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# An Inclusive Growth Dividend: Reframing the Role of Income Transfers in India's Anti-Poverty Strategy<sup>§</sup>

**ABSTRACT** Both theory and evidence suggest that unconditional universal income transfers can not only reduce poverty, but also improve productivity and achieve development goals more broadly. Given recent policy initiatives in India to support farmers with income transfers (at an estimated cost of around 0.4 percent of GDP), we propose an expansion of this approach to cover *all* citizens, as one component of India's portfolio of social protection programs. Specifically, we propose that India implements an inclusive growth dividend (IGD), pegged at 1 percent of GDP per capita, which reaches all citizens and grows equally for all with the economy's growth. This will be both fiscally feasible and practically implementable and would be a powerful practical and symbolic commitment to universally shared prosperity. We review global evidence on the impact of income transfers and argue that an IGD would be a highly cost-effective way of directly reducing poverty, with limited administrative costs of targeting, reduced risk of exclusion errors, lower leakage of benefits, and *lower* disincentives for work compared to most targeted programs. It would also improve financial inclusion and formal savings, relax borrowing constraints for productive investments, and improve female empowerment. Further, successfully delivering an IGD would augment the capacity and credibility of the Indian State. Over time, it could create an attainable benchmark against which to evaluate (and improve) the quality of public expenditure. Finally, we note that an IGD could be a powerful tool for the Government of India to promote the objectives of equity and efficiency given the vast differences in income levels and state capacity among Indian states.

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## 1. Introduction

There has been a global surge in academic and policy interest in using universal basic income (UBI) to alleviate poverty and enable inclusive prosperity.<sup>1</sup> In the Indian context, several scholars and policy commentators have argued over the past decade that inefficient and poorly implemented welfare schemes should be replaced with direct income transfers to the poor.<sup>2</sup> The 2016–17 *Economic Survey of India* gave further policy salience to the idea of a UBI for India by recommending its active consideration. Parallel investments in the *Jan-Dhan, Aadhaar, Mobile (JAM)* infrastructure required to implement direct benefit transfers (DBT) into beneficiary bank accounts, have also made it feasible to implement the idea.

The move to income transfers as a component of India's anti-poverty strategy has also been reflected in actual policy in the last two years, especially in the context of farmers' welfare. The State of Telangana's early 2018 launch of the *Rythu Bandhu* Scheme (RBS), which gave farmers an unconditional payment of ₹4,000 per acre, pioneered this approach. Since then, such policies have been replicated at both the state level (as in the *Krushak Assistance for Livelihood and Income Augmentation (KALIA)* program

1. While the discussion in developed countries has been motivated mainly by concerns of needing to find policy responses to rapid automation and job destruction, the discussion in developing countries has focused more on the benefits of income transfers relative to targeted in-kind transfers because of weak state capacity for implementation (seen, for instance, from considerable targeting errors and leakage in benefits).

2. A non-exhaustive list of references making this argument includes Kapur, Mukhopadhyay, and Subramanian (2008a; 2008b), Bardhan (2011; 2016; 2018), Banerjee (2016), Ghatak (2016), Joshi (2016), Mundle (2016), and Ray (2016). Note that not all of these pieces call for universality in income transfers, with some like Kapur, Mukhopadhyay, and Subramanian (2008a; 2008b) putting more emphasis on replacing in-kind benefits with cash transfers for program beneficiaries. Davala *et al.* (2015) make the argument for basic income without explicitly calling for the substitution of other programs. Critics of income transfers in India primarily worry that it will lead to a substitution of in-kind welfare programs and an abdication of the responsibility of the government to guarantee minimum levels of basic goods and services. Representative references include Shah (2008), Dreze (2018), and Roy (2019a). Khosla (2018) provides an excellent summary of the key issues with a focus on the Indian context.

in Odisha) and the national level (through the PM-KISAN program). The *Pradhan Mantri Kisan Samman Nidhi Yojana* (PM-KISAN) was launched in December 2018. At first, it provided ₹6,000/year per family with cultivable landholding up to two hectares, subject to some exclusions. The first Cabinet meeting of the NDA Government after re-election in 2019 extended the scheme to *all* farmers, regardless of landholdings. Today, it is likely the world's largest income transfer scheme. With the extended coverage, it aims to reach 14.5 crore farming households (or roughly half the country) with an estimated cost to the Central Government of ₹75,000 crores for the year 2020–21, or roughly 0.4 percent of GDP at current prices.<sup>3</sup>

As a result, the relevant questions regarding the role of income transfers in India's anti-poverty strategy have shifted from whether to have them at all to how to think about the design, coverage, and scope of such a policy. This paper, therefore, focuses on the following main questions: Should these income transfers be made universal, covering all citizens regardless of whether they are farmers? Should income transfers supplement other programs, or should they substitute existing welfare programs? Considering both the broad development strategy and also the opportunity cost of resources, how might such a policy fit in with other anti-poverty and social welfare policies? How can such a policy be both fiscally viable and mitigate the concerns regarding UBI raised by skeptics? How can the needs and preferences of beneficiaries be taken into consideration accounting for heterogeneity in these over time and space?

While much has been written about income transfers in recent years, this paper is motivated by: (a) the need for this debate to reflect recent evidence on actually implementing income transfer policies in India as well as data on beneficiary preferences and experiences, (b) the greater political willingness to implement income transfers at scale (seen in the PM-KISAN program), which makes it especially policy-relevant to provide both conceptual clarity and a practical roadmap forward, and (c) the urgency of strengthening India's social protection architecture in light of the economic hardship induced by COVID-19 and the associated lockdowns to slow the spread of the virus. In addition to providing a concise discussion of the conceptual issues, we offer a specific policy proposal that we believe is implementable at scale and will deliver almost all the benefits of UBI while mitigating

3. PM-KISAN was launched during the 2019 Interim Union Budget of India and came into effect from December 1, 2018 (Government of India 2019a; 2019b). For the year 2019–20, the estimated cost of the scheme was ₹87,217.50 crores, which amounts to roughly 0.5 percent of GDP at current prices (Source: <https://www.indiabudget.gov.in/doc/eb/sbe1.pdf>).

several of the concerns that have been raised by skeptics. We summarize the core argument below.

Theory and evidence point to several advantages of unconditional universal income transfers as a tool not only for anti-poverty policy but for achieving development goals more broadly. Such transfers directly reduce poverty and have the following attractive properties: limited administrative costs of targeting and lower risk of exclusion errors (since they are universal); lower leakage of benefits because of fewer intermediaries between fund disbursal and receipt; *lower* disincentives for work compared to most targeted programs;<sup>4</sup> greater sociological acceptability because of the lack of “rank reversal” in incomes that often happens under targeted programs; improved financial inclusion and formal savings, which can, in turn, mitigate risk and enable consumption smoothing at a lower cost than credit (which is subject to higher costs of financial intermediation); relaxing borrowing constraints for productive investments, and improved female empowerment (especially if transfers to children are sent to their mothers’ accounts).

However, we believe that one reason that policy has moved more slowly despite the endorsement by the *Economic Survey* is that policy discussions of universal income transfers have been conflated with those of a UBI. Specifically, the term “basic income” connotes an amount sufficient for survival, and most academic and policy discussions of a UBI have focused on transfers large enough to nearly eliminate poverty, ranging from 3.5 to 4 percent of GDP (Government of India 2017; Joshi 2016) to 10–11 percent of GDP (Bardhan 2016; Ghatak 2016). As a result, the fiscal math simply does not work out.<sup>5</sup> It is impossible to implement such a large universal transfer without either cutting other major anti-poverty programs or substantially increasing the tax to GDP ratio (currently around 18 percent). Alternatively, a large transfer automatically necessitates some targeting, which negates several key advantages of universality.

As we discuss in detail, even if we were to believe that income transfers are a more efficient way of achieving the goals of existing welfare

4. This point is not well understood by many commentators who continue to believe that unconditional income transfers will reduce work incentives. As we discuss in Section 2, the need to phase out targeted benefits with income growth usually leads to a high marginal tax rate on income just in the range where people are climbing out of poverty. This is typically a much bigger disincentive to work than the income effect of a universal unconditional transfer that is not phased out.

5. Not all proposals of UBI involve committing such a large amount to UBI only. For example, Bardhan (2018) argues that about 10 percent of GDP is potentially mobilizable by eliminating regressive subsidies and imposing some fresh taxes and that should be equally allocated to fresh public expenditures on health, education, infrastructure, and UBI.

programs, it is politically and practically infeasible to cut major categories of government welfare spending. In contrast, it is much more feasible to direct the *incremental* rupee that is earmarked for welfare spending towards income transfers.<sup>6</sup> This is exactly what is happening with the *Rythu Bandhu*, KALIA, and PM-KISAN schemes. While no existing scheme has been replaced to finance these programs, they still represent a landmark policy pivot to spend the *marginal rupee* allocated to farmers' welfare on direct income transfers as opposed to increases in distortionary subsidies, procurement prices, or loan waivers. Our proposed policy follows exactly this same approach.

Specifically, we recommend that India adopt an “inclusive growth dividend” or IGD for every citizen that is pegged at 1 percent of GDP per capita to be deposited directly into the bank account of every citizen on a regular monthly basis.<sup>7</sup> This would provide every citizen with a supplemental benefit of around ₹120 per month (at current estimates).<sup>8</sup> The amounts for children under 18 should be transferred into the accounts of their mothers (or the next responsible guardian). We believe that such an approach, which is modest in magnitude but ambitious in reach (by being truly universal), can achieve almost all the benefits of income transfers discussed above while mitigating almost all the concerns raised to date regarding the potential costs of a UBI, as we discuss further below.

First, the terminology of an IGD sets a very different set of expectations than a UBI. The term “dividend” makes it clear that this is one component of a *portfolio* of income streams that people would have. The word “inclusive” reflects the progressive aspect of the proposal: since the amount is the same for all citizens, the marginal value of the transfer is correspondingly greater for the poor. Finally, the word “growth” captures the idea that the amount will grow along with the growth of the overall economy. Thus, an IGD would be one component of people's income which reaches all citizens and

6. A similar point was made by former Chief Economic Adviser, Arvind Subramanian, in conversation with one of us (see Muralidharan and Subramanian 2015 for more details).

7. The specific terminology and proposal were introduced by one of us in a joint op-ed with Paul Niehaus and Sandip Sukhtankar (Muralidharan, Niehaus, and Sukhtankar 2018a) and in short internal notes for the Ministry of Finance put together by Muralidharan in 2017–18. One of the main goals of this paper is to flesh out the full details of such a proposal and place the recommendation in the larger policy context and more fully distinguish it from the related but distinct discussions of a UBI.

8. This is obtained by taking the latest estimate of GDP per capita at current prices (2018–19), which is ₹142,963 (see Government of India 2020, Statement 2, p. 5). Taking 1 percent of this gives a monthly figure of ₹119, which we round off to ₹120.

grows equally for all with the economy's growth. It would, thus, be a powerful practical and symbolic commitment to universally shared prosperity.

We now discuss the various benefits of such an approach. The biggest advantage of our proposed scheme is simply that it is affordable enough to actually be implemented. Indeed, the value envisaged by the IGD is quite similar to that of PM-KISAN (which works out to ₹500/month per household or ₹120/month per person) and so it can be implemented simply by roughly doubling the budget for PM-KISAN and making the program truly universal.<sup>9</sup> This would allow benefits to also reach landless laborers, who are typically more likely to be destitute and needy than farmers who own land. It would also reduce the likelihood that farmers continue to engage in economically unviable cultivation just to get the PM-KISAN benefit. It would be easier to implement by further reducing eligibility and verification costs. Also, by being at the individual level, it would limit the potential for gaming the scheme (by households splitting to double the value of the transfer). Further, as we discuss in Section 3, an IGD would advance several other social goals, including female empowerment, financial inclusion, and savings (and be a complement to the *Jan-Dhan* Scheme). It would also augment both the capacity and the credibility of the Indian State by building and demonstrating the ability to deliver a benefit to every citizen—a first in independent India.

In addition to the well-known benefits of income transfers discussed above, we believe that a critical long-term benefit from an IGD may be to increase the quality of *all* public expenditure by providing an attainable benchmark against which government programs can be assessed. As we document in Section 2.1, evidence suggests that there is a lot of “value destruction” in public service delivery in India because the government incurs large costs in providing services of such low quality that people opt for paid market solutions despite the public services being “free”. Credibly delivering an income transfer every month to every citizen will, over time, allow the government to consider whether it is more cost-effective to directly provide a service or simply provide a fiscally equivalent income transfer directly to intended beneficiaries (to use on market-provided solutions). In many cases, beneficiaries themselves can exercise this choice (as suggested

9. As we discuss later, we do not envisage any exclusions from eligibility at this point simply because we believe that it is a powerful symbol of inclusive development and state capacity for the government to demonstrably reach every citizen credibly month after month. One option for excluding the affluent would be to have a “give it up” equivalent option at the time of filing tax returns, whereby citizens who earn above the income tax exemption limit can indicate on their tax returns if they would prefer to forgo their IGD.

by Muralidharan, Niehaus, and Sukhtankar 2018b, in the context of the public distribution system (PDS)).

In other words, income transfers would become a low-implementation cost “index fund” for development spending and in-kind programs would need to demonstrate that their targeting, administrative, and implementation costs deliver more value than their cost. Over time, programs that deliver less value than their cost could be replaced with income transfers while those that deliver more value can be retained. Note that this approach does not make any blanket assumptions regarding the quality (or lack thereof) of government service delivery. Rather, it raises the accountability of government spending by providing a fiscally equivalent benchmark.<sup>10</sup> This can have major long-term positive implications for the quality of government expenditure, both by scrapping programs whose value is less than their cost and by forcing programs to become more efficient to deliver value in excess of their cost.

An IGD will also promote inter-state equality, equity, and efficiency. First, as an equal payment to all citizens, an IGD clearly meets the equality consideration. Second, because the marginal value of an IGD is much higher in poorer areas, it is progressive by construction.<sup>11</sup> It is also progressive by being directly based on the population, which favors poorer states. Finally, since it will be financed out of the general tax pool (which the rich contribute more to), it is also progressive on the financing side. Thus, an IGD is a powerful tool for promoting equity across the country.

The IGD’s contribution to efficiency is more subtle. A vexing challenge for the Government of India is that economically disadvantaged states also have weaker governance. For instance, teacher and doctor absence rates in public schools and clinics are consistently higher in states with lower per capita income (Chaudhury et al. 2006). Similarly, welfare programs

10. To continue the analogy from investing, the powerful insight of John Bogle was that fund managers all claim to have “alpha” (i.e., they claim to be able to beat the market). But most actively managed funds deliver less value over time than low-cost index funds because the fees of the former destroy considerable value. Of course, in the case of public spending, it is possible that many projects have positive “alpha” (which they will if they are true public goods), but it is also true that many programs have negative “alpha” where beneficiaries are better off with an income equivalent. Our point is simply that an IGD will make these trade-offs clear.

11. We estimate that it would increase per capita income by 16 percent for the poorest 5 percent of the rural population, and by 13 percent for those between the 6<sup>th</sup> to 10<sup>th</sup> percentiles. The corresponding figures for the urban population are a 12 percent increase for the poorest 5 percent and a 9 percent increase for those between the 6<sup>th</sup> and 10<sup>th</sup> percentiles. At the top end of the distribution, the IGD would increase per capita income by 2 percent for the top 5 percent of the rural population and by 1 percent for the top 5 percent of the urban population. See Table 1 in Section 3.3 for details.

like the NREGS disproportionately benefit better-off states because poorer states lack the administrative capacity to effectively avail of Government of India funds (Aiyar 2014). Thus, to the extent that the Government of India's expenditure on welfare programs aims to reduce inter-regional inequality, direct transfers to citizens may be more efficient than in-kind programs because of weaker governance in poorer states.

Our proposed scheme is a specific version of the idea of a universal basic share (UBS) scheme proposed by Ray (2016), where a share of GDP as opposed to an absolute amount is committed to a universal basic income scheme.<sup>12</sup> Two key benefits of a UBS relative to a UBI highlighted by Ray (2016) are that it is inflation-proof and automatically indexed, and also that it is a flexible, not fixed, commitment that co-moves with GDP.<sup>13</sup> Our proposal also builds on a very similar idea mooted even earlier by Sunil Khilnani, who made the case for a "Citizen's Growth Dividend".<sup>14</sup> Khilnani (2010) emphasizes that the political case for such an approach is recognizing citizens as individuals as opposed to groups (which are the de facto basis on which political mobilization takes place). Both Ray (2016) and Khilnani (2010) emphasize the shared solidarity and "equity-like" sharing in a country's prosperity, which we also highlight here. A similar argument has been made in the context of the US by Shiller (2009).

Thus, our primary contribution is to expand on the conceptual framework described in short essays by Shiller (2009), Khilnani (2010), Ray (2016), and Muralidharan, Niehaus, and Sukhtankar (2018a) and provide a more comprehensive treatment of the relevant issues from a broad development policy perspective, with an emphasis on the Indian policy context. In particular, we move beyond discussing universal income transfers as a redistributive policy aimed at supporting the poor, to highlight that they can also be a powerful tool for alleviating micro-economic constraints to development, and thereby improving productivity and boosting economic growth. In practical terms, we also note that the adoption of universal income transfers may be sub-optimally delayed if discussed alongside the question of which in-kind programs to substitute away from. While some substitution will likely make

12. Ray (2016) proposes a benchmark of close to 9 percent of GDP for UBS, which would be fiscally impossible without substantially raising tax revenue or cutting other expenditure. However, he also notes that it is possible to start with a smaller amount and increase it over time.

13. Ray (2016) and Moene and Ray (2016) also discuss additional possible advantages of a UBS scheme, such as creating a broad-based support for tax collection capacity and economic growth among citizens.

14. We thank Pranab Bardhan for pointing out this reference to us, which was not known to us at the time of writing the first draft.

sense over time, we emphasize that this should happen gradually, only after credibly building and demonstrating the capacity of the government to consistently deliver income transfers to all Indians, and ideally based on beneficiary choice. We also ground our discussion of the IGD with evidence on the quality of public expenditure and the track record of implementation of income transfers and other social programs in the Indian context and present a very specific idea that is feasible to implement in the near future.

The rest of the paper is organized as follows. In Section 2, we review the broad conceptual issues involved in thinking through the trade-offs regarding various aspects of the design of income transfer programs as well as the relevant evidence from India and other developing countries. In Section 3, we flesh out the IGD approach in detail and provide specific illustrations of the general aspects of income transfer programs discussed in Section 2 in the Indian context. Section 4 provides an implementation roadmap, and Section 5 has some concluding observations.

## 2. Key Conceptual Issues

In this section, we review the various arguments and related evidence from India and other developing countries regarding the role of unconditional income transfers as a tool of development policy. We focus on the key conceptual arguments and broadly review the evidence. In particular, we consider the argument regarding the relative value of spending the marginal rupee spent on anti-poverty policies on income transfers as opposed to the direct provision of goods and services aimed at the poor; supplementation versus substitution; the pros and cons of targeted versus universal programs, and the potential impact of an unconditional income transfer scheme such as the IGD on wasteful consumption, work incentives, gender empowerment, relaxing borrowing constraints, providing partial mitigation of consumption risk, and facilitating saving for the poor.

### *2.1. Income Transfers versus Direct Provision of Goods and Services*

A key consideration in assessing the case for income transfers is the question of opportunity costs and whether the same resources could be spent better. Critics of income transfers have argued that it would crowd out resources for spending on other important categories of public expenditure, such as education and health, which may have a greater long-term impact on improving citizens' welfare (see, for instance, Aiyar 2019; Roy 2019a). As some critics have put it, the move towards income transfers represents giving up

on the idea of a “developmental state” and moving towards a “compensatory state” (Roy 2019a). Taken to the extreme, such an approach could lead to the abdication of core responsibilities of the state.

How should we assess this criticism? There are two key concepts to keep in mind while assessing the opportunity cost of funds that may be allocated to an income transfer program. The first is expenditure on public goods versus redistribution, where redistribution includes publicly provided private goods (like education, health, or food) where the government provides free or highly subsidized services to make them accessible to the poor. The second is the quality and effectiveness of public expenditure on redistribution and publicly provided private goods.

Most economists (including us) believe that the returns to spending on public goods and infrastructure significantly exceed the costs, especially in countries like India. Examples of such investments include transportation and market integration (such as roads, railways, and ports), communications (Internet cables), public health (anti-vector campaigns, water, and sanitation), and basic research. The return to these public goods likely exceeds their costs because their social benefit is the sum total of private benefits across millions of individuals. Moreover, since the market on its own is unlikely to provide the socially optimal amount of these public goods, the case for public leadership in ensuring adequate provision is clear.

However, in practice, the patterns of public expenditure in India suggest that substantial funds are allocated to further broadly redistributive goals. These include subsidies to make items (such as food, fuel, and fertilizer) cheaper for the poor, as well as investments in publicly provided private goods (such as government-run schools, clinics, and fair-price shops that distribute subsidized food under PDS). Here, an important rationale for public provision is the ability to offer the service at low or no cost to the poor (which is a redistributive goal).<sup>15</sup>

Analysis of public expenditure in India suggests that a much larger fraction of social sector spending goes to redistribution rather than public goods. For instance, in agriculture, public expenditure on interest, fertilizer, and electricity subsidies is much greater than spending on public irrigation or agricultural research and extension.<sup>16</sup> Similarly, in health, expenditure on

15. The National Rural Employment Guarantee Scheme (NREGS) has elements of both public good creation (through construction of rural assets) and redistribution (through creating jobs for the rural poor).

16. Interest subsidies alone account for ₹21,175 crores in the budget for the Ministry of Agriculture and Farmers’ Welfare in the 2020–21 Union Budget. Further, fertilizer subsidies under the Ministry of Chemicals and Fertilizers are worth ₹71,309 crores. Together, expenditure

curative services (a private good) is greater than that on public goods with substantial positive externalities such as vector control and immunizations. This is also true in education, where the majority of expenditure is on teacher salaries (for providing education) rather than on public goods such as setting standards and syllabi and running public examination systems.<sup>17</sup>

Thus, to assess the relative value of expanding income transfers versus expanding public provision of goods and services, we need to assess the quality of public expenditure in doing so. This is an area where a considerable amount of research has been done in the past 15 years, and several pieces of evidence suggest that the quality of expenditure on public services under the status quo is quite poor.

Take the example of schooling, where the public spending per student in government schools is over three times higher than the total cost per student in affordable private schools. Yet high-quality evidence finds that private schools are still at least as effective at improving student learning (Muralidharan and Sundararaman 2015).<sup>18</sup> The main drivers of greater productivity of spending (defined as learning outcomes produced per rupee spent) in private schools are much lower teacher salaries (allowing them to hire more teachers, which leads to smaller pupil–teacher ratios and less multi-grade teaching) and better accountability (which leads to lower teacher absence rates and greater time on task). Millions of parents choose to pay out of pocket for these private schools—even though public schools are available for free or even at a *negative* cost (because they provide students with free books and mid-day meals).

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on just these two subsidies is over 11 times the total budget for the Department of Agriculture Research and Education (₹8,363 crores). In addition, state budgets also spend more on electricity subsidies for groundwater than on investments in public irrigation.

17. The reasons for this pattern of expenditure are beyond the scope of this paper, but one broad explanation is that India adopted universal adult franchise-based democracy at a much lower level of per capita income than most other OECD countries. Thus, India faced political pressure for redistribution and subsidized or free access to services at a much lower level of development compared to historical norms (see Muralidharan and Subramanian 2015, for a more extended discussion).

18. Note that a naive comparison of student learning outcomes across public and private schools will yield an incorrect impression that private schools are better. This comparison does not account for the fact that parents of children attending private schools are typically more educated and affluent than those of parents attending government schools. Muralidharan and Sundararaman (2015) address this concern using a large-scale randomized experiment where randomly selected students (using a lottery) in government schools were provided a voucher to enable them to attend a private school of their choice. Tracking outcomes over time for lottery winners and losers allows for a more accurate comparison of the effects of attending private versus government schools.

The health care situation is even more striking. Over 70 percent of primary health care visits in rural India are to fee-charging private providers, even when the village has a public health clinic. Private providers are less qualified but exert more effort (Das et al. 2016). Further, Das et al. (2016) show that private providers with lower qualifications deliver comparable quality of care as in the public sector but at less than one-fourth the cost per patient seen. Just like in education, an important mechanism for the greater cost-effectiveness of private providers is lower pay and higher effort.

The flight of the poor towards market solutions is at least in part a consequence of the poor accountability of public sector service providers. This is starkly illustrated by the high rates of teacher and doctor absence across India (25 percent and 40 percent, respectively). Overall, the government incurs large costs in providing services that are of such low quality that most people do not want them. In other words, there is considerable “value destruction” in the status quo of public service delivery since the service provided is valued considerably lower than the cost of providing it. Thus, while there is a strong need to improve the quality of government services, the evidence suggests that value for money under the status quo is low and that the returns to simply increasing spending along existing patterns are likely to be low. Further, evidence from multiple studies suggests that improving governance can be many more times more cost-effective at achieving the same level of effective increase in the presence of a program on the ground than spending more on the program itself.<sup>19</sup>

One way of doing this is to improve top-down governance, which is what the existing evidence is based on. However, another way of forcing the public sector to improve its efficiency is by eliminating the captive market of poor households by enabling the poorest to avail of services from both public and private providers.

The above discussion highlights that providing some income support should be seen as a *complement to public services and not a substitute*. Over time, once the state shows that it can credibly reach the poorest through income transfers, it opens up a set of policy options whereby the poor can choose between status quo public services and an equivalent cash transfer.<sup>20</sup>

This approach makes no assumptions regarding the relative merits of provision of services by the state or the market. We recognize that there is

19. See Muralidharan, Niehaus, and Sukhtankar (2016) for evidence in the context of NREGS, Muralidharan et al. (2017) for evidence from education, and Muralidharan et al. (2019) for evidence from a cash transfer scheme for farmers.

20. Such an approach has been outlined in the case of the PDS by Muralidharan, Niehaus, and Sukhtankar 2018b.

enormous heterogeneity in both provider quality and beneficiary preferences across time and space. Rather, our point is that having income transfers be part of the portfolio of policy options to reach the poor can empower beneficiaries to have a stronger voice in how social sector funds (spent in their name) are actually spent. Over time, the public sector would need to show that it can deliver more value than an equivalent income transfer and compete for the business of the poor who will be empowered with more options after their incomes are augmented.

To summarize this section, we believe that expenditure on pure public goods—especially productivity-enhancing infrastructure—should not be crowded out to make fiscal space for income transfers. However, we believe that at least one component of the budget allocated for poverty alleviation and publicly provided private goods could fruitfully be used for income transfers instead. This informs our view of income transfers as one key component in a portfolio of social protection policies. Such an approach will empower citizens to choose from a broader menu of service providers (including private and non-government providers) and to increase the accountability of public provision through greater choice and competition.

## *2.2. Substitution versus Supplementation*

Most of the existing discourse on the UBI has assumed that the fiscal space for UBI/income transfers would come from existing programs, which would be replaced with income transfers. However, this has almost never been successfully done in practice. There are several reasons for this including the considerable political economy challenges of shutting down existing programs that benefit millions of people, and the risk of imperfect implementation of cash transfers.

Recent evidence illustrates how implementation challenges are non-trivial. Starting in 2015, the Government of India attempted a pilot in the three Union Territories of Chandigarh, Puducherry, and Dadra and Nagar Haveli. The government replaced PDS entitlements (subsidized foodgrains) with DBT into bank accounts.

However, a process monitoring study with over 10,000 household surveys (Muralidharan et al. 2017) reported that though government records showed that over 99 percent of transfers had been made successfully, *nearly a third of households reported not having received their transfers*. This likely reflected a combination of funds going to an inactive account, passbooks not being updated, and no outbound notification of fund transfer.

In ongoing work with other co-authors, one of us has found similar issues in the flagship Prime Minister's Maternity Benefits Scheme or *Pradhan*

*Mantri Matru Vandana Yojana* (PMMVY), where we monitored implementation quality in Jharkhand.<sup>21</sup> Officials at more senior levels (district and above) indicated that no eligible woman was being excluded. However, at more junior levels, 30 percent of supervisors and 50 percent of Anganwadi workers reported cases of beneficiaries not being registered and hence not receiving their payments. This is corroborated by our survey of actual eligible beneficiaries, where less than 40 percent of eligible women reported receiving their most recent payment. Since payments may arrive late, this should be interpreted as the fraction of women receiving benefits on time. However, given the goal of providing funds to pregnant and lactating mothers during the key stages of child development, delayed payments are still a significant marker of weaknesses in last-mile delivery.

This field experience highlights how non-trivial it is to ensure that all beneficiaries have bank accounts that are seeded with *Aadhaar* details as well as eligibility details, and that transfers are made reliably. Given the implementation issues that we have documented across sectors and states, we feel that for political and ethical reasons, it is not prudent to embark on income transfers based on mandated substitution of other benefits.

Further, given the political difficulty of scrapping or replacing existing programs that have millions of beneficiaries, the many benefits of having predictable income transfers comprise one part of the portfolio of anti-poverty strategies that are not getting realized. In part, this is because there is no way to make the fiscal space for the large transfers (envisaged under most UBI proposals) that would be needed to eliminate poverty without also replacing existing programs.

So, from a practical policy perspective, we feel that “less is more.” Starting with a modest supplementary income transfer to all citizens will allow us to get started on the path towards realizing the many benefits of income transfers while mitigating several concerns that have been raised by critics. We refer to this approach as an inclusive growth dividend or IGD (which we explain in more detail in the next section).

Our recommended approach is also consistent with how income transfers are playing out in practice in India. The political economy of expenditure reform is that it is much more difficult to change existing spending than it is to improve the quality of new spending (Muralidharan and Subramanian 2015). We see this playing out in the introduction of income transfers as the preferred policy instrument for supporting farmers over the past 15 months, starting with the RBS in Telangana, and then followed up by the KALIA

21. This is based on ongoing work by Muralidharan with Paul Niehaus, Sandip Sukhtankar, and Jeff Weaver.

program in Odisha and the PM-KISAN program on a nationwide basis. Note that these are all *supplemental* programs that do not replace any existing programs or subsidies. However, they do considerably improve resource allocation at the margin because the marginal rupee earmarked for farmer support was spent on these transfers rather than the much more distortionary default options of farm loan waivers and increases in minimum support prices (MSPs).

### *2.3. Targeted versus Universal Income Transfer Programs*

The pros and cons of targeted versus universal social welfare programs have been discussed extensively in the public economics and development economics literature (see, for instance, the discussions in Banerjee, Niehaus, and Suri 2019; Currie and Gahvari 2008; Ghatak and Maniquet 2019; Hanna and Olken 2018). This section summarizes the key trade-offs.

Compared to targeted income or benefit transfer schemes that are aimed at the poor and are therefore subject to means-testing, IGD is an unconditional stream of cash income paid by the government to every member of society—it is paid regardless of whether an individual is working, of his or her existing income, and whoever he or she lives with.

There are three aspects of the design of such a program. First, it is an income transfer as opposed to an in-kind transfer like food, housing, or fuel.<sup>22</sup> Second, it is universal, that is, it is not targeted to any specific group based on socioeconomic or demographic criteria (such as age, gender, marriage or family status, and family composition), and it is provided at the level of the individual as opposed to the household. Third, it is unconditional and not contingent on the recipient satisfying any compliance criteria or being deemed as deserving. This makes an IGD distinct from conditional transfer schemes that are contingent, for example, on parents sending their children to school.

From the economic point of view, the absence of means-testing or targeting is the most salient aspect of programs like a UBI or an IGD.<sup>23</sup> The main reasons for this design are explained as follows.

Any program that is not universal has substantial direct and indirect administrative costs of targeting the relevant group (Hanna and Olken 2018). It also creates scope for errors of inclusion and exclusion (namely those who are not eligible but get it, and those who are eligible but not get

22. We use the term income transfer rather than cash transfer to capture the idea that the income will go into a bank account and not be handed out as cash, which may be more susceptible to impulsive spending.

23. See Hanna and Olken (2018) and Ravallion (2016) for excellent reviews on different forms of targeting.

it, respectively).<sup>24</sup> Also, other than the standard inefficiencies associated with subsidies of any kind, targeted schemes create scope for corruption and leakage in the implementation process. Additionally, citizens' efforts to be added to the list of beneficiaries, legitimately or illegitimately, are another set of costs.<sup>25</sup> Finally, scholars and practitioners have argued that "programs meant for the poor" become "poor programs". Specifically, the argument is that universal programs tend to have broader political support and are therefore better funded and implemented.<sup>26</sup> As we show in Section 3, an IGD would augment consumption by 7–8 percent for the median rural household and 4–5 percent for the median urban household, which are non-trivial increases even for the median recipient.

Universal schemes are more expensive than targeted schemes for the same total level of benefits, and so, for a given budget constraint, they require scaling down benefits. Also, being lumpsum in nature, they cannot respond differentially to specific needs of individuals or groups, which may vary over time or across individuals. However, given weaker state capacity as well as the problem of a lot of people living on the margins of subsistence, the case for a universal income transfer scheme is stronger in a developing country like India than in developed countries since the welfare consequences of exclusion errors are higher (see Ghatak and Maniquet 2019, for a more detailed discussion).

To illustrate the argument in the Indian context, suppose we extend the PM-KISAN to all citizens. Assuming an average family size of 4.6 and a population of 132.7 crores, we get 29 crore additional families, which is almost exactly double the current coverage of the scheme. In per capita terms, a transfer of ₹6,000 per family per year translates to approximately

24. There is a trade-off between inclusion (Type I error) and exclusion errors (Type II error). If the goal is to minimize exclusion errors (e.g., in the spirit of "no one left behind"), then it is likely that inclusion errors will go up. Conversely, attempts to reduce leakage and inclusion errors will typically be accompanied by an increase in exclusion errors, as shown in ongoing work by Muralidharan, Niehaus, and Sukhtankar (2020). Hanna and Olken (2018) carry out a simulation exercise, using data from Indonesia and Peru, about the trade-off between these two types of errors.

25. See Khosla (2018) for a good review of the various kinds of costs associated with targeting. From an economists' perspective, the deadweight losses associated with these efforts are a substantial cost that is rarely accounted for in discussing the costs and benefits of targeting.

26. In the Indian context, this point has been raised by Jean Dreze, who argues, for instance, that the PDS in Tamil Nadu works better than in other states, in part because it is universal and, therefore, has broader political support (Dreze 2010). In the US context, a similar point has been made to explain why Medicare (which is universal above age 65) is better financed and politically more secure than Medicaid (which caters only to the poor). See Brown and Sparer (2003) for a discussion.

₹1,300 per person per year, or around ₹110 per person per month. This is roughly the same figure for the IGD we obtain from using a benchmark of 1 percent of GDP (₹120 per person/month). At current prices, this would translate to around 9.5 percent of total Central Government expenditure or about 13.2 percent of tax revenue.

A good example of a contrasting proposal based on larger transfers to fewer (poorer) people is the idea of *Nyuntam Aay Yojana* (NYAY) floated by the Congress Party in the run-up to the 2019 Parliamentary elections. NYAY would have given ₹6,000 per month (as opposed to per year, as under PM-KISAN) to the poorest 20 percent of families. This works out to be about 2.5 times the amount that would be needed if PM-KISAN was extended to all families, and accordingly, the total expenditure would have amounted to 2.5 percent of GDP and nearly 25 percent of total government expenditure. Even if the amount of the financial support is scaled down to say, 1 percent, of GDP, the key feature of NYAY is that it is targeted at the poor, which raises the problems of targeting mentioned above, as well as the problems of reduced work incentives due to the phase-out period (described in Section 2.5).<sup>27</sup>

PM-KISAN is also a targeted income transfer scheme—it is aimed at all landholding farmers (subject to some exclusion criteria such as having a family member who pays income tax or is a professional) and so excludes all those who are involved with agriculture but do not own land (such as agricultural laborers and tenants), and of course, those who are not engaged with agriculture. PM-KISAN is a substantial improvement over input subsidies and loan waivers, and targeting based on landholding is easier than doing so based on income. Yet it will still have non-trivial costs of targeting, including costs of verifying landholdings and costs of gaming (by households that choose to split landholdings to take advantage of the non-linear features of the benefits schedule). Making the scheme universal would avoid these costs.

#### *2.4. Will People Spend Cash Transfers Badly?*

One frequently raised paternalistic concern about income transfers relative to the in-kind provision of benefits is that people may squander the cash on inessential consumption. All else equal, beneficiaries should prefer income transfers as they allow individuals freedom of choice to spend the money based on their specific needs and priorities. However, if the preferences of

27. See Ghatak (2019a) and Muralidharan (2019) for discussions on the design weaknesses of NYAY.

the individual are different from that of the policymaker (which can be due to behavioral biases, or insufficient intergenerational altruism, or gender bias), there may be grounds for paternalistic intervention. If so, unconditional income transfers may not be the most efficient intervention, and there may be a case for other policy instruments that restrict how the value of the benefits may be spent.

While there is some evidence that people spend more when they receive windfalls (like lottery winnings, as suggested by Imbens, Rubin, and Sacerdote 2001), there is no such evidence on small steady streams of income. Indeed, evidence from developing countries suggests that, on average, cash transfers to the poor do not cause them to work less or spend their money on inessential consumption. Evans and Popova (2017) review evidence from 19 studies with quantitative evidence on the impact of cash transfers on expenditure on temptation goods (mainly, alcohol and tobacco), as well as 11 studies that surveyed whether respondents reported that they used transfers to purchase temptation goods (these 30 studies span Latin America, Africa, and Asia). They find either no significant impact or a significant negative impact of transfers on expenditures on alcohol and tobacco. Restricting attention to randomized trials, they find a negative but statistically insignificant effect.

Bastagli et al. (2016) reviewed evidence on the effects of cash transfers on individuals and households through a literature review from 2000 to 2015, covering 201 studies and reporting increases in household food expenditure, school attendance, use of health services, dietary diversity, savings, livestock ownership, and purchase of agricultural inputs. A pilot study of UBI in eight Indian villages in Madhya Pradesh reports similar findings (Davalala et al. 2015).

In addition to giving beneficiaries freedom of choice, by not making the transfers contingent on any behavioral norms of recipients, universal income transfer schemes would enable us to avoid setting up entire administrative machinery aimed at monitoring compliance. This not only avoids the direct and indirect costs of running such a bureaucracy, but it also removes the patron-client relationship that is inherent in any system of monitoring and rewards between the state and its citizens that is undesirable in a democracy.

### *2.5. Effect on Work Incentives*

A major concern about any income transfer program is the potentially negative effect on work incentives. Using a standard labor-supply framework where individuals choose between income and leisure, an increase in

non-wage income would increase the demand for leisure. This informs the standard view that income transfers will reduce labor supply.

However, this theoretical argument is not robust to allowing for subsistence considerations or market frictions (Ghatak and Maniquet 2019). In situations where income levels are so low that subsistence considerations matter, which is the case with low wages and low levels of non-labor income, a good proportion of the population will be working very hard (i.e., using up all their available time endowment on work) to earn a minimum income level to meet their subsistence needs. For them, an income transfer that is not large will not affect their labor supply but can push them above subsistence, resulting in potentially large welfare gains.

Once we allow for frictions in the labor, credit or insurance markets, the likelihood of a potentially negative effect of income transfers on labor supply will be further reduced (Baird, McKenzie, and Özler 2018). To the extent to which greater income allows better nutrition, which, in turn, leads to greater productivity, there could be an increase in labor supply due to a higher effective wage rate. Also, to the extent to which income transfers relax liquidity constraints or enable individuals to take greater risk given access to a steady stream of income, there could be an increase in labor supply in self-employment, an issue we discuss in detail in Section 3.

While we do not have much direct evidence regarding the effect of unconditional income transfer scheme on labor supply yet, Banerjee, Karlan, and Zinman (2015) re-analyze the results of seven randomized controlled trials of government-run cash transfer programs from six countries worldwide to examine their impacts on labor supply. Across the seven programs, they find no systematic evidence of an impact on either the propensity to work or the overall number of hours worked, for either men or women. Baird, McKenzie, and Özler (2018) also review the evidence on adult labor market outcomes in response to cash transfers, and the general picture that emerges is that these generally had little or no effect on overall labor supply, and to the extent to which there was an effect, it was positive with some substitution away from wage labor to work in self-employment.

One of the very few long-standing nationwide cash transfer programs that most closely resembles a UBI was introduced in Iran in 2011. It faced political criticism for its alleged disincentive for work, especially for the poor. However, careful analysis shows that there was no evidence of reduced labor supply, and if anything, the labor supply of women and self-employed men actually went up (Salehi-Isfahani and Mostafavi-Dehzoeei 2018).

Evidence on the labor supply effect of cash transfer programs in developed countries does not appear to suggest a potentially large negative effect,

either. For example, Marinescu (2018) reviews empirical results from the US and Canadian negative income tax experiments, the Alaska Permanent Fund Dividend, and the Eastern Band of Cherokees casino dividend program, as well as a few other assorted studies and finds that, overall, the programs analyzed suggest either no effect on labor market supply or a slight reduction in work and earnings. Taken together, there is no systematic evidence across various cash transfer programs that they have a negative effect on labor supply.

Finally, comparing across potential designs of income transfer programs, a small universal unconditional transfer will likely have smaller adverse effects on work incentives compared to a larger transfer to fewer (poorer people) for at least two reasons. First, the smaller transfer implies a lower-income-effect-based increase in the demand for leisure. Second, under targeted schemes, the benefits decrease with means. This may create strong negative incentive effects due to a potentially high marginal tax rate in the range of income where the benefits are phased out.

To take a concrete example of the problem of targeted schemes in the Indian context, let us consider the NYAY proposal, which targeted families in the bottom 20 percent of the population. The proposal was to either pay the eligible families the difference between ₹12,000 and their actual income or simply a flat amount of ₹6,000 per month. However, there is no way to directly verify the incomes of the poor (e.g., via payroll or income tax) as they work in the unorganized sector. As a result, both versions of the scheme create strong incentives to under-report income since the marginal tax rate as someone crosses the threshold of qualifying for this scheme is 100 percent (every rupee hidden is one rupee gained in benefits) or more (crossing from below the threshold to above the threshold entails losing the entire benefit).

This illustrates that while income effects of unconditional cash transfers may deter effort in theory, targeting can actually exacerbate poverty due to the disincentive to climb out of official poverty (since the phasing out of benefits with increasing income is equivalent to a high effective marginal tax rate on incomes earned by the poor).<sup>28</sup>

28. While the theoretical argument is clear, there is less direct evidence on the incentive effects of targeting in developing countries (Banerjee, Niehaus, and Suri 2019). One piece of indirect evidence is from a field experiment that finds that households try to appear poorer when participation in surveys is incentivized (Stecklov, Weinreb, and Carletto 2018). Hanna and Olken (2018) provide a brief and useful review of this literature. One interesting point they make is that in developing countries that use proxy-means tests for eligibility for benefits programs, the greater the noise in these formulas, the lower the implied labor supply distortions

## 2.6. Female Empowerment and Improved Intra-household Targeting

A large literature shows the positive effects of cash transfer schemes on female empowerment (see, e.g., Bastagli et al. 2016; Duflo 2012, for reviews). Direct recent evidence on this point is presented by Field et al. (2020), who randomize whether NREGS payments for women's work in Madhya Pradesh are paid into the account of the head of household (typically male) or of the female worker herself and find that sending money into female accounts (combined with training on how to use the accounts) significantly raises the labor supply of women on both NREGS and the open market. The authors interpret this result as direct evidence of increased female empowerment from depositing money into their accounts.<sup>29</sup>

Giving women control over more resources may also improve the intra-household targeting of anti-poverty programs. Most targeted schemes attempt to reach poor individuals by targeting poor households, but as Brown, Calvi, and Penglase (2019) show, intra-household inequality may mean that many poor individuals live within non-poor households. Using data from Bangladesh, they apply a new approach to calculating individual-level poverty rates that takes intra-household inequality into consideration. They find that women, children, and the elderly are at risk of living in poverty even within households with per capita expenditure levels that exceed the poverty threshold. Thus, universal untargeted income transfers (with the allowance for children going to mothers) may actually *improve* targeting to the most vulnerable members of society relative to a system that targets transfers based on mean household income.

## 2.7. Relaxing Borrowing Constraints for Productive Investments

Critics of income transfers often caricature them as band-aids for poverty, diverting resources from policies and programs that would have enhanced productivity and provided a more long-term sustained pathway out of poverty (e.g., Aiyar 2019; Roy 2019a). There are two problems with this argument. First, what may seem like a “band-aid” to policymakers can be quite substantial for those living on the margins of subsistence. Second, and more importantly, in contrast to the standard trope of income transfers

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due to the phasing out, for the same reason that incentive schemes are less effective when performance is noisily measured. However, there is no direct evidence regarding this point.

29. Additional recent evidence on increased female empowerment from being the recipient of income transfers is provided by Almás et al. (2018), who used a randomized experiment from Macedonia that varied the gender of the parent who received a conditional cash transfer for secondary school attendance.

reducing incentives for work, there are several theoretically sound reasons to believe that they may *increase* the productivity of the poor by providing an important source of working capital. Also, having a source of consumption insurance will enable the poor to make risky investments. In this section and the next, we discuss these two channels in detail, where having a regular income flow can relax borrowing constraints as well as provide a threshold level of insurance, outlining the theoretical arguments and providing supporting empirical evidence.

An extensive literature on returns to capital in developing countries suggests very high rates of return that often exceed prevailing interest rates (see Banerjee and Duflo 2005, for a review). For example, in a well-known study, de Mel, McKenzie, and Woodruff (2008) consider the effect of one-time randomized capital grants worth at most 10–20 percent of the capital stock of microenterprises in Sri Lanka and estimate the returns to capital to be 60 percent per year, which is substantially higher than market interest rates, and conclude from this that these enterprises are indeed credit-constrained. Experiments with similar-sized grants were carried out in other countries, such as Mexico, Ghana, and India, and yielded similar rates of return (see Banerjee, Niehaus, and Suri 2019, and Baird, McKenzie, and Özler 2018, for reviews of the literature).<sup>30</sup>

Despite these high rates of return to capital, only a small fraction of individuals in developing countries have access to bank loans—Banerjee, Niehaus and Suri (2019) report a figure of 12 percent for India from the most recent financial inclusion surveys. For the poor in India, a well-known survey of the economic lives of the poor (Banerjee and Duflo 2008) suggests that among those who have at least one loan (about 66 percent of the rural poor and 70 percent of the urban poor), a very small fraction comes from bank loans (6 percent in rural and 7 percent in urban areas).

However, despite high returns to extra capital for existing business owners, the *average* returns across all potential borrowers may not be as high. This, in fact, is the general conclusion that emerges from experimental evidence from microfinance from six countries (Banerjee, Karlan, and Zinman 2015). In a study based in India (Banerjee et al. 2015), there was no significant effect on business earnings, on average, but a strongly positive and persistent impact on those who had a pre-existing business. Even in the

30. There are also experimental studies that look at the effect of large capital grants, such as Bandiera et al. (2017) and Blattman et al. (2016). In the former study, the average capital transfer was 90 percent of the per capita annual consumption expenditure of the group that was targeted for the intervention. Because of our focus on IGD, which involves much smaller amounts, we do not discuss these.

aforementioned studies on capital grants to microenterprises, which found high average rates of return, returns vary considerably. The key implication of this finding is that lenders need to exert considerable costly effort to screen borrowers to identify those who are likely to have high returns on capital and are able to repay their loans.

These intermediation costs may help explain why even microcredit interest rates are not low. The India study mentioned above had an annual interest rate of 24 percent, which is considerably higher than bank interest rates, largely reflecting the costs of intermediation to poor borrowers with small loan amounts. It is not surprising then that several microfinance studies have take-up rates of less than 20 percent. Further, microfinance seems to have a limited impact on consumption in most studies, suggesting that credit expansion might not be enough to effectively reduce poverty.

Rather than take a pessimistic view on microcredit, a more optimistic implication of the above results is that people have either investment or consumption smoothing opportunities that generate an internal rate of return of around 25 percent, but that these returns are mainly absorbed by interest costs (which in turn, reflect intermediation costs). In this view, an IGD offers the potential of delivering similar returns to the capital since there is no intermediation cost or interest. More generally, it may help poor households move from a “credit cycle” where they borrow first for a consumption event and then repay in installments (at high-interest cost) to a “savings cycle” where they first pay themselves (through automatic savings of their IGD) and then use their savings to finance consumption or investments. Repeated over several cycles, moving out of a “credit cycle” to a “savings cycle” can generate very high rates of return.

Finally, an IGD may also make it easier for the poor to access formal credit. Recent evidence from developed country contexts suggests, in contrast to many models of credit constraints, that lenders assessing borrowers’ creditworthiness care more about their cash flow (since this determines their capacity to service the loan) than about their collateral (since this is typically illiquid; Drechsel 2019). In such a setting, the presence of an IGD may considerably increase the assessed creditworthiness of the poor, which may crowd in formal credit at lower interest rates than the status quo.

The final point worth noting regarding an IGD and credit is that most lenders require repayment on a rigid schedule, which may prevent borrowers from undertaking investments with a delayed pay-off (Field et al. 2013). An IGD can help alleviate this problem by providing a stream of income that can help to make interest payments while the loan is deployed to undertake productive investments that may have a delayed payoff schedule.

## 2.8. *Mitigating Risk to Enable Productive Investments*

In their book *Portfolios of the Poor*, Collins et al. (2009) highlight that the poor (defined as those who live on no more than \$1.90 a day) face considerable risk and seasonality in their income streams. Thus, they may live on \$3 one day, \$1 the next day, and nothing the day after. Yet, beyond informal risk-sharing, the poor in developing countries have little access to formal insurance systems. Banerjee and Duflo (2008) report that only 10–11 percent of households had access to any kind of insurance, whether for health or life.

From this point of view, financial inclusion of the poor with even a small fixed periodic transfer to their bank accounts can go a long way in mitigating risk. This risk not only imposes significant welfare costs but also constrains the ability of the poor to undertake income-generating activities because of the extreme risk aversion that comes from living on the margins of subsistence. Banerjee, Niehaus, and Suri (2019) review the experimental evidence on the degree to which small enterprises or farms may be constrained by lack of insurance (as entrepreneurs or farmers do not want to expose themselves to the risk that comes with additional investment, whether it is their own money or borrowed money). The evidence, mostly in the context of agriculture, suggests that with insurance, farmers choose crops that are riskier but have higher average returns, and there is a higher investment.

A particularly striking example of how small the relevant investments might be for generating substantial returns is provided by the experimental study of Bryan, Chowdhury, and Mobarak (2014). Working with a sample of poor households in rural Bangladesh, which suffer considerable hardship in the lean season, they offered a randomly selected subsample a payment of 600 taka in 2008 (around \$8.50) conditional on migrating to nearby urban areas, and an additional bonus of 200 taka (approximately \$3) if the migrant reports to the survey team at the destination. This, effectively, is the cost of a bus ride. They find that 22 percent of the selected households send out a seasonal migrant, and family members of migrants have significantly higher food expenditure (30–35 percent), which, in turn, improves their caloric intake by 550–700 calories per person per day. They also find that treated households are more likely to remigrate after incentives are removed in subsequent years. This raises the question as to what was stopping these households from taking advantage of migration opportunities given that the costs are relatively small. Their favored answer is risk-aversion. Since there is uncertainty about the returns to migration, and there is the potential for a downside (as the authors find in the data), households at the margin of subsistence (as these were) may not be willing to pay the “search” cost to take advantage of the opportunity.

The lesson from this study that is particularly relevant from our point of view is that relatively small sums of income transfers can have potentially large effects on income generation, other than contributing towards providing some subsistence support.

### *2.9. Alleviating Savings Constraints*

Irrespective of access to credit and insurance, savings can help both to smooth consumption and to accumulate resources for productive investments. Yet in the absence of access to formal banking, saving is difficult due to the risk of theft, demands by friends and extended family, and the temptation to spend on inessential consumption.

There is indeed a demand from the poor for institutional savings opportunities. In an experimental study on expanding access to bank accounts to small enterprise owners in rural Kenya, Dupas and Robinson (2013) find a very high take-up rate (nearly 87 percent), which is in sharp contrast to the lower take-up rates for microfinance (of around 30 percent across studies). Not only that, they found that women (as opposed to men) used bank accounts more actively, increased their total savings, and invested in their businesses.

With the significant progress in financial inclusion through the *Jan-Dhan Yojana* in recent years, many more among the poorer sections now have access to saving opportunities than what earlier studies suggested.<sup>31</sup> Further, recent evidence suggests that payments into bank accounts in India boosted savings. Specifically, Somville and Vandewalle (2018), using a randomized controlled trial in Chhattisgarh, show that savings increased significantly when earnings were directly deposited in beneficiary bank accounts, as opposed to being given out in cash. Thus, an income transfer program combined with bank accounts is likely to meaningfully boost formal savings of the poor.

## **3. An Inclusive Growth Dividend for India**

Based on the discussions above, we now introduce the main policy idea of this paper and our specific recommended way to incorporate income transfers into the portfolio of anti-poverty strategies for India. Specifically, we recommend that India should adopt an “Inclusive Growth Dividend” or IGD

31. In a review published a decade ago, Banerjee and Duflo (2008) reported that only 6.4 percent of households in the rural areas and 24 percent in the urban areas of India in their sample had a savings account.

for every citizen, pegged at 1 percent of GDP per capita, to be deposited directly into the bank account of every citizen on a regular monthly basis. At current estimates, this translates to a benefit of around ₹120 per person per month. The amounts for children under 18 will be transferred into the accounts of their mothers (or the next responsible guardians). We believe that such an approach, which is modest in magnitude but ambitious in reach (by being nearly universal), can achieve almost all the benefits of income transfers alluded to in the previous section while mitigating almost all the concerns raised to date regarding the potential costs of a UBI. We also believe that it can be an effective policy not just for social protection, but for broader economic growth by alleviating several constraints to productive investments. We discuss these as follows.

### *3.1. Terminology*

As mentioned above, many of the advantages of income transfers as an anti-poverty strategy have been discussed extensively in the context of a UBI. However, there are important ways in which an IGD is different, which is reflected in the terminology.

Perhaps, most important is the fact that the term “basic income” connotes an amount that is adequate to live on. This sets the expectation that the amount of the transfer will be large enough to eliminate poverty. This, in turn, means that the amounts involved are large enough that they would be infeasible to implement without either eliminating other schemes or substantially increasing tax collections—both of which are practically and politically daunting tasks. Thus, setting the expectation of the value of the income transfer too high may have had the negative consequence of delaying progress on using income transfers as one component of an anti-poverty strategy.

In contrast, an IGD sets a very different set of expectations. The most important word here is “dividend”, which makes it clear that this is one component of a portfolio of income streams that people would have. The word “inclusive” captures the built-in progressivity of the idea: since the amount is the same for all citizens, the marginal value of the transfer is correspondingly greater for the poor. Finally, the word “growth” captures the idea that the amount will grow along with the growth of the overall economy. Thus, an IGD would be one component of people’s income that reaches all citizens and grows equally for all with the country’s growth. It would thus be a powerful practical and symbolic commitment to universally shared prosperity. We now discuss the various benefits of such an approach.

### 3.2. *Affordable Enough to Be Feasible*

As discussed above, most of the existing discussions of a UBI in India, including those by Pranab Bardhan, Vijay Joshi, Arvind Subramanian (in the *Economic Survey*), and one of us (Ghatak), have had a benchmark value ranging from 3.5 percent to 10 percent of GDP per capita. In practice, it will be impossible to find the fiscal space to reach this value of transfer without eliminating other programs, which, as discussed above, is both politically and practically difficult. This may be one important reason as to why there has been limited policy traction for a UBI in India.

In contrast, at 1 percent of GDP per capita, the total cost of an IGD (with no exclusions whatsoever) would be in the range of ₹190,000 crores. While this is a non-trivial amount, it is entirely feasible to fund such an allocation. As we mentioned earlier, this is 2.5 times the budget allocated for PM-KISAN, whose estimated cost to the Government of India is ₹75,000 crores for 2020–21. Also, recall that the per capita allocation of PM-KISAN (₹6,000 per household) is quite similar to that of the IGD for an average-sized household (with 4.6 members). Thus, the amounts envisaged here are more likely to be in the realm of fiscal feasibility for a *supplemental* transfer.

Further, while PM-KISAN is a substantial improvement over NYAY in terms of design (as discussed in Section 2), using the funds allocated to PM-KISAN for an IGD would be even better. First, and perhaps most important, it would also reach landless laborers and those without formal title to land, who are typically more destitute and needy than farmers who own land. Second, by being independent of occupation, it would reduce the likelihood that farmers continue to engage in economically unviable cultivation just to get the PM-KISAN benefit. Third, from a practical perspective, by being at the individual level and not the household level, it would limit the scope for gaming the scheme by households splitting to double the value of the transfer. Further, as we discuss below, an IGD would advance several other social goals, including female empowerment, financial inclusion, and savings.

Finally, if the limited fiscal capacity for a universal IGD makes some targeting necessary, it would make sense to target on the basis of region (say district or block) and make the transfer universal within that region. This way, most of the practical benefits of being a universal program will be achieved (especially low-targeting cost) with benefits availing to the most economically disadvantaged regions of the country. Thus, it would be feasible and sensible to start with an IGD in the 20 percent of the lowest-income

districts at a cost of 0.2 percent of GDP. Such an approach is similar to how programs such as NREGS or aspirational districts have been initially rolled out in the most disadvantaged parts of the country.

### 3.3. Progressive, Inclusive, and Sustained Poverty Reduction

By construction, an IGD is a highly progressive program. An amount of ₹120 per month per person may seem like a pittance to someone living in Delhi or Mumbai, but the same amount can augment the consumption of the very poor by a non-trivial amount. Based on our calculations, Table 1 depicts the distribution of per capita expenditures at various percentiles of the income distribution for rural and urban India.

**TABLE 1. Rural and Urban Monthly Per-capita Consumer Expenditure (MPCE) at Percentile Distributions of Household Consumption Expenditures, 2018–19**

Percentile	Rural		Urban	
	MPCE (monthly, ₹ at current prices)	IGD as a percentage of MPCE (%)	MPCE (monthly, ₹ at current prices)	IGD as a percentage of MPCE (%)
0–5	734	16	986	12
5–10	937	13	1,279	9
10–20	1,102	11	1,573	8
20–30	1,273	9	1,917	6
30–40	1,432	8	2,286	5
40–50	1,598	8	2,656	5
50–60	1,782	7	3,068	4
60–70	2,008	6	3,585	3
70–80	2,315	5	4,310	3
80–90	2,825	4	5,477	2
90–95	3,597	3	7,528	2
95–100	6,305	2	14,468	1
<b>Average</b>	<b>2,012</b>	<b>6</b>	<b>3,700</b>	<b>3</b>

Source: Authors' calculations.

Note: This calculation is based on the percentile distribution of household average per capita expenditure using NSS 2011–12 figures (68<sup>th</sup> Round, NSS 2013), adjusted for inflation. We use an annual 5 percent inflation rate to get the 2018–19 figures so as to be comparable to the IGD figure based on the 2018–19 per capita GDP. The IGD as a percentage of MPCE is Rs 120 divided by MPCE. In the Appendix, we present an equivalent table (Table A.1) based on NSS 2017–18 figures (adjusted for inflation) taken from Subramanian (2019).

As Table 1 makes clear, the 5<sup>th</sup> percentile rural household has an MPCE of ₹734. Thus, while ₹120/month per head will not eliminate poverty, it is large enough to allow the poorest households to augment their basic consumption by a highly meaningful 16 percent in rural areas and 12 percent in urban areas.

The IGD would augment monthly consumption by 9 percent or more for the bottom 30 percent of the rural population and by at least 8 percent or more for the bottom half of the rural population. These are non-trivial amounts.

This may not seem significant at first glance, but one should take two facts into account. First, while about 22 percent of the population is below the poverty line (according to 2011–12 estimates), there is a great deal of heterogeneity among the poor, and so a monthly sum of ₹120 will not be trivial. Second, these figures are for India as a whole, and once one takes into account the great heterogeneity among states, this sum will be especially meaningful for poorer states and districts.

For example, in Table 2, we present the MPCE in rural areas by state (at current prices) according to National Sample Survey (NSS; Table T4 NSO Draft Report on Consumer Expenditure, 75<sup>th</sup> Round, 2017–18). Even though for India as a whole, the IGD as a fraction of the MPCE is 6 percent, for the eight poorest states, the figure is at least 7 percent.

Further, by being universal, IGD minimizes the risk of exclusion errors, which represent an important way in which existing programs do not deliver on their goals of alleviating poverty. In addition, if benefits are linked to *Aadhaar*, the benefits would be portable, which is something that very few programs are able to do at present (though this has recently been announced for the PDS). The importance of portability of benefits will only grow as migration and urbanization grow in the coming years. The universal coverage would also make an IGD a powerful symbolic program of national unity as perhaps the only program to date that equally reaches every citizen of the country in a reliable and predictable manner.

Finally, by pegging the value of the transfer to a fraction of GDP per capita, the structure of the IGD has built-in indexation and will grow over time at the rate of *nominal* GDP growth, which will account for both inflation and real economic growth. Critics of income transfers with respect to income-based anti-poverty programs as opposed to in-kind benefits point out that the real value of the former is often allowed to be eroded by inflation for fiscal reasons in a way that the latter is less susceptible to. For instance, the value of the National Old Age Pension Scheme had a nominal value of ₹200/month in

TABLE 2. Rural Average MPCE by State, 2018–19

<i>States</i>	<i>Rural</i>	
	<i>MPCE (monthly, ₹ at current prices)</i>	<i>IGD as a percentage of MPCE (%)</i>
Odisha	1,411.32	9
Jharkhand	1,415.54	8
Chhattisgarh	1,445.09	8
Bihar	1,585.80	8
Madhya Pradesh	1,620.98	7
Uttar Pradesh	1,626.61	7
Assam	1,715.26	7
West Bengal	1,816.57	7
Gujarat	2,161.31	6
Karnataka	2,196.48	5
Rajasthan	2,248.55	5
Maharashtra	2,278.10	5
Tamil Nadu	2,382.22	5
Andhra Pradesh	2,468.05	5
Haryana	3,061.85	4
Punjab	3,299.65	4
Kerala	3,755.55	3
<b>All India</b>	<b>2,012.15</b>	<b>6</b>

Source: Authors' calculations.

Note: States are arranged in ascending order in terms of rural MPCE based on 2011–12 NSS data (adjusted for inflation, using the adjustments noted for Table 1). In the Appendix, we present an equivalent state-specific table (Table A.2) based on 2017–18 NSS data. The state-specific NSS data for 2017–18 was kindly shared by Himanshu.

2006 but was not adjusted upwards for over a decade, prompting concerned economists (including one of us—Ghatak) to write to the finance minister to request an increase of this amount in 2018. In contrast, by being linked to a fraction of GDP, the IGD makes these increases automatic and will ensure a sustained impact on poverty reduction over time.<sup>32</sup>

32. As noted earlier, the IGD is a variant of the idea of a “universal basic share” put forward in Ray (2016). The approach is also similar to how social security benefits in the USA are indexed to the rate of wage growth in the economy, capturing not only inflation but growth in real worker earnings over time.

### *3.4. Rank Preservation and Psychological Well-being*

There is an important sociological problem with targeted programs, which is that they can often cause “rank reversals” on the ground. This was a major shortcoming of NYAY. For instance, by providing transfers to people who are in the poorest 20 percent of the population but not those who are right above, this design would reverse the prosperity order between households just below and just above the threshold. Given the well-established evidence that people care about relative income and status as well as absolute income and poverty (Veblen 1899), such ranking reversals can be quite unpopular and may also be a cause for the targeting errors that happen in targeted programs. Further, there is also evidence of negative psychological effects on non-recipients of transfers when some of their neighbors do receive transfers (Haushofer, Reisinger, and Shapiro 2015).

An IGD elegantly avoids all such sociological and psychological challenges by being both universal and not excluding anyone, and also by preserving relative ranking of economic status within communities. Of course, the net distributional impact of an IGD will depend on the structure of the tax system that finances it. But since people do not directly map sources of tax revenue to specific expenditure categories, the salience of these issues is mainly a function of the nature of the expenditure.

### *3.5. Female Empowerment and Improved Intra-Household Targeting*

Consistent with the evidence reviewed in Section 2, it is reasonable to expect that an IGD where the allowance for children under 18 is transferred into the bank accounts of their mothers would, over time, increase female empowerment. Women would have greater control over household resources and will also gain increased autonomy to travel to visit banks and ATMs to access the money (which they will have to do in person to authenticate themselves using *Aadhaar*).

This aspect considerably strengthens the appeal of income transfer schemes like the IGD as they can be aimed at individuals rather than families, and mothers can be given the transfers intended for children. Further, as discussed in Section 2, intra-household inequality is a non-trivial concern in India (highlighted, for instance, by Jayachandran and Pande 2017), and thus, an untargeted universal income transfer with the IGD for children going into their mothers’ accounts may do a better job of targeting *individual* poverty.

### 3.6. *Work Incentives*

Another advantage of the IGD approach is that the value of the transfer is too small to have any adverse impacts on incentives to work, especially compared to the higher potential disincentives from making larger transfers to fewer people. Adjusting for inflation, the amount of ₹120 per person per month is 8.9 percent of the rural poverty line and 6 percent of the urban poverty line. While non-trivial, this is unlikely to have serious effects on work incentives.

Further, as discussed in Section 2, an important attraction of an IGD is that there is no phase-out of the benefits, which means that there is no disincentive to work during that period. Even if there is a phase-out at a high level of income (say, high enough to be above the threshold for income tax payments of ₹5 lakhs/year) at that point, the marginal tax rate from losing the IGD is under 0.2 percent.

More importantly, an IGD could actually increase worker productivity. Estimates of migration in India suggest that rural to urban migration is sub-optimally low given the disparities in earnings in rural and urban areas (Munshi and Rosenzweig 2016). However, there is also credible evidence from Bangladesh that people often do not invest in profitable opportunities like migration because they are so poor that they cannot afford to invest in “searching” for a better job in an urban area, including transportation and sustenance costs to conduct such a search (Bryan, Chowdhury, and Mobarak 2014). In such a setting, even very modest income transfers to people that are predictable and reliable can significantly improve productivity by increasing their ability to search for better opportunities and take on the small risks needed to “invest” in such a search.

### 3.7. *Financial Inclusion, Savings, Credit, Risk, and Insurance*

An IGD would also directly promote financial inclusion in the country and help the poor build savings in a secure bank account. Some sense of how important a development goal this would be is provided by Badarınza, Balasubramaniam, and Ramadorai (2016), who show, using the All-India Debt and Investment Survey of 2012, that households at the 25<sup>th</sup> percentile of the Indian wealth distribution and below had *zero* financial assets/savings. Even at the median, the financial savings were only ₹2,200 per household.

This figure has likely improved in recent years with the large-scale expansion of *Jan-Dhan* bank accounts. Yet a large number of accounts remain dormant with a zero balance. As of December 2018, the finance minister

responded to a Lok Sabha Parliamentary question saying that out of 33.6 crore *Jan-Dhan* accounts created, 23 percent were dormant.

In the World Bank's 2017 Global Findex, 80 percent of Indians surveyed reported having accounts at formal financial institutions; 77 percent of rural Indians reported having accounts (Demirgüç-Kunt et al. 2018). However, among those with accounts, 48 percent did not make any deposits or withdrawals in the previous 12 months. Such inactivity, in turn, leads to banks automatically deeming the accounts dormant, which makes them unusable without reactivation. Thus, a large fraction of the enormous efforts undertaken by banks and governments to boost financial inclusion is wasted because the accounts that are opened under these schemes get deactivated due to lack of activity in them.

There is almost no doubt that having a regular inflow of funds into these accounts will lead to greater usage of these accounts, and, by definition, these accounts will be active due to the monthly deposits they will receive.

### ***3.8. Creating Broad-based Demand***

In addition to supporting increased productivity at the micro-level for the reasons noted above, an IGD could also be an engine for broader economic development by boosting aggregate demand. Commentators on the Indian economy have highlighted that India has mainly had top-down economic growth over the past two decades (see Chawla 2016; Roy 2019b for illustrative discussions on this point). Specifically, they have argued that the top 10 percent of the population earns enough to drive consumption. This demand trickles down to sustain the next 30–40 percent working in smaller (mostly informal) enterprises, while the bottom 50 percent lead a hand-to-mouth existence.

By putting more money in the hands of the poor, an IGD could help reverse this pattern and provide a bottom-up boost to the economy. Not only will it increase income, but it will also provide predictability of future income—a key driver for demand. Recent evidence on unconditional income transfers provided to entire communities in Kenya finds an economic multiplier of 2.7 (Egger et al. 2019). More generally, both theory and evidence suggest that a broader consumption base promotes economic development by allowing firms to recover the fixed costs of investing in more productive capital and technology (Matsuyama 2002).

In the Indian context, experimental evidence has found that improving implementation of the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) (by reducing leakage, payment delays, and

uncertainty) led to a substantial reduction in rural poverty (Muralidharan, Niehaus, and Sukhtankar 2020). The study also finds longer-term benefits, including increases in credit, assets, the number of non-agricultural enterprises, and employment in these enterprises. These results suggest that improving wages and incomes of the poor, through social protection, can have large positive multiplier effects on the economy through boosting credit and demand. Thus, in addition to the direct benefits to the poor, an IGD is likely to have a substantial multiplier effect on the economy by boosting domestic demand, and thereby delivering a high public return on investment. Boosting demand may be especially important in times of constrained demand, like the current scenario where incomes of the poor have been severely reduced by the lockdowns to contain the spread of COVID-19.

### *3.9. Augmenting State Capacity and Credibility*

Implementing an IGD would involve identifying every citizen, matching him or her to a bank account (or to a parent or guardian's bank account), and being able to reliably send monthly transfers to over 1.3 billion people. Simply doing this would be a tremendous achievement. It would have the indirect benefit of developing demonstrable state capacity to credibly reach every citizen and reliably deliver a benefit for the first time in independent India.

Building such capacity, in turn, opens up an entire range of tools for better policy going forward. In the longer term, the IGD infrastructure may enable a strengthening of tax collection capacity by connecting every citizen to the state and vice versa. Also, there are several critical policy areas for citizens' welfare that require scarce resources to be priced, including water and air (the lack of pollution in the latter instance). Most economists believe that a policy that increased, say, carbon taxation or water pricing, and rebated the proceeds to all citizens would be welfare enhancing. Yet such policy instruments cannot be feasibly implemented right now. Successfully implementing an IGD will make such instruments feasible and thereby augment state capacity to better price scarce resources to reflect their social cost while using income transfers to mitigate the effect of such price increases on the poor.

Remarkably, building such state capacity is no longer a pipe dream and would be a logical culmination of the investments in the past decade in the *Aadhaar* platform combined with *Jan-Dhan* accounts and mobile seeding. The final key step in making this capacity universal is to strengthen the "plumbing" of financial inclusion by making the pipes transport funds every

month to keep them from becoming rusty. In this sense, the IGD would be a fitting next step for the broader vision of augmenting state capacity to better identify citizens and deliver benefits to them.

Building the capacity to deliver an IGD would also improve the options available to the government to deal with crises and natural disasters. This point is clearly seen in the context of the current crisis caused by COVID-19 and the lockdowns to prevent its spread. The main policy response to protect the poor and vulnerable has been to increase the allowance of free foodgrains through the PDS and to increase the budgetary allocation to NREGS. This is in large part because these are the existing programs where budgets can be allocated without needing to also build an all-new system to deliver resources to the vulnerable. Implementing an IGD would necessitate having a database of citizens and bank accounts (including a mapping into various benefits they are eligible for), which will make it easy for governments to respond to future crises by augmenting income transfers.

Finally, delivering an IGD would augment not only state capacity but also state credibility by consistently delivering a benefit to every Indian every month, which would be a first in independent India. As discussed in Khilnani (2010), it would be a policy that puts the individual citizen at the center of at least one government policy and be an instrument that puts the government in the service of every citizen.

### *3.10. IGD as a Benchmark for Development Spending and Enabler of Choice*

Finally, an important long-term benefit of building the infrastructure to deliver an IGD is that it can improve the accountability of *other* government programs by making cash transfers an attainable benchmark against which they can be evaluated. There has been an increasing push from policymakers to consider replacing poorly performing programs with income transfers instead. This was the spirit of the pilot of replacing PDS with DBT in three union territories. In a similar vein, the NITI Aayog and the Ministry of Women and Child Development have been preparing for pilot studies that would substitute take-home rations (THR) in the Integrated Child Development Services Scheme, which are believed to be poorly implemented, with DBT.

However, as the discussion in Section 2.2 highlights, the recent field experience in monitoring the implementation of these schemes suggests that there are non-trivial challenges with the quality of last-mile implementation of income transfers. These are meaningful enough that we do not feel

comfortable endorsing any attempt to mandatorily replace existing in-kind benefits with an income equivalent—whether this be for the PDS or THR or any other such program.

Further, data collected from ongoing work reveal that there is considerable heterogeneity in beneficiary preferences regarding income versus in-kind benefits.<sup>33</sup> For instance, we asked beneficiaries in Jharkhand to state the value of income transfer at which they would be willing to forego their THR entitlements and found substantial variation, with some beneficiaries willing to accept an amount that was much below the fiscal cost of the program (suggesting that the in-kind program was destroying value relative to the cost), whereas others stated an amount that was considerably above (suggesting that in-kind provision was providing more value than the cost). Similar heterogeneity is observed in both stated and revealed preference in the PDS.

The combination of implementation challenges with income transfers and the demonstrated heterogeneity of beneficiary preferences over income versus in-kind transfers has convinced us that the only politically and ethically prudent way of proceeding with any kind of substitution is by offering beneficiaries a choice between in-kind benefits (which is the default in most cases) and a fiscally equivalent income transfer. This is an approach that we have recommended in the PDS (see Ghatak 2019b; Muralidharan, Niehaus, and Sukhtankar 2018b) and is one that may be applicable in other cases of publicly provided private goods as well.

However, embarking on a choice-based framework itself requires the state to have demonstrated the capacity to credibly deliver income transfers. This is why we think that an IGD can be a foundation for improving the quality of expenditure in several other areas of social sector spending. Once income transfers are credibly established as a feasible option that the poor can depend upon, it opens the possibility of offering program-level choices to beneficiaries between income and in-kind assistance.

It is possible that in-kind provision may deliver more value than market options (because the government does not have a profit motive, marketing costs, and can procure in bulk). But it is also possible that market options may do better (because costs are higher under government provision and accountability of front-line personnel is low). Again, though on average the data in India suggest that the market is more efficient, we do not prejudge the outcome (both because of heterogeneity and because it is possible for the government to get more efficient).

33. This ongoing work is being conducted by Muralidharan jointly with Paul Niehaus, Sandip Sukhtankar, and Jeff Weaver.

The point, rather, is that allowing the choice allows much more accountability in government programs and will empower beneficiaries by providing them with one more option. For instance, in ongoing work in Maharashtra, where we are studying the impact of providing a choice between PDS grains and income transfers via DBT, we see that the take-up rate for DBT is around 25 percent.<sup>34</sup> Yet nearly all beneficiaries *value having the option*.

These data also highlight why the default discussion of a UBI that simply assumes that existing welfare programs can be folded into an income transfer is both naïve and unrealistic. People do value their in-kind benefits and often prefer them to income transfers. Conversely, in cases where the performance of the in-kind benefit is poor, they highly value having the option of an income transfer.

In the long term, both public and market provision of goods and services are important, especially for each to keep a check on the other through choice and competition. The problem with the status quo is that the poor constitute a captive market for government provision where they have limited options for both voice and exit (Hirschman 1972). Empowering them with choice improves both their outside options, and thereby their ability to drive improvements in public delivery.

Thus, income transfers would become a low-implementation cost “index fund” for development spending and in-kind programs and subsidies would need to demonstrate that their targeting, administrative and implementation costs deliver more value than their cost. Over time, programs that deliver less value than their cost could be replaced with income transfers while those that deliver more value can be retained.

#### 4. Making It Happen

In practice, making an IGD happen requires two main things: the money for the transfers and ensuring implementation capacity to actually deliver the transfers credibly and reliably. For the purpose of this paper, we assume that the main constraint is the former and assume that the investments in *Aadhaar*, *Jan-Dhan* bank accounts, and mobile seeding provide enough of a foundation for implementation to happen if there is political will behind the program. Since the political will for large-scale income transfers to nearly half the Indian population has already been demonstrated in the context of

34. This is based on ongoing work by Muralidharan with Paul Niehaus, Sandip Sukhtankar, and Jeff Weaver.

PM-KISAN, this seems like a reasonable assumption. This section will, therefore, focus on financing, and considers the case for an IGD being driven at both the level of the Central and state governments.

#### *4.1. Central Government*

Constitutionally, most service delivery functions (including primary education and health) are primarily in the domain of state governments. Yet the Government of India plays a large role in the design and delivery of public services as well as welfare programs. It does the former through Centrally Sponsored Schemes (CSS) such as *Sarva Shiksha Abhiyan* for education and the National Rural Health Mission for health, as well as central schemes such as PDS and NREGS. In the case of CSS, the Government of India makes funding conditional on matching contributions by states and spending according to guidelines established at the national level. In the case of PDS and NREGS, the funding is primarily from the Government of India, though implementation details vary across states.

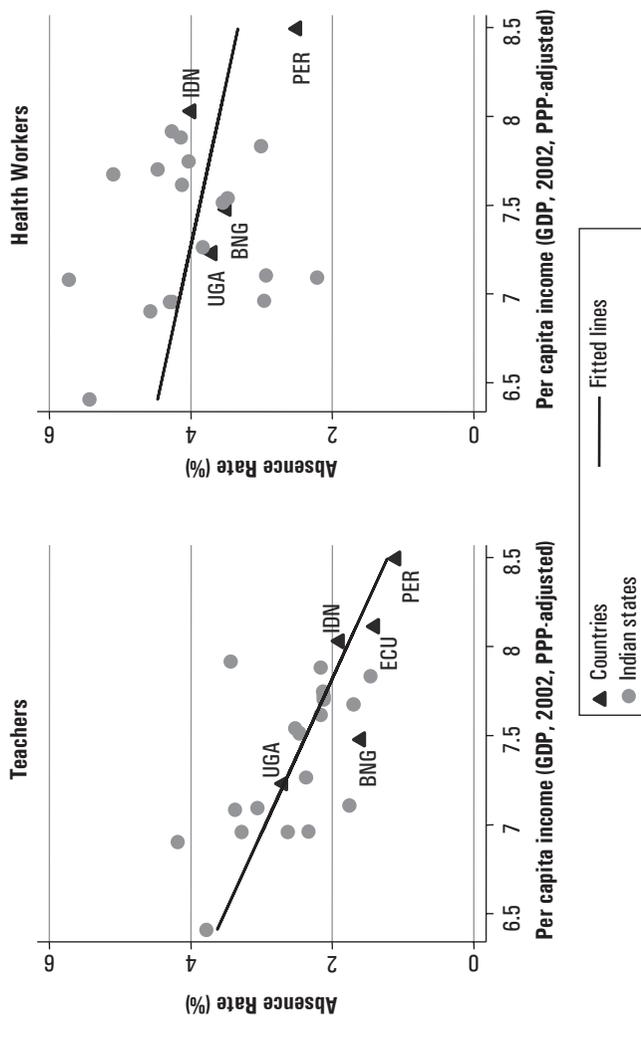
The main rationale for the Government of India playing such an active role in welfare and service delivery programs is that it seeks to achieve an element of national parity and common minimum standards in the delivery of these programs. Thus, the principles that govern the active intervention of the Government of India in these areas are equality (treating every citizen equally), equity (providing additional resources to more disadvantaged areas), and effectiveness (which is why these schemes prescribe minimum standards and guidelines).

An IGD would satisfy all three principles. The equality principle is built into the IGD by construction, by virtue of being the same amount for all citizens. The IGD also satisfies the equity principle as shown in Section 3.3. It is highly progressive, with a higher marginal impact on consumption for the poorest.

The subtle point is the one about effectiveness (or efficiency) and, in particular, the tension between equity and efficiency. Since a key principle for the Government of India (and also for the Finance Commissions) is equity across regions, several programs have provided additional funding for economically and socially disadvantaged states to help reduce regional inequalities, especially in key areas of human development such as health and education.

The problem, however, is that we have fairly robust evidence that the quality of governance is weaker in the poorer states. This point is clearly illustrated by Figure 1 from Chaudhury et al. (2006), who show that states with lower per capita income have significantly higher rates of teacher and health worker absence in the public sector.

**FIGURE 1. Absence Rate of Teachers and Health Workers in the Public Sector in Indian States**



Source: Chaudhary et al. (2006).

Note: BNG = Bangladesh; ECU = Ecuador; IDN = Indonesia; PER = Peru; UGA = Uganda. India's national averages are excluded due to the inclusion of the Indian states. For Indian states, income is their official per capita net state domestic product.

Given that teacher and health worker salaries are the largest component of public expenditure on education and health, this is a direct measure of the leakage of public expenditure. Calculations from follow-up research on teacher absence in India indicate that the fiscal cost of teacher absence alone is over ₹10,000 crores/year (Muralidharan et al. 2017). These figures are based on salaries in 2010 and are likely to be much higher when we use salary figures after the implementation of the 7<sup>th</sup> Pay Commission.

Another way of seeing the problem of weak public service delivery is to look at the private market share of health and education. Using all-India data on the presence of a private school in villages, Muralidharan and Kremer (2008) show that private schools are more likely to exist in villages with higher rates of public school teacher absence and also show that the correlation between state GDP per capita and private school presence is *negative*. The relationship also turns out to be negative *within* states, with a greater share of private schools in districts with lower consumption per capita (estimated with state fixed effects). In other words, the flight to private options is not simply a function of growing income, but rather likely to be a direct consequence of poor public provision.

Turning to health, Das et al. (2020), using all-India data on the quality and availability of healthcare providers in rural India, show that states such as Uttar Pradesh and Bihar deliver lower-quality healthcare at a higher per-unit cost than better-performing states like Tamil Nadu. The high unit cost is in part a reflection of low usage, which, in turn, is driven by low quality and reliability.

The tension between equity and effectiveness is also seen in the case of the NREGS, which is a flagship program of the Government of India. While it is meant to be a pro-poor program, a key challenge is that implementation quality varies considerably across states. Evidence on NREGS suggests that while it is progressive within states, it is actually *regressive* between states, with better-off states availing more NREGS funds than poorer states. For instance, calculations by the Accountability Initiative show that in 2011–12:

Poorer States such as Uttar Pradesh, Bihar, West Bengal, and Madhya Pradesh, which together account for 59 per cent of the country's rural BPL population, generated only 34 per cent of employment through MGNREGA. On the other hand, Andhra Pradesh and Tamil Nadu, which house eight per cent of the BPL population, accounted for 23 per cent of the total employment generated that year. (Aiyar 2014)

These results highlight the vexing challenge that the Government of India faces in terms of satisfying the equity goals of public expenditure. On

the one hand, the poor states need more assistance to help meet horizontal equity goals across the country. On the other hand, the quality of public expenditure is systematically lower in these states, and weak state capacity in poorer states makes it more difficult to even complete the procedures needed to obtain the Government of India's funds in the first place (as seen in the NREGS example). This creates a "Samaritan's dilemma" where the marginal reach and quality of the Government of India's expenditure on welfare is lower in places that need it the most.

An IGD is especially attractive in such a setting by allowing the Government of India to promote equity while circumventing (at least for one component of funding) the weaknesses in governance in the poorer states. In other words, since the "wedge" between the cost of provision and on-the-ground delivery of services is higher in poorer states, sending one component of funds earmarked for equity directly to citizens will improve the efficiency of those funds relative to the counterfactual of sending all the additional "equity" funds through state governments.

It is important to clarify that an IGD does not, in any way, suggest giving up on improving the quality of governance in poorer states. Rather, it is consistent with our portfolio approach whereby one component of funding for India's anti-poverty and development strategy is allocated to direct income transfers. Recommending an IGD does not, in any way, preclude the Government of India from introducing other performance-based metrics for transfers.<sup>35</sup>

However, we strongly believe that an IGD provides a more broadly acceptable way for the Government of India to redistribute resources to poorer states (which will happen because it is based on population, which is greater in poorer states). In particular, because it so transparently satisfies the principles of equality and equity, and directly contributes to poverty alleviation, we believe that citizens in high-income states will be more supportive of this form of redistribution relative to those that go through governments (as in the case of other Centrally Sponsored Schemes).

Of course, fiscal space is tight, and there are several competing demands for funds (including say for implementing the New Education Policy or health initiatives like *Ayushman Bharat*). At the same time, there is clearly a political demand for direct alleviation of poverty, as seen by the major commitment to the PM-KISAN program. Implementing an IGD is a natural extension of this approach at a similar cost per beneficiary.

35. Indeed, the terms of the reference of the Fifteenth Finance Commission include making recommendations regarding performance-based funding to states.

Recognizing the importance of political messaging and that good economics needs to also be good politics, implementing an IGD would also be directly consistent with Prime Minister Narendra Modi's stated goal of leading a government that is characterized by *Sabka Saath, Sabka Vikas, Sabka Vishwaas* (with everyone, for everyone's progress, and enjoying everyone's trust). However, while this is a laudable goal, it is not easy to achieve in practice. An IGD provides a practical and implementable way of doing so through its combination of universality (*Sabka Saath*), promoting broad-based development (*Sabka Vikaas*), and building public confidence in the government by credibly delivering a benefit to every Indian every month (*Sabka Vishwaas*). While implementing a scaled-up IGD may take some time, it should be feasible to do so in a couple of years at most, which will provide enough time for the IGD to be taken back to the voters as a demonstrable achievement.

If short-term fiscal constraints are binding, it would also make sense to start an IGD in the most disadvantaged districts (or even blocks) in the coming year and assess and evaluate its performance before scaling up over the next three years to achieve universal coverage before the next elections. Given potential fuzziness in targeting at the district level, it may even be possible to randomize the roll-out within a universe of districts or blocks identified as eligible over a three-year period and use a lottery to phase the program in. This would allow the generation of credible estimates of impact—including general equilibrium effects and multipliers—prior to scaling up.

#### 4.2. State Governments

Even if the Government of India chooses not to make a fiscal commitment to an IGD for the entire country in one shot, there is nothing that prevents a state government from implementing an IGD on its own volition, potentially targeting the poorest districts or blocks within the state with a similar approach as identified above. The simplicity of the idea means that any state can implement it on its own without needing to explicitly coordinate with the center.

One promising option may be for mining-rich states such as Odisha, Jharkhand, and Chhattisgarh to make use of funds in their "District Mineral Foundations" (DMFs) for an IGD pilot and evaluation. The DMFs were created to ensure that a fraction of the royalties from natural resources were returned to the citizens of mining districts. In practice, however, DMFs have accumulated large amounts of unspent funds, in part, because of onerous requirements for projects to be designed and approved for using DMF funds. An IGD using DMF proceeds would be especially appropriate for a pilot

and evaluation given that it would pay citizens a “dividend” based on the mining resources that the citizens have a natural claim over.

It is worth recalling that the leadership of the State of Telangana in designing and implementing the RBS and its demonstrated practical and political success is what led to the rapid replication of the idea across the country. The idea of an IGD is similarly ripe for state-level leadership if the Center decides to wait.

## 5. Conclusion

We have made the case for an IGD pegged at 1 percent of GDP per capita, to be paid unconditionally to every Indian citizen as a modest (in amount) but ambitious (in reach) way of making income transfers a part of the portfolio of anti-poverty strategies in India. The amount of the transfer is very similar to the amount being offered under PM-KISAN, and the fiscal impact is, therefore, within the realm of practical feasibility. We have argued how it avoids some of the criticisms that can be applied to a more generous UBI scheme, that there is a strong case for such a scheme in India, and that it is consistent with key principles that guide our inclusive growth strategy: equality, equity, and efficiency.

At the time of revising the paper for publication, the country is dealing with the COVID-19 crisis, and the role of income transfers in the relief package is very much at the center of discussion. One key lesson from the unique nature of this crisis is its twin demand- and supply-side problems, which make income transfers and in-kind transfers more of complements than substitutes. After all, what good is only income when supply chains are disrupted? Similarly, how does it matter if shops are well-stocked when a person has no money? Cash versus in-kind transfers is a reasonable debate in normal times, but given the current crisis, these are complementary measures. This complementarity between income and in-kind transfers strengthens the case for our view of income transfers as one component in a larger portfolio of social protection programs.

The current moment (June 2020) is especially appropriate for an IGD for several reasons. First, there has been a sharp reduction in incomes resulting from the lockdowns to slow the spread of COVID-19. The Indian economy is highly demand constrained, suggesting that the economic multiplier from an infusion of purchasing power may be especially high, even higher than the multiplier of 2.7 estimated recently in Kenya by Egger et al. (2019). Second, historical evidence suggests that times of economic hardship can lead to increased conflict as people compete over a shrinking economic

pie (see, for instance, Miguel, Satyanath, and Sergenti 2004). An IGD can mitigate this risk and provide a powerful symbol of social solidarity that all Indians experience together regardless of their station. Third, an IGD would be a portable benefit (unlike NREGS or the PDS under the status quo), accessible anywhere in the country, and therefore, especially suitable to support migrant workers. Indeed, the existence of an IGD might have mitigated some of the heart-rending sufferings of migrant workers seen during the COVID-19 crisis.

Responding to the hardship caused by COVID-19 and the lockdown imposed to slow its spread requires us to both support and reform the Indian economy. The policy should aim to both support the vulnerable and the broader economy in the short run and promote long-term development goals. An IGD-led nationally portable social protection architecture would do exactly this.

## Appendix

**TABLE A.1. Rural and Urban Monthly Per Capita Expenditure (MPCE) at Percentiles of Household Consumption Expenditure, 2018–19**

Percentile	Rural		Urban	
	MPCE (monthly, ₹ at current prices)	IGD as a percentage of MPCE (%)	MPCE (monthly, ₹ at current prices)	IGD as a percentage of MPCE (%)
0–10	616	19	945	13
10–20	782	15	1,326	9
20–30	913	13	1,595	8
30–40	1,028	12	1,858	6
40–50	1,136	11	2,140	6
50–60	1,257	10	2,463	5
60–70	1,405	9	2,843	4
70–80	1,598	8	3,381	4
80–90	1,899	6	4,189	3
90–100	3,058	4	7,425	2
<b>Average</b>	<b>1,363</b>	<b>9</b>	<b>2,816</b>	<b>4</b>

Source: Authors' calculations based on Table 2 in Subramanian (2019), which he reports is based on Tables T3 and T4 of the 2017–18 NSO draft Report on Consumer Expenditure (75<sup>th</sup> Round). We use an annual 5 percent inflation rate to get the 2018–19 figures, so as to be comparable to the IGD figure calculated based on the 2018–19 per capita GDP. The IGD as a percentage of MPCE is obtained as ₹120 divided by the MPCE.

As Table A.1 makes clear, the 10<sup>th</sup> percentile rural household has a monthly per capita expenditure (MPCE) of ₹616. Thus, a sum of ₹120/month per head allows the poorest households to augment their basic consumption by 19 percent in rural areas and 13 percent in urban areas. The IGD would augment monthly consumption by 13 percent or more for the bottom 30 percent of the rural population, and by at least 11 percent or more for the bottom half of the rural population.

Although for India as a whole the IGD as a fraction of the MPCE is 7 percent, for the eight poorest states, the figure is at least 8 percent.

**TABLE A.2. Rural Average MPCE by State, 2018–19**

<i>States</i>	<i>Rural</i>	
	<i>MPCE (monthly, ₹ at current prices)</i>	<i>IGD as a percentage of MPCE (%)</i>
Chhattisgarh	1,093.86	11
Odisha	1,209.87	10
Jharkhand	1,246.18	10
Bihar	1,282.55	9
Madhya Pradesh	1,293.33	9
Uttar Pradesh	1,331.69	9
West Bengal	1,569.11	8
Maharashtra	1,571.19	8
Karnataka	1,624.08	7
Gujarat	1,699.60	7
Rajasthan	1,736.24	7
Assam	1,780.26	7
Haryana	1,945.87	6
Andhra Pradesh	2,044.61	6
Tamil Nadu	2,313.94	5
Kerala	2,772.31	4
Punjab	2,840.14	4
<b>All India</b>	<b>1,600.28</b>	<b>7</b>

Source: Authors' calculations based on 2017–18 state-level MPCE data kindly shared with us by Himanshu, who collected these from a single, three-part question on consumption expenditures carried in the PLFS July 2017–June 2018 Round. These are not comparable to the usual consumption survey rounds that the NSO collects. We use an annual 5% inflation rate to get to the 2018–19 figures so as to be comparable to the IGD figure calculated based on the 2018–19 per capita GDP. The IGD as a percentage of MPCE is obtained as ₹120 divided by MPCE.

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# Comments and Discussion\*

Chair: Ashok Lahiri

Member, 15<sup>th</sup> Finance Commission

## Abhijit Banerjee

MIT

Thank you for having me here. Ashok Lahiri already did most of the job. So I get to say irresponsible things because all the responsible fiscally wise stuff has been said. I like this paper and that is probably not surprising. Let me start by agreeing with your conclusion since, I guess as is my duty, I will disagree with many of the specific points. The idea of an inclusive growth dividend is very much what we call Universal Ultra Basic Income in our new book, *Good Economics for Hard Times*. First, it does have the advantage of putting your money where your mouth is. Unlike Ashok, I am actually not particularly concerned about the fiscal side: Either we are going to become a ₹5 trillion economy soon, and therefore there is nothing to worry about, or else this is not happening, and then maybe we really should be thinking about potential social tensions that that particular prospect might unleash and what we need to deal with it. Therefore, either way this might be a good idea.

I will also emphasize the two big selling points that Karthik said right at the end. One is that the IGD does create a useful benchmark. I think asking the question as to whether any proposed scheme is better than giving cash is always a good idea. I also like the argument that this is the way to substitute for extremely inefficient transfers, at least in the longer run. I think establishing a credible mechanism for delivering cash is central to that project. To have a conversation about removing distortionary subsidies, we have to have good mechanisms for compensating the losers. With a credible mechanism, we actually probably do not need a one-for-one compensation. I think of the amount of electricity that gets used by farmers because of the form of the subsidy: some of it turns out to be not very useful for them and is costly for

\* To preserve the sense of the discussions at the India Policy Forum, these discussants' comments reflect the views expressed at the IPF and do not necessarily take into account revisions to the conference version of the paper in response to these and other comments in preparing the final, revised version published in this volume. The original conference version of the paper is available on [www.ncaer.org](http://www.ncaer.org).

the country. I think all those ideas will play out soon, but I think having a good compensation mechanism in place is a good idea.

Let me now come to where I think more thought is needed. There are three questions that we will have to think about. One is how much? I think the idea they have that it should be roughly consistent with what PM-KISAN has suggested, is one way to go. I think our job as social scientists is not to take the political economy too literally. I do not know where this number came out of, but I would not guess that it came out of a great deal of deep thinking about exactly where the marginal returns are. So I am going to assume that the figure of ₹6,000 per year per family is just a guess, and some other guess could have been as good. Let me now proceed to argue that it is too little. So I think the first order point is that this is not just a supplement to income, it is more than that, it is going to do additional good things and that is why we can justify it. Let me take that proposition seriously. Is 120 rupees just 120 rupees, or more than that, as Karthik is claiming elaborately, talking about insurance and credit and all those things?

I think there are three mechanisms that he talked about: One is through insurance, one is through human capital investment, and one is through income-raising opportunities. Let me say that ₹120 per month provides almost no insurance. It is a tiny amount of money, even for very poor people. The real risks are much bigger, and I think the government is aware of it. Think of the *Fasal Bima Yojana*, which hasn't really taken off yet, but the amount of losses they are covering in principle are more of the order of many thousand rupees. As regards the idea that this is going to be compensation for either large income loss because of price variation, weather shocks, and health shocks, all those things have to be dealt with in other schemes. They are just too big. They are relatively rare, thankfully, and very large. I don't think that this is the scheme to do that. The amount of money is too small. For most of the people affected by it, this is 5–7 percent of their consumption at most and that is a loss people absorb all the time. That loss is not what ruins people, it is things like when, suddenly, you have to spend ₹5 lakh on a surgery. I think there are other schemes, like *Ayushman Bharat*, that will be needed to deal with that. I don't think insurance is a big argument here.

As for human capital investment, there is just not much evidence. I think the evidence is that human capital investment moves kind of linearly. So, spending for a while scales linearly with consumption. Hence, if you give people ₹6,000, and they spend 10 percent of that on health and education, they will spend 10 percent more. Therefore, you are going to get ₹600 more, and this is not going to be transformative.

The more positive evidence is the idea that when people get some extra cash in their hand, they actually make investments that have very high returns. The returns are sometimes quite stunning: 5–7 percent per month or more, up to 20 percent+ per month. I think that is where the really optimistic ideas come from. And they come in two flavors. A bunch of them come from conditional cash transfers across the world (mainly Latin America), and the rest from lumpsum transfers, again across the world. Both have been studied extensively. There have been lots of randomized control trials (RCTs), lots of other evaluations that are quite credible. If I look at the amount that is being proposed in this paper and compare it to the amounts in the studies that have positive results (which are the ones they cite), all those are basically bigger, much bigger, than the amount they are talking about. Just to give you some examples, in Latin America, the minimum, across 16 countries, was \$6 per month in 2008 dollars, and the average is substantially higher. So that is a much bigger number than the one that they are talking about, which is roughly a quarter of the \$6 minimum. In Kenya, there is another conditional cash transfer of \$21 per month. In Malawi, it is actually closer to what they are proposing, but Malawi is an incredibly poor country. Ethiopia is another example, and the median there is \$12 per month. So the amounts are much bigger, 5–10 times bigger. That is something to keep in mind.

It is hard to do this comparison quite right because, on the one side, these are not PPP-adjusted and that is sort of across the board. But India is a bit cheaper than the other countries. Thus, maybe the PPP adjustment would make the Indian number a little bigger. It is also not GDP per capita-adjusted; some inputs that you buy are priced relative to income per capita. For instance, land is more expensive in Mexico than in Malawi. I don't know how to do those adjustments, but the order of magnitude of the inclusive growth dividend seems smaller in general.

Now, why should I worry about it? If it is linear in investment, then you still get returns. But there is no evidence that the returns are necessarily linear. In fact, Maitreesh and co-authors have a very nice paper for Bangladesh where they estimate the threshold at which people get out of poverty and the necessary lumpsum payment to enable people to do so, and the lumpsum they are suggesting is of the order of \$165 in 2007. That is probably now a much bigger number. We did a similar estimate for India, and there we said that the critical investment is of the order of ₹7,400 in 2008, so that is again a much bigger number.

Is the IGD amount enough to have some positive impacts on earnings? One possibility is that maybe you have to make a lumpsum investment (i.e., it is not linear), but you can get to the lumpsum by saving a little at

a time. Here it is worth noting that despite all the talk about savings and how *Jan-Dhan* has increased savings, the numbers are remarkably small. An RCT shows that *Jan-Dhan* increased savings from 1–2 percent of annual income. So there is no evidence that people are going to save enough, that if you give them a very small amount of money per month, they are going to get \$200 by saving. In fact, in a whole bunch of studies, the savings rates are between 0 and 2 percent across the board—none of them has found low-income people saving a lot. I don't believe that what is going to happen is that if you give them this money, they are going to save it all up and then start their business. Therefore, I don't see a very obvious mapping from this intervention to the kind of income growth opportunities suggested in the paper. I think this is going to be just an income supplement.

What then are the design choices? One is to spend more. The second is that if we do not want to spend more, we have to think about whether we want to lump it up for people. So do you want to make yearly payments rather than monthly payments? It seems to me that that would avoid the problem of saving, and might very well be valuable. So one design choice may be to make one-yearly or even two-yearly payments. One advantage of that would be that you could still think of the IGD basis being an individual, and then offer each individual the option of choosing whether they would take one two-yearly payment over these monthly payments. I suspect a bunch of people would. That also has the advantage that you do not have to worry about what a family is. If a group of people say that they will give up monthly transfers and take one lumpsum transfer, then that group of people can be defined to be a family.

Some targeting would be another solution. Given that this amount is actually very small, it should be easy to limit its take up, for example, by insisting that a person has to go and sign every week to get the money, so that most middle-class people will not do it. That is extreme, but the general point is that you can limit take up quite easily and therefore get the amount up. These are interesting design choices to think about.

Another set of issues we should think about is whether it is worthwhile to consider some geographical targeting—there could be greater coverage in some areas because poverty is extremely geographically concentrated in India. We know where it is, so we could target those areas, which is easy because it does not require individual data. Another thing we could do is make it conditional on outcomes. For example, when a mine closes, do you want to increase transfers? Or when environmental policies are drafted, do you want to do something so that the losers are at least partly compensated?

Finally, should we have conditionalities? I personally like the idea of making age at marriage a requirement. If you violate the law, you do not get it.

So I think this is a great launching pad, a great way to start a conversation. I am sure we will have an interesting conversation here, but we should continue it further.

## **Arvind Subramanian**

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First, it's great to be here and I enjoyed the paper very much. When I read it, I felt the paper was pitching not to the converted but the converter himself, and it was great to see that. I want to make just two or three big points.

The first is that I agree with what Abhijit said, but for completely different reasons, I think that the amounts involved in the growth dividend, in my view, are not politically incentive-compatible. The authors mentioned PM-KISAN, but I think we have to leave that aside for a second because it came late, and it came as a response to other things. So it is a little bit more complicated.

But let us start with the revealed preference of four such schemes in the last few months. Let us just talk about *Rythu Bandhu* and the Congress proposal. What is for me fascinating about *Rythu Bandhu* was that, first, it was a scheme that was highly regressive, even to those within the farming community, and second, it excluded all non-farmers, that is, it was almost completely non-universal. Just a very small set of people were getting this. Yet, why did the Chief Minister of Telangana, K. Chandrashekar Rao, think that this was politically incentive-compatible? By excluding a lot of people, why wouldn't jealousies be raised, questions be raised? In fact, because of non-universality, he was able to give more money than the scheme proposes. So I think that big amounts for beneficiaries are absolutely politically necessary. If you take the Congress scheme as well, it is targeted in order to make the numbers big for the beneficiary. So, the numbers have to be big for beneficiaries to be politically incentive-compatible.

Going back to *Rythu Bandhu*, we can broadly agree that it was "successful" because they did very well in the election, and everyone said *Rythu Bandhu* was part of this. So here is a scheme that is regressive and excluded a lot but was able to give a lot of money to beneficiaries and therefore

proved very popular. So, in that sense, the two lessons I take away from this are (a) the amounts have to be big, and (b) what I think allowed the Chief Minister to do this was the political opportunity created by the agrarian crisis, which gave rise to the perception that there is a community deserving of this and so a lot of people were willing to not get this in order so that the few others could get it. Thus, it is the combination of opportunity plus relatively big amounts which seemed to work despite regressivity and exclusions.

Hence, if you want to push this idea it seems to me that you need some kind of political opportunity. I do not think giving this meagre amount of ₹120 a month is going to cut political ice with people. Of course, it is going to be politicians who create this political opportunity, but I suspect the sums are still far too small for a politician to say, “Vote for me because I am going to give you ₹120 a month.”

My second point is on implementation. I do not think the Finance Commission can decree such a growth dividend. However, one way forward for these kinds of policies is a cooperative federalism framework on the expenditure side, just as GST was the result of cooperative federalism on the tax side. I think it is desirable for the states and the Center to come together because (a) the magnitudes can be bigger, and (b) the scope of what can be eliminated is correspondingly greater. For example, I have had these discussions with state finance ministers where they have said, “I want to do a UBI, and I am willing to cut, but leave it to me what to cut.” So why do we not have mechanisms where, from the existing Centrally Sponsored Schemes, the Center says, “I am not going to tie the aid by saying you must do MGNREGA”; instead suppose that the schemes could be untied, so that state governments could have the freedom to decide what they want to cut in order to finance a UBI.

In the current political conjuncture, GST worked in part, or in large part, because there was the BJP at the Center and 17 BJP states sitting around the table to achieve consensus. We still have that configuration today, maybe even more. So why do we not use this cooperative federalism model, but on the expenditure side?

The problem with what I am proposing is that we will have to have an option or a menu-based approach where states can do it on their own. By definition, cooperative federalism means that no one party can appropriate the political benefit from doing a UBI. So there is a political incentive-compatibility challenge. But if the Center were to untie some of the schemes, and perhaps have some conditionality, linking the untying to a UBI, it could perhaps work.

My last point is about universality. Since there are resource constraints, we should be open to thinking of models of quasi-universality where you target out rather than target in. I think there are many ways in which you can do it. For example, my colleagues and I proposed that one version of PM-KISAN would be to give it to the entire rural population, but take out the top 10 percent or 15 percent based on the Socio Economic and Caste Census data. Implementation-wise, targeting out could be easier than targeting in and could also be politically acceptable because the very rich (those targeted out) would be excluded.

The last point relates to this whole debate on the compensatory state versus the redistributive state. In terms of politics, this is a choice only in la-la land. I don't think any state government really says, "Because I am going to do UBI, I will implement my education schemes any worse or any better." So, the debate becomes a little bit of a theoretical argument, and I have less sympathy for that.

## General Discussion

The Chair, Ashok Lahiri, provided some initial comments and questions. He was primarily concerned about the cost of the program and how it would be financed. The Government's fiscal deficit has remained at over 3 percent of GDP for the past 11 years, and revenues have declined from a peak of 11 percent to 9.1 percent in 2018–19. Thus, he was skeptical about implementing the program without an offsetting reduction in other programs. He believed that it represented a premature move from a focus on development to a welfare state. He also argued that giving up on efforts to improve targeted income schemes in favor of a universal program was a counsel of despair. However, he thought that the suggestion of initially introducing the program in the most disadvantaged districts with an opportunity to assess its performance had merit.

Indira Rajaraman was unconvinced that a negative correlation between the States' per capita income and teacher absentee rates provided a measure of governance that was a sufficient basis for abandoning efforts to provide public goods and services in favor of more generalized transfers. She suggested that the same correlation would exist for the supply of paved roads and water supply without suggesting that efforts to supply those public goods should be abandoned.

Rajnish Mehra and Rakesh Mohan both questioned the assertion that the IGD, the inclusive growth dividend, would not crowd out other programs.

Government expenditures were 10.6 percent of GDP in 2018–19. Three major items, viz. interest (3.1 percent), subsidies (1.6 percent), and defense (1.5 percent) totaled over 6 percent. Thus, the IGD, as free cash to all citizens, would represent a quarter of the remaining program funds. Given the magnitude of the need for public services, they thought the program would require a tax increase or greatly expanded foreign borrowing. Mehra also argued that the program's efficacy could only be resolved by beginning with a test program along the lines of that suggested by Ashok Lahiri.

Dilip Mookerjee was enthusiastic about the proposal, but he was concerned that a universal scheme is not targeted at the poor and, thus, somewhat ineffective as an anti-poverty scheme. Second, he was worried about the reliance on bank account transfers as the primary delivery mechanism. About 35 percent of the population does not have functioning bank accounts. They are among the most vulnerable to corruption schemes. Also, he thought that the program needed a means of responding to localized crises, like droughts. In some cases, in-kind transfers are more effective than income payments.

Pranab Bardhan argued that from a political perspective, the amount of the transfer was too small to induce workers in informal sectors to mobilize behind the scheme. Further, the suggestion that the program be indexed to a percentage of GDP would intensify the current debate over the accurate measurement of GDP growth. He also agreed with the concerns about substitution with other important public goods. He believed that the addition of a universal basic income would necessitate tax increases, and the country cannot continue to ignore the failure to tax wealth in all its different forms.

Kaushik Basu argued that it was important to broaden the tax base to include wealth, particularly with an inheritance tax. He also agreed with Dilip Mookherjee that, initially, the delivery of the transfer to everyone would be costly, but it would decline as more people began to use bank accounts. He thought it would be useful to introduce a degree of targeting by inducing the wealthy to forego the program.

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