentina, Dominican Republic, Guatemala, Jamaica</td>
<td>El Salvador, Panama</td>
<td>Brazil, Chile, Ecuador, Nicaragua, Peru</td>
<td>Belize, Mexico</td>
</tr>
<tr>
<td>Asia and Pacific</td>
<td>1990-2005</td>
<td>China, Indonesia, Rep. of Korea, Lao PDR, Nepal, Sri Lanka</td>
<td>Bangladesh, Cambodia, Taiwan</td>
<td>India, Mongolia, Philippines, Vietnam</td>
<td>Thailand</td>
<td>Malaysia</td>
<td></td>
</tr>
<tr>
<td>Middle East and North Africa</td>
<td>1990-2005</td>
<td>Kyrgyz Republic, Tajikistan, Turkmenistan, Uzbekistan</td>
<td>Djibouti</td>
<td>Egypt, Mauritania, Morocco, Tunisia</td>
<td>Pakistan</td>
<td>Iran, Jordan</td>
<td></td>
</tr>
<tr>
<td>Emerging Europe</td>
<td>1990-2005</td>
<td>Belarus, Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Kazakhstan, Latvia, Lithuania, Macedonia, Moldova, Poland, Ukraine</td>
<td>Albania, Georgia, Russian Federation</td>
<td>Azerbaijan, Hungary, Serbia, Slovenia, Turkey</td>
<td>Armenia, Estonia</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Advanced Countries</td>
<td>1980-2005</td>
<td>New Zealand, Norway, Portugal, United Kingdom, United States</td>
<td>Austria, Belgium, Canada, Finland, Germany, Luxembourg, Sweden</td>
<td>Australia, Italy, Japan, Netherlands, Spain, Denmark, France, Greece, Ireland</td>
<td>Switzerland</td>
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</tr>
<tr>
<td></td>
<td>1990-2005</td>
<td>Norway, Portugal, United States</td>
<td>Belgium, Canada, Finland, Germany, Italy</td>
<td>Austria, Japan, Luxembourg, New Zealand, Spain, Sweden, United Kingdom</td>
<td>Australia, Denmark, France, Greece, Ireland, Norway, Netherlands</td>
<td>Switzerland</td>
<td></td>
</tr>
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Table 1, confirm that large increases in income inequality have been observed in all regions:

- **Advanced Economies:** Inequality increased in 15 of 22 advanced countries. The Gini coefficient increased by more than 3 points in eight countries. This followed increases in equality in most countries over the previous decade.
- **Emerging Europe:** Inequality increased in virtually all (20 of 22) Emerging European countries. Most of this increase happened between 1990 and 1995, during the transition to a market economy. The Gini coefficient increased by more than 3 points in 15 countries and by more than 5 points in 12 countries.
- **Latin America and the Caribbean:** Inequality in this region has been substantially higher than in most other regions. Over this period, inequality increased in 11 of 20 countries, and the Gini increased by more than 3 points in seven countries. However, nearly all countries in the region have experienced a decrease in inequality since 2000.
- **Sub-Saharan Africa:** This was the only region where average inequality decreased over the whole period. Still, the Gini coefficient increased in 10 of the 26 countries, rising by more than 3 points in seven countries.
- **Asia and the Pacific:** Inequality increased in 13 of 15 countries in the region. The Gini coefficient increased by

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more than 5 points in six countries (including China) and by more than 3 points in nine countries.

• Middle East and North Africa: Inequality increased in nine of 12 countries in the region. The Gini coefficient increased by more than 5 points in four countries and by more than 3 points in 5 countries.

However, possibly the most striking message is the enormous difference in inequality between advanced and developing countries, which is substantially larger than changes in average regional inequality over time. Between 1990 and 2005, average inequality in each region changed by less than 4.5 percentage points. In contrast, while average inequality in the two most unequal regions (Sub-Saharan Africa and Latin America) exceeded a Gini of 0.45 every year, average inequality in the two most equal regions (Emerging Europe and Advanced Economies) was less than 0.34, a difference of 11 percentage points.

Differences in the redistributive impact of fiscal policy explain the bulk of the differences in inequality between these regions. The different role of fiscal policy in advanced countries, compared to fiscal policy in developing countries, provides a basis for identifying inequality-reducing fiscal reforms in the latter.

The Redistributive Impact of Fiscal Policy in Advanced Countries

Taxes and public transfers have played a significant role in offsetting the increase in inequality in advanced countries. Over the past two decades, fiscal policy decreased inequality by about one-third in OECD countries.

Although income taxes are important in many economies, most redistribution in OECD countries is achieved through the expenditure side of the budget, especially via non-means-tested transfers (including public pensions and universal child benefits). On average, the redistribution achieved by public cash transfers is twice as large as that achieved through taxes. On the tax side, personal income taxes achieve the greatest amount of redistribution.

The redistributive impact of fiscal policy is even higher if in-kind transfers, such as public education and health spending, are included. The Gini coefficient for disposable income decreases by as much as another 6 points when these are taken into account. Indirect taxes, on the other hand, are typically highly regressive. The effective indirect tax rate, calculated as the share of consumption taxes in total household income, is on average, three times higher for low-income families than it is for those in the top decile of the income distribution.

The Limited Redistributive Impact of Fiscal Policy in Developing Economies

Fiscal policy plays a much more limited role in reducing inequality in developing economies. Their higher income inequality is often explained by lower levels of taxation and public spending, as well as a greater reliance on less progressive tax and spending instruments.

Average tax ratios for advanced economies exceed 30 percent of GDP. Ratios in developing countries generally fall in a range from 15 to 20 percent of GDP. Consequently, spending is also substantially lower in developing countries. This is especially true in Asia and the Pacific and in Sub-Saharan Africa, with low transfer spending explaining most of the difference.

Three-quarters of the difference in disposable income
inequality between Latin America, the region with the most unequal distribution of income in the world, and advanced countries can be explained by fiscal policy. Six Latin American economies (Argentina, Brazil, Chile, Colombia, Mexico, and Peru), have fiscal policies that reduce income inequality by only about 2 percentage points, from 0.52 to 0.50. This compares to a decrease of about 20 percentage points in 15 European economies, from 0.46 to 0.27.

Low tax and spending levels are compounded by a heavy reliance on regressive tax instruments as well as by the low coverage and benefit levels of transfer programs.

- **Indirect Taxes**: Greater reliance on indirect taxes and narrower consumption tax bases limit the redistributive potential of taxes in developing countries. These taxes have only a small progressive impact on income inequality in developing countries. Taxes on imports, which continue to be important in low-income economies, often appear to be among the most regressive, while excise taxes—such as those on fuel, alcohol, and tobacco—tend to be progressive. Although the distributive impact of value-added taxes is mixed, there is strong evidence that the exemption of small businesses (including agriculture and the informal sector) can lead to more progressive incidence.

- **Direct taxes**: Personal income and property taxes in developing countries are generally progressive. However, high levels of tax noncompliance combined with narrow income tax bases can contribute to low income tax ratios and low income tax progressivity. Often this results due to widespread exemptions and the preferential treatment of capital and other income. Resource taxation can be progressive as well as efficient, though it is applied mostly to foreign incomes.

- **Expenditures**: Low spending and poor targeting limit the redistributive capacity of transfer programs. A large informal sector further complicates the development of such programs. In most developing economies, participation in social insurance schemes is restricted to high-income workers in the formal sector and to public sector employees. In the early 2000s, the share of the population above the legal retirement age in receipt of a pension in developing countries was, on average, about 40 percent. This compares to 90 percent in European countries. In addition, expenditure on social assistance programs is often low and poorly targeted. Moreover, the fiscal space for expanding more distributive social transfers is constrained by large expenditures on regressive universal price subsidies, especially energy price subsidies.

In-kind public spending has been found to be regressive in many developing countries, although individual components can be progressive. This regressivity reflects lack of access by low-income households to key public services such as education and health. Aggregate education and health spending is regressive in many developing economies, especially in low-income countries, as shown in figure 1. The progressivity of primary health care spending is dominated by the regressivity of higher-level health spending. The progressivity of primary education spending is dominated by the regressivity of secondary and tertiary education spending. However, future in-kind spending increases to finance the expansion of basic education and health services in developing countries are likely to be much more progressively distributed.

The recent expansion of “conditional cash transfer” programs provides a promising approach for enhancing the distributive power of public spending in developing countries. These programs target income transfers at poor households and continued receipt of the transfer occurs only if households invest in the education and health of family members. These programs have been adopted in many developing countries, including some low-income African countries, albeit on a smaller scale. Roughly 17 economies in Latin America are currently operating conditional cash transfer programs. Typically program expenditures fall below 1 percent of GDP. The largest programs, in Brazil and Mexico, have reduced the Gini for disposable income by 2.7 points. These programs alone have accounted for about a fifth of the recent decreases in inequality. However, these programs are most cost-effective when targeted at the poorest households, which tend to be most disadvantaged in terms of human capital. Thus, expansions need to be carefully designed in order to continue to generate human capital impacts and avoid labor supply disincentives.

**Enhancing the Redistributive Role of Fiscal Policy in Developing Economies?**

The challenge in developing countries is to enhance the redistributive role of fiscal policy, while also promoting growth and maintaining fiscal sustainability. This requires strengthening the resource mobilization capacity of governments. But it equally requires the development of more comprehensive social protection systems, including better-targeted safety net programs.

Tax policy should focus more on broadening tax bases rather than increasing tax rates. Expanding corporate and personal income tax bases by reducing tax exemptions, closing loopholes, and improving tax compliance can raise revenues to finance progressive transfers. Expanding the consumption tax base (e.g., through broader adoption of the value-added tax) can increase tax revenues. These consumption taxes can be designed to mitigate adverse distributional impacts (e.g., through appropriate treatment of small businesses and the application of excise taxes to luxury goods). In many countries, eliminating
fiscally costly universal price subsidies, which are typically both inefficient and inequitable, can generate substantial resources in the short term. Especially important are energy subsidies, including tax subsidies (i.e., forgone tax revenues), which can escalate to very large percentages of GDP when international energy prices rise sharply.

However, continued tight revenue constraints and the large demands on these resources to finance broader development objectives means that greater emphasis will need to be placed on improving the progressivity of public spending. This can be achieved through greater reliance on better-targeted social expenditures aimed at protecting households from poverty and improving education and health outcomes among disadvantaged households. But it is also important that these social programs are monitored and implemented carefully to ensure that resources reach their intended beneficiaries.

Development of effective social protection systems can help promote tax reform and, more generally, structural reforms. Such reforms, even when well designed, can have an adverse impact on poverty and income distribution, and this has been a deterrent to reform in many countries. Increasing progressive public expenditures can help foster political support for reforms. Expanding targeted safety net programs can help reduce poverty, while expanding education, health and physical infrastructure programs can also benefit middle- and upper-income groups, promote growth, and thus broaden political support. The recent success of conditional cash transfer programs in many economies suggests that these programs should play a greater role in the social protection strategies in developing countries. Broadening the coverage of public pension systems would also play an important role in reducing inequality. Where their expansion is constrained over the short term by administrative capacity and fiscal constraints, greater use of targeted social pensions may be warranted.

Reference