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GROWTH, INEQUALITY, AND POVERTY

PROSPECTS FOR PRO-POOR ECONOMIC DEVELOPMENT

Edited by
Anthony Shorrocks and Rolph van der Hoeven

UNU-WIDER STUDIES IN DEVELOPMENT ECONOMICS

GROWTH, INEQUALITY, AND POVERTY

UNU WORLD INSTITUTE FOR DEVELOPMENT ECONOMICS RESEARCH (UNU/WIDER)

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ANTHONY SHORROCKS ANDROLPH VAN DER HOEVEN

A study prepared by the World Institute for Development Economics Research of the United Nations University (UNU/WIDER)

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Great Clarendon Street, Oxford OX2 6DP
Oxford University Press is a department of the University of Oxford.
It furthers the University's objective of excellence in research, scholarship,
and education by publishing worldwide in
Oxford New York
Auckland Bangkok Buenos Aires Cape Town Chennai
Dar es Salaam Delhi Hong Kong Istanbul Karachi Kolkata
Kuala Lumpur Madrid Melbourne Mexico City Mumbai Nairobi
São Paulo Shanghai Taipei Tokyo Toronto
Oxford is a registered trade mark of Oxford University Press
in the UK and in certain other countries
Published in the United States
by Oxford University Press Inc., New York

World Institute for Development Economics Research of the United Nations University
(UNU/WIDER), Katajanokanlaituri 6B, 00160 Helsinki, Finland

First published 2004

British Library Cataloguing in Publication Data
Data available
Library of Congress Cataloging in Publication Data
ISBN 0–19–926865–7(hbk.)
1 3 5 7 9 10 8 6 4 2

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List of Acronyms and Abbreviations

BNPP	Bank Netherlands Partnership Program
CAISTAB	Caisse de Stabilization
CFA	Communauté financière d'Afrique
CGE	Computable general equilibrium
DAC	Development Assistance Committee
DDSS	Direction de la Démographie et Statistique Social
DFID	Department for International Development
DNG	distribution-neutral growth
DSM	Direction des Statistique des Ménages
EA	enumeration area
ECV	Encuesta de Condiciones de Vida. Sample survey based on the Living Standards Measurement Surveys approach developed by the World Bank
EDG	equal distribution growth
ENV	Enquête de Niveau de Vie (INS survey)
EP	Enquête Prioritaire (INS survey)
EPM	The Enquête Permanente Auprès des Ménages
FGT	Foster, Greer, and Thorbecke
FGT1	headcount and poverty gap measure: Foster, Greer, and Thorbecke index 1984
FGT2	squared poverty gap measure: Foster, Greer, and Thorbecke index 1984.
GATT	General Agreement on Tariffs and Trade
GDP	Gross domestic product
GIS	geographic information systems
Globkom	Swedish Parliamentary Commission on Global Development
GLSS	Ghana Living Standards Survey
GMM	generalized method of moments
HIPC	Heavily Indebted Poor Countries
IBGE	Instituto Brasileiro de Geografia e Estatística
IFI	international financial institution
IES	income and expenditure survey
ILO	International Labour Organization
INEC	Instituto Nacional de Estadistica y Census (National Statistical Institute of Ecuador)
INS	Institut National de la Statistique of Côte d'Ivoire
INSTAT	Institut National de la Statistique of Madagascar
LDCs	least developed countries

LSMS	Living Standards Measurement Study of the World Bank
MDG	Millennium Development Goal
MTEF	Medium-term expenditure framework
NAS	national accounts
NGO	non-governmental organization
OECD	Organisation for Economic Co-operation and Development
OHS	October Household Survey
OLS	ordinary least squares
OPM	ordered probit model
PBG	poverty bias of growth
PCE	private consumption expenditure
PNAD	Pesquisa nacional por amostra de domicílios
POVCAL	Program for Calculating Poverty Measures from Grouped Data
PPP	purchasing power parity
PWT	Penn World Tables
SEWA	Self-Employed Women's Association
SOAS	School of Oriental and African Studies
UNDP	United Nations Development Programme
WDR	World Development Report

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Acknowledgements

This volume has its origins in an international conference on growth and poverty which took place in Helsinki in May 2001, and was attended by 150 persons from all around the globe. We would like to thank the paper presenters and other conference participants for their valuable contributions to the scholarly discussions, and the staff of UNU/ WIDER in Helsinki for their smooth running of the backstage arrangements. All helped to make the conference a great success.

We are grateful to the many people who were involved in the preparation of this volume. Tony Addison and Cecilia Ugaz assisted in the selection of papers. Numerous peer reviewers wrote anonymous reports on the draft chapters, offering incisive and useful comments on the substance and quality of each of the studies. We also thank the chapter authors whose careful attention to the points raised by the reviewers and editors significantly improved the quality of the published material. Adam Swallow liaised with Oxford University Press and ensured the efficient processing of the manuscript.

Special thanks are due to Anne Ruohonen, who handled most of the formatting and checking of the chapters, and to Lorraine Telfer-Taivainen, who not only had primary administrative responsibility for the original WIDER conference but also dealt with the final preparation of the manuscript.

Helsinki and Geneva

September 2003

Anthony Shorrocks

Rolph van der Hoeven

Introduction

ANTHONY SHORROCKS ANDROLPH VAN DER HOEVEN

INTRODUCTION

The relationship between growth, inequality, and poverty lies at the heart of development economics. It has been, and remains, one of the most controversial topics. Indeed, very few of the other core areas in development economics can compare with the shifts, reversals, and reaffirmations of views that have characterized the analysis of the interaction between growth, poverty, and inequality. Evidence that inequality and poverty rose in the 1980s and 1990s in many countries, including some of the OECD countries, rekindled the ongoing controversies, which have not so much evolved as fluctuated over the past 50 years.

From the 1950s to the early 1970s, the debate emphasized the likely trade-offs between growth and income inequality. This derived in part from Kuznets' famous 'inverted U-hypothesis', which posited that inequality rises during the initial phases of development and then declines after some crucial level is reached (Kuznets 1955). The idea of a trade-off between growth and inequality is supported by certain theories of growth. Kanbur (1998), for example, points out the obvious correspondence between Kuznets' empirical results and Lewis' labour surplus model (Lewis 1954). The latter predicts that in an economy with an 'unlimited supply of labour' the profit share rises relative to the wage share until the labour surplus is exhausted. Similarly, Kaldor's growth model, in which capitalists have a higher marginal propensity to save than workers, implies that redistribution in favour of profits raises the growth rate (Kaldor 1967). However, this model applies more to developed countries—where the functional distribution of income largely consists of wages and profits—rather than to developing countries.

The mood shifted in the 1970s when attempts were made to identify redistributive mechanisms which aid poverty reduction without hampering growth. Studies also began, for the first time, to emphasize non-income measures of poverty in the related 'basic needs' literature. This change of focus was relatively short-lived, and went into reverse with the rise of neoliberalism and the so-called 'Washington Consensus' in the early 1980s. Bolstered in part by the successful experience in East Asia, growth itself would be the main vehicle for poverty reduction, achieved through trickle-down mechanisms not always clearly specified.

The 1990s saw a number of challenges to both the neoliberal analysis and the earlier view of a trade-off between growth and equity. An expanding volume of empirical evidence showed no consistent relationship between growth, inequality, and poverty across countries and over time. At the same time, studies suggested that in many developing countries in Africa, in transitional economies, and in Latin America, stabilization and adjustment policies had an adverse impact on poverty and inequality or, at best, did little to improve the conditions of the poor. Furthermore, a consensus emerged that the 'high performing' Asian countries, prior to the financial crisis of the late 1990s, combined rapid growth of per capita income with relatively low and stable inequality.

The recent literature that challenges the trade-off and trickle-down approaches has its roots in the pro-distribution arguments of the 1970s which constructed a model of 'distribution with growth' in which social groups are distinguished by asset ownership or mode of access to assets. Growth and distribution were related through income linkages between social groups via connections between the labour and commodity markets. Simulation experiments with this model indicated that if aggregate productivity increased then redistribution would lead to substantial improvements in the incomes of not only the poor, but other social groups as well.

More recent contributions have built on these ideas of how inequality and poverty reduce the capacity for growth, and vice versa. They also argue that lower initial inequality raises the likelihood that growth will reduce poverty. However, it has also been noted that income inequality is relatively stable within countries, providing some support for the pessimistic conclusion that poverty will tend to persist as countries grow.

In recognition of the importance of these issues, UNU/WIDER organized a conference on growth and poverty in May 2001.[1] Its purpose was to review current thinking on the topic, to seek and encourage fresh research, and to bring researchers from different backgrounds together to discuss whether the relation between growth, poverty and inequality can be put into a sharper perspective for policy-making. About fifty papers were presented at the conference. This volume contains a selection of those papers together with other material linked to activities at UNU/WIDER.[2]

The volume starts with an essay by Kanbur which captures well the tone of the debate on poverty at the beginning of the twenty-first century. It reviews why, with so much new research and improved data, there is profound disagreement on crucial issues of growth, poverty, and inequality within academic circles, and among organizations and various groups active in the development field. Before spelling out the different perceptions towards growth, poverty, and inequality, Kanbur points out that there is now harmony on a variety of issues which were contentious a couple of decades ago. The fierce debates on growth and poverty have unfortunately tended to obliterate these areas of agreement. One consensus to have emerged is the view that improved education

[1] This meeting was the first of a series of large-scale conferences at UNU/WIDER on poverty related issues, and focused on income poverty. Future meetings will give more prominence to the non-income aspects of poverty and well-being.

[2] Three of the papers have recently appeared in academic journals. The remaining papers were refereed, rewritten, and edited for this volume.

and health should be regarded on a par with improved income when assessing poverty alleviation and the social progress outcomes of economic policy.[3] A second point of agreement is that transnational 'goods' or 'bads' such as environmental spillovers, unstable financial markets, or research into tropical agriculture and diseases, have enormous spillover effects, and that public intervention is needed in these areas.

The old 'market versus the state' debate provides a third example of converging views, with a clear acceptance that both markets and states are important. Development practitioners, including NGOs, have demonstrated very practical approaches, and divisions are far less than they were at the end of the Cold War. Another related area of agreement is growing recognition of the importance of institutions in regulating markets, constraining governments, and determining the interaction between households in the market place. These areas of recent agreement are very broad, of course, and disputes may well resurface if and when policies are actually implemented. Nevertheless, it is important to note that some degree of consensus has been reached in a number of areas.

THE NATURE OF DISAGREEMENTS ON POVERTY AND GROWTH

Kanbur argues that much of the disagreement can be traced to differences in perspectives towards three key features of the framework of the debate, namely, aggregation, time horizon, and market structure.

As regards *aggregation,* progress in poverty reduction is often measured as the decline in the percentage of the population below a certain income poverty line, and much is made of the fact that according to this definition poverty has gone down in many countries. But such analysis needs to be qualified. First, the value of public services and access to market opportunities is rarely taken into account; often these services have deteriorated making people feel worse off. Second, a national poverty figure is composed from different groups (regional, urban-rural, gender) whose poverty experiences frequently move in opposite directions. Third, those working with the poor often think in terms of absolute numbers rather than percentages. While the percentage of the population in poverty may have gone down, absolute numbers may have remained stable or even increased, especially in countries with fast rates of population growth.

A second aspect concerns the length of the *time horizon.* For example, in discussing the consequences of trade reform, most commentators will have in mind a medium time frame. This is driven by the equilibrium theory on which many assumptions are based. Markets and factors of production need time to adjust to structural changes in the economy. Activists, however, are usually concerned with short-term aspects, not least because 'short-run survival trumps medium-term benefits'.[4] Yet, other groups

[3] Education and health are seen as both desirable outputs as well as a necessary inputs. However, opinions remain divided on the relative importance of aspects of poverty which deal with processes of change such as empowerment, and the attention these should be given in policy formulation and budgetary allocations.

[4] There is more agreement on this issue now, especially with regard to the 'safety nets' which are intended to compensate for short-term negative effects. But those concerned with negative effects argue that safety nets often cannot be put in place fast enough and cannot compensate for major structural imbalances which cause severe poverty.

have a much longer time horizon in mind, arguing, for example, that economic growth cannot be sustained given the environmental capacity of the earth. To achieve global poverty reduction such groups call for explicit redistribution from North to South as a substitute for substantial economic growth.

A third area of disagreement lies in the *assumptions of market structure*. Proponents of the optimistic view of events often assume a competitive market structure, with a large number of agents interacting without market power. Others, however, point to distorted market structures governed by big institutions and corporations (e.g. in the trade of many tropical products), the power of money lenders in villages, and the attitudes of large countries in trade negotiations, to give some examples. Kanbur argues that the perception of certain market structures determines the way in which the poor perceive the benefits and costs of policies such as trade liberalization, capital mobility, and privatization. He argues strongly for a more detailed analysis of the distributional consequences of economic policies in the context of non-competitive market structures.

In his final section Kanbur introduces what he calls the 'red herring' debate on growth. He cites empirical studies which demonstrate that growth is strongly correlated across countries and over time with reductions in national-level measures of income poverty. Such observations lie at the heart of the 'growth is good for the poor' position. He further argues that the group of analysts who have difficulty with this position never claimed that a zero growth rate is good for the poor, or that growth is always bad for the poor. What is at issue are the policies used to stimulate growth, and the fact that the 'growth is good for the poor' stance often implies policy packages prescribed by the international financial institutions and northern finance ministers. According to Kanbur, the real debate should focus on the alternative policy packages and their consequences for redistribution and poverty. Confusion on this issue is exacerbated by the common practice of using growth to mean both an increase in per capita income and as shorthand for 'growth-oriented policies'.

DIFFERENT VIEWS OF GROWTH, INEQUALITY, AND POVERTY

The next six contributions in this volume (Chapters 2–7) deal with various aspects of the growth and poverty debate outlined by Kanbur. The first is the paper by Dollar and Kraay entitled 'Growth is Good for the Poor'. This study, which has provoked wide debate, observes that the average incomes of the poorest fifth of society rise proportionately with average incomes, a direct consequence of the fact that the share of income accruing to the bottom quintile does not vary systematically with average income. Dollar and Kraay document this empirical regularity in a large sample of ninety-two countries spanning the past four decades, and show that it holds across regions, time periods, income levels, and growth rates.

This finding is not entirely unexpected. In fact, in any long-run equilibrium the income share of the poorest quintile must be constant. The share cannot grow forever at a positive rate, since the income share of the bottom quintile cannot, by definition, exceed 20 per cent. Nor can the share contract continuously without risking the likelihood that most or all members of the bottom quintile will be unable to sustain life. Distributional neutral growth, therefore, may be regarded as the norm. However, this observation does not imply that the income share of the poorest quintile cannot rise or fall in the short or medium term, or in response to particular circumstances or policies.

Dollar and Kraay go on to show that several determinants of growth—such as good rule of law, openness to international trade, and developed financial markets—have little systematic effect on the share of income of the bottom quintile. The authors, therefore, conclude that these factors benefit the poorest fifth of society as much as everyone else. The evidence also offers weak support for the view that stabilization from high inflation, as well as reductions in the overall size of government, not only raises growth but also increases the income share of the poorest quintile.

Finally, the authors examine several factors commonly thought to disproportionately benefit the poorest in society, such as public expenditure on health and education, labour productivity in agriculture, and formal democratic institutions. They find little evidence of their effects. According to the authors, the absence of robust findings indicates that relatively little is known about the broad forces that account for the cross-country and intertemporal variation in the share of income accruing to the poorest quintile. Based on these findings the authors argue that the growth enhancing policies of a good rule of law, fiscal discipline, and openness to trade should be at the centre of successful poverty reduction strategies.

The next chapter by Ravallion agrees that the poor in developing countries usually share in the gains from rising aggregate affluence and in the losses from aggregate contraction. He observes, however, that there are large differences between countries in how much poor people share in growth, and that there are diverse impacts amongst the poor in a given country. He argues, furthermore, that cross-country correlations are clouded in data problems and hide welfare impacts, and can therefore be deceptive for development policy.

Looking beyond the averages in the relation between poverty rates and growth, Ravallion emphasizes the importance of initial conditions. Ignoring extreme values, he finds that 95 per cent confidence interval estimates of the growth elasticity imply that a 1 per cent rate of growth in average household income will result in anything from a modest 0.6 per cent drop in the poverty rate to a more dramatic 3.5 per cent decline. Hence, the variance of the growth elasticity of poverty is extremely important.

Ravallion goes on to note that inequality increased in half of the cases with spells of positive income growth, which leads him to present a two-by-two classification of rising and falling household income and of rising and falling inequality. Amongst countries with rising average income and rising inequality, the median rate of decline in the proportion of the population living below the $1-a-day poverty line was 1.3 per cent per year. In contrast, in countries with rising average income and falling inequality, the median rate of poverty reduction was seven times higher (about 10 per cent). In countries with falling average income and rising inequality poverty rates rose by a dramatic 14 per cent, while in countries with falling average income and falling inequality, poverty rates rose by less than 2 per cent.

Ravallion argues further that, even when inequality is not rising, a high level of initial inequality can stifle prospects for pro-poor growth, as high initial inequality lowers considerably the growth elasticity of poverty. He goes on to point out that when negligible correlations are found between changes in inequality and indicators of policy reform, as in Dollar and Kraay, this does not imply as a matter of course that the outcomes of such reforms for the poor depend solely on the growth effects. Averaging across the diversity of initial conditions can hide systematic effects; in one group of countries initial conditions may ensure that the rich benefit, keeping inequality high, while in another group of countries initial conditions can lead the poor to benefit. In these circumstances, reform policies entail a sizeable redistribution between the poor and the rich, but in opposite directions for the two groups of countries. Across all countries one could then well find zero correlation between growth and changes in inequality, or discover that the average impact of policy reform on inequality is not significantly different from zero. Yet, these results mask the fact that non-random distributional change is going on below the surface. An example is trade liberalization, which has been shown to decrease inequality in some countries and increase inequality in others.

The next contribution is by Heltberg which elaborates the elasticity of poverty as discussed by Ravallion. Heltberg first reiterates that the magnitude of the elasticity of poverty with respect to distribution-neutral changes in mean income depends on the location of the poverty line and, hence, should not be treated as a constant across countries or time. It tends to increase monotonically with mean income, holding the poverty line constant and depends strongly (and negatively) on the degree of inequality. As a consequence, an unequal income distribution is a serious impediment to effective poverty alleviation. Heltberg infers from these observations that the 'growth versus redistribution' dichotomy is misleading. Furthermore, he cautions against simplistically decomposing poverty changes into growth and distribution components, because the growth effect is itself a function of the degree of inequality. The manner in which growth and inequality interact to shape poverty is not additive. Heltberg admits that redistribution often has limited potential given existing structures, and that growth therefore remains a necessary condition for poverty alleviation. Yet, the level of inequality, and changes therein, still matter. This is because (i) for any given level of average income, the level of inequality affects the degree of poverty; (ii) inequality strongly affects the growth elasticity of poverty, with lower inequality contributing to an acceleration of poverty reduction for a given rate of growth; and (iii) if recent cross-country regression studies are to be believed, initial inequality, especially asset inequality, is harmful for growth. For these reasons, Heltberg argues that inequality remains important, and that there is a continuing need to search for effective policies for reducing inequalities, or at least for preventing them from rising.

While Ravallion emphasizes the importance of initial conditions, and is therefore cautious against findings that 'no correlation means no impact (on poverty)', Gundlach, Pablo, and Weisert in Chapter 5 take issue with the finding by Dollar and Kraay that higher primary educational attainment of the workforce is not correlated with increases in the income of the poor. They use a broader measure of human capital which accounts for international differences in the quality of education, and derive significant correlations suggesting that an increase in quality-adjusted education raises the relative income of the poor as well as average incomes. Thus, education is not distribution-neutral. It seems to improve the income distribution, allowing the poor to benefit disproportionately from growth. As a consequence, they support a focus of economic policies on education in order to reduce poverty and to speed up development.

THE ARGUMENTS FOR INCREASED REDISTRIBUTION

In Chapter 6, Naschold observes that changes in consumption, income distribution, and levels of poverty are intrinsically linked. He uses three methods to assess the relationship between these variables across countries, concentrating in particular on the differences between countries at different stages of development. An important finding is that consumption elasticities of growth vary significantly between the least developed countries (LDCs) and other developing countries, a result strongly supported by all methodologies. In addition, he finds that the distribution of income matters for poverty reduction, particularly so in LDCs. Simulations of poverty trends suggest that for poverty reduction in this group of countries, changes in distribution can be as important as changes in the level of consumption. In order to make substantial progress towards halving poverty by 2015, Naschold argues that LDCs will have to improve the distribution of income (or at least prevent it from getting worse) as well as achieving higher rates of economic growth. While distribution issues are clearly important for poverty reduction, he concludes that we need to know more about what drives changes in inequality if we are to identify ways in which policy can support efficient improvements in the distribution of national income.

The next contribution by Dağdeviren, van der Hoeven, and Weeks, begins with an overview of past and present literature on inequality and poverty in general, and on methods and incidence of redistribution in particular, emphasizing the growing consensus that countries with relatively egalitarian distribution of assets and incomes tend to grow faster. They argue that reducing inequality cuts both ways. A pro-poor growth path not only directly benefits the poor in the short run, but also creates in each subsequent period the lower inequality initial conditions which enhance future growth prospects. The authors go on to show empirically that economic growth has tended to be no better than distribution-neutral (echoing the points made by Dollar and Kraay and Ravallion in the earlier chapters). This leads them to explore in more detail the relationships between growth, inequality, and poverty, and to carry out three simulation exercises based on: (i) a 1 per cent distribution-neutral increase in per capita GDP; (ii) a 1 per cent increase in per capita GDP distributed equally across income percentiles; and (ii) a 1 per cent redistribution of income from the richest 20 per cent to the poorest 20 per cent. Countries are then classified according to which of those three simulations yields the greatest reduction in poverty.

For the overwhelming majority of middle-income countries, the simulation exercises demonstrate that poverty reduction is most effectively achieved by a redistribution of current income. Redistribution with growth is the second best option, while distribution-neutral growth is a poor third. In contrast, low-income countries require a growth strategy. Nevertheless, for most of these countries redistribution with growth is more effective than the (distribution-neutral) status quo growth.

The authors conclude by discussing several policies that make growth more equitable. They point out that objections against redistribution in developing countries, based on the argument that redistribution is costly and requires a minimum set of administrative capacities, should be set against the fact that status quo economic policy making is also costly and requires a minimum set of administrative capacities. Hence, under both scenarios, one often needs to operate in a second best environment. Policies for redistribution should therefore also be pursued.

POVERTY REDUCTION AND MICROECONOMIC ANALYSIS

The previous contributions emphasized that poverty can be reduced at a faster rate when pro-poor growth strategies are applied and when special redistribution policies are undertaken. However, as Ravallion and Dagdeviren *et al.* argue, there are no blanket policy proposals—the scope and nature of pro-poor growth strategies and of redistribution policies depend on the initial situation and on specific country circumstances. This, in turn, calls for improved microeconomic studies which can inform poverty analysis and contribute to the design of pro-poor policies. The next four chapters illustrate a variety of new approaches to distributional analysis.

Demombynes *et al.* use a new methodology in Chapter 8 to produce disaggregated estimates of poverty for three developing countries: Ecuador, Madagascar, and South Africa. The countries are very dissimilar—with different geographies, stages of development, quality and types of data, and so on. Nevertheless, the authors demonstrate that the methodology works well in all three countries and produces valuable information about the spatial distribution of poverty within these countries, information that was previously not available. Their methodology is based on a statistical procedure which combines household survey data with population census data, by imputing into the latter a measure of economic welfare from the former. Like the usual sample-based estimates, the poverty rates produced are also estimates and are subject to statistical error. They demonstrate that the poverty estimates produced from census data match well the estimates calculated directly from the country's surveys. The precision of the poverty estimates produced with this methodology depends on the degree of disaggregation. In all three countries the constructed poverty estimators allow a level of disaggregation far below that which can be achieved with surveys. They then illustrate how the poverty estimates produced with this method can be represented by maps, thereby conveying an enormous amount of information about the spread and relative magnitude of poverty across localities (as well as the precision of estimates) in a way which is quickly and intuitively absorbed, particularly by a non-technical audience. Such detailed geographical profiles of poverty can inform a wide variety of debates and deliberations amongst policy-makers as well as civil society.

In Chapter 9, Bandyopadhyay describes the dynamics of growth and the convergence of real per capita incomes across Indian states over the period 1965–97, and then attempts to analyse some of the factors underpinning such income dynamics. A number of specific issues are addressed: the trend towards equality in the cross-sectional income distribution across Indian states; the possibilities for interregional mobility; and the persistence of differential growth performance.

Unlike standard practice, Bandyopadhyay examines interstate income inequalities in terms of the behaviour of the entire cross-sectional distribution. This approach essentially posits a law of motion of the cross section income distribution which allows researchers to study not just the likelihood, but also the potential causes, of poorer economies becoming richer than those currently rich, and of the rich regressing to become relatively poor. Over the period 1965–97, Bandyopadhyay finds a strong tendency towards polarization resulting from the formation of two income 'convergence clubs'; one at 50 per cent of the national average, the other at 125 per cent of the national average. Although cohesive tendencies were observed in the late 1960s, these weakened considerably with the reform policies of the following decades, with increasingly polarizing consequences. Unequal investment in infrastructure contributed significantly to the observed polarization, particularly with respect to the lower income club. Indicators of macroeconomic stability—principally capital expenditure and fiscal deficits—also help explain the lack of convergence and the trend towards polarization among Indian states.

The tenth contribution in the volume, by Grimm, analyses Ivorian income distribution data over the period 1992–98, and examines the link with the profound economic and sociodemographic changes which occurred in the 1990s, including the devaluation of the CFA franc in 1994 and the accompanying structural adjustment programmes. Microsimulations show that both the negative income growth in Abidjan and the positive income growth in rural Côte d'Ivoire were related to rising inequality. However, the devaluation of the CFA franc, and the structural adjustment programme (including the recovery of international aid), coupled with the price boom in the coffee/cocoa sector, caused a significant redistribution between rural and urban areas. Within-region inequality increased and between-region inequality decreased, leading to a rise in the proportion of the urban population among the poor.

Grimm's findings comply with most of the short and medium-term predictions of computable general equilibrium (CGE) models applied to the Ivorian case. However, recent movements in world prices of export crops show that a large part of the Ivorian population remains vulnerable to external shocks. Furthermore, the political instability evident since December 1999, and the subsequent freeze of international aid, discouraged and hindered private investment. In 2000 and 2001, Côte d'Ivoire experienced negative GDP growth, suggesting that the Ivorian economy today faces a crisis comparable to that of the early 1990s.

In Chapter 11, Ferreira and Leite ask whether more education really means less poverty, and undertake to answer this question by means of a microsimulation for the Brazilian state of Ceará. They conclude that a rise in the average endowment of education resulting from a broad-based expansion of enrolment coupled with a reduction in dropout rates would very likely make a substantial contribution to poverty reduction. Just how substantial depends on the way in which the structure of returns to education develops over time. Increased enrolment and a reduction in dropout rates would not, however, have the same impact on inequality. While the simulated educational expansion would be moderately equalizing if returns flattened in the future, it would be neutral if returns did not change; and inequality would actually rise if returns increased at the same time as the expansion took place.

Their second conclusion is that a combination of policies which succeed in expanding education in a more targeted way would help make educational expansions more progressive. At best, an increase in mean schooling leads to a small reduction in inequality. A more targeted effort, focussing on reducing illiteracy and keeping in school those most likely to leave, can play an important role in reducing income inequality. So a targeted exercise should not be a substitute for, but rather a complement to, a broader expansion of educational opportunities. Ferreira and Leite stress that all results depend heavily on what happens to returns to education, which are determined by the interaction between the relative supply of and demand for different skills. Given that gains in labour earnings to the poor are very sensitive to changes in demand for unskilled labour, stagnation of demand for unskilled labour is of particular concern, but could not be modelled in the paper.

Household dynamics play a crucial role in the analysis. As women acquire education and enter the labour force, their fertility behaviour also changes, reducing the number of children in the family. In income terms, each of these tendencies is positive for the families to which they belong. The model attaches great importance to such gender-sensitive effects on the overall welfare of poor families. But a large supply of female labour may generate downward wage pressure or enhance job competition. The extent to which Ceará will be able to capitalize on a more educated labour force depends, in large measure, on how effectively it can produce an overall growth strategy generating sufficient labour demand.

These four chapters, all stress the importance of looking in more detail at the microeconomic aspects of poverty analysis, applying simulation techniques and other methods to household data. However, it is also recognized that the outcomes of microsimulation exercises are often very sensitive to macroeconomic and growth variables. Hence the need, as expressed in the papers of Kanbur, Ravallion, and Dağdeviren *et al.* to pay attention to the distributional effects of macroeconomic and growth policies, and not to take the distributional outcome of such policies for granted.

POLICIES FOR POVERTY ALLEVIATION AND GROWTH

The final chapter by Bigsten and Levin reviews recent theoretical and policy research dealing with the relationship between economic growth, income distribution, and poverty. They do not find any systematic pattern of change in income distribution during recent decades, nor any systematic link from fast growth to increasing inequality. In contrast to previous studies, they claim that the level of initial income inequality is not a robust explanatory factor of growth, but admit that some recent empirical studies have found a negative impact of asset inequality on growth. Possible channels for this are credit rationing, reduced possibilities for participation in the political process, and social conflicts. Among the strategic elements that have contributed to reduced poverty, Bigsten and Levin emphasize agricultural and rural development; investment in physical infrastructure and human capital; efficient institutions that provide the right set of incentives to farmers and entrepreneurs; and effective social policies to promote health, education and social capital, as well as safety nets to protect the poor. They conclude that growth can be substantial if the policy and institutional environment is right.

CONCLUSION

The range of views covered in this volume makes a consensus of opinion unlikely. However, some general inferences can be drawn—the first being the difficulty of drawing general conclusions. Many of the chapters show that sweeping statements such as 'growth is good for the poor', 'education is good for the poor', or 'redistribution reduces poverty more than growth' can be supported by cross-country regressions. But since these observations have little or no policy implications, they tend to blur the debate on growth and poverty rather than illuminate it.

What the chapters in this volume show, each in their own context, is that initial conditions matter, specific country structures matter, and time horizons matter. Ravallion shows that initial conditions affect the speed with which growth can reduce poverty. Initial conditions and the structure of the economy also affect whether policies have a pro-poor or an anti-poor outcome—trade liberalization was mentioned as a case in point. Improved education is an end in itself, and can also contribute to reducing poverty; but its effect on inequality depends on supply and demand factors, which differ significantly across countries. Likewise, in some countries a redistribution of 1 per cent of income from the rich to the poor would reduce poverty more than a 1 per cent increase in total national income, but in other countries this is not the case. The later chapters in this volume support this attention to detail by illustrating how improved poverty analysis can better inform the debates on poverty.

Since the appropriate poverty reduction strategy is so country and context-specific, it seems clear that national creative solutions need to be encouraged. However, an emphasis on national policies also implies national ownership of such policies. While the term 'ownership' has recently acquired some negative connotations,[5] we use it here to refer to the benefits of ownership of policy analysis and an informed policy debate. Such a debate might hopefully lead to a more pro-poor set of development policies if consensus between different interest groups at the national level can be reached. It

[5] In negotiations with developing countries, international financial institutions have often insisted that countries 'own' their economic and fiscal policies, although these may well have been drawn up by the IFIs themselves.

might also lead to a sharpening of the issues and the various policy options without reaching consensus. In both cases, issues of poverty and inequality will have been put at the centre of public concern.

It is the task of UNU/WIDER and other UN research institutes to assist in such a debate and this is what we have attempted to do with this book.

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1 Economic Policy, Distribution, and Poverty: The Nature of Disagreements

RAVI KANBUR

1.1. INTRODUCTION

The end of history lasted for such a short time. If the early 1990s raised hopes of a broad-based consensus on economic policy for growth, equity, and poverty reduction, the late 1990s dashed them. The East Asian crisis and the Seattle debacle saw to that. In the year 2000, the governors of the World Bank, whose mission it is to eradicate poverty, could meet only under police protection, besieged by those who believe instead that the institution and the policies it espouses cause poverty. The street demonstrations in Prague, Seattle, and Washington DC, are one end of a spectrum of disagreement, which includes vigorous debate in the pages of the leading newspapers, passionate involvement of faith-based organizations, and the genteel cut and thrust of academic discourse.

The last 2 years have seen my involvement in an extensive process of consultation on poverty reduction strategies.[6] The consultation reached out to most interested constituencies in the academic, policy-making, and advocacy communities. It covered the international financial institutions (IFIs) and the myriad UN specialized agencies, government ministries in the North and the South, northern aid agencies, academic analysts in rich and poor countries, northern and southern advocacy non-governmental

[6] Most of this consultation was under the auspices of the World Bank's World Development Report on Poverty, of which I was Director until I resigned in May 2000.