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Assessment of the Benefits of combining Savings and Conditional Cash Transfers*

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1 Introduction

Because of its possible impact on production, investment, selection of technology and inequality, having access to the financial system is essential in today's economies. The benefits of having access to the financial system are not limited to a particular segment of the population. Large corporations and the wealthiest sectors of the population, as well as microenterprises and poor rural dwellers, can benefit from access to financial services. In fact, having access to–and using–the financial system helps the world's poorest people escape poverty (Aghion and Bolton 1997; Banerjee and Newman 1993; Banerjee 2004). Unfortunately, the poorest segments of the world's population have little access to the formal financial system and are forced to use imperfect substitutes, which are generally more costly and/or less efficient (Collins, Morduch, Rutherford and Ruthven 2009; Rutherford 2000).

In this paper, we study the possibility of expanding access to the financial system to the poorest sector of the population through the use of savings accounts, by means of an institutional change in the way conditional cash transfer programs (CCTs) operate. In

* The complete document is available at the Capital Project: <www.proyectocapital.org>.

particular, we discuss the potential benefits, challenges and conflicts that would be created if CCTs chose to deposit the transfers they grant recipients directly into savings accounts. Because of the scope of CCTs worldwide nowadays, this institutional change has the potential to affect millions of people.

Combining financial inclusion and CCTs is not a new idea. Various CCTs have started moving in that direction, modifying their payment systems (Maldonado, Moreno, Giraldo Pérez and Barrera Orjuela 2011). Nevertheless, the idea of trying to achieve greater financial inclusion by combining CCTs and savings has been little explored.

2 Access to the financial system and savings

For decades, there have been efforts around the world to improve the access of the poor to the financial system. Developing countries have paid special attention in recent decades to facilitating poor people's access to the financial system, mainly through (micro) credit. But poor households not only desire and need credit; they also desire and need savings and insurance (Collins **et al.** 2009).

According to Collins **et al.** (2009), appropriate money management is crucial for poor households. Because by definition they have little money, their margin of error is minimal. The poorest families also tend to face uncertainty about the security and regularity of their income. Not only can they not be sure whether they will receive any income, they also cannot know when that will happen. The more access they have to tools available in the financial system, the less they will have to worry about day-to-day survival and the more energy they can devote to planning how they will pay for their children's education, the family's health, etc. (Mullainathan and Shafir 2009).

This line of reasoning has led to a growing consensus among the academic community, governments and donor organizations that the poor need a varied basket of financial products and services. Moreover, the idea that offering credit may not be the best way to introduce poor people to the formal financial system is also taking hold. Access to the system through savings accounts is safer for new customers and does not require them to take any risk, because their resources are always available. The idea of offering formal savings accounts to introduce the world's poor to the financial system is therefore steadily gaining ground.

Savings accounts are expected to not only enable poor households to buy and sell, manage their (irregular) income, handle negative shocks and accumulate resources, but also to give those households the opportunity to learn to interact with the financial system and build a relationship with the financial institutions. Eventually, poor households can take advantage of the basket of financial products and services they need and desire.

One option that appears promising for providing financial services to poor households is to take advantage of the institutional development, infrastructure and coverage offered by CCTs. It seems especially important to study the possibility of CCTs depositing transfers to recipients in a formal savings account. Studying the combination of CCTs and savings is particularly relevant because it has been shown that the regulatory environment and the policies of governments and providers of financial services are more significant in determining financial inclusion than each household's specific socio-economic and demographic variables (Chaia, Dalal, Goland, Gonzalez, Morduch and Schiff 2009).

Before analyzing what could happen if CCTs and savings were combined, we will briefly describe what CCTs are and the challenges they face today.

3 Conditional cash transfer programs

CCTs currently exist both in very poor countries, such as Burkina Faso and Kenya, and in emerging economies, such as India or Turkey. These programs have even been implemented in developed countries such as the United States, France and the United Kingdom. CCTs are especially popular in Latin America, where most of the region's countries have or have had one. In Latin America, CCTs serve some 27 million households, representing more than 111 million people, or 21 percent of the population (Maldonado **et al.** 2011).

The main characteristic of CCTs is that they transfer money to poor households on the condition that the families invest in the human capital of their children (education, health and nutrition). In general, the main objective of these programs is to break the transmission of poverty from one generation to the next.

Although CCTs have been very successful on several fronts, nowadays they face various challenges. The following section describes the challenges we consider most relevant from the standpoint of program design. In each case, we discuss the role that a savings account could play in the recipient's life. We then indicate factors related to the impact of CCTs that have received little attention or about which there is no evidence.

On the design side, one particularly important challenge for the purpose of this study–which is not limited to CCTs, but refers to social protection systems in general—is how to design a system that will have a long-term influence. It has been suggested that public policy should go beyond a safety net and create a mechanism to level the playing field and promote equal opportunity. One challenge, then, is to link CCTs with these types of strategies and include mechanisms that give the programs a long-term focus, with a broader base of participants. As noted above, facilitating recipient households' access to formal savings accounts could contribute to achieving this objective. Another element related to the design of CCTs has to do with procedures for the recipients' graduation (Bastagli 2009). It is necessary to clearly define when a household is no longer eligible to receive the benefits. Efforts to do this have been criticized, and more work is needed in this area. One possible strategy to ease the "graduation" process could be to provide the households with a savings account. Another design challenge for CCTs is a review of the mechanisms for sanctioning families that fail to comply with the programs' conditions. When there is failure to comply, the programs generally suspend transfers to those households. In this case, the role that having access to a savings account could play is not clear. Savings could help households manage day-to-day expenses if the program is suspended, enabling them to keep their children in school and ensure that their members have access to health care. This, however, would imply that the "sanction" imposed by the CCTs was, de facto, less severe than initially desired. As a result, it is not clear that giving savings accounts to beneficiaries would be attractive to CCTs. Finally, an important challenge is how to design small auxiliary interventions that leverage the CCTs' effects on recipients' health, education and nutrition. Having access to savings accounts could help leverage the effects of CCTs. Savings accounts could give households financial security and enable them to shift their attention from meeting day-to-day expenses to investing in the human capital of their members (Mullainathan and Shafir 2009).

Among the challenges related to evidence of the effects of CCTs, there is a lack of it about the impact that these programs have on remittances. There is no solid evidence to indicate whether households that receive CCTs receive more or less in remittances than other households. If, because of its participation in a CCT, a household received less in remittances than it received before entering the program, having a savings account could enable it to accumulate resources to balance out its consumption in response to the decrease in the flow of remittances after its inclusion in the CCT program. On the other hand, a household participating in a CCT and owning a savings account could cause the person sending remittances to stop sending them. This could be the case if the remitter believes that the household is accumulating, in a formal savings account, the resources received from the government. Finally, it is also possible that if a household had a savings account, it would be easier for it to receive remittances, and the remittances would therefore increase. One challenge is to evaluate the direct impact of CCTs on savings and the impact of linking CCTs with access to the formal banking system. The next section offers a conceptual discussion of these last two points.

4 Conditional Cash Transfer Programs and Savings

If recipients of CCTs have savings accounts, how does that help, or how could it help, the programs attain their goals? And inversely, how do CCTs contribute, or how could they contribute, to formal savings and, more generally, to the inclusion of their recipients into the financial system? To answer these questions, it is necessary to analyze the connection between CCTs and access to formal savings accounts from the standpoint of each of the agents involved.

4.1 CCTs

Linking CCTs and savings has three potential benefits for the CCTs. First, the CCTs can reduce the cost they incur delivering the transfers. They can also decrease the possibility of corruption and resource leakage. And finally, the combination could leverage the payments' effects in both the short and long term. The latter could affect not only current recipients of the programs, both children and their parents, but also those who have graduated from the programs.

4.2 CCT recipients

Recipients of CCTs can benefit from the linkage of CCTs and savings through: (i) lower transaction costs for receiving transfers; (ii) having access to a financial tool that will enable them to better manage their finances, so they can stop worrying about that and focus on the family's welfare; (iii) being able to accumulate resources formally, so they can cope with negative shocks to their income, accumulate assets, and invest in physical and human capital; and (iv) having the possibility of accessing other financial tools, such as credit, insurance and remittance transfers. In short, linking CCTs and savings could help CCT recipients leverage the effects of the transfers in the short term and shift some of those benefits to the medium and long term. Moreover, the potential medium- and long-range effects of this combination are not limited to the people who receive the full transfer amounts offered by the CCTs; they also affect those who will receive smaller and smaller transfer amounts and those who have graduated from the program. Finally, in the medium and long term, the effects could extend not only to the new generation that is the main target of the CCTs, but also to their parents, complementing the current scope of the CCTs.

4.3 Financial institutions

Financial institutions can benefit from the linkage of CCTs and savings if the number of recipients who become customers is large, a significant percentage of them save (that is, they do not withdraw all of their funds as soon as they are deposited in the account), the recipients learn about finance and develop the level of trust in financial institutions necessary to begin to use other products, the financial products offered by the financial institutions are designed to meet the needs of the poor, and, if necessary, the government offers initial subsidies to help the financial institutions begin to serve this segment of the population.

4.4 Discussion

Combining CCTs with savings accounts seems to have the potential to benefit the programs, the recipients and the financial institutions. Achieving this union, however, is no small process. First, the linkage may not be appropriate in all cases. The CCT and the country's financial institutions must have the appropriate infrastructure and degree of institutional development. There must also be a regulatory framework conducive to this union. And it is desirable for CCT recipients to have a minimal level of financial education. The latter point could represent a major challenge, since CCT recipients include people who are elderly, have disabilities or are illiterate, and other vulnerable groups. Moreover, many of them have never set foot in a financial institution. The method used to educate and explain how to use the new payment system must therefore be adapted to the needs of each group; ideally, it should also be tested in pilot programs.

Another aspect that must not be ignored in the efforts to successfully combine CCTs and savings is training for the management and staff of the financial institutions. These people must be able to teach CCT recipients how to use the financial services they offer and must treat these customers with the same respect that any other customer deserves. Finally, another key point is implementation of the union of CCTs and savings. Zimmerman and Moury (2009) describe three possible ways of doing this, but indicate that other possible strategies certainly exist. Here we will discuss only the simplest linkage: the deposit of CCT transfers in savings accounts. While this is a very simple way to combine CCTs and savings, it has the potential to lay a very solid foundation for greater inclusion into the financial system over time. One criticism that Zimmerman and Moury level at this type of linkage is that the recipients may not have incentives to keep their funds in these savings accounts. Nevertheless, the nascent literature about access to savings accounts suggests that when this type of service is offered, a large percentage of people use it (Aportela 1999; Dupas and Robinson 2011; Prina 2012). Finally, it is important to pay attention to the design of the savings accounts to be offered. Bernatzi and Thaler (2004) and Madrian and Shea (2001) suggest that the design of the financial tools is crucial, because they can radically change people's behavior. This literature suggests that an appropriately designed savings account can facilitate the accumulation of savings. For example, if the savings account is designed so that the person must go every month to deposit his or her money, the accumulation of the person's savings is expected to be low. But if the action that the person must take is to go to withdraw money to cover expenses, the accumulation of savings is expected to be high.

5 Research agenda

Given how little we know about the effects of combining CCTs and savings, there is a rich research agenda in this area. In this section, we propose some topics that we believe should be research priorities, based on the potential benefits identified in Section 4. Because there are three agents involved in linking CCTs and savings, we will focus on discussing what we would like to know about each. If this research is carried out, we hope it will yield evidence for determining, with hard data, whether or not it is advisable to encourage the linkage of savings and CCTs. It should be noted that the list proposed here is not exhaustive.

5.1 CCTs

Although there is already some evidence about the reduction in transfer costs when CCTs start delivering their transfers electronically, instead of in cash (Lindert, Linder, Hobbs and de la Brière 2007), we believe it is important to continue studying this issue. It would also be worth studying additional effects of this change. It would be useful to understand to what extent internal processes in CCTs operations are modified when transfers are made electronically. Similarly, it would be helpful to identify the degree of institutional development necessary for CCTs to successfully make the transition to the delivery of transfers through savings accounts. Finally, it would be interesting to investigate what difference it makes, from a logistical and/or administrative standpoint, to make deposits in savings accounts instead of through prepaid debit cards.

5.2 CCT recipients

There is evidence about the decrease in transaction costs for recipients when payments are made electronically (Bill & Melinda Gates Foundation 2009; Maldonado and Urrea 2010; Duryea and Schargrodsky 2007). More research, and in different settings, would be helpful, however, because it would make it possible to understand the degree of external validity of this result. It would also be important to study the degree to which the recipients' financial security changes and to determine what problems they encounter when interacting with financial institutions instead of CCTs to receive their payments.

With regard to savings accounts, specifically, it would be important to obtain more evidence than currently exists about the acceptance of accounts, frequency of use, accumulated balances (González Rosas, n/d; Trivelli **et al.** 2011), crowding-out of other types of (informal) savings, and the effects of the accounts on social networks, etc. It is also important to determine what type of additional interventions are needed so that the change from receiving transfers in cash to receiving them in savings accounts is as smooth as possible for the households. Is it necessary to have an educational component during the transition? If so, how should the education be handled? Is it necessary to provide the recipients with financial education follow-ups during the transition period? If so, what type of follow-ups?

Particularly relevant for the CCTs, more research is needed on the effect of having a savings account and the capacity of households to escape poverty, cope with negative shocks to their income (Maldonado **et al.** 2011), start new businesses or invest in existing businesses (Maldonado **et al.** 2011), make home improvements (Maldonado **et al.** 2011), accumulate assets, etc. Also highly relevant is research on how spending on education (Maldonado **et al.** 2011) and health gets affected and how household members' levels of education and health of change. Similarly, it is important to identify changes in spending on food and on the diet/nutritional level of the household.

All of these impacts can be analyzed in the short term. It is also important, however, to verify what happens with them in the medium and long term. It would be particularly interesting to know if access to savings accounts allows a smoother transition from being a recipient to no longer being one. It would also be interesting to determine if a household's vulnerability to losing the gains it has made through its participation in the program decreases if it has a savings account. This issue is relevant for both, households that have graduated from the programs (which may still have school-age members), and households that no longer have members who make them eligible to receive transfers.

With regard to medium- and long-term impacts, it is important to determine if the integration of CCT recipients into the formal economy has an effect. It would also be interesting to document the extent to which recipients begin to demand other financial services, such as loans, insurance, electronic transfers, remittance delivery, etc. With regard to these latter topics, it would be helpful to identify the factors that are decisive, or at least those that correlate with recipients choosing one course of action or another.

5.3 Financial institutions

Finally, it is important to identify the type of accounts financial institutions could offer and the characteristics they should have if the institutions' services are to be profitable and the recipients are to be attracted to demand them and use them. It would also be important to determine the minimum scales required in terms of the number of new customers and/or deposits from them, so that serving CCT recipients is attractive to the financial institutions. It would be helpful to determine the importance of the level of trust the recipients must have in the CCT before they decide to use services offered by financial institutions. In this regard, more research is needed on how much demand for loans (Kaiser **et al**. 2012), insurance and other financial services increases once recipients have access to savings accounts. With regard to this topic, it would be very useful to identify the decisive factors in the increase of this demand.

Finally, if the institutions need government support or subsidies to begin to provide services to CCT recipients, it would be helpful to identify what type of support and/or subsidy is necessary and for how long it would be needed. Similarly, it is important to determine the degree of institutional development and what type of infrastructure the financial institutions should have in order to provide savings services effectively to CCT recipients. Along with this, it is important to have a clear idea of the type of regulatory framework that should exist in a country for the union of CCTs and savings to be feasible.

7 Conclusion

Despite all the apparent potential benefits of combining CCTs and savings, we currently know little about the subject. The little we do know, however, is encouraging. If these initial positive findings are confirmed and complemented with other positive results, a new, effective and replicable economic development policy could emerge. It is crucial to begin now to engage in rigorous research to corroborate the findings made so far and test the large number of hypotheses we have identified in this paper.

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