

Cash Transfers in Developing Countries: Local Multipliers, Aggregate Effects, and External Adjustment*

Arthur Mendes^a, Wataru Miyamoto^b, Thuy Lan Nguyen^c, Steven Pennings^a

^a *World Bank*

^b *University of Hong Kong*

^c *Federal Reserve Bank of San Francisco*

Abstract

What are the macroeconomic impacts of cash transfers in developing countries, and how do they change as programs scale up? To answer these questions, we build a two-region New Keynesian small open economy model and calibrate it to rich microdata from a randomized controlled trial (RCT) in Malawi. The model implies a local multiplier on temporary transfers of about one in treated regions, which depends on the degree of price stickiness, the share of liquidity-constrained households, and the extent of local bias in consumption. Spillovers to the rest of the country can be negative if the capital account is closed, as the transfer can appreciate real exchange rate and crowd out exports, but can be positive when capital can flow more freely and even larger when the exchange rate is fixed. A counterfactual scaled-up cash transfer program is likely to have smaller local and aggregate multipliers in Malawi, mostly due to its closed capital account. Our analyses suggest that macroeconomic frictions and the monetary policy regime are crucial to pin down the aggregate effects of scaled-up programs from local RCT estimates.

Keywords: cash transfers, randomized control trials, local multiplier, developing countries, capital account openness, exchange rate regime

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Email addresses: agalegomendes@worldbank.org (Arthur Mendes), wataru.miyamoto1@gmail.com (Wataru Miyamoto), thuylan.nguyen00@gmail.com (Thuy Lan Nguyen), spennings@worldbank.org (Steven Pennings)