

ECONOMIC ANALYSIS

1. Investing in a social protection program can yield savings for the government in the medium term as the poorest households become more resilient to shocks, build their human capital, and are able to improve their employment potential. Further, the cash transfer program can have positive multiplier effects in the short term, mainly through the effects on economic activity from the increased consumption of the poorest households.¹ To the extent that local economic activity is below potential (e.g., the collective result of a geographic concentration of individuals in poverty traps), short-term effects can translate into medium-term improvements.

2. The Social Protection Development Project supports three key programs of the Benazir Income Support Program (BISP). The project will support the expansion of coverage of the cash transfer program, strengthen the health insurance program (Waseela-e-Sehet), and restructure the BISP skill development program (Waseela-e-Rozgar [WER]).

3. All three programs are expected to have significant economic impacts. While cash transfers cannot ensure that households that are stuck in a poverty (nutrition) trap to graduate out of poverty, they can assist in smoothing consumption and help households withstand shocks. Through their effects on the stability of households and total nutrition, they are also very likely to enhance early childhood cognitive development and children's educational attainment, and help prevent stunting. Health insurance has a similar function, and assumes particular importance in conditions when public health facilities are inadequate, poorly managed, or providing poor service. Skills development facilitates movement out of poverty provided the program is evidence based and responsive to the skill needs of the target group.

A. Poverty and Vulnerability

4. Official estimates of poverty incidence² in Pakistan were last released for 2005/06, with the headcount index for poverty reported at 22.3%.³ The official estimates did not disaggregate poverty incidence by province, but a broad rural–urban breakdown was issued showing urban poverty at 13% and rural poverty at 27%. A decline in average annual gross domestic product (GDP) growth rates after 2007 and rising inflation, coupled with the impacts of the devastating floods of 2010 and 2011, suggest that poverty incidence may have increased significantly.⁴ Although independent researchers and the World Bank have estimated poverty using the government's household income and expenditure surveys since 2006, the estimates of poverty incidence have not been considered credible by the authorities and have not been officially sanctioned. A recent study using 10 indicators to create a multidimensional district-based profile

¹ As also reflected in the Financial Analysis (linked document 6), the type of social protection costs that dominate the BISP have, to some important degree, the potential to actually pay for themselves. Unfortunately, Pakistan does not publish the necessary data to enable the undertaking of a social accounting matrix (i.e., comprehensive input–output tables) exercise to estimate the different effects of the BISP. Such an exercise could help estimate the potential effects on additional economic activity and on additional tax revenue. The expectation of a very high short-term multiplier stream from the appreciation of the characteristics of BISP expenditures (i.e., low leakage to savings, low leakage to imports, low leakage to taxes = very high short-term multiplier).

² The national poverty line was notified by the Planning Commission through Vide Letter No. 1(41)/Poverty/PC/2002 as PRs673.54 per adult equivalent monthly consumption expenditure. This base poverty line has been adjusted over time by the inflation rate. Currently, the poverty line is set at PRs1,822 per adult equivalent monthly consumption expenditure.

³ Government of Pakistan, Economic Advisor's Wing. 2009. *Pakistan Economic Survey 2008–09*. Islamabad: Ministry of Finance.

⁴ GDP growth has averaged 2.9% for fiscal year 2007/08– 2011/12, while inflation averaged 13.8%. Figures were calculated from various issues of the Pakistan Economic Survey published by the Economic Advisor's Wing, Ministry of Finance.

of poverty estimated poverty incidence at 33% of all households in the country.⁵ Rural poverty was estimated at 46%, and urban poverty at 18%.

5. Vulnerability is also believed to be high in Pakistan. Analyses of income and expenditure data show that poverty rates change in response to a variety of factors. Weather-related shocks affect rural households dependent on agriculture. Power shortages affect household income-generating activities, microenterprises, and small-scale service establishments. Family issues, such as the sudden death or disability of an earning member of the household (generally male) equally has an effect on vulnerability. In recent years, this vulnerability has increased in Pakistan due to the repeated incidence of natural disasters (a major earthquake in northern Pakistan in 2005, floods that devastated the Indus basin in 2010 and 2011), the ongoing militancy in parts of Khyber Pakhtunkhwa and in the Federally Administrated Tribal Areas, and the wave of terrorism that has affected the country since late 2007 (which, in 2011, was estimated to have caused the deaths of more than 35,000 citizens and cost the country more than \$67 billion in direct and indirect costs).⁶

B. Short-Term Impacts of the Social Protection Program

6. The cash transfer was the first program launched by the BISP. The program was launched in the wake of rising food and fuel prices (a global trend observed in late 2007), and was aimed at assisting the poorest households in the country to manage this period of high inflation.⁷ The cash transfer program is one of the more well-researched programs in Pakistan, and recent impact evaluations have positive findings. The Ministry of Finance estimates that the cash transfer of PRs1,000 per month per household enhances the average income of the poorest households by 20%.⁸ It estimates that the value of the cash transfer could fund up to 25 days of flour requirements of a household of 5–6 members.⁹ A recent survey cited in a World Bank project document found that beneficiaries used their payments for productive purposes. Most households used the cash to buy basic food (32% of households), while others spent on medical care (23%) and settled debt (10%).¹⁰

7. Smoothing consumption was one aim of the cash transfer program, which seems to have had an impact in helping households withstand shocks. According to a 2010 qualitative baseline survey of the BISP, almost 70% of BISP beneficiaries mentioned an increased ability to deal with shocks as a positive impact of the cash transfer, while a further 24% said that it made a small difference.¹¹ The same study found that the cash transfer enabled households to access better quality services (private medical practitioners, for instance).

⁵ A. Naveed and N. Ali. 2012. *Clustered Deprivation: District Profile of Poverty in Pakistan*. Islamabad: Sustainable Development Policy Institute.

⁶ Government of Pakistan, Ministry of Finance. *Pakistan Economic Survey 2010–11: Cost of War on Terror for Pakistan's Economy*. Special Section No. 1. Islamabad.

⁷ A government survey in 2008 showed that 35% of households reported that they had been highly affected by food price increases. Households in the lowest income quintiles were more severely affected. See Pakistan Social and Living Standards Measurement Panel Survey 2008 to 2010 as reported in World Bank. 2013. *Pakistan: Towards an Integrated National Social Safety Net System. Assisting Poor and Vulnerable Households: An Analysis of Pakistan's Main Cash Transfer Program*. Report No. 66421-PK. Washington, DC.

⁸ Government of Pakistan, Ministry of Finance, Poverty Reduction Strategy Paper (PRSP) Secretariat. 2012. *PRSP Mid Year Progress Report FY 2011–12*. Islamabad: Ministry of Finance, September.

⁹ A. Channa. 2012. *Social Protection in Pakistan: A Profile of Existing Programs and an Assessment of Data Available for Analysis*. Background Paper for the Asia Research Centre, London School of Economics. 30 March.

¹⁰ World Bank. 2012. *Project Paper on a Proposed Additional Credit and Restructuring in the Amount of SDR96.7 million to the Islamic Republic of Pakistan for the Scale Up of the Social Safety Net Project*. Report No. 66707-PK.

¹¹ Department for International Development. 2012. *Pakistan National Cash Transfer Programme: Reducing Poverty, Getting Poor Children into School*. Business Case. London.

8. Findings from Pakistan are consistent with international evidence. The World Bank finds that reservations expressed by some policymakers regarding the impact of cash transfers on willingness to work and effects on local wages and prices are largely unfounded. The positive effects of consumption smoothing offset such behavioral responses, if present.¹² Since the marginal propensity to consume out of additional income is high for the poor, cash transfers were found to have a positive impact on consumption of essential items (particularly food). In the longer term, cash transfers have had a positive effect on poverty, particularly where transfers have been sizable or constituted a significant proportion of average household income.

9. The BISP cash transfer seems to have met its broad objectives. The potential impacts of the other two programs that the project intends to support are not entirely clear as they are still in the initial stages of implementation. International experience suggests that the poverty-related effects of health insurance (in the short term) and skills development (in the medium term) can be substantial. The economic impact of a health shock is twofold, and is felt both in terms of the cost of health care and the opportunity cost of lost workday income. The latter cost features as the more significant, and multiplies significantly in the case of a long or serious illness.

10. A study that used data from Indonesia found that if illness severely limits the physical function of an earning member, families could find alternative means of livelihoods to make up only 30% of the lost income on average.¹³ If health-care costs are also prohibitive, these, combined with the high opportunity cost of illness, can be devastating for households living below the poverty line. Literature on the poverty impacts of micro health insurance is limited, but a recent study from Bangladesh indicates that placement in a micro health insurance scheme is significantly associated with food sufficiency.¹⁴ The study postulated that links of insurance coverage with income and probability of living above the poverty line could also be strong if studied in a dynamic context (this used cross-section data).

11. The vulnerability of poor households in Pakistan to health-related shocks is well established. A study by the World Bank assessed that such shocks (related to death, illness, or disability) constituted 54% of the total shocks experienced in safety net recipient households over 3 years, and that expenditure to deal with such shocks constituted a similar proportion of the annual household expenditure for the poorest income quintiles.¹⁵ Similarly, the World Bank's analysis of longitudinal household data shows that serious illness in an adult household member can have catastrophic effects on household wealth (footnote 15). The panel data also showed that 18.7% of households surveyed reported having experienced a severe health-related shock in the previous year (footnote 14).

12. The survey found that health shocks were the most prevalent idiosyncratic shocks. Further, the negative impact of a health shock on caloric intake was found to be fairly significant (footnote 14). In general, the proportion of households facing catastrophic health expenditure appears to have been increasing over time—in the early 1990s, 3% of the population fell below the poverty line due to health expenditure, but at the beginning of the current decade this

¹² A. Fiszbein et. al. 2009. *Conditional Cash Transfers: Reducing Present and Future Poverty*. World Bank Policy Research Report. Washington, DC: World Bank.

¹³ P. Gertler and J. Gruber. 1997. Insuring Consumption against Illness. *NBER Working Paper*. No. 6035. Washington, DC: National Bureau of Economic Research.

¹⁴ S. A. Hamid, J. Roberts, and P. Mosley. 2010. Can Micro Health Insurance Reduce Poverty? Evidence from Bangladesh. *Sheffield Economic Research Paper Series*. No. 2010001. University of Sheffield, Department of Economics.

¹⁵ World Bank. 2010. *Delivering Better Health Services to Pakistan's Poor*. Washington, DC: World Bank. p. 70

proportion had increased to 4%. The fact that public health services, which are supposed to be free or subsidized, are in practice only accessible upon payment exacerbates the problem. Unlike the cash transfer and micro health insurance, both of which provide instant relief, a skills development program has longer term but more sustainable benefits.

C. Broader Socioeconomic Impacts

13. In the longer term, cash transfer programs where transfers are made in the name of women household members are empowering, and promote women's decision-making power within the household. A recent BISP evaluation shows that in 60% of cases, the female household member receiving the cash made the decision on how the extra funds were to be used.¹⁶ To the extent that the additional cash is used to buy essential food items, it improves the nutritional status of the family, particularly children. If the additional funds are used to access medical care, as research in Pakistan indicates, the positive externalities are also considerable.

14. The broader impacts of the health insurance program (*Waseela-e-Sehet*) are positive. The World Bank's work on health services accessed by the poor in Pakistan shows that during 2004–2005 the poorest patients using obstetric facilities in public hospitals in the city of Karachi were spending 20% of their average monthly income for each stay in facilities that were supposedly free of cost for them.¹⁷ The report also quoted another survey dating from the same period, which found that the difference in cost between private and public health services accessed by the poorest sections of society was minimal, and that out-of-pocket payments for health care are endemic in Pakistan (footnote 15). Health insurance thus not only serves to mitigate the effects of shocks, but can also enable beneficiaries to access medical services for routine care, and for cases such as child delivery that would often, in the absence of support, be dealt with by traditional birth attendants or through other nonformal support systems. The fact that health insurance may in the long term encourage institutional childbirth can have significant impacts on maternal and child mortality.

15. The skill development program (WER) can have medium-term benefits. In the shorter term, sending a family member for vocational training may actually entail costs for the household in terms of lost income (if the trainee was employed), but the stipend largely mitigates this effect. In the medium term, training can significantly increase income-earning potential in a country like Pakistan where the unskilled–skilled labor wage gap is significant. Cross-country evidence (as well as evidence from Pakistan) indicates that skills development can have very positive impacts on poor beneficiaries. The argument here is beyond general

¹⁶ United States Agency for International Development. 2011. *Final Monitoring Report for Benazir Income Support Program*. Islamabad.

¹⁷ World Bank. 2010. footnote 15. The study cited earlier work showing that an average stay in an obstetrics ward in a public hospital in Karachi cost a poor family PRs590. The average income for such families was estimated at PRs3,000 per month. The data was collected in 2004 from four public hospitals in Karachi.

considerations about returns to schooling, which can be positive and significant.¹⁸ Current resources annually invested (and planned) by the BISP for the WER seem to be having negligible impacts on the employability of beneficiaries, mostly due to fundamental design insufficiencies. The modifications being proposed under the ADB project are an effort to make the WER much more relevant to the economic circumstances and employment opportunities (wage and self-employment) of the targeted population group.

16. According to the latest Labor Force Survey, the average monthly wage for unskilled labor was PRs5,716 in 2010/11.¹⁹ This rose to PRs7,220 for those working as skilled labor in agriculture and fisheries, and to PRs8,560 for plant and machine operators and assemblers. The challenge is to ensure that courses being offered provide skills that are in demand in the job market, and that the quality of instruction is assured. The program has particular significance in Pakistan's current security and social context, where a demographic "youth bulge" is evident, but is occurring at the same time as a slowdown of the economy and in the midst of a precarious security situation. While young people are more often than not agents for positive change in society, they are also vulnerable to the lure of destructive ideologies if they see no hope for a better future.

D. Conclusion

17. All three proposed programs are expected to have positive impacts on household incomes and the household capacity to withstand shocks. Since the BISP beneficiaries are women, the program also promotes the idea that household access to better services and other social assistance is moderated through its female members—a concept that goes a long way toward promoting women's empowerment in the poorest sections of society.

¹⁸ A recent background paper for the World Bank's World Development Report on Jobs presents unified estimates of returns to schooling from the latest available surveys and patterns using the same specification and estimation procedure and data from 131 economies and 545 harmonized household surveys. This comprehensive effort addressed well-known empirical challenges in past work, such as (i) the definition of the dependent variable, (ii) the variables used as controls, (iii) sample definitions, and (iv) the estimation method. The paper shows that private rates of return for schooling across a range of countries are more concentrated around the mean than previously thought; and that private returns are higher (lower) in the higher (lower) schooling levels. Specifically, the authors find "*In agrarian economies, such as Kenya, Myanmar and Senegal, for example, the returns to schooling are high at all levels, probably as these are low income economies with a scarcity of human capital. In conflict-affected states, such as Afghanistan, Liberia and Sri Lanka, the premium to investing in primary schooling is high. In resource-rich economies, such as Botswana, Papua New Guinea and Peru, returns to schooling are high at all levels, suggesting that human capital skills are a complement to resources. Small-island states, such as Fiji, Tonga and Tuvalu, the returns are relatively higher at the primary level, emphasizing need for basic skills in such states. In urbanizing economies, such as Bangladesh, China and Morocco, premiums are high at all levels; in youth bulge economies, such as Egypt, South Africa and Tunisia, the returns to schooling are relatively lower; in formalizing economies, such as Brazil, Mexico and Turkey, the returns to schooling are relatively lower; and in aging economies, such as Argentina and Bulgaria, the returns are relatively lower.*" Also, the authors report "*returns to schooling continue to be healthy, at about 10 percent a year globally. By level of schooling, the returns to schooling are highest at the tertiary level, showing that the demand for higher levels of skills is increasing and that the demand for skills is global. At the same time the returns to schooling are high at the primary level, signaling continued need for basic skills. Overall the returns to schooling are low at the secondary school level as a result of the increased demand for skills, prompting the best secondary school students to continue their education at the tertiary level. The returns to schooling are relatively higher in poorer economies overall. They are uniformly high for primary schooling in low income economies. But they are also high for tertiary in low income economies. In general, the returns to schooling are low for secondary school graduates.*"

¹⁹ Government of Pakistan, Bureau of Statistics. 2012. *Labor Force Survey 2010–11*. Islamabad.