Social Protection Discussion Paper Series

A Lecture on the Political Economy of Targeted Safety Nets

by Lant Pritchett

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A Lecture On The Political Economy of Targeted Safety Nets

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Papers in the Safety Nets Primer as of July 2004[1]

Theme	Author
Program Interventions	
Cash Transfers	Tabor, Steve
Community-based Health Insurance	Tabor, Steve
Conditional Cash Transfers	Rawlings, Laura
Fee Waivers in Health	Bitran and Giedion
Fee Waivers in Housing	Katsura and Romanik
Food Related Programs	Rogers and Coates
Micro Credit and Informal Insurance	Sharma and Morduch
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Political Economy Aspects of Targeting	Pritchett
Public Attitudes and Political Economy	Graham, Carol
Safety Nets for Poverty Reduction	Ravillion
Targeting	Coady, Grosh and Hoddinott
Country Setting/Target Group	
Poverty and Aging in Africa	Subbarao, Schwartz and Kakwani
Transition Economies	Fox
Very Low Income Countries	Smith and Subbarao

1. Papers may be added or deleted from the series from time to time.

Abstract

This paper is the written version of a lecture that draws principally on my own research on safety nets and on my operational experience with the implementation of safety nets, drawing heavily on the crisis safety net programs in Indonesia from 1998 to 2000. As such it provides more *views* than *reviews of the literature* on the principal issues in the political economy of targeted safety net programs. Moreover, in keeping with the lecture format, the text is followed by a Q&A that clarifies (and perhaps tempers) views put perhaps too starkly in the text.

Five major issues are reviewed. First, the implications of some simple models of electoral politics which make the budget allocated to programs endogenous to their targeting design highlight the dangers in ignoring political economy. Second, the political economy of "safety net" versus "safety rope" programs is reviewed. Third, some of the literature on the perception of fairness of the targeting criteria is reviewed. Fourth, the issue of local versus central targeting of programs is discussed. Fifth, the political economy of program implementation that considers the fit between program targeting and the organizational culture of the implementing organization is considered.

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A Lecture on the Political Economy of Targeting Safety Nets[1]

Introduction

During the 1995-96 debate over the federal budget in the USA, the question of whether to means test Medicare (a health insurance program for the aged) benefits was raised. Representative Charles Rangel, a liberal Democrat who represents Harlem, a predominantly African American and poor district, argued *against* targeting. As the proposal was to trim the benefits of those households with incomes over $200,000 this was defending the view that the rich should continue to receive exactly the same benefits as the poor. Speaker of the House Newt Gingrich, a conservative Republican from an prosperous Georgia suburb, argued *in favor* of targeting Medicare benefits. He argued that the rich should receive *less* generous benefits than the poor. At first glance, such a situation seems a curious political inversion: one politician who regards himself as the defender of his poor constituents arguing *in favor* of spending on the rich, while a politician usually associated with defending the interests of the wealthy arguing *against* spending reaching the rich. Moreover, such political behavior seems to contradict both common sense and a fair bit of economics. Common sense suggests that fewer people sharing the pie, means larger slices: means-testing, or targeting, means more for the poor.

So what is it that an experienced politician like Rangel knows that traditional, non-political models and common sense do not capture? Why is it often said among policymakers that "programs for the poor are [budget] poor programs?" As political scientists, politicians and policymakers suspect, the size of the pie is unlikely to be fixed. If the budget for redistribution is politically determined, the impact of targeting on the poor cannot be determined by a technocratic evaluation of the hypothetical impact of a given targeting design alone; it must account for the effect of changes in the degree of targeting on the size of the budget available for redistribution. It is possible that "more for the poor is less for the poor" and that the less well targeted program will deliver greater benefits for the poor. Whether or not this will be the case in any given situation depends on the concrete realities of the political economy—which depends on many features.

There are three elements of **policy design** and achievable gains take place at the intersection of these elements.

Figure 1: Three Elements of Policy Design

Technically Correct

Achievable Gains

Administratively Feasible

Politically Supportable
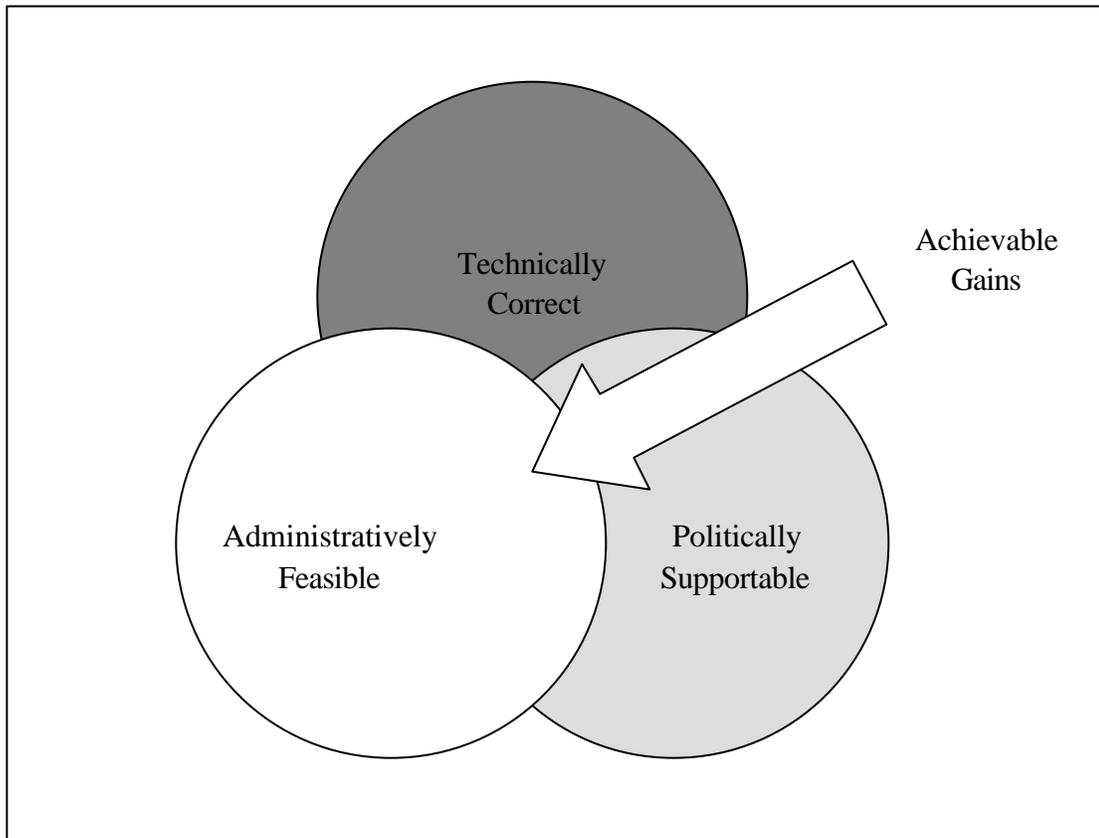
While the elements of *technically sound* and *administrative feasibility* are often addressed when designing policy, the *politically supportable* aspect is often underestimated or not considered at all.

This lecture will therefore focus on the importance of political supportability in designing safety net policies—not because it is the only, or even most important issue—but rather because this lecture has been given as part of an overall course that treats the other issues in some detail.

The rest of the paper will discuss each of the five dimensions of politically supportability[2].

- Section 1: Models of electoral politics.
- Section 2: Safety ropes vs. safety nets?
- Section 3: The role of perceptions of fairness
- Section 4: Reconciling central and local control of targeting.
- Section 5: The "organizational" politics of implementation.

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[2] We warn the reader up front that while this paper reviews the literature, the review leans heavily on the authors own work, both on the theory (principally with Jonah Gelbach) and on the practice (drawing on the author's experience with the crisis safety net programs in Indonesia).

Section I: A simple model of the electoral politics of targeted programs[3]

       In this section, I review models of two types. The first focuses on "indicator" targeting and discusses the basic structure and intuition of targeting models. The second section is a model of more general targeting which illustrates the dangers of ignoring the *political* economy.

I.A. Indicator targeting

       In less developed countries, policymakers sometimes cannot observe income among the poor.   One oft-proposed approach to redistribution is indicator targeting: targeting transfers on correlations between income and "indicators" like geography, gender or occupation. In a world of scarce resources for redistribution, dialogues like the following between a Technocrat Economist working on Design (TED) and a Policymaker Anxious about Targeting (PAT) are common:

TED: The current incidence of benefits from expenditures on program X is at best only modestly progressive. If we restrict X spending to the poor, we can reduce poverty and save money.

PAT: But the administrative costs of identifying the poor correctly would be prohibitive, and even if we had such information, what about incentive distortions?

TED: Don't worry if we can't observe actual income, we can find easily observable income indicators – like region of residence, economic sector, or ethnic background – that we can use to target income transfers to those most likely to need them. We can still do more with less.

PAT: But you assume that the budget will remain fixed. If I narrow the incidence by concentrating spending on targeted households, I also narrow the program's constituency. In fact, the ultimate outcome will be further cuts in the budget that wipe out any efficiency-related gains in poverty reductions from targeting. Even with a larger share of spending going to the poor, the absolute magnitude will fall sufficiently to make the poor worse off.

Who is right, TED or PAT?

       The theoretical foundation for the technocrat economist's argument is straightforward and impeccable.   Indicator targeting is possible whenever some observable characteristic related to income is available to determine who will receive transfers. Indicator targeting is attractive for two reasons. First, targeting on observable characteristics avoids incentive problems that arise when transfers are conditioned on outcomes like income or employment[4]. Second, incomes in developing countries are administratively unobservable, especially for the poor.

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[3] This section draws heavily on Gelbach and Pritchett (2000) and Gelbach and Pritchett (2002).

[4] Akerlof (1978) was an early paper on the theory of indicator targeting and refers to this as "tagging".

But the policymaker's objections to the technocrat economist may have merit. The possibility that targeting transfers may affect their magnitude is not lost to economists, and concerns regarding political viability are frequently registered in discussions of the expected gains from targeting[5].

Gelbach and Pritchett (2000) build a simple model with four features.

First, there are three income groups: poor, middle and rich. There is an indicator that is correlated with poverty that can be used to target. With this target some of the poor get the transfer, but so also do some of the middle group, who happen to have the same "indicator"—for example, there are middle income people in poor regions. "Leakage" is the fraction of the targeted transfer that goes to the middle class.

Second, the model is such that maximizing poverty reduction from a *fixed* budget requires indicator targeting so that, absent political economy considerations, indicator targeting would be chosen.

Third, in the model the middle income group has good times and bad times. The political support for redistributive transfer from the middle income group depends on their demand for insurance—that is, as with any type of insurance, they view the value to them of a redistributive program lies in transferring income from good states to bad states (e.g. "unemployment").

Fourth, with this model Gelbach and Pritchett (2002) contrast two possible political equilibria with two types of policymakers. The first kind of policymaker we consider is "sophisticated" in the sense that she takes account of the politically driven budgetary endogeneity when choosing how much (if at all) to target the budget. The second kind of policymaker is "naïve" (as, we believe, is the literature to date): she chooses the degree of targeting under the (false) assumption that the budget for redistribution is fixed and then seeks to maximize social welfare by targeting the benefits to the poor.

When the policymaker takes account of political constraints, she can never do worse than when she behaves naively. The logic of this result is simple: any budget size and degree of targeting feasible for the naïve policymaker also are available to the sophisticated policymaker, while the converse is not true. So the first conclusion is obvious, but often ignored: a policymaker who accurately takes into account the reaction of voters to targeting can always do better than one who ignores electoral politics—even if the policymaker has no intrinsic concern for the middle class.

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[5] Glewwe (1990) reports that the outcome of the standard approach to indicator targeting, maximizing the poverty reduction achieved for a fixed budget, for urban *Cote d'Ivoire* is to give all the budget to households *born* in the East Forest Region. As Glewwe stresses, this example paints a particular stark picture of the fundamental political economy problem inherent in indicator targeting: it would be folly to even propose such a scheme to a policymaker, in spite of its apparent technocratic merits.

The second result in this simple model is that leakage is not necessarily bad for the poor—even from the point of view which considers *exclusively* the welfare of the poor there can be either "too much" or "too little" leakage. If one begins where leakage is "small" so that middle income agents are sufficiently unlikely to receive the targeted transfer[6], a shift towards more targeting of transfers can actually reduce the political support for the program enough to reduce the equilibrium welfare of the poor. So the poor are worse off from "better" targeting that reduces leakage. A leakier bucket may be better for redistribution of the poor.

But this result is not universal. If leakage is large so that middle income agents are very likely to receive the targeted transfer, then there is always some positive amount of targeting that will increase poor agents' utility in political equilibrium.

The main point of this model is that, while "leakage" is often discussed as if one wanted to eliminate it altogether, it is easy to construct models that explicitly bring in considerations of political economy in which *even from the point of view of the poor* more leakage is better.

I.B. Electoral politics and targeting

Standard economic analysis suggests that when the budget for redistribution is fixed, income transfers should be targeted to (i.e. means-tested for) those most in need. A large literature has considered informational constraints, incentive compatibility, and efficiency losses, but some degree of targeting is generally found to be optimal in the models examined.[7] However, both political scientists and economists long have recognized the possibility that targeting might undermine political support for redistribution.

Gelbach and Pritchett (2002) formalize this recognition, developing a simple economy in which both non-targeted (universally received) and targeted transfers are available for use by the policymaker. When the budget can be taken as fixed, full use of the targeted transfer is optimal. However, when we allow the budget to be determined through majority voting (with the policymaker choosing the share of the budget to be spent on each type of transfer), the optimal degree of targeting is *zero*.

More strikingly, GP show that in this model, if the policymaker consistently ignores political considerations, the resulting equilibrium actually *minimizes* the welfare of the poor. That is, a policymaker who was acting strictly in the interests of the poor and took "poverty reduction" as their sole objective but ignored electoral politics would not

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[6] What is "small" and "sufficiently unlikely" depends on a complex combination of parameters in the model.
[7] Examples in a variety of settings include Akerlof (1978), Atkinson (1995), Besley and Kanbur (1990), Diamond and Sheshinski (1995), Kremer (1997), Nichols and Zeckhauser (1982), Sen (1995), Stern (1982), and Viard (1996).

just not do the "optimal" thing for the poor—but would do the "pessimal" thing for the group they were trying to protect.

Even though this second result is particular to this model and a set of assumptions -- as is every other theoretical result – it is worth stressing because this implies that political considerations cannot generally be regarded as simply another small extension of standard models. That is, the literature often approaches the issues as if it were likely to be valid to take a sequential approach: first find the technocratically optimal design and then consider smallish changes to the design to accommodate politics. But in this model the technocratic approach doesn't need to be adjusted a bit—in fact it gets it exactly wrong and chooses not just not the best, but the worst possible policy.

It is important to note that this result is established in a highly stylized model and alternative models could also be used. But the force of the result, and the simple economic logic behind it, suggest that standard models of targeting likely are not robust to political considerations in a wider class of settings. It is worth noting that our model does yield optimality of targeting in the special case when political considerations do not matter. Thus it is *not the (modeling of the) economy*, but rather the *polity*, that drives our results. As a result, future models and actual policies advocating the use of targeting through means-testing should account explicitly for the role of political considerations.

I.B.1. A model of electoral politics and targeting

This subsection works through the details of one particular model, not so much because this particular model is canonical but rather to illustrate the features that any such model would have and the fundamental problem that is being modeled. To illustrate this combination of specific and general I present the model in a table, with commentary on each feature. Essentially any "optimal" targeting that takes political economy into account must have a model of the "budget response to targeting." My apologies to the lay reader, but I cannot make this any clearer without doing an injustice to the clear and careful theory my co-author Jonah Gelbach created, I think the main points come through even for those that do not read "economicsese".

Table 1: Structure of a simple model of targeting and electoral politics

Model of GP (2002)	Commentary
Population has *three types of agents*: *low income*, *middle income* and *rich*	To be interesting, a political economy model must have at least three groups. Two group models (e.g. "rich" and "poor") are both empirically unrealistic, but also do not generate interesting electoral politics. Models with a continuum have an infinite number of groups.
There are three types of jobs, each of which pays either a low wage, a medium wage or a high wage. An worker may work in a job paying less (to avoid taxes) but not more than his/her maximum marginal product.	A key issue of targeting is "incentive compatibility" so that workers will choose to work at their maximum marginal product. If the targeting schemes makes middle workers better off when "pretending" to be poor or to be unemployed this will make the equilibrium costly.
Poor and middle income agents have some probability p of being "unemployed" (having zero pre-transfer income) and probability q = 1 - p of being employed. Rich agents are always employed.	This feature introduces uncertainty. Without uncertainty the model hinges exclusively on the tension between desire of the middle class to "soak the rich" and the efficiency losses from excessive taxation.
Workers in jobs paying the low wage (the maximum for the poor) pay no taxes; by contrast, jobs paying the medium and high wage are taxable at the proportional rate . For heuristic purposes one can think of the medium and high as the "formal" sector.	Any model has to build in a structure of taxation. This assumption guarantees that the poor always favor more taxes while this, plus the above assumption that the rich are always employed, implies the rich always favor less taxes. This makes the middle group decisive on tax rates.
Two types of transfers are available: universal (each agent receives N dollars) and a targeted transfer for all low wage workers.	This creates two types of transfer, untargeted and targeted which means some structure of targeting has to be assumed.

This set up of the economy is specific, but perfectly standard. The principal task in the model is to investigate properties of political equilibria in a "game" played between a policymaker and the electorate. The strategy space for the policymaker is the distribution of the budget between universal (N) and targeted transfers, while the strategy chose for the electorate is the tax rate (and hence the budget).

We assume that the policymaker chooses a level of targeting, k, defined as the proportion of the budget devoted to the targeted transfer. After the policymaker proposes the degree of targeting an election is held to determine the level of taxation. The model requires that an equilibrium tax rate receives support from a majority of the population. In the present case, we will assume that no majority is possible without support from at least two types of agents. This assumption about voting powers of the three groups does not restrict the population shares, as it is possible that a given type of agent represents

more than half the population but for some reason has less than half the political power in society[8].

Define t*(k) as the tax rate that solves the middle group's optimization problem over the tax rate for any given level of targeting. On the other hand, because poor voters never pay taxes but always receive transfers, they must favor all tax increases and oppose all reductions, no matter what the degree of targeting. Both middle income and poor agents prefer t*(k) over all lower tax rates. Therefore t*(k) defeats all other tax rates in any election requiring support from two or more agent types. This (plus technical assumptions) implies that t*(k) is the majority voting equilibrium given k. In this case the "budget response function"—that is, how the available budget responds to choices of targeting – is given by this majority voting equilibrium determined by the preferences of the middle-income voter.

A targeting-taxation policy (k, t) is politically feasible if and only if t = t*(k). That is, a policy is *politically feasible* if and only if, given that the degree of targeting is k, the accompanying tax rate is the one that would be chosen through an election of the kind just described.

In this model the naïve equilibria (NE) in which the policymaker sets the degree of targeting assuming the budget is fixed is full targeting (k=1, 100 percent of the targeted transfer, none to the universal transfer). [9] The only possible NE is (1, t *(1)).Therefore, there is a unique NE where all revenues are spent on the targeted transfer and none on the universal one.

The sophisticated policymaker recognizes that the politically feasible tax rate will depend on the degree of targeting. Because the politically feasible tax rate t* is the solution to middle income voters' first-order condition, it must vary continuously with the degree of targeting k. Any value of k at which this maximum is obtained, k*, is then an optimal choice for the sophisticated policymaker, so any policy (k*, t *(k*)) is thus a sophisticated equilibrium (SE).

But in this model the utility of both poor and middle-income agents is strictly *decreasing* with the degree of targeting for politically feasible equilibria. The reason is that the budget decrease from increased targeting exceeds the increase in the share of the budget going to the targeted households.[10]

In this model full targeting would be optimal *if* the budget could be taken as fixed. The intuition here is simple: when the budget is fixed, increasing the degree of targeting

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[8] But this is very restrictive about the types of political situations being modeled. It may well be that the rich are sufficiently politically powerful they need no support and hence they are decisive. Alternatively, the middle group could require no support from rich or poor. Assuming that at least two groups need to agree simply makes the voting interesting.

[9] Because of the formal sector work constraint, "full targeting" may not mean setting k = 1, i.e. spending all revenues on targeted transfers. Except at very low tax rates, doing so would lead at least some agents to forgo formal sector work.

[10] By contrast, the opposite is true for the own-utility of rich agents.

amounts to reallocating consumption from rich and employed middle class agents to poor and unemployed agents. Since this process contracts the income distribution while maintaining the mean level of income, it must increase the integral of utilities (under the assumption that the marginal utility of income decreases as income increases). However, when the budget is determined by majority voting, the equilibrium tax rate and, consequently the total budget fall sharply enough that transfers to poor and unemployed agents actually decrease with a rise targeting. Thus any increase in the degree of targeting induces a mean-preserving spread of the income distribution, reducing social welfare.

While the details of the model are complex the intuition is simple. The "naïve but altruistic" policymakers attempt to maximize the welfare of the poor by choosing k. If they assume in this maximization that the budget is fixed – in Figure 2, this implies horizontal – then they will always push to maximize targeting (since, as with any optimization, they are attempting to find a tangency of the utility of the poor and the budget set and this will push them into a "corner" solution at the extreme of k=1).

The key insight is that in a political situation it would be extraordinary if the budget set were in fact fixed. If the "true" budget set is not horizontal, then acting as if it is cannot possibly lead to the true optimum degree of targeting. In the particular case illustrated in Figure 2 where the true budget set that takes into account the electorate's response to targeting, the "naïve" equilibrium leads to a zero budget and hence is the worse outcome for the poor among the politically feasible possibilities. In fact, choosing zero targeting (k=0) and devoting all of the budget to the uniform transfer would produce higher utility for the poor than would full targeting.

Figure 2: A graphical presentation of the model of targeting and electoral politics
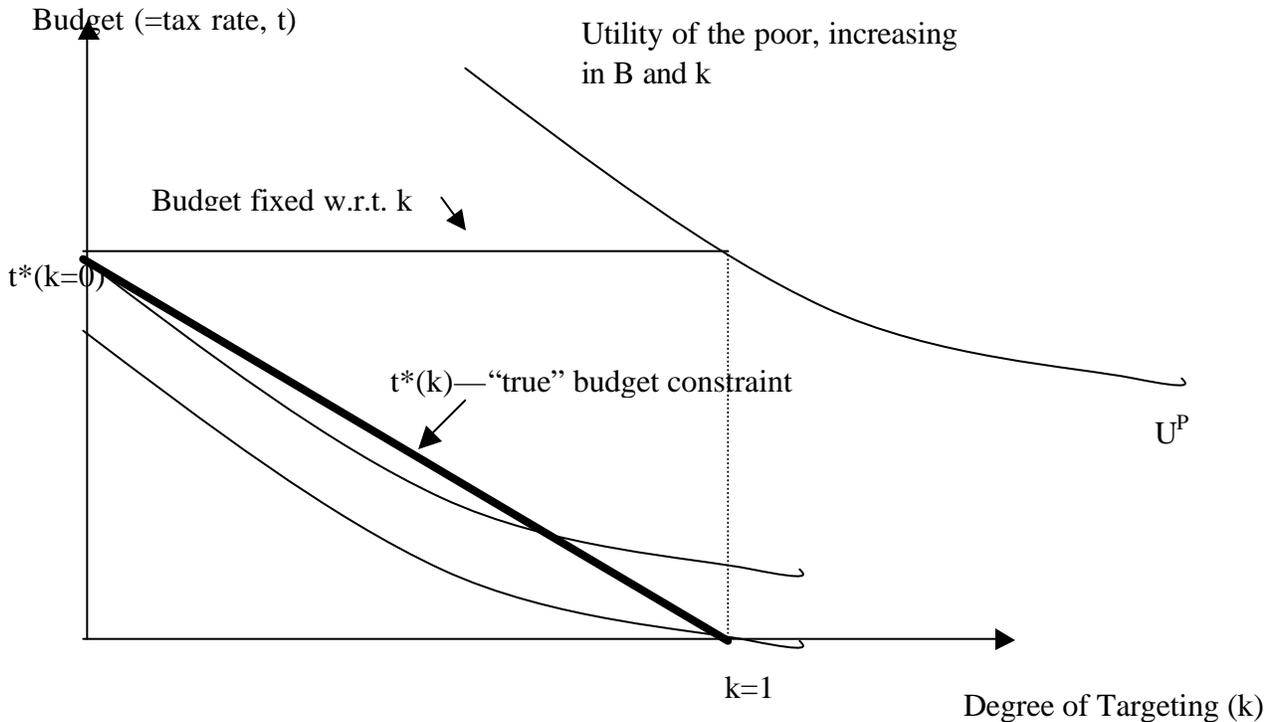
Reliance for policy advice on a literature that takes budgets as fixed has to be based on the notion that accounting for politics introduces only a small change to the policy environment. Yet we have constructed a plausible model that stands on its head the conventional wisdom regarding the optimal targeting. Where the conventional approach is to take the budget as fixed and maximize social welfare with respect to the degree of targeting, we show that this procedure minimizes social welfare in a political equilibrium. Where conventional wisdom suggests that at least some targeting should be used, we show that social welfare is maximized in political equilibrium only when all revenues are spent on universal transfers and none spent on targeted ones. Where conventional wisdom says that targeting should benefit the poor, have ambiguous effects on the middle income, and redistribute from the rich, we show that targeting redistributes from the poor, makes the middle income worse off, and benefits the rich in political equilibrium. It seems difficult to imagine a more complete reversal of what admittedly reasonable, other-things-being-equal analysis would suggest.

But the point is not that this particular simple model is right and other simple models are wrong. The point is that to choose the level of targeting that maximizes the utility of the poor requires postulating some relationship between the available budget and the degree (and structure) of targeting chosen. The assumption that the budget is fixed is a *possible* model, but not a particularly plausible one as there is little theory or evidence to support the notion that voters do not care about their own well-being. There are many other models of the shape of the "budget response function" besides ours, but in all of them the optimal degree of targeting will be different from the naïve assumption of fixed budgets.

Policymakers should target taking account of *all* the constraints – both economical and political – they actually face.

I.C. *Examples and a cautionary tale*

It is hard to say what constitutes evidence of a particular model as most (including mine) are too simplistic to be taken seriously as adequate accounts. But there are several instances where increased targeting was followed by a reduction in overall benefits.

- In the mid-1970s **Sri Lanka** provided every citizen with a rice ration at subsidized prices. At around 5% of GDP, the program's fiscal cost was felt to be unaffordable, so in 1978 the government constituted a reform committee with a mandate to cut the budget. They restricted the ration to the poorest half of the population. In 1979 the rice ration was replaced by a food stamp program (so shifted from "in kind" to cash), still intended to be targeted to the bottom half of the population. Since the introduction of targeting, the real value of benefits per household among those receiving the transfer has fallen to 40 percent of its previous level, from Rs 425 to Rs 170—mainly by erosion by inflation. While it is impossible to say what would have happened to the program's budget had benefits remained universal (since 5 percent of GDP

simply might have been unsustainable) the fiscal cost of the program is now just 0.7 percent of GDP. While overall budgetary pressure may explain part of the reduction in the rice ration program's size, it cannot explain an 82 percent reduction in the program. More of the savings came from reductions in the magnitude of the transfer rather than from better targeting. One cannot run history in reverse, but would the erosion of the real value by inflation have occurred if the program had not become more sharply targeted?

- In **Colombia**, an existing food subsidy was first transformed into a targeted food stamp program and was subsequently eliminated. The distinction between the technocratic and political economy approaches is illustrated nicely by the World Bank's (1994) assessment of the Colombian policy shift: "Although the program seemed effective and well targeted … it lacked political support and was discontinued." The analysis here suggests the possibility that the program's loss in political support may have occurred because, rather than in spite of, the effectiveness of its targeting. We recognize that this case is only one piece of evidence, and that it is difficult to infer causality from simple before-and-after examples. However, the Colombian case is certainly consistent with our predictions.

A cautionary tale. Support for targeting does not follow simple ideological lines with the "left" supporting targeting and the "right" opposed; rather debates on targeting find disagreement *within* both the left and the right. Those who place high weight on the welfare of the poor and believe the budget for redistribution is exogenous should support targeting. But many of the left oppose targeting, which is the right position for those who believe that available budget responds strongly to the degree of targeting. By contrast, while those who primarily want a small state and low taxation level may not favor using tax and transfer policies to improve the plight of poor groups, such people may still support targeting if they believe it will lead to lower budgets (and hence taxes) than universal transfers. For instance, Lal (1994) accuses those who oppose targeting as being "distributivist":

> "An implicit objective of those who argue *against* targeting and in favor of *universal* welfare states is distributivist. This is not surprising as they are by and large socialists who subscribe to the common end of egalitarianism."

The simple matrix below suggests that actual views of targeting are better understood when we consider *both* ideology and beliefs about the responsiveness of the budget. Both pro-poor technocrats and fiscal conservatives could favor targeting—but for very different reasons: the former because they thought the poor would be better off (and taxes were (roughly) fixed) and the latter because they thought taxes would be lower because the tax cut possible with more targeting was large.

Table 2: Pro-poor technocrats and fiscal conservatives prospective

		Pro-Poor Technocrat (*"left" - concerned about welfare of poor*)	Fiscal Conservative (*"right" - concerned only about level of taxation*)
Beliefs about the Budget Reaction Function	Flat *"unresponsive"*	Favor Targeting	Oppose Targeting
	Steep *"responsive"*	Oppose Targeting	Favor Targeting

I.D. Crisis programs in Indonesia—a first cut

In *Indonesia*, a crisis "safety nets" program was launched in 1998 in response to the deep macro crisis. A variety of targeting mechanisms (administrative, self-selection) were used in a variety of programs. The striking fact is that all of the targeting mechanisms achieved surprisingly similar results—much less well targeted than a "perfect" transfer but much better targeted than *any other* component of government spending.

In response to the economic, natural, and political crises that enveloped Indonesia from August 1997 (beginning of depreciation) to May 1998 (Soeharto resignation), the new government announced support for a set of "safety net" (JPS) programs in the July 1998 budget. In the face of the economic and political instability and the enormous (and growing) social consequences, there were both pragmatic and benign motivations for/within the programs. These included:

- The need for both the new government and the international financial institutions and bilateral agencies to be seen to be *responding pro-activel*y to the impacts of the crisis in order to sharply differentiate themselves from the past.
- The desire to *mitigate the impacts* of the shock on both households and communities.
- Many were interested in *protecting certain key social services*, notably health and education.
- There were Keynesian motivations to *sustain aggregate demand* both nationally and locally to halt the collapse in output.
- Some wanted to use the crisis and the new program to *reorient government attention to poverty.*

The outcome of the mix of those motivations and the constraints on program design imposed by availability of data produced a set of programs with varying targeting design. The magnitude of the budget for the JPS programs was not the result of costing out programs or based on any historical baseline but was an amount determined by

macroeconomic, political, and financial forces with which programs could be designed. This meant that programs needed to be targeted.

However, the Indonesian people had never relied to any significant extent on government safety net programs prior to the crisis. The country had neither the economic apparatus nor the political mechanisms (nor the inclination) required to deliver large scale transfer programs all over the archipelago.[11] Therefore, establishing crisis programs in Indonesia in 1998 did not merely mean expanding an existing net, but *casting an entirely new one*.

The Indonesian government's approach was to group the JPS effort in five major areas. These included: (a) targeted sales of subsidized rice, (b) work creation programs, (c) scholarships to students and block grants to schools, (d) targeted health care subsidies, and(e) community block grants.

There are two striking facts about the targeting outcomes:

- Despite exactly the *same* targeting mechanisms *de jure* across all districts, the targeting outcomes were very *different*.
- Despite *different* targeting mechanisms across programs (*de jure)* the targeting outcomes across programs were (to first order) the *same.*

Table 3 shows that, in each program, roughly half the districts have either uniform or pro-rich targeting while roughly half had targeting substantially better than a uniform transfer.[12] Table 3 reports "targeting ratios" which are the share of the non-poor in the SSN program recipients divided by the non-poor's share of the population. So if there is "perfect" targeting and the non-poor get nothing then TR=0, if benefits went to people independently of income then TR=1 because the non-poor's share is equal to their share in the population. So the aggregate TR for the rice program of 0.91 meant that, on average the non-poor's share in the beneficiaries was very near their share of the population. While there was some distribution around this level, 57 per cent of the districts reported targeting close to this near uniform (untargeted by income) distribution.

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[11] Before the crisis, Indonesia was one of the most rapidly growing economies in the world, where "official" absolute consumption expenditure poverty fell by almost 50 percentage points (from 60 to 11 percent) between 1970 and 1996. The general poverty strategy of the previous government was: (a) social spending, largely focused on the provision of 'social services' such as health, family planning, and education, (b) "development" programs that aimed at poverty reduction through increasing productivity (such as credit subsidies, left -behind villages program (IDT), etc), (c) some small programs for very limited disadvantaged groups (e.g. disabled, orphans), and (d) family and communities providing 'mutual social insurance' in times of difficulty (there was some subsidized health care, compulsory social security program, and unemployment protection for formal sectoremployees but this was of very limited reach).
[12] This heterogeneity of targeting performance across regions with the same project design is similar to the finding in Coady, Grosh, and Hoddinott (2002) that across the range of programs they examine there were large variations across countries within the same type of program.

Table 3: In Distribution of targeting ratios across the districts of Indonesia

Program	Mean TR	Std Dev	Percent of districts in each targeting ratio class				Total
			<0.7 (sharply pro-poor)	0.7-0.9 (pro-poor)	0.9-1.1 (near uniform)	>1.1 (anti-poor)	
Subsidized rice	0.91	0.10	2.39	38.57	57.00	2.05	100
Employment creation	0.87	0.27	23.02	26.98	32.01	17.99	100
Primary scholarship	0.86	0.26	20.73	31.64	34.55	13.09	100
Lower secondary scholarship	0.86	0.25	23.10	28.16	35.38	13.36	100
Upper secondary scholarship	0.86	0.38	33.47	14.88	14.05	37.60	100
Used Health Cards	0.83	0.29	25.69	35.42	20.14	18.75	100
Source: Author's calculations based on February 1999 SUSENAS.							

Source: Pritchett, Sumarto and Suryahadi 2002.
Note: TR=fraction of total benefits to the non-poor—"perfect" targeting? TR=0, uniform distribution? TR=1

Even though the programs had very different administrative and targeting designs, the participation incidence of the various JPS programs appears remarkably similar. While there are differences in the targeting indicators (the range of QIII/QI (middle/poor) ratios is 20 percentage points (0.59 to 0.79)) the JPS program incidence is *similar* in two respects. First, when compared the "perfect" targeting (zero leakage to the 80 percent of the population which was non-poor) the JPS programs were far from that standard.

Second, the JPS programs were also similar when compared to the benefit incidence of other general programs (see figure 2 below). In particular, the JPS programs do substantially better than a uniform transfer, while nearly every other substantial component of public expenditure appears as progressive as a uniform transfer (primary schooling), worse than uniform (secondary school spending) or *much* worse (hospitals, tertiary schooling, fuel subsidy).

Figure 2: JPS Participation Incidence versus Benefit Incidence of Education, Health, Kerosene Subsidy
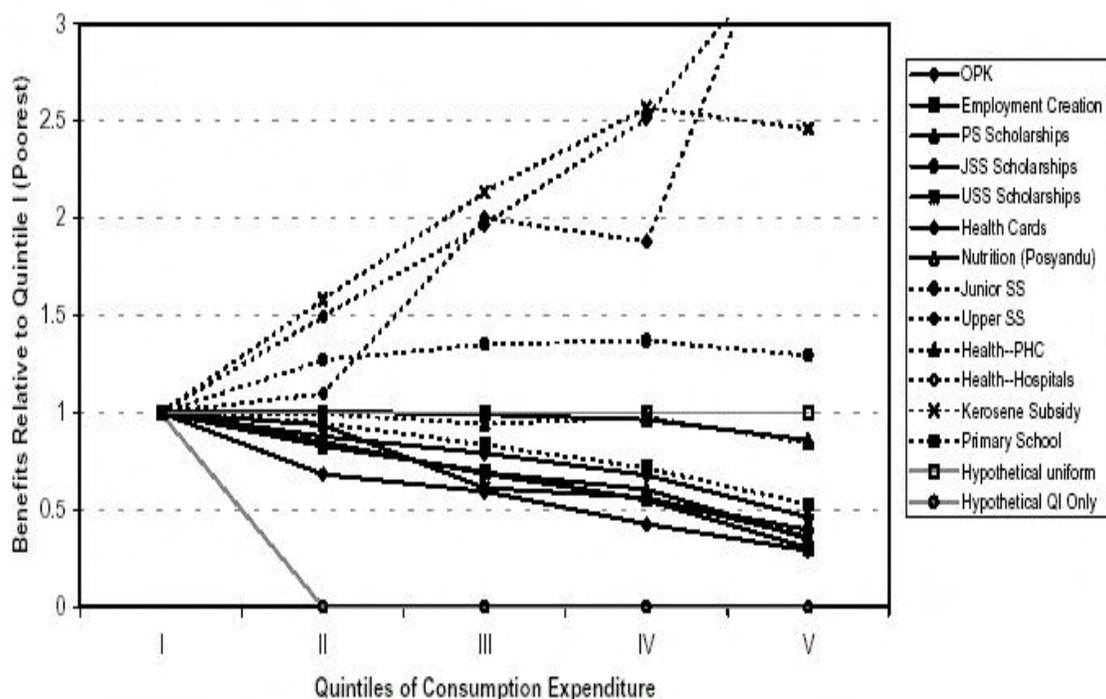
Source: Pritchett, Sumarto and Suryahadi 2002.

One possible explanation of the mild (better than uniform but not sharply pro poor) and similar expenditure targeting of the JPS programs is that some mix of national and local political economy considerations preclude sharp expenditure targeting (Gelbach and Pritchett, 2002). If this is the case, then while some targeting will produce a pro-poor distribution of benefits, it is possible there is no program design that would produce a substantially more targeted distribution of benefits than that observed. If this is the case then some targeting mechanisms will produce more progressive benefit incidence than no targeting, but no *de jure* targeting design would be able to produce extremely sharp targeting (except perhaps for very small programs) as it would be thwarted politically.

On the other hand, many targeted transfer programs enjoy wide popularity. For instance, public employment schemes that provide income in exchange for work have evoked broad support; the Employment Guarantee Scheme in Maharashtra, India and the public employment programs in Chile in the 1980s are examples. No one believes that *all* targeting is politically non-viable, just that the structure and degree of targeting determines its political appeal: **targeting and budgets are not independent**.

I.E. Electoral politics: Long historical view

Before moving on to the next sections, it is worth a final word about the long-historical view of the evolution of social programs. Basically the historical evolution in OECD countries over the 20th century has been three trends. First, rising per capita incomes. Second, expansion of the right to vote to larger and larger fractions of the population. Third, a huge trend towards greater tax revenue—devoted principally to "social transfers"—which are mostly not very sharply targeted.

Figure 4: Social Transfers as a share of GDP, 1930-1995
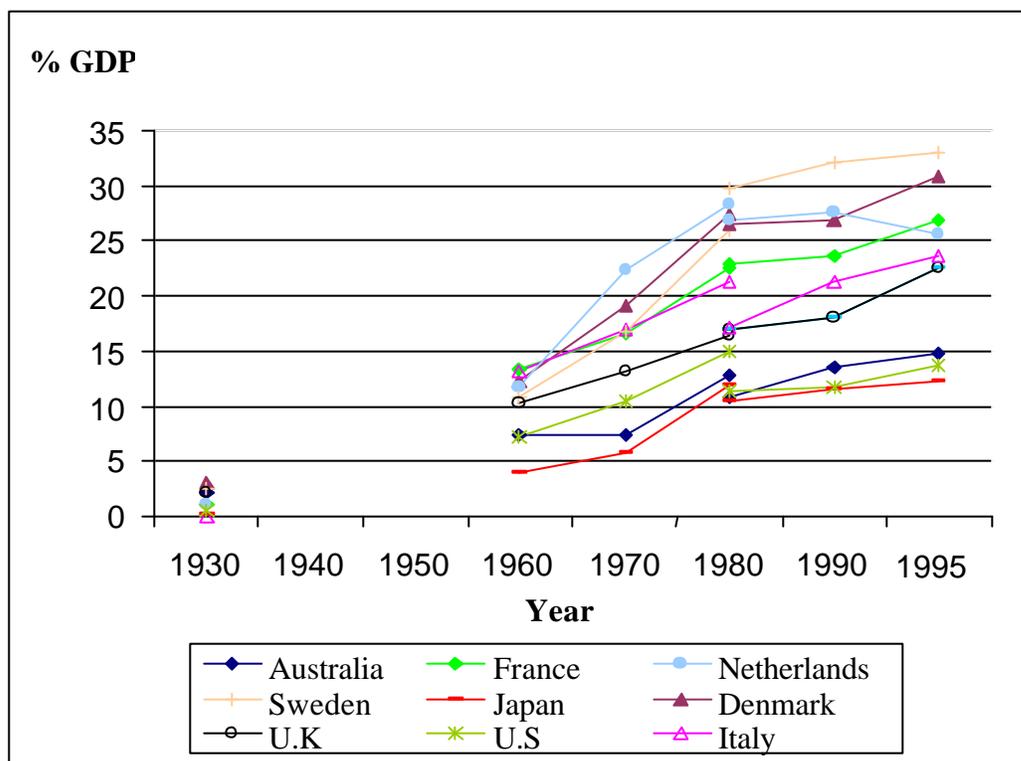
Source: Lindert (2004:1:14)
Note: There is a break in the data in 1980

This raises three points, none of which can be elaborated at length, but are worth some consideration.

First, "development" and democratization has in each instance led to an enormous expansion in social transfers—with no sign of large scale reversal. Large social transfers have proved enormously popular and — while not every country follows the OECD experience in lockstep or linear fashion—it is easy to imagine that the long-term trajectory in nearly every developing country will be towards larger and larger, not smaller and smaller, fractions of GDP devoted to social transfers. Now, this is not a suggestion that countries' commitments exceed their capacity to generate revenue effectively. But if history is any guide (and it isn't always) the future is not lower taxes

and lower transfers but higher taxes and higher transfers (with perhaps the exception of the former Soviet Union and Eastern European countries).

Second, most of the increase in social transfers is towards broad based programs with modest redistribution across individuals—very few of the expenditures are on sharply targeted programs. Most OECD social transfers are either broadly universal programs or transfers from good states to bad states for the same person (e.g. health insurance, unemployment insurance, old age insurance) rather than narrowly targeted redistribution.

Third, as a conceptual issue, if there are large market failures in the market for "risk reduction" one can think of much of the social transfers as mainly a "compulsory purchase" requirement and the "pure" tax component as correspondingly small. This would go a long ways in explaining why these very large tax/transfers in OECD countries are associated with very little in the way of efficiency loss (Lindert 2004).

Section II: Alternative perspective: Safety Ropes vs. Safety Nets (Levels vs. Risk)

The now ubiquitous metaphor of a "social safety net" is, after all, a metaphor not a description and the metaphor conflates two distinct objectives in the design of transfer programs. One objective might be to minimize a measure of income or expenditure *poverty.*[13] An alternative objective might be to *mitigate risk* — reduce households' vulnerability to the wide variety of potential adverse shocks they could face (e.g., death, accident, fire, crop loss, job loss) — whether or not the shocks push households below some absolute threshold.

An alternative metaphor is that of a "safety rope" such as used by rock climbers. Imagine climbers scaling a sheer cliff face. One mode of protection would be to place a net across the bottom of the cliff so that, no matter how high a climber reached, if they were to fall they would fall the distance to the net before reaching any protection—that is a "safety net." An alternative mode of protection would be to attach a length of rope to anchors set into the rock. This way no matter how high the climber got they would only fall from where they were to the length of the rope form the highest anchored piece of protection. This prevents climbers from the catastrophe of hitting the rocks at the bottom with the complete loss of the progress made.

II.A. Volatility of income and vulnerability to poverty—transient and chronic

As has been emphasized in recent literature on the changes in poverty status over time (Baulch and Hoddinott, 2000; Dercon and Krishnan, 2000; Jalan and Ravallion, 2000) changes in the average poverty rate mask enormous "churning" as households move in and out of poverty. All of the panel surveys in Indonesia show enormous

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[13] This general definition of poverty covers any of the class of Foster-Greer-Thorbecke (1984) measures of poverty which adjust for the intensity or depth of poverty and is consistent with either absolute or relative poverty lines.

volatility of households in and out of poverty over this period (for the IFLS see Frankenberg, Thomas, and Beegle, 1999.

While at least some substantial fraction of the *measured* changes in household consumption reflects the difficulty of measuring expenditures accurately, changes also reflect the large shifts in households' fortunes even over short periods of time — as households gain and lose jobs, harvests are good or bad, business goes well or badly. In fact, it is probably more accurate to talk of "households experiencing an episode of poverty" than of "poor households."

This volatility creates the demand not just for transfer programs to those whose incomes are chronically low (safety nets), but also for informal and formal *insurance*-like mechanisms and programs that would pay off not only when income was absolutely low, but also when households experienced negative shocks (safety ropes). [14]

If the targeting of social programs is judged exclusively on poverty or benefit incidence based on a cross sectional snapshot, then risk mitigation programs benefiting households who have suffered large shocks but who are not "poor" may appear to have large "leakage" (a type II targeting error, reaching people who are not intended beneficiaries) when in fact they are simply serving an ***alternative social objective***.

The undifferentiated metaphor of "safety net" can also confuse thinking about the political economy of transfer programs. [15] Government may want to implement "safety net" **and** "safety rope" programs for completely different reasons. [16] While a "safety net" program might be more popular the more effectively it transfers from richer to poorer households, a "safety rope" program might cause little net redistribution but be popular because it serves an important insurance function in transferring resources from good states to bad states.

Designing programs that deal with *shocks* to income (either at the economy-wide or individual level) requires mechanisms that allow individuals to be added to program participation dynamically. This requires either self-selection targeting or "open" administrative criteria — that is, the eligibility criteria need to have a mechanism for households to be added (and subtracted).

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[14] Sumarto, Suryahadi, and Pritchett (2000).

[15] In OECD countries, the distinction has been used to characterize different "systems", that is those that rely on means testing versus those that provide universal benefits (Esping-Andersen, 1990; Goodin et al., 1999).

[16] Economists would recommend poverty programs to a hypothetical benign social welfare maximizer if the social welfare function was built up from individual (household) utility functions with declining marginal utility, in which case a (costless) transfer from rich to poor is not a Pareto improvement but does raise social welfare. There is also an argument for poverty programs from an externality in altruism. In contrast, the normative case for government involvement in mitigation of risk is based on the argument that, if moral hazard and adverse selection are sufficiently large then welfare improving markets for insurance against these risks will not exist (and they will be "too small" in any case). This is potentially the case in a wide variety of insurance markets — but particularly affect the market for insurance of incomes.

Table 4: Differences in the economic rationale, positive model, and targeting for "safety net" and "safety rope" programs

	Nets or *"levels"*	Ropes or *"risk"*
Economic rationale	Equity	Insurance
Positive model of Government	Benign Social Welfare Function	Responding to middle class demand
Targeting	To Poor (transfer from rich to poor people)	To "shocked" (from good states of the world to bad states)

Note: "safety net" programs target levels of income/well being and "safety rope" programs target shocks or risks to income/well being

II.B. Empirics of nets and ropes

One way to compare "net" versus "rope" performance is to compare the static and dynamic benefit incidence. For an empirical illustration we return to the Indonesian SSN/JPS programs.

One common measure of targeting depends on *static participation incidence* (usually called "benefit incidence" but we only have data on participation as beneficiaries, not the magnitude so to be precise this is "participation" not "benefit" incidence). This is the relationship between household's program participation or receipt of benefits and the household's *level* of expenditure. This is the benefit incidence that is commonly displayed and figure 2 shows the standard "benefit incidence" graphs relating levels (quintiles) of incomes/expenditures to the likelihood a household benefited from different expenditures. Graphically the coverage ratio is the height at any given level (or range) of expenditures and hence the targeting is the slope (either at a point or over a range, such as comparing coverage for different quintiles).

The exact analogy can be made for *dynamic participation incidence* as a relationship between program participation and *changes* (absolute or proportionate) in consumption expenditures (or income).

Figure 3 shows the relationship between JPS program participation (described in the previous section) in December 1998 and the quintiles of the natural log *change* in household per person expenditures between May 1997 and August 1998.

Unlike static incidence the dynamic incidence is very different across the programs. Only for the employment creation programs were households substantially

more likely to participate if they experienced a bad shock to consumption expenditures (that is, consumption expenditures fell).

Figure 3: Dynamic Participation Incidence of the JPS Programs
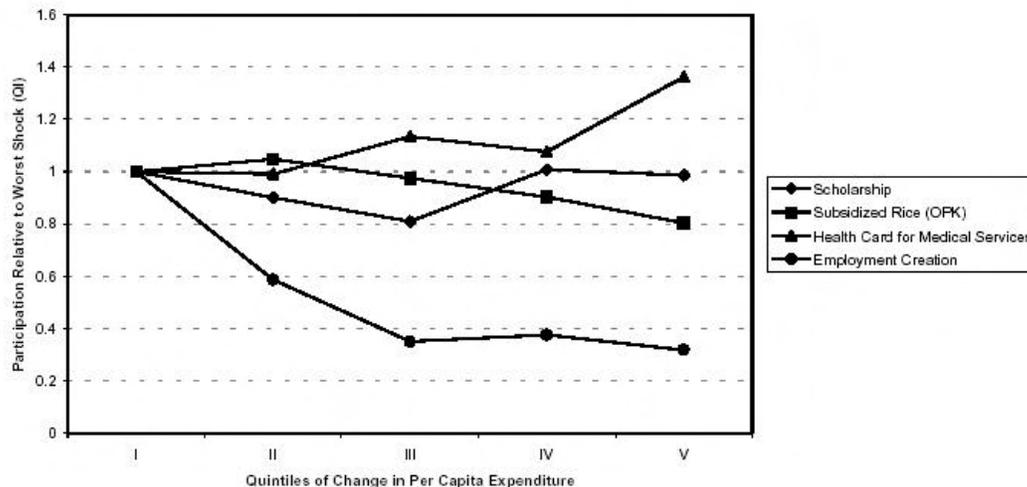
Source: Pritchett, Sumarto and Suryahadi 2002

Different programs can have different coverage and targeting performances, with respect to expenditure levels and shocks.[17] Hence one program's incidence graph could be steep with respect to expenditures at all levels of shock, flat (non-targeted) with respect shocks, or vice versa. A pure "safety rope" program could be sharply targeted with respect to shocks but flat in the expenditures dimension. Figures 4a and 4b show the combined static and dynamic participation incidence for two of the programs: OPK and employment creation. Not surprisingly, the programs using self-selection targeting (labor creation) has enormously better dynamic benefit incidence than the administratively targeted OPK program as households who need assistance have an easier time accessing program benefits.[18]

- "static participation incidence" (the relationship between program participation and household consumption expenditures) was substantially better than a uniform transfer, but substantially worse than perfect targeting, and remarkably similar for all of the JPS programs. This implies that some designed targeting produces much better targeting incidence than no targeting, but the *de jure* design is not as critical.

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[17] The graph of participation incidence including both *levels* and *changes* in (natural log) consumption expenditure is a three dimensional surface.

[18] This suggests that the *screening* argument for the use of "workfare" requirements (Besley and Coate, 992) appears to work well in *changes* but no in *levels*. These results contrasting the labor creating schemes to other programs are in some ways similar and in some ways different from findings about the public employment scheme TRABAJAR in Argentina (Jalan and Ravallion 2002, Ravallion 2002b).

They find that TRABAJAR was much better targeted in static benefit incidence — 76 percent of participants were from households in the bottom quintile — and had much better benefit incidence than other "protected" expenditures.

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- "dynamic participation incidence" — the relationship between changes in consumption expenditures and program participation — was very different among the JPS programs. The employment creation programs, which relied on self-selection targeting, were much more likely to reach those households experiencing large shocks to their expenditure than programs based on administrative targeting such as subsidized rice sales, scholarships, and health subsidies. This implies that, especially in a crisis, the dynamics of household welfare is important and this requires dynamics in targeting, either through self-selection (which is very expensive in benefits delivered per program expenditure) or through administrative flexibility.

Figure 4a: Probability of Household Participation in OPK Program by Quintiles of Level and Changes in Per Capita Consumption Expenditures
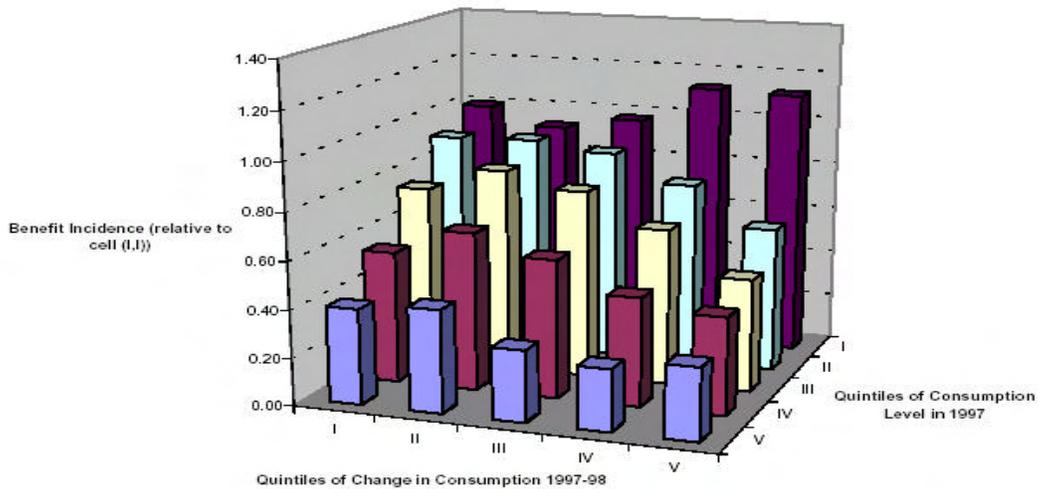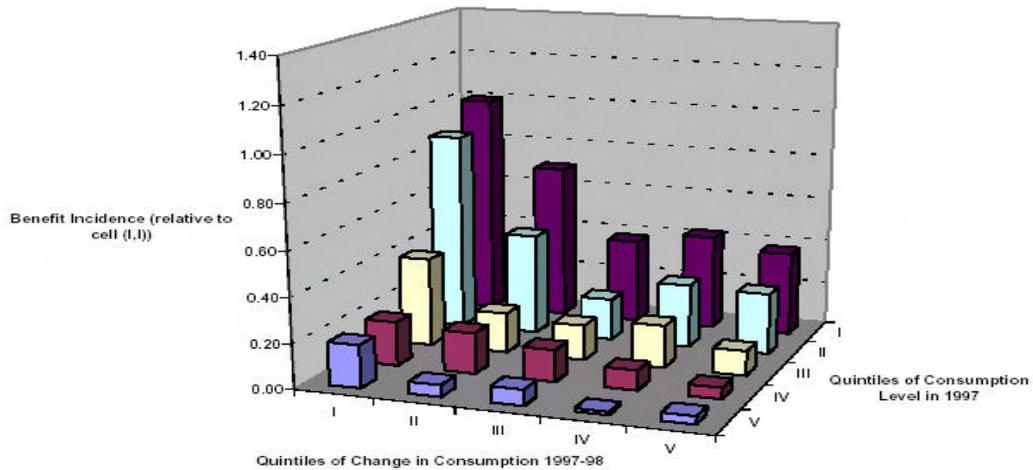

Figure 4b: Probability of Household Participation in Employment Creation Programs by Quintiles of Level and Changes in Per Capita Consumption Expenditures

Source: Pritchett, Sumarto and Suryahadi 2002

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II.C. Static and dynamic (not marginal and average)

In an important paper Lanjouw and Ravallion (1999) stress that, for decisions about program *expansion*, the relevant incidence measure is the *marginal* not the *average* incidence. In what they characterize as "early capture" programs, the non-poor are more likely to receive benefits than the poor from the beginning of the program. If this is so then marginal incidence will be higher than average incidence. An example might be secondary education in which the richer households are likely to be the first to enroll, so at low levels average incidence will be regressive. However, as schooling moves towards universality, the incremental child is likely to be from a poorer household than the average child already enrolled, so the marginal incidence will be more progressive than average incidence. In contrast, with "late" capture, the program is well targeted to the poor at low levels of coverage but as the program expands the marginal incidence is worse than average and hence targeting falls.

It is understandable that many government programs are "early capture" as richer and more informed and powerful households would be the first to gain benefits but that expansion would lead to better incidence.[20] But the Indonesian experience with the JPS program gives some (weak) indications that "safety net" programs were likely to be "late capture" programs — that is, it would be easier to create strong targeting of benefits in smallish programs, designed and designated for the poor.

Larger coverage does not lead to either better or worse targeting: There was no general tendency across the programs for marginal incidence to be above, or below, average incidence. This implies that neither small nor large is necessarily beautiful.

But the evolution of static incidence as program participation expands (which is sometimes called a program's "dynamic incidence") should not be confused with the sense descried here of program incidence of a program with respect to the changes over time in household's incomes (also called "dynamic incidence"). Sorry about having two names for one thing, but I only got to name one of them.

Section III: Attitudes/perceptions

So far the "electoral" politics have evaluation models in which program support was determined exclusively by self-interest. This however is a very limited model and a great deal of both electoral support and of implementation for targeted programs depends on the attitudes and perceptions about the targeting criteria. This section discusses briefly four criteria that might affect the perception about the "fairness" of a program.

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[20] Lanjouw and Ravallion (1999) show that even the anti-poverty programs tend to be "early capture" with higher marginal than average odds of participation (e.g. the Integrated Rural Development Program and the Public Distribution System), although the public works program is better targeted than either and marginal and average odds of participation are more similar than for the other two programs.

Fair treatment and framing: horizontal equity. A fundamental principal of fairness in many societies is that "like be treated alike." A danger of allowing discretion into targeting criteria is that choices are made in which, for whatever reason, persons who are similarly situated are treated differently

However, what constitutes "like" categories that deserve similar treatment is often hotly contested, as well as the issue of whether more favorable treatment of persons of disadvantaged groups are eligible for preferential treatment. Most people would agree that people of different ages can be treated differently but that people of different religions should not be (but this needn't be universal). Men and women are treated alike in some regards but no one questions the equity of programs targeted to women. One hotly contested issue is whether it is fair to have special treatment for members of ethnic minorities that are disadvantaged.

One issue in individuals' attitudes towards targeting is the concept of "framing." Individuals form attitudes at least in part on their perception of social categories. If the perception is that "people like me" do not or (if something were to happen) could not benefit from a program, then those individuals will tend not to support it.

A final issue is attitudes towards the causes of poverty. Alesina and Glaeser (2004) have done work on the political economy of social spending, showing how important differences between Americans and Europeans in their perceptions of the causes of poverty lead to differences in political support for social transfers. Crudely put, if one perceives poverty to be the result of the lack of effort then large transfers are unlikely to be regarded as "fair", whereas if poverty is perceived to be primarily the result of forces beyond the individual's control (either circumstances of birth or structure of the economy) then transfers are more likely to be perceived as legitimate.

Process and administrative fairness. As any targeted program depends on separating individuals (or localities) into "eligible" and "non-eligible" categories, it is important not only that those categories be perceived as "fair" and legitimate in the social context but also that there be some mechanism to determine whether the decision was correctly taken. This has two forms.

First, there should be some mechanism of appeal to an authority outside of the local administration of the program. This reassures people that decisions are being taken fairly without local prejudice.

Second, a mechanism for updating the eligibility at the request of a claimant is often an important part of maintaining the perception of program fairness. Particularly when eligibility changes over time (e.g. people age in or out, or people lose income/assets and become eligible or gain income/assets and become ineligible) a *process* for updating eligibility is important. A dynamic process for updating mitigates some of the risk of having static (e.g. level) criteria for eligibility.

Effectiveness: do the programs "work"? A final consideration in the attitudes and perceptions that affect the political viability of programs is whether they are perceived as "effective." This is less an issue in targeting than in overall program design, but there are elements of targeting. In particular, the more stringent the targeting the more difficult it is for the program to be effective. There are many examples. Suppose a job training program only accepts all those who have been unemployed versus on those unemployed for more than a year. Clearly the latter group is more a target for intervention—but is also likely to consist of harder cases and hence the success rate is likely to be low. Similarly, pushing micro-credit to be available only to the "poorest of the poor" is going to mean the program is reaching segments of the population that are simultaneously more important but also more difficult to create success. This consideration needn't imply moving away from sharp targeting, but the implications of managing expectations should be taken into account.

On another note, many are convinced that being able to demonstrate benefits in a concrete and credible way—through a truly rigorous, independent and scientifically valid evaluation study--was a key element in securing the continuation of PROGRESA in Mexico (with a name change) across a substantial change in government.

A preference for "in-kind" versus cash transfers—even among economists who believe fully in the fungibility of in-kind benefits—is often justified by an appeal to the perception that "in-kind" transfers are more effective.

Obviously corruption in SSN programs subverts all three of these criteria. Corruption is probably more damaging to political support for SSN programs than would be equivalent losses in, say, infrastructure construction precisely because it undermines sense of fairness, process, and effectiveness.

Section IV: Local vs. Central

A recent strand of the literature on targeting has examined the possibilities of using "communities" to target benefits to households. The idea is that local communities have quite good information on both the level and shocks to households' welfare, and hence, *if* local decision-making structures could be employed to use that local knowledge, then targeting could be improved without the high cost of improving administrative targeting or self-selection targeting. However, note the "if" in the previous sentence is a very big "if".

To use the superior local knowledge about conditions, communities must be given discretionary power to allocate benefits. But this discretion could either lead to superior targeting or to elite capture (Platteau 2000, Bardhan and Mookerjee 2000) or to community pressures for more "spreading" of the benefits.

Whether community discretion leads to better or worse targeting depends entirely on the interplay between national politics and local politics and the pressures brought to

bear at each level. There is no "general" theory about this – nor can there be – and little empirical evidence. I briefly discuss three cases on which there has been some empirical work: Mexico, Bangladesh, Indonesia.

Mexico: Progresa/Oportunidades.   The PROGRESA (now Oportunidades) program is the classic example of "top down" targeting design. The regional allocations and the household eligibility within regions are both determined by strict applications of a formula (that depends on household demographics and an evaluation of household asssets). One conjectured political economy rationale for the elimination of any local discretion was that previous "safety net" programs in Mexico had been plagued by the suspicion that they were being used as political patronage (in regional allocations) and to reinforce patron-client relationships at the local level. Therefore eliminating any local authority in determining eligibility was perceived as an important element in establishing program credibility as a "new" type of social program.

Bangladesh: Food for Education. Galasso and Ravallion (2002) use data from Bangladesh's Food-for-Education Program to show that power in community decision making clearly affected outcomes. They show that in this particular instance centralized allocations to villages were not particularly pro-poor and therefore any pro-poor element in the program was the result of local decisions.

Indonesian JPS. We examine this issue with the Indonesian JPS with three bits of evidence: discussion of the OPK, examining the non-income determinants of program receipt, and evidence from the Local Level Institutions study linking individual and community social characteristics and program distribution.

OPK distribution at the village. The OPK program was designed to allow the eligible households to purchase 20 kgs of rice per household at a subsidized price (1000 rp/kg while the market was around 3000 rp/kg). The SUSENAS and 100 Villages Survey data indicate unambiguously that the *de jure* program distribution was not followed. While the rice allocated to a village area was (nearly always) based on the number of eligible households, almost twice as many households received the rice than if the program guidelines had been followed and almost a quarter of households in the richest group still receive the program benefits (see the benefit incidence above).

These quantitative findings accord well with anecdotal reports, as from the beginning of the program observers noticed that the local leaders responsible for implementation were not adhering to the list of eligible households, but rather were distributing the rice amongst a much larger group. As a result, while each eligible household in many cases received lesser amount of rice than stipulated in the program, other households, which were not officially eligible, also received an allocation (Tim Dampak Krisis SMERU, 2000). Apparently the centrally planned administrative guidelines often proved socially unacceptable at the community level (Sumarto and Suryahadi, 2002).

It is not at all clear whether the deviations at the local level were a "good" or "bad" thing. There are three main arguments made by village heads (*kepala desa*) to justify the practice of allowing subsidized rice to be given to non-eligible households.[21]

- The official list is not an accurate list of those who are in need as, due to the crisis, many households which formerly were not poor are also now in need of assistance.
- Even if the list were accurate, the distinctions drawn are too fine: the differences between those households who are entitled and those who are not does not justify one group receiving 10-20 kg of rice while the remainder receive nothing.
- Village heads and community leaders argue that the targeted distribution of this central government benefit is inconsistent with the spirit of community solidarity and self-help (*gotong royong*). The village heads point out that, if everyone is expected to contribute their labor to community projects, then everyone should also benefit from the unexpected windfall of assistance from the central government.

These arguments raise important questions about the structure of "optimal feasible" targeting: communities may know better than the central government and the BKKBN (acronym for family planning organization) classification about the best distribution of rice within any given community. Furthermore, local leaders may know better what is socially and politically feasible. Rice that went to "non-eligible" households, while inconsistent with the program guidelines was not necessarily mis-targeting. Moreover, local social pressures around "fairness" clearly led to more uniform distribution, though one with less benefit for the poor.

On the other hand, providing too much discretion, and particularly discretion without conditions for adequate local oversight, can lead to abuses. Olken *et al.* (2001) show that local politics appeared to play some role in the way village heads distribute OPK rice. Anecdotal reports exist of local leaders abusing discretion in the OPK and in other social programs.

Household demographic and social characteristics and JPS program allocation. The 100 Villages Survey, in addition to having multiple rounds, also has information on household participation in a variety of social organizations. We can examine empirically whether these social characteristics played a role in program allocations, over and above the household's wealth (as proxied by assets), education, consumption expenditures and other characteristics.

Perhaps the most interesting result is the contrast between the JPS programs and the "credit" programs run by the government that channeled resources to specific activities. A person who belonged to the government administrative apparatus was much more likely to have gotten credit than a household which was not. At the same time,

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[21] This draws on reports of visits as well as the authors' own experiences.

living in a village in which *other people* participate in the village governance organizations reduces the likelihood of receiving credit. JPS programs do not appear to have been "captured" by local governments or their agents.

The implementation of targeting will be influenced by household and community characteristics and that influence does not necessarily lead to more "pro-poor" targeting. The *de jure* design can work either to limit these influences or to accommodate them by providing explicit local discretion, along with checks on that discretion.

- Targeting designs of many of the programs were not followed strictly during implementation of the programs. In practice, community and individual characteristics — that were *de jure* irrelevant — played a role in targeting. In the sales of subsidized rice program, community influence led to the program going to other than just the eligible individuals. In other programs, individual characteristics appear to have influenced targeting.   This implies that local conditions will influence implementation, but communities may well demand less sharp targeting than centralized administrative criteria.

- By not building scope for local discretion into the program design (e.g. by not allowing the decisions on rice eligibility to be made in a public village meeting) this meant that the *de facto* decisions were not transparent.

Table 5a lists possible costs and benefits of centralized targeting while table 5b lists costs and benefits of decentralized.

Table 5a: Centralized targeting formula

Benefits	Risks
Stronger funding	Criteria perceived unfair/unreasonable
Avoids "races to the bottom"	Allows little discretion
Protects local disadvantaged	No internal support locally

Table 5b: Completely decentralized targeting

Benefits	Risks
More responsive to regional differences	Local preferences not benign
Better monitoring (benchmark)	Local politics less pro poor than national
Local internal constituencies	Races to the bottom
	Uncertain funding

One possibility is to combine central criteria and local discretion in a "top down – bottom up" combination. The national program could make regional allocations and criteria for targeting but which stipulate *local processes* to be followed, either in making the local decisions or in making exceptions to the criteria. Or, explicit local discretion could be built in by specifying proportions of the regional/local availability to be allocated according the strict criteria with a certain number left to local discretion.

For instance, a scholarship criteria could make allocations to individual schools of X scholarships with the stipulation that 90 percent are allocated in a formulaic way while 10 percent are allocated with local discretion.

Obviously it is important to dictate in the structure of the program the criteria for the local processes in terms of the procedures for decision making, the transparency of the selected candidates, etc.

Table 5c: Possible mix of national allocations and local discretion

Benefits	Risks
Insists on process but allows local knowledge	Local capture
Funding	Disconnect with local government
	No institutional base for sustainability

Vietnam. Top down: national programs with uniform criteria and implementation (poverty Vietnam): "Vietnam's spectacular success in reducing poverty took place in the absence of a mechanism to measure poverty or target the poor based on international standards. The distribution of agricultural land to rural households in the early 1990s, a process eminently vulnerable to capture by local elites, was remarkably egalitarian."[22] Current targeting methods in Vietnam include: Household expenditure, poverty mapping, income-based, local classification, self-reporting and wealth ranking.

Box 1 describes the trade-offs between centralized and decentralized targeting under discussion in Vietnam today.

Box 1: Improving Targeting Mechanisms in Vietnam: A Practical Proposal

The General Statistics Office's main strength is in estimating poverty levels at very *aggregate levels* by computing poverty rates based on the household-expenditure method. The Ministry of Labor, Invalids and Social Affairs's strength is in identifying the poor at the *local level* via local classification of households in each *thon* (a commune that includes several villages). Some of the challenges of allocating the benefits to the neediest include: (1) the exclusion of migrants: what if they have settled in? (2) the exclusion of the non deserving poor: why should the children and spouses be penalized for the behavior of those members who engage in socially reprehensible behaviors? (3) how do you maintain the prestige of a village chief and attract committed and honest citizens to apply for the position?

Combining the strengths of these two institutions would be an effective way to improve targeting. However, no one covers the intermediate range (i.e. district level). Household expenditure surveys would require a very large sample to generate credible poverty rates for this level, while the local classification which relies on social knowledge would be ineffective if hundreds of households were involved. Poverty mapping would be a good candidate, however the mobility of people in Vietnam would change the true poverty rates of those in the districts. Therefore, the construction of poverty maps would need to take advantage of both household surveys as well as administrative records on migrants.

Source: Vietnam Development Report 2004, pp 121-123

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[22] Vietnam Development Report 2004, p 113.

Section V: Internal and Organizational Politics

A final element of political economy is a subject that practitioners know is tremendously important, but on which there is almost no published theory and little economics literature—organizational politics. There are two questions. First, is the question of the politics of the "fit" between the organization responsible for implementing a program, its *ethos* and internal culture. Second, is the inter-organzational politics within governments.

V.A. Organizational fit

In his classic book on the behavior of large bureaucracies (Wilson 1989) tells the story of when the U.S. agency responsible for administering Social Security and Medicare (medical insurance for the aged) was asked to take on an additional function of administering an added "safety net" component of disability insurance, making payments to those unable to work. A naïve view of bureaucracy (that they always want to expand) would suggest the head of the agency would be delighted to take on this new function—additional budget, additional staff, additional powers.

But the head of the agency argued strongly *against* his agency taking on this new function. His argument was that the existing *ethos* of the organization was of "client service" because both Social Security were not seen as "means tested" but rather "tax contributory" programs. He argued that irrespective of actual facts about actuarial fairness of pay-as-you-go pension systems citizens felt--and his organization's employees were trained to feel—that these were taxpayers' contributions being returned to them. This allowed them to create an internal culture in which the Social Security beneficiaries were the "client" and entitled to good service and decent treatment. (Wilson argues that, in fact, the agency was impressively effective). The agency head felt that the disability "insurance" was a means-tested program which was not viewed as contributory and in which there was a fair possibility of fraud as claimants pretended to be disabled when they were not. This would mean the administering agency would have to determine eligibility on criteria that could be contested (unlike the rules based formula of Society Security) creating an aura of treating claimants as "suspicious" and possible cheats.

This story illustrates a more general point, which is that most successful large organizations have a clear sense of what it is the organization is about—and usually the clearer the better. This is true in the private sector[23] and public sector (Wilson 1989). If *either* the substance or the very act of targeting is inconsistent with the culture of the organization being asked to take on the task, there will be problems.

Two examples from Indonesia illustrate the point.

Table 6 shows the coverage of the poor of various programs, all of which were launched in July-August of 1998. What is striking is that six months later *half* of all

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[23] The classic reference is Barnard, originally published in the 1940s, but is a mainstay of the strategic consulting literature (e.g. Peters, Collins and Porras).

households in Indonesia were receiving subsidized rice[24]. This is just astoundingly successful scaling up. In contrast, no other program was reaching more than 12 percent of the relevant population. This, at least in part, is due to differences in program fit with organizational culture.

The rice program was administered by the existing logistics agency, BULOG, which had a long-standing responsibility to price stabilization which involved the purchase, transport, and sale of rice (among other commodities). So their "mission statement" (if they were to have one) would be "We move rice." The program design called for BULOG to sell to each village once a month the quantity of rice stipulated by the targeting formula. The rice was available at the sub-district BULOG warehouse and villages had to transport from there to the village. The *targeting* of the program to the households was enforced (or not) by the village heads. Therefore, while in previous times BULOG had moved rice for price stabilization now it was being asked to move rice for Safety Net purposes. This was perfectly consistent with existing organizational structures and practices and hence a great fit.

In contrast, the public works ministry was asked to create labor-intensive employment programs. But after months and months of working with them it was very difficult for them to propose and implement a SSN program. By the time the revised program was begun, the crisis was nearly over. This was in part because their organizational mantra was "we build stuff." That is, their prized output was stuff. Asking them to take on a task in which the primary purpose was employing unskilled labor at low wages – with building stuff only a secondary objective – was too much for them. They continually resisted wages low enough to have adequate self-selection because they feared they could not attract sufficiently skilled labor and they resisted "labor intensive" designs because they were not attractive from an engineer's criteria of design. So, after a brief spurt of activity the "labor intensive" programs (in which, in retrospect, they were providing an effective "safety rope") were phased out due to disagreements between the Ministry of Public Works and the World Bank on SSN program design.

Table 6: Coverage of the poor in the Indonesian crisis safety net programs as of February 1999.

Program	Quintile I coverage
Subsidized Rice	52.64
Employment Creation	8.31
Primary Scholarship	5.80
Lower Secondary Scholarship	12.15
Upper Secondary Scholarship	5.40
Used Health Card	10.60

Source: Pritchett et al. 2002

There are other examples. The Indonesian Ministries of (Basic) Education and Health may or may not be receptive to "safety net" elements, in part depending on how

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[24] The fact that this is substantially more than the *de jure* eligible population is discussed above.

they interact with the organizational culture. There was substantial resistance to scholarships paid directly to students because the Ministry felt (perhaps not unreasonably) that the budget should be devoted to protecting the quality of the schools from budget cuts and so rather than being directed to *individuals* the scholarship budget should be devoted to *schools*.

This is often a problem when the agency has been a direct service provider and is being asked to take an intermediary role (e.g. administer "demand side" transfers like scholarships or vouchers).

A second example is in micro-credit. The Bank Rakyat Indonesia (BRI) was an enormously successful example of expanding credit to small borrowers. But it did so on a commercial basis and the organizational culture was a 'business" relationship with clients. Hence an attempt by the BRI to reach smaller and poorer borrowers with different lending instruments was resisted by the staff as they saw it as not profitable and their incentives and ethos focused on profitability (Horn-Welch 2002).

V.B. Organizational implications

In addition to the politics *within* organizations there are also the obvious politics *across* organizations in deciding on implementation, which can affect political support.

The location of "social fund" implementation agencies directly in offices of the Presidency in several Latin American countries had both a pragmatic element of "cutting through" the existing bureaucracy and a political element of allowing the President to take credit for the resulting benefits. The obvious risks and costs and benefits of the allocation of funds on a political basis – an age-old staple of politics – have to be considered carefully.

Conclusion

As noted above, this paper is a background note for a much larger training course on Safety Net programs. Therefore almost everything is either taken for granted (justification of poverty focus and targeting) or ignored as there are many important problems in the design and implementation. This note focuses exclusively on the political economy of targeted programs and has five major messages.

- Electoral politics matter and doing the best for the poor requires taking a view on the "budget response function"—how will the support for the overall budget for transfers depend on the way in which it is targeted. This is a consideration of the first order, not a detail to be considered later. It is theoretically possible and in some instances empirically plausible that "more for the poor" and *more* leakage would have been better for the poor.
- Targeting needs to be clear on whether a "net" is a better metaphor than a "rope" and whether the program is primarily targeting a low *level* of well-being or *shocks* to well-being.

- Beyond "self-interest" models of political support, targeting needs to take into account perceptions of targeting legitimacy, including, at a minimum, horizontal equity, process fairness, and effectiveness.
- The trade-off between central, rules-based eligibility and localized discretion needs to be considered carefully. Almost certainly some mix of each is desirable.
- Whether a new program should be located in a new organization or in an existing Ministry—and if so, where—if often one of the key determinants of program success. Unfortunately, beyond general concern for organizational "fit" and the obvious internal governmental politics (everyone wants credit for good things) there is little theoretical or empirical guidance.

Questions and Answers
(Collected from previous presentations and discussions, edited)

Question: In your discussion in Section I of the paper you concentrate on coalitions between the poor and the middle class - with the middle class voting on the basis of whether they can participate in a program or not. I would think that there are at least some cases where the "rich" would support targeting strongly -- they have an interest in addressing poverty for some reason (from altruism, from a distaste of being confronted daily from the worst manifestations of poverty, from fear of crime or revolution, from belief that a literate, well-fed workforce is in the nation's interest or whatever), but because they hold such a large share of the economy's wealth or income and in the most taxable forms, will pay for a disproportionate share of the budget. Would they not then favor targeting? Is their weight in the political process either in coalition with the poor or solo not likely to be substantial?

Answer: Good question. As the very subtle footnote 8 mentions this model is only a model of those situations in which the middle class (defined in the model's terms) are "decisive" in voting. We make this assumption to make the politics interesting, not because it is accurate. It is perfectly possible that in many countries "the rich" defined as those that do pay taxes but never receive targeted benefits are sufficiently in control they do not need a coalition with either poor or rich. Moreover, we have to rule out a "rich/poor" coalition via the structure of our model.

So, yes, there are many situations in which the political economy will lead to more targeting if it is possible in a way that *improves* the well-being of the poor without sacrificing political support. One way that I like to think about targeting is that it is a "bundled" good. In our models (with Gelbach) the "bundling" is that the middle class are really trying to buy insurance (transfers from their good states into their bad states) and this is "bundled" with transfers from them to the poor. As targeting improves the relative price of buying insurance is higher so the middle class buy less (or even zero) and since the transfers to the poor are bundled they lose out.

But one could just as easily think of a model in which the motivation for a transfer was really geared to benefiting the poor, for instance due to altruism. In this case the inability to distinguish the poor from the non-poor (or to raise complex and heated issues the "deserving" poor from those receiving the transfer due to moral hazard—that is, allowing the transfer to affect their contribution to the economy) is another form of bundling. So the buy a transfer to the poor I have to buy a certain amount of leakage to the non-poor. In this case an improvement in targeting (reducing leakage) leads to the good really being purchased being cheaper (since per unit devoted to the transfer more fulfills the purchaser's objectives) and hence they buy more.

So leakier can be better, or leakier can be worse. The general point is that targeting affects the demand for redistribution and we need to think through the politics of that together with the design. Will targeting of the type being proposed increase or decrease the polity's demand for transfers?

Question: In your discussion in Section I of the paper you seem to assume that a government/polity can fairly easily raise taxes to support programs that benefit a wide swath of the population. Is that assumption valid for low or lower middle income countries? Is the "budget response function" severely bounded by tax capacity on the upward side in these cases?

Answer. This question is so hard it requires three answers, none of which I am completely confident of because this is one of the hardest areas of all for me. But the basic answer is "yes" for the reasons given in the answer above. Strictly speaking in our model the middle class are the marginal taxpayers. If "the rich" are the marginal taxpayers already then it may be upward limited already. But let me give three other answers to this question.

First, think of an "earmarked" program of the contributory or "compulsory purchase" type like, say, health insurance. In this case the question is really one of the scope of the compulsory purchase. If everyone is in the formal sector this is easy. The question really is, how much of a discouragement to formalization is the "taxation" implicit for the transfer programs. This is a very hard question. The "simple economics of mandated benefits" (Larry Summer's phrase) suggest that if there is no redistributive component (e.g. an "actuarily fair" price is paid) then mandated benefits are fully offset in wages and employers and workers are roughly indifferent in any case, better off if the market would not have existed without compulsion.

The problem of course is the cost of imposing the compulsory purchase when a significant fraction of the economy is outside of the formal sector. I really wish I knew the answer to that. As Colombia's health sector reforms show, this is a very hard problem.

Second, there is the jointly related issues of the marginal cost of taxation and the *net* benefit incidence. That is, the model assumes there is a broad tax based that is roughly proportional (e.g. an income tax). In this case (a) a rise in the tax is feasible, (b) a rise in the tax has low distortion/welfare cost, and (c) the net benefit incidence of even a uniform transfer is strongly progressive (since the tax is proportional to income and benefit flat). But what if the choice is either (a) a very narrow and potentially growth distorting tax (e.g. more profit taxes on the formal sector) or a broad but regressive tax (like a sales tax). Here it is the case that the "upside" is much less buoyant for transfers.

Any real consideration of transfers should be tailored to the *actual* marginal cost of funds—which could be very high or could be very low. And yes, in a low income economy it is likely to be high.

But, that is an argument for improving and broadening the tax base in the medium to long-run—as happened with the OECD—as much as an argument for narrow targeting in the short.

Third, remember, this stuff is competing with other *expenditures* as well as with taxes so while in the formal model "taxes" and "budgets" were synonymous in the real world "safety net" programs and social programs of all types are competing with jets for the military, embassies abroad, higher salaries for teachers, roads, and subsidies of all kinds. All of the time one will see expenditures that have *horrible* benefit incidence wipe the political mat with "well targeted" programs. In the Indonesian example the reasonable well-targeted safety net programs at the same time *billions* of dollars were being spent to bail out banks (what is the incidence of that you might ask?) and *billions* of dollars were going to fuel subsidies, where we *know* the incidence is much worse. So the program budget upside is also on revenues.

Question: In your discussion in Section I of the paper I you assume that the safety net programs being discussed are financed with a government's own revenues and thus the polity of interest is the nations' voters. How should we think about cases where the safety net programs are wholly or largely funded by international assistance -- either bilateral grants or multi-lateral loans? How does the political preference of the "donor" affect things?

Answer. Here it is clear that the "donor" may have "altruistic" preferences (as the stakeholders of donors are always the globally rich) and hence prefer sharp targeting while the "recipient" politics could be one of several types, and the hard part is how to distinguish. One government type is the rich/altruistic government above in which case targeting is happy. Another type is a patromonalist state in which transfers are leaky in the worse sense—not only do they not go to the poor, they go explicitly to finance political supporters/"clients" etc. This is the worst of all worlds as it both reduces the share to the poor and it decreases the typical taxpayers willingness to pay. In this case the donor will fight for better targeted transfers based on criteria that are open, transparent, related to need, etc. and it will be good if more targeting can be achieved.

I of course emphasized the hard case. It could be that the donor, to satisfy its stakeholders, pushes for greater targeting even though in the domestic political economy that will reduced total domestically available budget. That is a bad thing.

The impossible question for you, dear reader, is what situation is the country you are working on in? Is pushing for greater targeting on the side of angels because the money will come out of patronage or on the side of Newt because it will reduced support for otherwise unobjectionable public sector transfers? Only an analysis of the concrete situation will suffice, there are not general rules.

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