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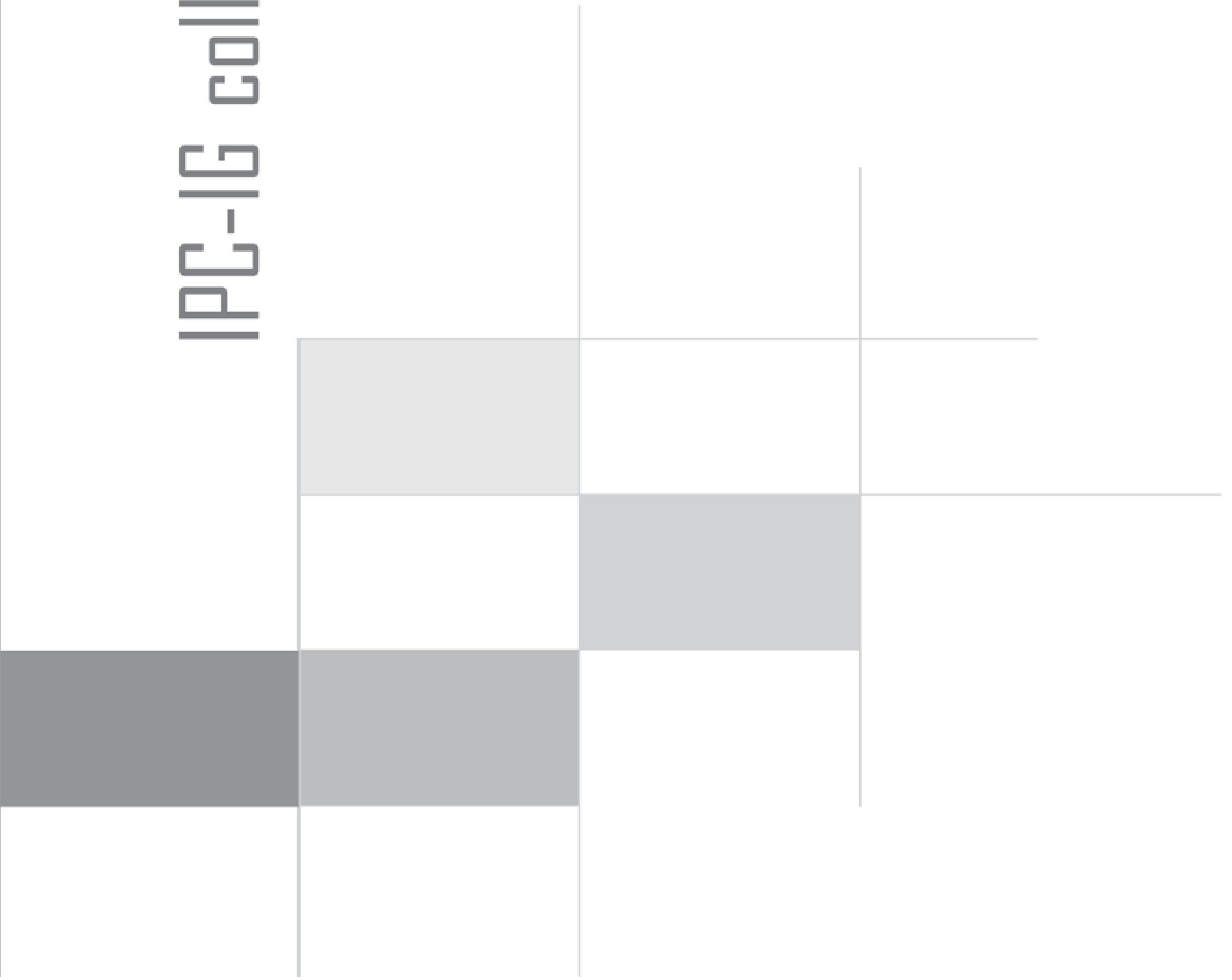

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Brasilia, Brazil - September, 2009

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International Policy Centre for Inclusive Growth
United Nations Development Programme

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The International Policy Centre for Inclusive Growth is jointly supported by the Poverty Practice, Bureau for Development Policy, UNDP and the Government of Brazil.

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ISBN: 978-85-88201-04-0

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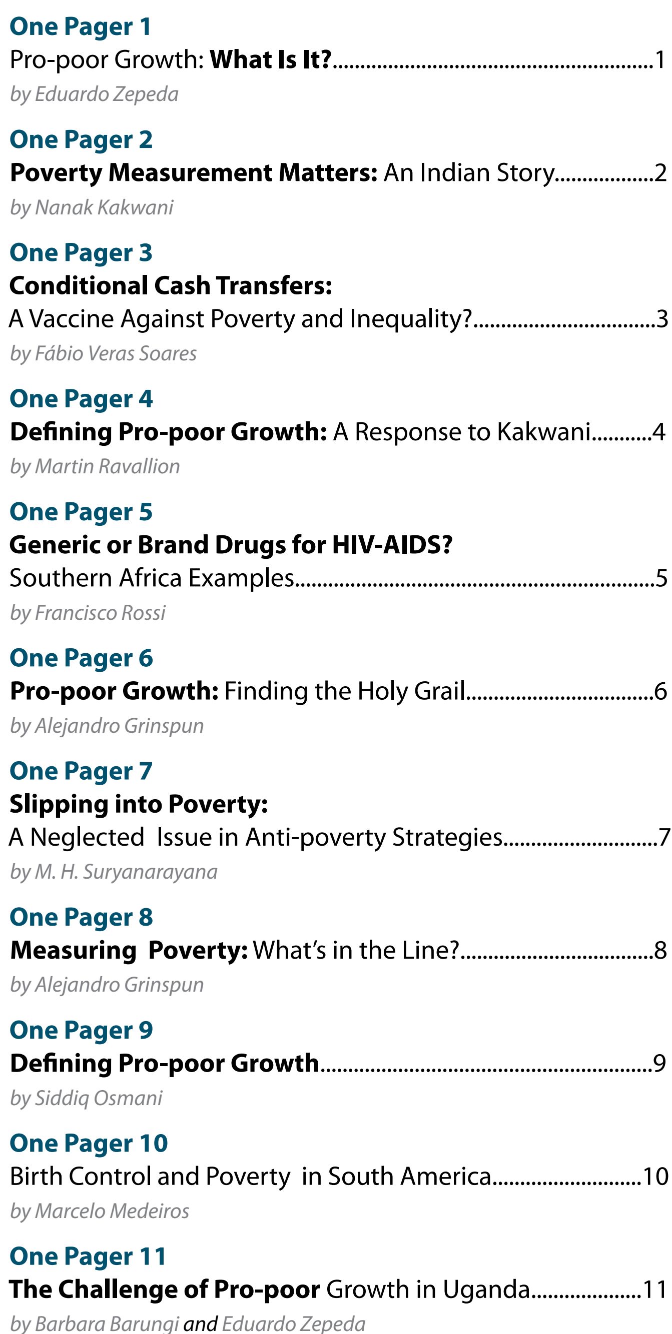

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FOREWORD

The International Policy Centre for Inclusive Growth (IPC-IG), a joint initiative between the Government of Brazil and the United Nations Development Programme (UNDP), is a global centre of excellence. Over the years, IPC-IG has left a deep mark on the analytical and empirical exploration of development issues, as well as on policy debates and dialogues. The Centre's work extends globally, regionally and at the level of individual countries through its superb research and policy work, excellent knowledge products, and outstanding outreach and communication.

One of the crown jewels of IPC-IG's work is its series of One Pagers, which provide readers with a deep but succinct perspective of many development issues. The One Pagers have covered issues ranging from employment guarantee schemes to the achievability of the Millennium Development Goals, from conditional cash transfers to poverty lines, from the feminisation of poverty to South-South collaboration. It is quite common to find the One Pagers in government offices and university libraries, and on the websites of research centres throughout the world. In many countries they have been translated into local languages for wider dissemination. The most popular of IPC-IG publications, the One Pagers have gained an enviable and widespread visibility and acceptance because of the topics they cover, their focused analysis, their policy perspectives and, last but not the least, their concise presentation in terms of both format and language. In a nutshell, they may be short, but they are invaluable.

I am very pleased that the Centre has decided to bring together, in the current volume, the ninety-nine One Pagers produced by IPC-IG. The endeavour brings all of these insights together, offering readers access to a mine rich with many and varied gems. I congratulate colleagues in IPC-IG for undertaking such a valuable initiative, which all of us—the admirers of One Pagers worldwide—will find extremely useful. We will be looking forward to a second volume in the future.

Selim Jahan
Director
Poverty Practice
Bureau for Development Policy, UNDP
New York

ACKNOWLEDGEMENTS

The International Policy Centre for Inclusive Growth (IPC-IG), formerly the International Policy Centre, links the development community to cutting-edge research. The One Pager series has proven to be an important means of transmitting knowledge and stimulating public debates on development policy.

This collection of ninety-nine One Pagers would not have been possible without the valuable input of a number of individuals. We are grateful for the generous contributions of more than sixty authors who gave us their time without any monetary or material remuneration. Special thanks go to the previous Directors of the Centre, Professor Nanak Kakwani and Professor Terry McKinley, for popularising the One Pagers.

The meticulousness and brilliance of Roberto Astorino in the layout and design add to the attraction of the One Pagers. Thanks also go to Rosa Maria Banuth for first-rate design work on preparing the One Pagers for this book. Francisco Filho is to be applauded for his outstanding communication strategy and for the wider dissemination of the One Pagers. The various feedbacks and comments received daily in response to the publications in this series demonstrate the success of his labour. Mention must also be made of the hard work and enthusiasm of Andre Lyra in keeping the One Pagers alive on IPC-IG's website.

IPC-IG is grateful to have Andrew Crawley, who joined the IPC-IG team and extensively improved the quality of the texts through his excellent copyediting. The translators of the One Pagers, Sabine Couffin (French), Salomon Blajberg (Portuguese) and Maria Julia Mendonza (Spanish), also deserve special mention for the quality of their work. The earlier One Pagers were translated by numerous UN volunteers, to whom we are grateful.

Last but not least, we thank all IPC-IG staff for the ongoing debate and stimulating discussions, some of which eventually take form as articles in the One Pager series.

Degol Hailu
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Pro-poor Growth: **What Is It?**

by Eduardo Zepeda,
International Poverty Centre

There is a growing consensus among development practitioners and thinkers that growth alone is not enough to reduce poverty. The centre of the discussion is now on pro-poor growth, which takes us well beyond the trickle down theories of a few decades ago. However, as important as this shift in development thinking is, there is still much to be done in defining what pro-poor growth is, how we assess and measure it and, more importantly, how we translate this knowledge into effective policy making.

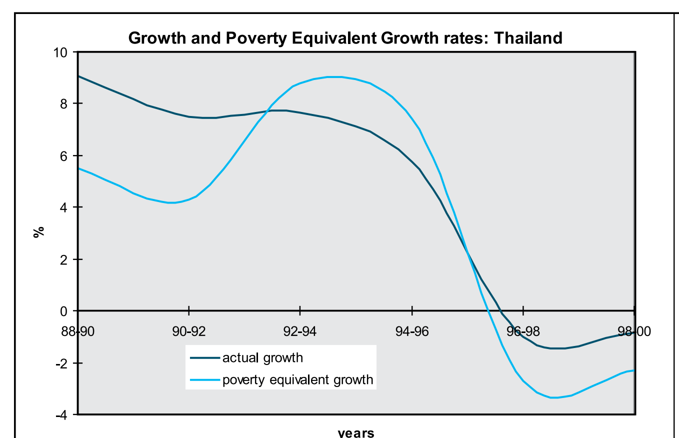
A recent IPC working paper by Kakwani, Khandker and Son (KKS) provides clues to increase our understanding of the meaning of pro-poor growth. Growth usually will allow for some poverty reduction. From time to time, however, growth may also be accompanied by an increase in poverty. Recession, on the other hand, normally tends to aggravate poverty, although there is always room for shielding the poor during downturns.

Ravallion (2004) defines pro-poor growth as any increase in GDP that reduces poverty. Such a definition is too broad: it implies that most real world instances of growth are pro-poor, even if poverty decreases only slightly and income distribution worsens during a period of strong growth. A more appropriate definition has growth as pro-poor if in addition to reducing poverty, it also decreases inequality. Despite being an improvement, this definition still does not reflect well what should be understood as 'pro-poor growth' and falls short of providing straightforward answers to various plausible combinations of growth, poverty reduction and inequality changes.

In their paper, KKS propose a simple and sensible definition, according to which growth is pro-poor, relatively speaking, if it benefits the poor proportionally more than the non-poor. Their methodology helps to overcome the ambiguities of most former approaches and is flexible and general enough to remain valid, whatever poverty measure is used.

The KKS methodology can readily be applied to household surveys designed to measure income and poverty. The procedure implies estimating a growth rate that gives more weight to the incomes of the poor; the weights depend on the poverty measure being used. This hypothetical rate is called the "poverty equivalent growth rate (PEGR)". If PEGR is larger than the actual growth rate, which occurs when the incomes of the poor grow more than the average income, then growth is pro-poor; if PEGR is equal or less than the actual growth rate, growth is said not to be pro-poor.

To illustrate the explanatory power of the PEGR, let's consider one of the three cases discussed in KKS's paper. Thailand's economy grew at a rate of 7.5% from 1988 to 1996, it then entered into a crisis that reduced GDP by an average of 1% between 1996 and 2000. During the growth years, poverty decreased from 33% to 11% and increased to 16% during the recession years.



According to Ravallion's definition, Thailand was on a pro-poor path throughout the growing years 1990-1996. But the PEGR methodology proposed by KKS tells a different story. In the graph plotting a smooth path of both actual growth rates and poverty equivalent growth rates, one can see that growth was actually pro-poor only during the latter part of the booming years, between 1992 and 1996, when the equivalent growth rates were larger than actual growth rates. The graph also makes apparent that the recession that followed was particularly anti-poor, since the equivalent growth rate was lower than the actual one.

KKS's methodology thus appears to allow for a much richer interpretation of how growth affects poverty. It should be welcomed as an important contribution to both theoretical and empirical analysis, and as a tool to better inform policy making.

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One Pager number 1
Published: September, 2004
Available at: <http://www.ipc-undp.org/pub/IPCOnePager1.pdf>

Poverty Measurement Matters: An Indian Story

by Nanak Kakwani,
International Poverty Centre

India entered a new era of rapid economic growth in the 1990s when it began its economic reforms. At its 6% growth rate, most would expect a strong reduction in poverty. In line this, the official estimates from two large surveys showed that poverty in rural areas fell from 37.3 in 1993-94 to 27.1% in 1999-2000, while in urban areas it fell from 32.4 to 23.6%. Deaton´s (2001) alternative poverty estimates indicated a smaller, but still significant reduction: from 36.2 to 28.8% nation-wide over the same period.

Things could not have been better, and the BJP-led government that had enthusiastically supported economic reforms rallied for the 2004 election full of complacency under the slogan of "India Shining". The May 2004 elections spoke differently. The party in power stepped down because the majority of the poor did not vote for them. Although a direct link between poverty and elections is always a difficult one, to say the least, one still should wonder: Don't People like growth and poverty reduction?

The answer might well be simpler. It might just be that a large one third of the population, the poor, might not have seen their living conditions improving, and thus overwhelmingly rejected the BJP-led government. If one looks carefully behind poverty estimates, one can see that poverty might have been underestimated in 1999-2000.

Given the large sample size involved, the most reliable estimates of poverty in India for the period should come from the 50th Round of the National Sample Survey (NSS) of 1993-94 and the 55th Round of 1999-2000. However, these two surveys are not fully comparable. Indeed, the 55th Round questionnaire was different from that in earlier surveys (Sen 2001), and that difference might have led to an underestimation of the true incidence of poverty in 1999-2000.

All surveys prior to the 55th Round used a 30-day recall questionnaire for all consumption items. Since many consumption items are purchased frequently, most food is purchased daily, a monthly recall period tends to underestimate the true expenditure because people tend to forget some of their purchases. To partially correct for this, the 55th Round questionnaire added a 7-day recall period to be applied to some of the expenditures, mainly the most frequent ones. This change, which was intended to improve poverty estimates turned out to be counterproductive. People gave mutually consistent responses when they were asked over these two recall periods, the 7 and 30-day ones. Since it is easier to remember over 7 days, people gave the 30-day figure as, roughly, the 7-day amount times 4. Thus, on the most frequently consumed items, a comparison based on the 30-day recall periods of the 1993-94 and 1999-2000 NSS led to an overestimation of consumption in 1999- 2000; and from there, to the alleged reduction in poverty. Interestingly, four small surveys, conducted between 1993-94 and 1999-2000, all showed an increase in poverty.

If people were given only the 7-day recall period, the consumption estimates obtained from the 55th Round would have been more accurate than those obtained from the earlier surveys, but still not comparable. Instead people were asked to report expenditures on the basis of both recall periods at the same time. This made it difficult to judge the accuracy of expenditures reported in the 55th Round and render its comparability even more difficult.

To work around this newly introduced flaw in the data, Deaton produced comparable poverty estimates. But, in arriving at his estimates, inevitably, he had to make a series of assumptions. Basically, he estimated the percentage of poor in 1999-2000 from the expenditure distribution of the items included in all surveys with a consistent recall period of 30 days. But his procedure has the shortcoming that it does not incorporate 1999-2000 data on the consumption of goods that are most frequently consumed by the poor. The 1999-2000 data supporting his estimates refer to such items as fuel, light, miscellaneous goods and services, non-institutional medical services, rent and taxes; these items accounted for only 20% of the total expenditure, and for hardly 5% of expenditures by the poor. It is inconceivable that one can ever hope to obtain any reliable estimates of poverty in 1999-2000 using so little information from the 55th Round. The fact is that there is no way now to get a comparable figure for 1999-2000 and by the same token, an assessment of the impact of economic reforms on poverty.

Even worse, the change in methodology of the 55th Round will also have serious implications in the comparability of future surveys. It is unfortunate that India's 50 year record comparable household survey system has been changed, and as such, it will no longer be possible to trace long term trends in poverty there.

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One Pager number 2
Published: September, 2004
Available at: <http://www.ipc-undp.org/pub/IPCOnePager2.pdf>

Conditional Cash Transfers:
A Vaccine Against Poverty and Inequality?

by Fábio Veras Soares, International Poverty Centre

Conditional Cash Transfers (CCT) have been regarded worldwide as the latest 'silver bullet' to fight poverty and inequality. This reputation is largely based on the positive evaluations of the Latin American experiences, such as *Progresa* in Mexico, *Bolsa Escola* and *Bolsa Alimentacao* in Brazil (now unified into *Bolsa Familia*), and *Familias en Accion* in Colombia. Defenders of such programmes emphasize that their virtues consist in attacking both long- and short-term poverty and inequality.

The short-term strategy is based on cash transfers to poor families with an immediate effect on poverty, depending on the level of the benefit and the efficiency of the targeting strategy. The long-term effect depends on the effectiveness of the conditionalities attached to the transfers, both in terms of their enforcement and their real power in boosting human and social capital. Conditionalities include compulsory children's attendance at school, mandatory visits to health centres, and monitoring of nutrition and immunisation. In general, these conditionalities focus on children in order to break the intergenerational transmission of poverty.

Some specialists argue that the conditionalities are not necessary since cash transfers already address the credit constraints faced by poor families. Thus, their increased incomes help improve education, health and nutrition achievements. However, conditionalities can also have other relevant effects. For instance, they can help to change some cultural features that jeopardize the chances of children of poor familys from getting out of poverty. For example, there is evidence in Brazil that families whose heads worked while they were children are more likely to send their children to work. In cases like this, conditionality might prompt a cultural change that would protect these children from an early entry into the labour market.

In the real world, specific CCT programmes differ in design, implementation and goals. Examining the Brazilian experience can be informative. During the 1990s, there were several municipal and state-level programmes whose design inspired the Federal *Bolsa Escola*, which started in 2000. The only Federal programme in place in the late 1990s in Brazil was the *PETI (Programme for the Eradication of Child Labour)*. Whereas the main direct goal of the municipal and state-level *Bolsa Escola* programmes was to increase school enrolment and attendance, the chief goal of *PETI* was to reduce child labour in hazardous activities by means of increases in school enrolment and attendance.

The evaluations of these two programmes show that they were successful with regard to their objectives. *Bolsa Escola* increased both enrolment and attendance rates, but had no effect on child labour (Cardoso and Souza, 2004), whereas *PETI* increased enrolment and attendance rates as well as reduced child labour (Soares and Pianto, 2003). None of them had a substantial impact on poverty, due to the small value of the cash transfers.

Why, unlike *PETI,* did *Bolsa Escola* not have the side effect of reducing child labour, despite increasing both enrolment and attendance rates? A distinguishing characteristic of *PETI* was that it provided resources to participant municipalities to offer extra-curricular activities in order to keep children busy during the whole day. There is evidence that where these after-class activities were widely used, child labour declined more sharply. Moreover, since *PETI* was a smaller programme and more clearly focused, it could more easily achieve its goals.

A large-scale programme, such as the new Federal programme, *Bolsa Familia,* certainly faces problems in enforcing its conditionalities, and therefore, in achieving positive externalities, such as reducing child labour. However, the problems in enforcement of conditonalities are not the only threat to the long-term goals of CCT programmes.

One of the main doubts hanging over CCTs is how their long-term goals will be achieved without improving the supply of quality education and health services for the targeted population. Besides enforcing conditionalities, it is necessary to improve the quality of social services so that the promises of a break in the intergenerational cycle of poverty can be fulfilled. Now that there is a mountain of evidence about the success as well as the limitations of CCTs (mainly in Latin America), it is certainly time to pay attention to the quality of public services so that the glowing promises of a long-term decline in poverty and inequality are not short-lived.

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One Pager number 3
Published: October, 2004
Available at: <http://www.ipc-undp.org/pub/IPCOnePager3.pdf>

Defining Pro-poor Growth: A Response to Kakwani

by Martin Ravallion,
World Bank

In its first One Pager, the International Poverty Centre discussed the meaning and measurement of 'pro-poor growth' and came out strongly in favor of a definition proposed by its Director, Nanak Kakwani, according to which growth is pro-poor if its rate is higher for the poor than the non-poor; roughly speaking, if inequality falls. This comment offers an opposing view.

Consider the example of China. Today, China's income poverty rate is probably slightly lower than the world's average; in 2001, 17% of China's population lived below $1 a day (at 1993 PPP) compared to 21% for the developing world as a whole. But it was a very different story around 1980. Then the incidence of poverty in China was one of the highest in the world at 64%. Economic growth was the main proximate cause of this rapid decline in poverty.

By Kakwani's definition this was not pro-poor growth, but rather growth that was biased *against* the poor. But it is surely hard to accept any definition that does not identify as 'pro-poor' what was possibly the most successful sustained record against poverty in recorded history.
I would argue that it makes more sense to say that growth is 'pro-poor' if some agreed measure of poverty falls with that growth. In other words, 'pro-poor growth' means growth that is deemed to benefit the poor.

If we follow common practice of measuring poverty in terms of purchasing power over commodities, then China's growth has unquestionably been pro-poor. This may be considered too narrow a definition. Some people would prefer to allow for relative deprivation, as measured by income relative to the mean in society. This can be done by letting the poverty line rise with mean income, although naturally growth will then have less impact on measured poverty. My preferred definition of 'pro-poor growth' can thus handle relative poverty, when one thinks that people care about their relative position as well as their absolute standard of living.

Only in the extreme case in which relative income is all that matters to welfare will this approach give us something like Kakwani's definition of pro-poor growth. This would mean that an equi-proportionate increase in all incomes was not deemed to benefit the poor or anyone else. That position would seem so implausible in China or anywhere else as to be rejected out-of-hand. By my definition, on the other hand, growth is typically pro-poor in that as a rule, though certainly not always, the incidence of poverty tends to fall with growth. This has been demonstrated repeatedly, on better and bigger data sets, since the 1990 *World Development Report* was published.

The real issue is not *whether* growth is pro-poor but *how* pro-poor it is. One can measure this by a 'distribution-corrected' rate of growth, which scales the ordinary growth rate up if the distributional change that accompanies growth is pro-poor, or down if it is not. This shows us how Kakwani´s and my definitions are linked: while mine focuses on the distribution-corrected growth rate, Kakwani's focuses solely on the distributional correction.

The deeper challenge remains of explaining why poverty falls so much faster in some settings than others. Again take the example of China. Its rate of pro-poor growth in the 1990s was a hefty 4% per annum. However, progress for the poor has been uneven over time and space since the early 1980s. I would argue that the sectoral and geographic composition of growth was critical. China could well have achieved even more rapid poverty reduction if its growth process had been more balanced. By my definition, China's growth would then have been even more pro-poor than it was, as poverty would have fallen faster. Thanks to its relatively equitable allocation of land in the wake of the early reforms to de-collectivize agriculture, China´s agrarian reforms starting in the late 1970s were crucial for kick-starting pro-poor growth. Important too was reduced taxation of farmers and macroeconomic stability.

More generally, the task of making growth more poverty-reducing entails some combination of higher growth and a more pro-poor distribution of the gains from growth. Both factors are influenced by initial conditions, institutions and policies in specific country settings. While there may well be trade-offs between what is good for growth and good for distribution, it should not be presumed that this will always be the case; some of the factors that impede growth may also prevent the poor from fully sharing in the opportunities unleashed by growth.

None of this says that inequality is unimportant. Initial inequalities in a number of dimensions, not just incomes, and how they evolve over time can be crucial to the extent of poverty reduction. They can affect both the extent of growth and how its benefits are shared. Clearly, the pace of poverty reduction would have been even higher in China if not for the steep rise in income inequality. Growth was definitely pro-poor in China, but rising inequality made it less so.

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One Pager number 4
Published: November, 2004
Available at: <http://www.ipc-undp.org/pub/IPCOnePager4.pdf>

Generic or Brand Drugs for HIV-AIDS?

Southern Africa Examples

by Francisco Rossi,
International Poverty Centre

The recent UNAIDS report on HIV-AIDS doesn't leave much space for optimism—almost five million people became newly infected with HIV-AIDS during 2003, the greatest number in any single year since the beginning of the epidemic. The number of people living with HIV-AIDS continues to grow—from 35 million in 2001 to 38 million in 2003. In the same year, almost three million died from AIDS. More than 20 million have died since the first case of AIDS was identified in 1981.[1]

Over the last decade, antiretroviral (ARV) agents have been developed which have shown impressive short to medium term impact on reducing HIV-AIDS related mortality and morbidity. Indeed, ARVs make the difference between life and death. The World Health Organization (WHO) has estimated that, in 2004, 6 million people living with HIV-AIDS in the developing world need antiretroviral therapy, yet only 440,000 are receiving these medications; 150,000 of them in a single country, Brazil.

The low incidence of ARV therapy is due to, among other factors, its high cost. The cost of standardized treatment, known as "first line triple therapy", reaches US $10,000 with brand-name patented drugs for one patient per year of treatment. This is an unreachable cost for countries with average per capita incomes that do not go above US $1,000 per year. However, a humane approach to Intellectual Property Rights (IPR) opens the door to be able to escape from death, for the cost of the ARV treatment using generic drugs reduces the cost of the same treatment to US $ 300. In 2004, 450,000 people are being treated in developing countries. About one third of them in Brazil, thanks to this country's strong posture about IPR in the case of ARVs.

A humane provision on IPRs allowing for a widespread use of generic ARVs can make a difference in the fight against AIDS. The findings of a recent UNDP mission to the 4 countries with the highest prevalence of HIV-AIDS cases, all of which are in Africa, clearly underscores the benefits of antiretroviral treatment (ARVT) based on generic drugs. The "3x5 initiative", led by the WHO and UNAIDS, aims to increase to 3 million, from the current 0.5 million, the number of people under ARVT by the end of 2005. This initiative will mean an increase in the number of people under ARVT from less than 20 thousand to up to 150 thousand in the 4 countries selected.

Country	People on ARVT	Goal 2005 (3x5)	% of GNP with generics	% of GDP with brands
South Africa	5,500	120,000	0.032	1.06
Botswana	18,500	150,000	0.865	28.85
Zambia	12,000	120,000	1.000	33.33
Mozambique	3,800	100,000	0.833	27.78

Sources: GNP: Human Development report 2001. UNDP. People on ARVT and goals 2005 were collected by a UNDP mission to these countries in August 2004. Generic costs were calculated with an average of US $ 300/year and brand US $ 10,000/year.

For these 4 southern Africa countries, the cost of providing ARVT according to the goals of the 3x5 initiative will significantly decrease with generic drugs. Costs do not exceed 1% of GDP for any of the four countries considered by the mission. South Africa will come down to one thirtieth of the cost with brand-name drugs. For the other 3 countries, reductions are so dramatic that they mean converting the 3x5 initiative from bluntly unaffordable to clearly feasible. The cost comes down from more than 25% of the GDP to less than 1% of GDP.

Intellectual property rights (IPR) have played a crucial role on prices of brand-name ARV, specially after the 1994 Marrakesh Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). This agreement established an international minimum frame on IPR, which allows innovator industries to set high prices internationally. TRIPS agreement includes legal mechanisms to properly balance the needs of the society and the patent owner, such as compulsory licenses, governmental use and parallel imports. These allow states to break patent exclusivity by granting permission for public or private enterprises to produce generic versions of brand-name drugs in case of national emergency, national security, epidemics and other emergencies of public health, as well as in cases of anticompetitive practices. The figures showed here suggest that TRIPS legal mechanisms are a matter of survival for these countries. Not only for the people living with HIV-AIDS, but also for the national economy. For this reason, it is of the outmost importance that bilateral and regional free trade agreements do not undermine TRIPS provisions by adopting more stringent IPR rules.

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One Pager number 5
Published: November, 2004
Available at: <http://www.ipc-undp.org/pub/IPCOnePager5.pdf>

Pro-poor Growth: Finding the Holy Grail

by Alejandro Grinspun, International Poverty Centre

A lively debate followed the release of two IPC One Pagers that contrasted Ravallion's and Kakwani's definitions of 'pro-poor growth'. According to Ravallion (World Bank), 'pro-poor growth' is any growth in mean income that benefits poor people—a definition Kakwani (IPC) finds wanting as it would encompass the vast majority of growth episodes so long as poverty decreases, which it typically does. He proposes instead that growth is pro-poor if it benefits the poor proportionally more than the non-poor. In the exchange that followed, it became clear that what is considered 'pro-poor' depends, in part, on the choice of standards for gauging the distributional impact of a growth episode.

Ravallion's definition does not seem to pass a reasonable test of 'pro-poorness'. In the words of Howard White (Sussex), a growth episode that gives every rich person $1 million and just 1 cent to a single poor person cannot possibly be deemed pro-poor —especially considering that, in most instances of rapid growth with rising inequality, the prices of basic needs items consumed by the poor tend to grow faster than the prices faced by the average person, as Dave Gordon (Bristol) noted. Alberto Minujin (Unicef) dismissed Ravallion's statement about the poverty-reducing impact of growth as merely an empirical observation, not a definition. Pro-poor growth does not just happen; it is the result of explicit policies—and this is as true for income poverty as for other dimensions of well-being. Citing a recent Unicef study, Minujin shows that disparities in child well-being—specifically in the reduction of U5MR—between rich and poor worsened during the 1990s in countries that failed to follow pro-poor policies. If they had, the consequences for child well-being could have been dramatic: the number of 'lives saved' would have doubled if every household had enjoyed the same U5MR reduction as those in the top quintile.

Michael Lipton (Sussex) prefers to call 'strongly pro-poor' that growth process in which incomes rise proportionally faster for the poor than the non-poor. But unlike Kakwani, he reserves the term 'weakly pro-poor' for those instances in which growth benefits the poor considerably, albeit less than the non-poor. Much of the disagreement concerning pro-poor growth would dissipate if one could establish empirically the tradeoffs between changes in absolute poverty and in inequality between rich and poor. For Lipton, it is not enough to say that 'inequality matters'. Distribution between the richest and second-richest deciles may not be relevant to whether growth is pro-poor; distribution between the poor and the non-poor is, and so is distribution around the poverty line.

Like Lipton, Siddiqur Osmani (Ulster) agrees with both Kakwani and Ravallion, though only up to a point. Simply reducing poverty cannot be a sufficient condition for growth to be pro-poor. There *has* to be a bias in favor of the poor. But Osmani questions some of the implications of Kakwani's 'pro-poor' criterion. A country with high growth may reduce poverty more than one with sluggish growth, even if the poor reap proportionally fewer benefits than the non-poor in the former and more in the latter. Yet by Kakwani's definition, the country with the better record of poverty reduction would have a less pro-poor performance than the country with the weaker record. So while agreeing that the true test of 'pro-poorness' is the existence of a policy bias in favor of the poor, Osmani proposes that this bias be defined differently – not in relation to how well the non-poor do, but in relation to a country's past record of poverty reduction. He then defines 'pro-poor growth' as a growth process that reduces poverty *more* as compared to the 'benchmark' scenario. This will clearly vary across countries and over time so that what is pro-poor growth in one case may not be so in another.

Frances Stewart (Oxford) endorses Osmani's approach, but not his specific choice of benchmark. Osmani's criterion might, for instance, disqualify an egalitarian country with a good track record of poverty reduction if, in the future, it underperformed but still did reasonably well as compared to other countries. Stewart thus suggests an alternative approach that identifies, for each country, the growth rate that would halve poverty by 2015. In turn, Howard White proposes three different criteria of 'pro-poorness'. The first calls for the share of the poor in income growth to exceed their existing share. About half of all growth episodes qualify as pro-poor by this definition, which White considers weak as it may coexist with a growing absolute gap between rich and poor. A second criterion, which very few past growth episodes meet, requires that the poor´s share in incremental growth surpass their share in population; in other words, the absolute gap between rich and poor should not widen during growth. The third and final accords with Stewart's in that the share of the poor in incremental growth exceeds some international norm. By this definition, about half of growth episodes are pro-poor, though not the same half as by the first criterion.

Finally, Quentin Wodon (World Bank) calls for more robust tests of pro-poor distributional changes. Simple average relationships between growth and summary poverty measures, such as headcount changes, are inadequate because they depend on the effect of growth on those closest to the poverty line, making judgements highly sensitive to the choice of poverty lines. Besides, growth may reduce the proportion of a country's poor, but with adverse impacts on the very poor. Thus, a key issue when assessing 'pro-poorness' is whether to give more weight to the poorer of the poor. Another issue is whether to use a relative or absolute standard for measuring distributional changes.

So after all is said and done, when can growth be deemed pro-poor? Well, the jury is out. Stay tuned for more.

One Pager number 6
Published: December, 2004
Available at: <http://www.ipc-undp.org/pub/IPCOnePager6.pdf>

Slipping into Poverty: A Neglected Issue in Anti-poverty Strategies

by M. H. Suryanarayana,
International Poverty Centre

The question of targeting welfare programmes has received considerable attention in developing countries, particularly in the context of economic reforms. But what is little appreciated is that poverty reduction is not simply a matter of reducing the deprivation of the current poor. To sustain the process, it is also important to ensure that the vulnerable non-poor do not slip into poverty.

Take the case of India. Its ongoing adjustment programme puts great emphasis on enhancing the cost-effectiveness of different policy instruments, as has been the case with the reform programmes in several other poor developing countries, such as Jamaica, Sri Lanka and Zambia. The main reason for such emphasis is the avowed need to achieve macroeconomic stability by eliminating the deficit in the government budget. As elsewhere, it is welfare programmes intended to fight poverty that have become the soft targets for budget cuts. Government expenditures are said to be in excess of revenues due to, among other things, what are called *targeting errors*. These errors occur while implementing any welfare programme either because of its failure to reach the target population—for instance, the poor—or due to excessive coverage and the consequent leakage of benefits to the non-poor. Apart from the inevitable administrative and working expenses incurred on any programme, it is the 'errors of inclusion' arising from excessive coverage of benefits that are said to involve explicit unwarranted costs in the government budget.

The workings of a democracy in a multiethnic society like India are such as to impose the need for coalitional politics; in order to compete for the popular vote, political parties must build broad coalitions that can articulate the interests of large swaths of the population. In pursuit of such coalitions, Indian political parties have avowed to carry out economic reform programmes without any adverse impact on the poor, who constitute a majority of the country's voters. To avoid alienating this large bloc of voters, successive Indian governments have therefore placed great emphasis on reducing the fiscal deficit primarily by minimizing leakage of benefits to the non-poor.

Such a strategy overlooks the need for an exhaustive safety net not only for the poor, but also the vulnerable. Consider, for instance, the experience of revamping the Indian public distribution system, which sells food grains at subsidized prices to the population. Its emphasis, until the mid-1990s, was on universal coverage. Since then, however, it has been reformed so as to eliminate the non-poor from the beneficiary net, yet with little attention being paid to covering all of the needy poor.

And what about the vulnerable non-poor, who risk sliding into poverty for a variety of reasons, including lack of credit or illness? Available micro evidence from India, Kenya, Peru and Uganda suggests the need for exploring policy options for extending a measure of social protection to the vulnerable non-poor as well.

To illustrate this point, let us look at micro data from the Indian state of Andhra Pradesh. About 65% of the households in 36 villages in the districts of Nalgonda, Khammam and East Godavari in Andhra Pradesh were poor 25 years ago. Thanks to an array of government programmes, 14% of households managed to move out of poverty. One would expect a concomitant reduction in aggregate poverty in these villages. Surprisingly, though, poverty continues to be about the same after a quarter-century of development efforts. The reason is that, over the same period, about 12% of non-poor households have moved *into* poverty due to financial and health crises. These households needed suitable policy support, for instance in terms of timely access to credit and medical facilities (Krishna et al., 2004a). Similar findings are reported from 20 villages in western Kenya. During the past 25 years, 19% of households in these villages managed to cross the poverty line. But this progress does not get reflected in the aggregate poverty ratios for these villages because a similar proportion of households fell into poverty for reasons like ill health, medical care and expenses on funeral rites (Krishna et al., 2004b).

What these examples show is that sustained poverty reduction cannot be achieved simply by a set of safety net interventions *only* for the current poor. It is equally important to put in place appropriate policies for the vulnerable non-poor in order to prevent their descent into poverty. This calls into question the wisdom of narrow targeting of programmes. A suitable, multi-pronged strategy for poverty reduction requires an appreciation of the asymmetric causes for mobility into and out of poverty—and appropriate strategies to prevent the former and promote the latter.

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One Pager number 7
Published: December, 2004
Available at: <http://www.ipc-undp.org/pub/IPCOnePager7.pdf>

Measuring Poverty: What's in the Line?

by Alejandro Grinspun, International Poverty Centre

Despite a long pedigree that dates back to late Victorian England, the notion of a 'poverty line'—a welfare threshold expressed in monetary terms—is not without its problems. Critics contend that the idea of a *discrete* cut-off point separating the poor from the non-poor is conceptually flawed as poverty and well-being can best be seen as a *continuum*. There is, in fact, considerable movement into and out of poverty that studies relying on a fixed poverty line fail to capture.

By focusing on the private means to satisfy human needs, income or consumption reflects well-being only indirectly. But this is just one way of assessing poverty. It matters, for instance, whether an individual also has access to welfare-enhancing public goods and services. This is why monetary measures are often combined with more 'direct' indicators of welfare such as life expectancy, nutritional and health status, education, and housing conditions. Combining monetary and social indicators not only better captures the multiple dimensions of deprivation, but may also shed light on its chronic or transient nature.

In practice, though, money-metric measures are the most widely used proxy for poverty. The question then becomes, what welfare level determines the cut-off point between poor and non-poor?

The answer is not so simple, as poverty measures can be highly sensitive to the methodological choices and assumptions made in constructing a poverty line. The differences can be far from trivial. Székely et al. (2000) have shown that, depending on the choice of equivalence scales, assumptions about economies of scale in consumption, and methods of treating zero and missing incomes or adjusting for income misreporting, the Latin American headcount ratio ranged from 12.7% to 65.8%, and the poverty gap from 4.5% to 37.9%, in the late 1990s!

Poverty measures are often rough estimates, at best. Take income. Apart from its inability to fully capture a person's command over commodities—due, for instance, to regional variations in prices, costs of living or the availability of essential goods—incomes from surveys are known to be grossly under-reported. Yet the extent of under-reporting cannot be gauged properly, partly because of limitations in the national accounts which do not contain reliable data on informal and home-based activities, a crucial source of earnings for the poor. Adjusting for misreporting can sometimes introduce new biases, instead of correcting them.

Even determining the food component of a poverty line is far from straightforward. Should one examine the actual consumption patterns of the poor or rather select a food basket that will yield the required calories at the lowest cost? Typically, nutritional requirements are reported as national averages, even though needs vary by sex, age and activity levels. And while equivalence scales may be used to account for differences in household structure, there is little guidance for choosing between alternative scales despite their varying impact on poverty figures.

Calculating the non-food share is more problematic still. Despite a consensus that non-food essentials should be part of a poverty consumption bundle, it is not obvious what those items should be. Thus, a modest allowance for non-food expenditure is often made by scaling up the food poverty line by some multiple, which typically reflects what poor households spend on non-food items rather than what they *ought* to spend in order to avoid deprivation. This method of estimating the non-food share tends to understate the scale of poverty, particularly among children when combined with the use of calorie-based equivalence scales; children may require fewer calories than male adults, but have many other needs that must be paid for.

Poverty comparisons can also be biased by subtle differences in survey definitions—such as the inclusion of different income sources or consumption aggregates—or the choice of deflators to correct for temporal price changes. Instead of re-pricing the same food basket and re-calculating the non-food share in each period, adjustments for price changes are often made by multiplying the total poverty line by a general consumer price index. The problem is that cost-of-living indices do not capture well the consumption patterns, and hence the prices, that matter to the poor. Similar issues arise when using purchasing power parity factors to correct for varying costs of living across countries.

Ultimately, one must recognize that poverty lines—however defined—will always represent an arbitrary cut-off point that, alone, may not offer the best guide for policy making. More important than searching for the 'single best' poverty line is to explore the sensitivity of poverty estimates to the choices and assumptions behind the statistics, as well as the use of alternative lines and measures. What matters, after all, is to find robust measures that allow users to assess time trends in poverty, analyze its determinants and profile, and establish poverty rankings without having to accept the normative judgments that inevitably underlie any single measure.

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One Pager number 8
Published: December, 2004
Available at: <http://www.ipc-undp.org/pub/IPCOnePager8.pdf>

Defining Pro-poor Growth

by Siddiq Osmani,
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Martin Ravallion and Nanak Kakwani have reopened a debate in which they have been engaged for some time. I find myself in agreement with both—not with their definitions of pro-poor growth, but with their criticisms of each other. That is to say, I find both their definitions problematic.

Ravallion's definition is identical with the concept of poverty-reducing growth—any growth that reduces poverty is said to be pro-poor. In my view, simply reducing poverty cannot, in general, be a sufficient condition for 'pro-poorness'. There has to be something more; in particular, the growth process must exhibit a bias in favor of the poor.

In that sense, Kakwani's definition is a move in the right direction. He calls a growth process pro-poor only when the poor benefit proportionately more than the rich. But he takes the bias to an extreme, leading to potentially counterintuitive implications. Compare two scenarios. In situation A, the growth rate is low but the poor benefit proportionately more than the rich. By contrast, the growth rate in situation B is much higher, but the poor benefit proportionately less. Assume further that, because of higher growth, poverty is reduced more in scenario B than A. By Kakwani's definition, we shall characterize A as a case of pro-poor growth but not B, even though the poor have actually done better in the latter! Something surely must be wrong with our definitions if a growth process that reduces poverty more cannot be described as pro-poor, but one that reduces poverty less can.

Clearly, some rethinking is required. We first need to clarify the object to which the quality of pro-poorness is to be attributed, bearing in mind the distinction between the *rate* and the *nature* of growth—the latter usually denoting its distributional impact. Is pro-poorness meant to gauge the nature of growth, or the totality of the growth process? If it merely refers to the nature of growth, then it will no longer matter if 'pro-poor' growth happens to reduce poverty less than growth that is not deemed 'pro-poor', and Kakwani's definition would be the natural one to adopt.

But if the nature of growth is what we are after, why bother to coin a new term? We already have the concept of 'equitable growth', which requires growth to be such as to benefit the poor proportionately more than the rich. Kakwani's definition does not add anything new to this notion.

I believe our interest in pro-poor growth goes beyond a concern with the distributional impact of growth. It stems from a general dissatisfaction with our past experience with growth that has made a small impact on poverty in the developing world. We are not simply dissatisfied with how the poor have fared relative to the rich, but also with the scale of poverty reduction in absolute terms. While distributional questions underlie the search for equitable growth, it is the absolute impact on poverty that drives our present concern with growth. As such, the quality of pro-poorness is to be attributed not just to the nature of growth but to the totality of the growth process, including its rate.

Ravallion's definition refers to the totality of the growth process, whereas Kakwani's stresses the existence of a bias in favor of the poor. We clearly need to combine the strengths of both. The concept of pro-poor growth must refer to the absolute magnitude of poverty reduction, yet contain an element of bias in favor of the poor. The critical question is how this bias is defined. I believe we must first identify a benchmark that will allow us to gauge the 'pro-poorness' of growth.

Where shall we get the benchmark from? Since our concern with pro-poor growth derives from our dissatisfaction with past growth experiences, these can be taken as the benchmark. This means pro-poor growth demands a break with the past that makes growth more conducive to poverty reduction. There has to be a bias in favor of the poor relative to the benchmark experience; from the point of view of the poor, there must be an improvement over business as usual.

'Pro-poor growth' can thus be defined as a growth process that reduces poverty more than it does in the benchmark. In general, pro-poor growth must involve more than just poverty-reducing growth. Only in the case where the benchmark involves no reduction of poverty would Ravallion's definition fit the bill, as a special case.

Of course, the benchmark will vary across countries and over time; what is pro-poor growth in one case may not be so in another. While there might be practical difficulties in identifying the benchmark precisely, it should not be too difficult to identify a period in any country's experience during which growth was not deemed favorable to the poor.

In any case, identifying a benchmark will only be necessary if we wish to answer whether a particular growth process is pro-poor or not in some absolute sense. In practice, a more common concern will be a comparative one—whether a particular set of policies is likely to be more pro-poor than another. In this comparative context, all we shall need is to compare the poverty-reducing effect of alternative sets of policies. Such a comparative exercise could command agreement, even if people disagree on the precise identification of the benchmark.

One Pager number 9
Published: January, 2005
Available at: <http://www.ipc-undp.org/pub/IPCOnePager9.pdf>

Birth Control and Poverty in South America

by Marcelo Medeiros,
International Poverty Centre

The idea that inducing birth control is an important strategy for poverty reduction is still popular in groups with reasonable political power. For instance, concerns about increases in fertility became part of the debate about the results of cash transfer programs that deliver benefits proportionally to the number of children in the household, like *Bolsa Escola* in Brazil and *Progresa* in Mexico. Moreover, a study of the entrepreneurial elites in Brazil has shown that about one fourth of the people interviewed believe that birth control should be the main initiative to fight poverty in the country (Reis & Cheibub, 1995). The rationale behind this is very intuitive: many children in a family means more mouths to be fed by few hands, as children are usually economically dependent on their parents. Thus, the fewer children in poor families, the better for poverty reduction in the country.

When one considers that a couple with ten kids has much higher chances of being in poverty than a couple with no children, the argument for active birth control policies seems to be perfect. Moreover, transferring to the poor—especially poor women—the responsibility of avoiding the reproduction of poverty through the generations may sound comfortable to some.

However, evidence suggests this argument is wrong for the majority of South American countries. Although higher fertility may lead some families into poverty, the poor families have an average size similar to the non-poor. In most of the countries in the region, fertility rates are not high, around 2.4 children per woman. These are average rates, but as the low income portion of the population is clearly in the majority in these countries, the average is representative of the poor. Such rates show that, generally speaking, poor women already use some kind of birth control. Of course there are exceptions, but they are not very common.

The table shows what would be the effect on the incidence of poverty of simulated restrictions in the number of children in Brazilian households. In the columns are the maximum number of children a household would be allowed to have in the simulation. Without any restrictions, the observed incidence of poverty in the Brazilian population is 33% for the poverty line used.

The simulation shows that even if no woman in Brazil had a single child in the last 15 years, the proportion of poor in the population would still not fall bellow 30% (Medeiros, 2003). This is a clear sign that, in a realistic perspective, an increase in birth control would result in few changes in the present incidence of poverty and would have high social costs. In the present, policies to achieve sharp reductions in fertility may have to be very intrusive in family decisions; they can also become a trap for the future. A reduction of 20% in South American fertility levels is enough to make them go below reposition levels. If this happens, in the next generations, we will have an inverted population pyramid, with high demographic dependency, and, therefore, we may be transferring the poverty from today's children to tomorrow's elderly. Poverty eradication policies will not gain from focusing on reductions in family size. The problem, as stated in many studies, is of increasing family income.

Incidence of Poverty After Simulated Restrictions in the Number of Children Born – Brazil – 1999

Years ago implemented	No children %	1 child %	2 children %	3 children %	4 children %
15 years	27	34	36	35	34
10 years	30	35	35	34	34
5 years	32	34	34	34	33

Source: Medeiros (2003), using a poverty line of R$ 80.97 (around US$ 43), values from September 1999.

The small impact that reductions in the current fertility rates would have on poverty does not lead to the conclusion that access to contraceptive methods is unecessary for poor women. There is no doubt that the freedom to decide the size of one's family is an important reproductive right. Guaranteeing this access is both a matter of ensuring women's reproductive rights and of keeping fertility rates low. Poor women want to control their reproduction and need the State to provide the means to do that. What they do not need is birth control policies that force them to do so.

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One Pager number 10
Published: January, 2005
Available at: <http://www.ipc-undp.org/pub/IPCOnePager10.pdf>

The Challenge of Pro-poor Growth in Uganda

by Barbara Barungi, UNDP Regional Service Centre, Johannesburg and Eduardo Zepeda, International Poverty Centre, Brasilia

Uganda's economic recovery an African model, provides an insightful illustration of two growth periods: in the 1990s when strong growth was accompanied by poverty reduction, and more recently, when growth occurred at the same time as poverty increased. These divergent patterns in poverty performance can be explained in terms of both structural and policy factors, but on the whole, they underscore the need to have strong and sustainable pro-poor policies and institutions.

A recent paper by Kappel et al (2004) provides a wealth of information and insights. The proportion of people living below the national poverty line had declined from 56% in 1992/93 to 34% in 1999/00; between 1999/00 and 2002/03, poverty increased to reach 38%. The growth performance of the economy during the second period was clearly inferior to the first one. Using changes in GDP per capita as the measure of growth, for example, the annual rate of growth declined from an average of 4.3% between 1993 and 2000 to 2.9% between 2000 and 2002. Assuming everything else remained the same, this lower rate of growth should have been responsible for the slow down in the pace of poverty reduction in Uganda, but it can hardly account for the reversal in poverty trends—something must have changed drastically. For one thing, while inequality in Uganda, measured by the Gini coefficient, increased throughout the whole period, that is, from 0.364 in 1992/93 to 0.395 in 1999/00 and to 0.428 in 2002/03, it did so at a much faster rate during the last years; in fact, the speed of increase almost doubled, from an average annual change of 1.2% in the first years to 4.1% in the last three years.

Fast growth and poverty reduction during the 1990s were due to the immediate benefits of recovery from civil war and from overcoming the economic mismanagement that prevailed during much of the 1980s. It was also the result of economic reforms that, among other things, introduced market regulation in the cash-crop sector of agriculture, liberalizing, for example, the coffee market. In a country where 85% of the population lives in rural areas, the role of agricultural production is key to understanding the performance of the economy. According to Kappel et al, the two main factors explaining the rapid reduction of poverty and the strong growth of the 1990s were increases in the production of cash crops and high international prices for Uganda's export products, mainly coffee, cotton, tobacco and tea. The economic reforms of the 1990s implied greater reliance on market conditions. When market conditions are favourable, as in the 1990s, particularly in the second half of the decade, the economy fares well, but when markets do not perform well, the economy suffers, especially the poor. By November 2001, the price of *robusta* coffee had decreased by almost 90% relative to its peak in 1994. According to figures from the Economic Commission for Africa (2003), total revenue from coffee exports decreased from 270 to only 85 million dollars between 1997/98 and 2001/02. On top of this, the prices of cotton, tobacco and tea also decreased. The economic environment had changed drastically, the pace of the economy slowed down and poverty increased.

Rapid growth and the substantial reduction in poverty of the 1990s are a welcome outcome for Uganda, especially for Uganda's poor. According to a minimalist definition, the performance of the Ugandan economy was clearly pro-poor during the 1990s and not pro-poor after 2000 because there was poverty reduction in the first years but not in the second. However, a more demanding definition of pro-poor would tell us that the 1990s were not pro-poor and that the years after 2000 are a case of *immiserising* growth. But whether the 1990s should be considered as pro-poor or not pro-poor is a question that can lead to different policy conclusions. Accepting that the performance of the 1990s qualifies as pro-poor would, most likely, lead to a continuation of the same policy framework. In this scenario, one risk is to be unpleasantly surprised, as happened with the poverty reversion of the 2000s. If, instead, the informed dominant view holds that the 1990s were not benefiting the poor sufficiently, as a stricter definition of pro-poor suggests; then, policy makers and stakeholders are forced to look more carefully into ongoing policies. The poverty outcomes of the years between 2000 and 2003 will only reinforce such a stance.

While closely considering alternative policies, it is worth keeping in mind at least two points. First, one should look carefully into building appropriate safety nets to protect the poor in Uganda from market shocks, as well as making sure that current investments in the assets of the poor have a large and sustained impact on their capacity to generate income as cash crop growers, as subsistence agriculture peasants, or as workers in urban settings. Second, when designing and implementing economic reforms, countries must ensure they are strongly pro-poor from the start. The early adoption of a pro-poor path, strictly defined, facilitates further and faster reductions in the incidence of poverty, and thereby, many argue, stronger growth.

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One Pager number 11
Published: February, 2005
Available at: <http://www.ipc-undp.org/pub/IPCOnePager11.pdf>

Ending World Poverty: Is The Debate Settled?

by Jan Vandemoortele, Poverty Group, UNDP

Poverty reduction strategies look strikingly similar, even for countries that face very different challenges. This could suggest that the debate on poverty has been settled—that achieving the Millennium Development Goals is merely a matter of applying 'good' policies at the country level (Vandemoortele, 2004).

In essence, the emphasis on 'good' policies asserts that social and economic rights are best realised within the context of rapid growth. But not everybody shares this faith in the power of economic growth or sees poverty reduction as an automatic by-product of macro-economic stability.

Recent data on China, for instance, show that growth and poverty reduction do not always go hand in hand. Although its economy expanded very rapidly, the number of China's poor remained unchanged between 1996 and 2001. It is a moot question why such a stunning record of growth for five consecutive years failed to make any difference for the estimated 212 million people who struggled to survive on less than $1 per day.

The centennial anniversary of flight offers a relevant analogy. The main protagonists in the race to invent the first flying machine were Samuel Langley and the Wright Brothers. Langley's strategy was to focus on power to get his theoretically stable machine aloft. The Wright Brothers focused on design to become airborne. Similarly, there are two paradigms for Human Development: one that believes in the overwhelming power of economic growth, another that emphasises the design of pro-poor policies.

Evidence shows that global progress towards the Millennium Development Goals has not been pro-poor. The one-sentence summary of the global database is that progress since 1990 should have been twice as fast for the world to be on-track to achieving the 2015 targets. Progress was particularly disheartening for basic education.

In addition, much of the progress has bypassed the very people most in need of it. Indeed, evidence indicates that the poorest people benefited little from the progress in health, education and nutrition. No matter how it is measured, it is increasingly difficult to deny that disparities are widening in most countries.

Yet, the prevailing economic model pays little attention to inequalities, maintaining that everybody benefits from growth. But to argue that 'growth is good for the poor' is beside the point. The question is not whether poor people would be better off without growth; it is whether growth produces the most dramatic and lasting reduction in human poverty.

History shows that it does not. A key lesson from the pursuit of gender equality is that one should not assume that what works for men will automatically benefit women. That lesson applies equally to the assumption that the poor will benefit in a fair way from aggregate growth.

The poverty debate has *not* been settled. Distinctions among policy options and choices have *not* become extinct; particularly in the areas of job creation, taxation, public investment, trade reforms and financial sector liberalisation.

Most economists are reluctant to admit it, but the profession has only a partial understanding of what causes rapid economic growth, let alone what makes it pro-poor. Our knowledge about important aspects of growth and distribution equals, at best, our ignorance.

Conventional wisdom often recommends sweeping one-size-fits-all solutions that invade the national policy space and inhibit tailor-made approaches. But workable solutions are always home-grown and context-sensitive. Additionally, such solutions depend on a new partnership between developing and developed countries and between poor and rich people.

Currently, the dimension of 'money changing hands' dominates that partnership—centred on foreign aid and domestic transfers. It is time to shift the focus from 'money changing hands' to 'ideas changing minds'. This shift will require a quantum leap in imagination.

As long as developed countries and better-off people are unable or unwilling to change their theories, perceptions and convictions, the Millennium Development Goals will remain elusive. A missing ingredient on the part of the better-off partners is their ability and readiness to listen.

Repeating standard recipes and lamenting about poor implementation will only extend the legacy of broken promises.

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One Pager number 12
Published: March, 2005
Available at: <http://www.ipc-undp.org/pub/IPCOnePager12.pdf>

Chinese Boxes: Whatever Happened to Poverty ?

by Alejandro Grinspun, International Poverty Centre

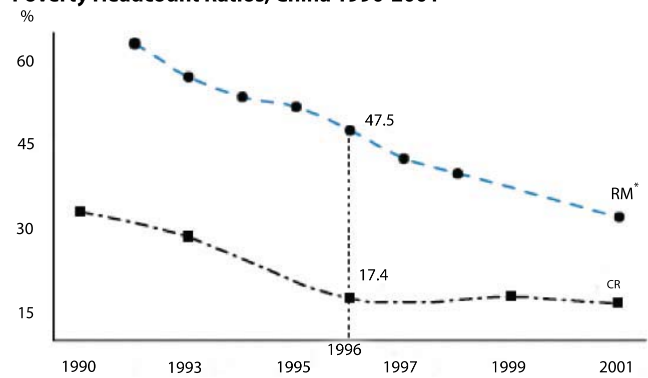
The debate over he scale and trend of poverty in China has been raging for some time. Some authors claim its record of poverty reduction has been even greater than official statistics show. Others maintain the official data grossly understate rural poverty but overstate the rate of poverty reduction since the late 1970s. Still others stress that lack of data on urban poverty, which has been rising since the mid-1990s, badly distorts the country's overall poverty picture. Considering that nearly one in four of the world's people lives in China, this controversy is of great consequence when assessing global poverty—including whether the world is on track for meeting the first millennium development goal by 2015.

A new paper by Reddy and Minoiu (RM) gauges the extent to which China's most recent $1/day poverty estimates are sensitive to the choice of key underlying parameters. RM construct alternative purchasing power parity (PPP) conversion factors, with their associated poverty lines, at 1993 prices. They draw on both national accounts (NA) and household surveys to translate income shares into a consumption profile for China, and express the mean consumption levels in 1993 constant prices using both the official and an *adjusted* consumer price index (CPI). The former assumes that the food and non-food shares in total expenditure are the same across the income spectrum, whereas the latter reflects more closely the prices faced by individuals at or near the poverty line.

During the 1990s, developing-country consumption figures from surveys typically grew slower than those derived from NA, while the opposite was true for income. The discrepancy between these two sources can produce large distortions in the shares accruing to different quantiles, and thus affect poverty rates. Even though expenditure is normally judged a better measure of *permanent income* than is current income, reliable consumption surveys unfortunately are not available for China. So RM had to construct a consumption profile from the country's income series. Departing from standard practice, they assess the consumption shares for *each* income decile, instead of assuming a constant share across the distribution.

Opinions differ as to the appropriate PPPs for China, which has never taken part in an official benchmark survey of the International Comparison Program. Clearly, the choice of method for converting international prices into a country's local currency will yield very different poverty lines, with potentially large implications for poverty assessments. Drawing from existing GDP estimates and using alternative consumption PPPs at the base year, RM obtain a set of poverty lines that vary enough to permit an analysis of the robustness of Chinese headcount ratios from 1990 to 2001. After obtaining the poverty lines in 1993 local prices, they proceed to test alternative deflators to account for inflation. Since the official CPI does not capture the varying consumption patterns of different income fractiles, RM use survey data to obtain the food and non-food shares in total expenditure for each separate decile. This method allows them to better reflect the living costs faced by those at the bottom of the distribution.

Poverty Headcount Ratios, China 1990-2001



RM*: Headcount ratios based on the use of decile-specific consumption shares and survey data to scale incomes.
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Regardless of the assumptions made, RM find that, on the whole, China did enjoy a remarkable reduction in consumption poverty -during the 1990s, ranging from 36% to more than 50% depending on the income estimates used. But while the trend of poverty reduction is robust to the choice of poverty line, the extent of poverty is not. The headcount ratios reported by RM differ markedly from those of other authors, and are from two to almost three times as high as those by Chen and Ravallion (CR). The two series also reveal a striking contrast with regard to recent poverty trends. While RM show a continuous drop in poverty during the 1990s, CR estimates flatten after 1996 despite per capita GDP growth rates at around 7% per annum through 2001.

China's stunning record of poverty reduction is heartening, but must be interpreted with caution. Poverty measures are greatly influenced by the assumptions made, which may not only affect their magnitude but even the report trends. This, of course, still begs the question whether China's success has been matched by progress in other dimensions of well-being. In light of some credible evidence of rising urban poverty, deteriorating rural health care, and worsening nutrition among low-income groups during the 1990s, this is a question well worth exploring further.

One Pager number 13
Published: April, 2005
Available at: <http://www.ipc-undp.org/pub/IPCOnePager13.pdf>

Vietnam: **Jobs, Growth & Poverty**

by Hyun H. Son,
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Vietnam has experienced high growth and substantial poverty reduction for more than a decade. From 1990 to 2003 GDP grew at an annual rate of 7.5 %, while the share of the population surviving under the poverty line declined from 58.2 % in 1992/93 to 37.4 % in 1997/98, and to 28.6 % in 2002 (Kakwani and Son 2005). Given that Vietnam is a capital- and land-scarce country, like many others in the developing world, employment generation must have been the mechanism through which growth translated into poverty reduction.A quick look at employment and growth casts doubts on this presumption, however.

One basic indicator linking growth and employment compares the per cent change in employment with the per cent change in GDP: the employment elasticity of growth. The higher the elasticity, the more employment is being created by the given growth rate in GDP. Looking at Vietnam's data we observe that elasticities are low, but less so in more recent years (1998-2001). It is only after breaking down data by sectors that one can see higher estimates, such as in services (1.78) and industry (0.89) for 1998/01. These suggest an employment-based reduction in poverty but, can job creation in only some sectors support a nationwide sustainable reduction in poverty?

One should always be cautious when interpreting employment elasticities. Comparing changes in employment and production tells us how many more, or fewer, people are employed for a given change in output, but does not explicitly say anything about the intensity of work. For example, GDP might be growing rapidly based on a more appropriate and intensive use of employment, but with a slow increase in total employment. Keeping the intensity of work constant, rapid GDP growth with no additions to employment might originate in marked increases in productivity.

Employment Elasticity of Growth, Vietnam 1992-2001

	Total	Agriculture	Industry	Services
1992-1997	0.26	0.37	0.22	0.52
1998-2001	0.37	-0.13	0.89	1.78

In the Vietnamese case, rather than a weak or partial job-enhancing process, the observed patterns in employment elasticity might be reflecting positive changes in the intensity and productivity of labour; which might be, in turn, associated with economic reforms. Initiated in the mid-980s, the Doi Moi economic reforms intensified in 1989 with measures aiming at promoting competition. Growth rates rose to over 8 % early in the 1990s, but increases in employment lagged behind at a rate of 2.3 % per year. One can presume that the intensity of employment was on the rise and that "true" labour productivity was also improving. Observed labour productivity in industry grew, for example, at a rate of 13.3 % per year. Strong growth, higher productivity and small increases in inequality supported poverty reduction. Thus, even if employment elasticity was low, particularly compared with the 0.7 to 0.8 of neighbouring countries such as Korea, Taiwan and Indonesia (Osmani 2005), Vietnam's growth can be judged as broad-based.

Performance between 1998 and 2001 is affected by the Asian crisis; but also by further reforms, such as the 1999 Enterprise Law. The higher employment elasticity observed in these years owes much to both a slower growth rate and much faster employment creation. Led by the private sector, employment in services and industry grew by more than 8% per year. Strong job growth in this period might also be explained by the exhaustion of the absorption of excessive labour of previous years.

As employment in urban settings boomed, employment in agriculture decreased, releasing possibly redundant labour. The key to poverty reduction in Vietnam hinges upon agriculture. Up to 60 % of the reduction in poverty can be attributed to higher incomes within agriculture. Granted, the productivity increase in agriculture was only 2.6 % per year, but this was spread across 70% of the total workforce. To be sure, land reform also played a crucial role in poverty reduction: the ensuing egalitarian distribution of land allowed for the sharing of benefits from improvements in agricultural productivity.

The empirical evidence and theory suggest that sustained reductions in poverty are often accompanied by strong employment creation processes. However, this is not easy to observe in practice. The basic indicator of the link between growth and jobs, the employment elasticity of growth, always requires careful interpretation. The case of Vietnam illustrates well these caveats. While showing a persistently low elasticity of employment on the whole, the significant reduction in poverty that was achieved can be attributed to strong growth, an egalitarian distribution of assets and benefits, and to an employment-enhancing process. This included a higher intensity of employment, enhanced productivity of labour and more jobs.

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One Pager number 14
Published: May, 2005
Available at: <http://www.ipc-undp.org/pub/IPCOnePager14.pdf>

Leaky Bucket

by Nanak Kakwani and Hyun H. Son, International Poverty Centre

Consider a situation when we need to transport water from one place to another place in a leaky bucket. Some of the water would always leak out. If all water leaked out, it is obvious that we would stop our efforts to carry water. Our decision to carry the water or not will depend on how leaky the bucket is and on how big is our need for water at the destination. For instance, if bringing a little water to the other end can save a life we will be perhaps willing to accept that, say, 99 % of the water leaks out. This is an extreme situation. Societies, however, tacitly judge how much leakage they are prepared to tolerate while making a transfer to the needy.

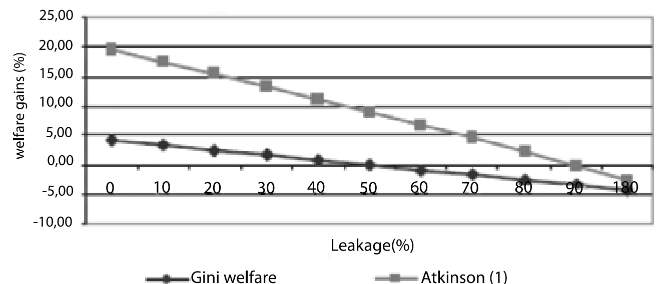
Imagine a hypothetical society consisting of two people: one poor and one rich with incomes $50 and $500. To have a grasp of welfare in this society we might think of a function where total welfare increases whenever the incomes of these two persons grow and whenever the increase in income of one individual does not decrease the income of the other. This is the famous *Pareto* optimality criterion. We may introduce a second property to this function to state that any transfer of income from the rich to the poor also increases social welfare. This is called the Pigou-Dalton principle of transfer. The basic idea behind this principle is that the gain of $1 by the poor is more valuable than the loss of $1 to the rich. Taken together, these criteria imply that any redistribution of income from rich to poor will increase social welfare provided that total income available to society does not decrease.

In accordance with the above principle, any redistributive policy that reduces inequality without reducing the average income of the society in question should be considered as good. If the redistribution of income from rich to poor is welfare enhancing, why do governments not always redistribute incomes from the rich to the poor, and reduce both inequality and poverty? There are, of course, many reasons of political economy why this is so. But there is also one catch in the welfare function that it is useful to think about explicitly: the money must be carried from the rich to the poor in a leaky bucket (Okun, 1975). There is no costless transfer of money from the rich to the poor: some of the money will always disappear in transit so the poor will not receive all the money that is taken from the rich. The leakage basically represents inefficiency. The issue is how much inefficiency a society is or should be prepared to tolerate? The answer depends on how much importance the society gives to reducing inequality.

Policies dealing with inequality and recommending income transfers are usually framed within one of the two most widely used social welfare functions or measures of income inequality. The Gini index is the one most widely used measure of inequality. The social welfare function implied by the Gini index is defined as mean income multiplied by one minus the Gini index. The other most widely used is Atkinson's social welfare function, whose construction allows for different degrees of inequality aversion expressed by the parameter $\mathcal{E}$. The larger $\mathcal{E}$ is, the greater is inequality aversion and, thus, the greater will be tolerance of leakages.

To illustrate how these two types of social welfare functions interplay with leakages and inequality, let us chose $\mathcal{E}$ as equal to 1. Suppose we transfer $25 (5% of the income of the rich) from the rich to the poor. If the society can be better described by a Gini social welfare function, then transfers will stop when the leakage is greater than 50%. At this point the per cent change in social welfare becomes negative and total welfare is reduced. If the society can better be modeled by Atkinson's welfare function, then waste can go up to 90% before the transfer is regarded as undesirable. Thus, a society behaving along the lines of an Atkinson welfare function with moderate aversion to inequality ($\mathcal{E} = 1$) is much more concerned with inequality than a society behaving according to the Gini welfare function.

Impact of Leak Age on Welfare



Leaks, in the more general sense of the term adopted here, can occur due to several factors, including administrative cost corruption, reduced or misplaced work effort, distorted saving and investment decisions, possible changes in socioeconomic attitudes, and targeting errors. All of these should be, and usually are, carefully weighed when analysing the efficiency of redistributive policies. But the lesson here is that the choice of inequality indicator itself, and thereby a social welfare function, is not an inconsequential matter. Careful attention must be given, which is not often the case, to the choice of indicators and the analytical framework. Society's concerns with inequality and poverty should be properly addressed and reflected in policy evaluations.

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One Pager number 15
Published: June, 2005
Available at: <http://www.ipc-undp.org/pub/IPCOnePager15.pdf>

India Needs an Employment Guarantee Scheme

by Santosh Mehrotra,
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India reduced poverty during the 1990s. However, since income inequality increased at the same time and in a generalised way, the momentum on poverty reduction might decline in the future.*

Only employment-intensive growth will make continued poverty-reduction attainable. Again, the prospects for a strong employment generation process are not bright. The capacity to create jobs in tandem with production in manufacturing fell in the 1990s. It is only in services where urban employment has been growing rapidly. That confines the majority to depend upon India's slow-growing agriculture for a source of income. Agriculture still accounts for 59% of total employment. Most poor families are in casual employment or self-employed, while those with regular employment are least likely to be poor.

Thus, direct action by the government to spark job creation could dramatically reduce rural poverty. The government has introduced a bill in parliament providing a minimum guarantee of employment to poor households. The proposal is to give a statutory right to 100 days a year of employment at the minimum wage in each state to one person per household. On the basis of a minimum wage for all states of R$ 60 per day, 100 days work will raise two-thirds of India's population above the poverty line. It will initially cover the 150 poorest districts in the country.

The scheme can bring a number of benefits. In fact, labour-intensity can be very high in such work as watershed development, land regeneration, and prevention of soil erosion. This would protect the environment, but also enhance land productivity and increase output in future.

It would also have positive second-round effects on incomes, by raising rural wages and thus investment in human capital. One reason children of poor parents drop out of school is because they cannot afford schooling costs; raising incomes would reduce school drop outs. Add to this the increase in land productivity—together these can have profound economic growth effects.

Besides, improving watershed development could reduce damage to life and property caused by frequent flooding, and save future costs in government flood relief. The benefits of the employment guarantee scheme spread beyond its immediate impact on poverty.

Over the long run, the bill's implementation would not obviate the need for transfer of labour out of agriculture, where few have regular employment; most are self-employed or casual labourers. Much of the new regular wage jobs should be for low-skilled workers. This implies a growth strategy of manufactured exports requiring low-skilled labour, and producing low-skill intensity goods for the domestic market—rather unlike the current strategy.

But with a 222 million work force in agriculture, even a fast transfer out of agriculture will not pull all the working poor out of poverty. Hence direct employment creation through the act is an essential component of policy.

Is the employment guarantee scheme feasible? The economist Jean Dreze has estimated the total cost of the programme with phased implementation rises from 0.5% of GDP in the first year (2005) to 1% of GDP in the last year of the inception phase (2008). Thereafter, the ratio will decrease, as the number of below-poverty line households decreases. The consolidation of existing employment generation schemes with the programme of employment guarantee will increase efficiency in resource use.

The scheme, and these costs, are modelled on a similar scheme implemented successfully for 20 years in Maharashtra. But the preceding calculations assume a labour-material ratio of 60:40. The corresponding ratio is much lower in Maharastra, and unit costs could come down with more labour intensity.

These costs are not outrageously high but they are not low either. However, reverting the downward trend on the already low tax base of India will provide enough resources to pay for the employment guarantee act. Compared to central tax revenues for low-income countries of 14.1% of GDP over 1990-2001, or 22 for China in 2003, India's centre collected around 9% of GDP average between 2001 and 2004. Despite rising incomes in India the ratio of central taxes to GDP has actually fallen from 10.6% in 1987/8 to 9.3% now.

There are still at least 200 million poor people in India, and increasing inequality could lead to serious social tensions and urban turbulence. The social consequences of rising inequality in India in the midst of 200 million poor—a given if the current pattern of jobless growth continues—can be dire. There is a case for direct government intervention to create jobs: the employment guarantee act might be a good option.

* *Nota bene*: See Kakwani's One Pager 2 on the debate on poverty and inequality in India. (OnePager's editors).

One Pager number 16
Published: August, 2005
Available at: <http://www.ipc-undp.org/pub/IPCOnePager16.pdf>

Three Models of Social Protection

by Alejandro Grinspun, International Poverty Centre

For a decade or so, social funds were supposed to be present in every strategy against poverty. Modeled after Bolivia's *FSE* (1986) and supported by multilateral banks, country after country set up its own local version culminating in Mexico's *Solidaridad*, before they faded away. A new model has now grabbed the attention of governments and donors. In 1997, Mexico created *Progresa* (now *Oportunidades*), a program that gives cash to female heads of poor families every two months in exchange for sending their children to school, improving their diets, keeping up with their vaccination schedules and attending health clinics. The idea behind a conditioned cash transfer is that it mitigates current poverty (through the income supplement) while preventing future poverty (by creating incentives for families to invest in human capital). *Oportunidades* provides cash to five million families, a quarter of the population; children are said to be growing taller, healthier and staying more in school, with larger declines in dropout rates and increases in transition rates from primary to secondary school among girls due to the program's graduated-transfer schedule.

The success of *Oportunidades* has spawned emulation. *Familias en Acción* operates in Colombia since 2001, targeting mothers from the 20% poorest households with a food subsidy and monthly transfers. In a short time, total household consumption has improved noticeably, with most spending going to protein-rich food and children's clothes, and attendance is up at schools and health posts. After a shaky start in 2003, Brazil's *Bolsa Familia* now reaches eight million families with monthly grants largely spent on food; 75% of its outlays are on the bottom two quintiles, and another three million families will be added next year. In Nicaragua, too, total household spending among the poorest jumped by 40% in the first two years of the *Red de Protección Social*, the bulk on food consumption. School enrolment and attendance are also up, while the proportion of child workers is down. But nothing compares with the dramatic drop in stunting among children below five, from 42% to 37%, in just two years. This suggests a well designed, properly implemented and regularly evaluated cash transfer program can greatly benefit the poor. Yet these programs may not be suitable in every setting, nor are they the only model for shielding poor people and helping them exit poverty.

Just last August, India passed the landmark *National Rural Employment Guarantee Act*, hailed as the most important piece of legislation since 1947. Under the Act, every rural household is entitled to 100 days of guaranteed employment at the legal minimum wage or else an allowance if work is not provided within 15 days of registration. What is remarkable about the law is that, through its guarantee of wage employment, it seeks to safeguard the 'right to work' enshrined in the Constitution, which itself is seen as pivotal for the realization of the 'right to food'. Unlike a conditioned transfer where eligible families get the benefit only so long as they comply with certain conditions, here it is the State that has an enforceable obligation to provide employment to anyone willing to take it. On one case, families have to 'earn' the benefit; on the other, they are entitled to it. Since the guarantee applies to unskilled manual labor, it is expected to be self-selecting; only a needy person would normally want to perform such work. A conservative estimate puts that number at 40 million families who, like most of village India, have been bypassed by the economic boom unleashed by the 1991 reforms. Essentially, the bill provides a universal entitlement to relief employment on demand. While mainly intended to protect families from hunger, its potential multiplier effects extend well beyond this. If well implemented, *NREGA* can help boost agricultural growth and wages, create durable rural assets, revitalize local markets and industries, and contain migration to the city. The granting of household not individual entitlements worries some, who fear competition for work could exclude women. Critics say the Act is wasteful, prone to corruption and, with a price tag of $10 billion a year, unaffordable. But due to its phased roll-out over five years, *NREGA* is not expected to take up more than 1% of GDP when implemented nationwide—a price worth paying for lifting millions from destitution. The fact that redistributing even 1% of GDP can so impact the lives of India's poor suggests how little they share in their country's wealth.

In South Africa, a proposal for a universal basic income grant has raised a storm. Recommended in 2002 by a government expert panel, it consists of a monthly *solidarity grant* that would be paid to every legal resident from cradle to grave, regardless of income or age. Many dismiss the idea as impracticable, but a broad coalition of supporters has kept the debate raging. They claim it is affordable *and* feasible, and would give effect to the 'right to social security' written into the 1996 Constitution by providing a modicum of economic security to the more than half of South Africans trapped in long-term poverty. Many of these are so deprived of income they cannot access government services, which undermines the efficacy of public social spending, while strategies for stimulating job growth are unlikely to help but a small proportion of the unemployed, estimated at over 40%, many without social assistance of any kind. The idea of an unconditional basic income for all may sound utopian, but there is already one place where it exists. It is Alaska, where up to 2004 every person was receiving an annual dividend of $2,000 after just one year of residence. Alaska has the smallest gap between rich and poor of any US state.

These different models may not be replicable across countries. Very poor countries may be ill-suited for targeted transfers that require sophisticated institutional capacity for screening beneficiaries and monitoring compliance with program conditions. Highly unequal countries may be ill prepared for entitlement programs ostensibly favoring the poor. Determining the extent to which implementation capacities and aversion to poverty affect a program's feasibility is a matter of empirical research. At least, there appears to be more than one model countries can choose from. And this, by itself, is good news.

* *Nota bene*: See Mehrotra´s One Pager 16 on India Employment Guarantee Act. (OnePager's editors).

One Pager number 17
Published: October, 2005
Available at: <http://www.ipc-undp.org/pub/IPCOnePager17.pdf>

Headcount Poverty Comparisons

by S. Subramanian, Madras Institute of Development Studies, Chennai, India

The most elementary, and also the most widely employed, means of assessing the extent of poverty in any society is to obtain a simple headcount of the poor. The poor are those whose incomes fall short of a stipulated poverty line. The commonest measure of poverty is the *headcount ratio*, H, which is the proportion of the poor in the total population. An alternative, and far less routinely used headcount index, is the *aggregate headcount*, A, which is the total absolute number of the poor. A problem for the measurement of poverty—and one which is only rarely acknowledged by professional economists—is that the headcount ratio and the aggregate headcount can provide contrary poverty rankings. For example, if in some initial time period 30 persons in a population of 100 are poor, while in a later time period 40 persons in a population of 200 are poor, then the headcount ratio *declines* from 30 per cent to 20 per cent, whereas the aggregate headcount *rises* from 30 persons to 40 persons. This type of problem is often encountered. For example, using a poverty line of 2.15 Purchasing Power Parity dollars per person per day, the global headcount ratio has been estimated to have declined from 66.7 per cent in 1981 to 52.9 per cent in 1991, while over the same period, the global aggregate headcount has been estimated to have risen from 2,450 million to 2,735 million.[1]

A strong argument in favour of the headcount ratio over the aggregate headcount is that the former, unlike the latter, satisfies what one might call a '*Likelihood Principle*', which is the requirement that a poverty measure should convey some information about the probability of encountering a poor person in any given society. On the other hand, the aggregate headcount, unlike the headcount ratio, satisfies a principle called the '*Constituency Principle*.' This is a general principle of well-being comparisons formulated by the economist-philosopher John Broome, and it demands something like the following. If a given set of individuals has been identified as the only constituency which is of relevance in ascertaining the 'goodness' of a state of affairs, then the 'goodness' of alternative states of affairs should be compared only in terms of the interests of the identified constituency in the states under comparison. When we speak of poverty, it seems eminently reasonable to designate the *poor* population as the only relevant constituency for ascertaining the extent of poverty. And if this is the case, it follows that additions to either the incomes or the size of the non-poor population should be treated as wholly irrelevant information when it comes to making poverty comparisons.

It is easy to see that the headcount ratio, in contrast to the aggregate headcount, violates the Constituency Principle. Here is a simple example. Imagine an initial situation in which we have a two-person society, with the incomes of the two individuals being Rs.1,000 and Rs.3,000 respectively, and with the poverty line set at Rs.2,000. It is clear that the headcount ratio for this society is 50 per cent. Suppose now that a person with an income of Rs.3,000 joins this society. Then, the headcount ratio will decline to 33.33 per cent. With the addition of a third person with an income of Rs.3,000, the headcount ratio will decline further to 25 per cent. Add one more person whose income is Rs.3,000, and the headcount ratio will come down to 20 per cent. And so on. If we simply keep inflating the size of the non-poor population, before long we will be in a position to claim that we have—by measuring poverty in terms of the headcount ratio—almost completely eradicated poverty, even though precisely *nothing* has been done to redress the poverty of the only person who represents the constituency of the poor in the society under review.

So where does this leave us? The headcount ratio H satisfies the Likelihood Principle and violates the Constituency Principle, while the aggregate headcount A satisfies the Constituency Principle and violates the Likelihood Principle. Leaving poverty judgments entirely up to either H or A could be a risky proposition. This suggests the possible wisdom of a 'compromise solution', whereby we look at both H and A, in a bid to avoid the extreme judgment of either principle in isolation. In this note, I only pose the problem, without considering solutions for it, simply in order to underline the fact that the problem has rather serious conceptual and practical implications for the measurement and comparison of poverty.[2]

References:

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2. See S. Subramanian (2002): 'Counting the Poor: An Elementary Difficulty in the Measurement of Poverty', *Economics and Philosophy*, 18; and S. Chakravarty, S. R. Kanbur and D. Mukherji (2005): 'Population Growth and Poverty Measurement', forthcoming in *Social Choice and Welfare*.

One Pager number 18
Published: November, 2005
Available at: <http://www.ipc-undp.org/pub/IPCOnePager18.pdf>

Women's Earning Power and Wellbeing

by Nanak Kakwani and Hyun H. Son, International Poverty Centre

Most people belong to a household (or family). They share happiness, sorrows and, more importantly, resources that are generated by household members. The vast majority of economic activities take place within households. A variety of decisions about labor force participation, education, expenditures, saving, asset accumulation, investments, marriage and fertility are made within households. What goes on within households critically affects growth, income distribution and poverty in a country.

Most economic analysis assumes that a household is a single decision making unit in which all individuals have the same preferences. Decisions within the household are assumed to be made in such a way that every individual within the household enjoys the same level of welfare. But here we are assuming too much.

Numerous studies show that there is systematic deprivation of women vis-à-vis men in many societies (Dreze and Sen, 1989). The very fact that there exits domestic violence against women in many households indicates that unitary decision models are unrealistic.

It is widely known that the probability of survival in South Asia is higher among male children than female children. This suggests that households treat male children differently from female children with regard to allocation of resources. In this respect, Sen's story of a large number of "missing women" in Asia and North Africa as a result of gender bias in the distribution of health care, food and other necessities is indeed very telling.

There is now an increasing focus on models of bargaining relationships within households. The main idea behind these models is that relative bargaining power of men and women ultimately affects the distribution of consumption not only between men and women but also between adults and children and between boys and girls.

It has been found that as women's contributions to household monetary income increase, they are more able to influence how household resources are allocated. The reason is that their greater earning potential gives them greater bargaining power.

Women generally contribute to household welfare by means of work that is unpaid, mostly performed at home. Their monetary contribution to household income is generally lower than that of men. This may be due to the fact that they have fewer opportunities for getting outside work and paid employment. Cultural factors indeed play an important role in the determination of who does how much housework.

Women's unpaid housework may be of critical importance in the determination of household wellbeing, but unfortunately it does not get as much recognition as paid work does. In order to get such recognition, many recent studies are advocating an inclusion of the imputed value of women's unpaid work in the construction of national accounts (see, for example, Levy Institute-UNDP, 2005). Even if women were able to achieve official recognition of their work, still their bargaining power within the household would likely be lower than that of men if they are not able to make monetary contributions to the joint resources of the household.

Women's contribution to household prosperity from outside gainful activities is the most important factor in the determination of their relative and absolute deprivation. Research tends to confirm this view. Our own research shows that in a middle income country, such as Brazil, women's contribution to household labor earning is less than half of men's despite the fact that women have more years of schooling compared to men. Thus, schooling alone does not explain the earnings disparity between the two. The other factors that play an important role are labor force participation rate, employment rate, labor productivity, hours of work and non-labor income. There are disparities between men and women with regard to all these factors.

Although women have as much to offer at work as men do, they generally are unable to play an active role in labor markets because they face many constraints within as well as outside the household. Some of these constraints could be eliminated by government's policies aiming to make the labor market less discriminatory. Such policies could enhance overall wellbeing in society and would have a more direct impact on enhancing women's empowerment than actions seeking recognition of unpaid work in official statistics.

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One Pager number 19
Published: April, 2006
Available at: <http://www.ipc-undp.org/pub/IPCOnePager19.pdf>

The Gender Pay Gap over Women's **Working Lifetime**

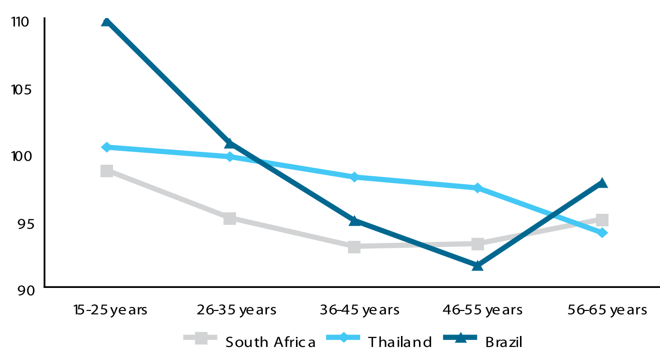
by Hyun H. Son and Nanak Kakwani,
International Poverty Centre

The gender pay gap exists universally but its size might vary from one country to another. A variety of factors cause the gender pay gap but two important ones are occupational segregation and gender discrimination in labour markets. It is common to observe gender differences by occupations and industries. These differences imply large variations in the jobs worked by women and men. For instance, female workers are in general more likely to be in clerical and service occupations or professional services such as education and training.

Gender discrimination occurs when people who provide labour market services and are equally productive are treated unequally because of gender. Inequality means that these people receive different wages for the same work or face different demands for their labour services at a given wage. Many economic theories suggest that labour market discrimination not only lowers the wages of the disadvantaged group but also raises the wages of the advantaged group.[1]

The figure presents the ratio of average hourly female wages to average male wages over a working lifetime. The hourly wage is adjusted for years of schooling, geographical locations (e.g., provinces or urban/rural) and race. The calculations are done for three countries: Brazil, South Africa, and Thailand.

Average Hourly Female Wage as a Percentage of Average Hourly Male Wage, all Workers



Source: Authors' calculation based on household surveys.

Two interesting patterns emerge from this figure: 1) the gender pay gap widens up to a certain point and then narrows for Brazil and South Africa (in Brazil women get even higher wages than men initially but then experience a sharp decline in wages; 2) a continuous but gradual increase in the pay gap between men and women over a working life span for Thailand. Another interesting point is that while the gender pay gap opens early in South Africa, it does so much later in Brazil and Thailand. These findings invite us to think beyond conventional analyses of the gender gap.

Social and cultural factors can play an important role in explaining a persistent gender pay gap. A recent study shows that the hourly pay of women relative to that of men tends to assume a U-shape over women's lifetime in the United Kingdom.[2] Women make choices to sacrifice their careers when they have children, with consequences for a reduction in their lifetime earnings. Thus, gender differences in the formal labour market stem from the division of parental duties between mothers and fathers in the home, with mothers being primarily responsible for the care of children.

Another reason for the pay gap is that men and women make different education and career choices. At school, boys and girls study different subjects, but boys' chosen subjects lead to better paying careers. Later, men and women specialize differently and work in different professions. As a result, average hourly pay for a female worker at the start of her working life is, in general, likely to be lower than that of a male worker (as observed for South Africa), even though she may be more qualified.

In order to narrow gender gaps, governments can provide affordable child care, so as to reduce the opportunity costs of working and raise women's productivity as formal workers. Governments can also pursue programmes that enhance girl's subject choices and improve career advice at school to ensure that girls are encouraged to pursue fields such as mathematics and science. Such public actions can help reduce the gender gap over a working life time.

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One Pager number 20
Published: June, 2006
Available at: <http://www.ipc-undp.org/pub/IPCOnePager20.pdf>

Do CCTs Reduce Poverty?

by Eduardo Zepeda,
International Poverty Centre

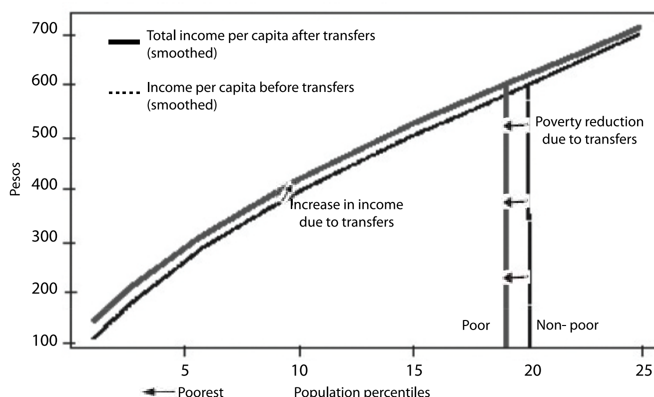
Conditional Cash Transfer (CCT) programmes, borne in Latin America, are often identified as a new generation of anti-poverty policies. They feature targeted transfers to poor households based on the condition that beneficiaries protect and build their human capabilities—e.g., children attend school or family members regularly visit health clinics.

Evaluations confirm that such transfers do reach the poor. They also help increase school attendance (including progression from primary to secondary school), promote more intensive use of basic health services and improve nutrition. Despite some initial concerns, CCTs also do not generally undermine the willingness to work except for the desirable reduction, in some cases, of child labour. In this note, we concentrate on their impact on income poverty.[1]

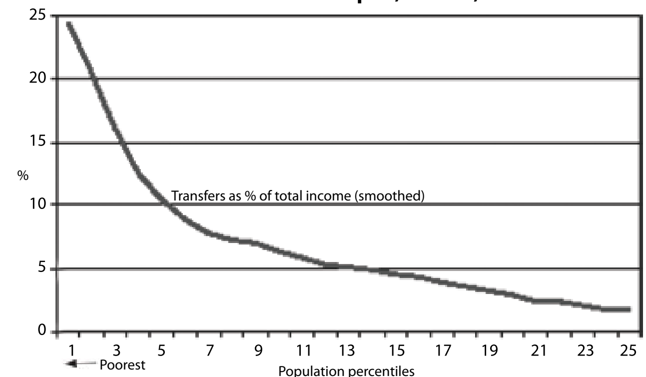
Certainly, CCTs are affordable: their budgets account usually for no more than 1-2% of GDP. In 2004, in the midst of expansion, Brazil's *Bolsa Familia* (including *Bolsa Escola*) and Mexico's *Oportunidades* reached 8 and 5 million households. These programmes do not suffer from much leakage to the non-poor. However, one major criticism is that CCTs appear to produce only a small reduction in poverty—even in countries with wide coverage such as Brazil and Mexico.

While this criticism might be valid, it is misleading. Graph 1 shows total income per capita (smoothed) for the poorest 25% of the population in Mexico before and after *Oportunidades* transfers. Assuming that 20% of the population is poor, these transfers reduce the incidence of poverty to about 19%. Similarly modest reductions in poverty result if lower incidences of poverty are assumed.

Graph 1
Income Per capita and CCTs in Mexico, 2004



Graph 2
Share of CCTs in total Income Per capita, Mexico, 2004



In Brazil, for a poverty line set at one half the minimum wage, the reduction in poverty is from 15% to 13%.[2]

But focusing on changes in the headcount ratio captures only a small portion of their total benefit. Their impact on poverty should be gauged by measuring the effect of transfers on all poor individuals, whether their income rises above the poverty line or not.

Graph 2 shows that for the 25% poorest in Mexico, cash transfers can represent a significant share of total income. The share of transfers in total income is highest for the poorest (rising to about 25%) and declines as income increases. In Brazil the share for the poorest rises to around 50%. Consequently, more bottom sensitive measures of poverty, e.g. poverty gap and severity of poverty, show larger changes in poverty. While the incidence of poverty declined by 5%, the poverty gap and the severity of poverty measures dropped by 12% and 19%, respectively.

Thus, an affordable CCT programme, featuring well targeted transfers, can make a major difference in the income of poor households. Of course, CCTs are no substitute for widespread employment generation, which could provide sustainable generation of income. In the short term, CCTs cannot be expected to significantly reduce poverty. However, they do, indeed, offer much needed income support to poor households. In this sense, they play a valuable role as basic social protection. If well designed, they could also have a longer run positive impact on enhancing the human capabilities of the poor.

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One Pager number 21
Published: September, 2006
Available at: <http://www.ipc-undp.org/pub/IPCOnePager21.pdf>

What Is Poverty?

by Nanak Kakwani,
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Reducing poverty has become a major concern of development policy. To inform policy, research on poverty has focused on income or consumption based poverty measures. Yet it is now increasingly realized that poverty is multidimensional, encompassing all important human requirements. Poverty is now widely viewed in terms of capability deprivation.

The income approach views poverty simply as lack of income (or consumption). Poverty exists when some persons in the society have so little income that they cannot satisfy socially defined basic needs. But lack of income is not the only kind of deprivation people may suffer. Indeed, people can suffer acute deprivation in many aspects of life, beyond those defined as basic needs, even if they possess adequate command over commodities (for example, ill health or lack of education and so on). The conceptual distinction between deprivation of this kind and that primarily resulting from inadequacy of income is of fundamental importance.

The higher a person's income the greater is his or her command over commodities. The possession and consumption of commodities (including services) provides people with the means to lead a better life. However, possession of commodities is only a means to an end. As Sen (1985) points out "ultimately, the focus has to be on what we can or cannot do, can or cannot be". Thus, the standard of living enjoyed by people must be seen in terms of individual achievements that are feasible and not in terms of the means individuals possess to achieve them. This line of reasoning led Sen to develop the ideas of functionings and capabilities. A functioning is an achievement, and a capability is the ability to achieve. Thus, the functionings are directly related to the kind of life people actually lead, whereas capabilities are the opportunities people have to lead lives of their choosing.

According to the capability approach, an individual is defined as poor if he or she lacks basic capabilities. What ought these basic capabilities to be? An answer to this question requires value judgments, which must reflect appropriately assessed social priorities. While, there is no universal agreement on what these basic capabilities are, it may still be possible to agree on some basic capabilities. For example, if a person is not able to be well-nourished, adequately clothed and sheltered, and not able to avoid preventable morbidity, then he or she can be classified as deprived of basic capabilities. Those capabilities that relate to health, education, shelter, clothing, nutrition and clean water can reasonably be regarded as capabilities that we can agree are basic.

Can one describe poverty purely in terms of capability deprivation? Take a millionaire with an incurable disease, which prevents the achievement of some basic functionings. This would surely be a case of serious capability deprivation, in spite of access to the best medical facilities. Yet, it would be odd to call this millionaire "poor". From a capability perspective, poverty arises when basic capability failure is caused by inadequate command over resources, whether through markets, public provision or other non-market channels. By examining capability deprivation alone, we cannot always identify persons who are poor.

One needs to make a distinction between poverty and capability deprivation in general. Whereas broad capability deprivation may be caused by a host of factors, poverty is concerned only with the inadequacy of command over resources needed to generate socially determined basic capabilities. Among these, income or entitlement to resources may not be the most important. Thus, a person may suffer capability deprivation but still may not always be poor.

Defining poverty from the capability perspective cannot be done independently of income. The capability to function with which one should be concerned is that derivable from income and wealth. Command over recourses and capability cannot be separated, but at the same it must be recognized that the link between them is far from simple. Individuals have different needs and, therefore, differ with respect to their ability to convert their incomes and resources into capabilities to function. Thus different individuals will require different resources to achieve basic capabilities.

It is best that any proposed income measure of poverty be constructed from capabilities. The choice of a poverty line should reflect the cost of achieving basic human needs. However, the most frequent measure used internationally, the $1 a day per person (or $2 a day), is not in accordance with the capability approach to poverty, that is, it does not reflect the inadequacy of command over the resources to achieve basic capabilities. A person can have an income sufficient to count as non-poor according to the $1 a day yardstick but not to attain income-dependent basic capabilities. If the reduction of poverty, as properly understood, is to be achieved, then new measures of its extent and distribution in the world will be required.

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One Pager number 22
Published: September, 2006
Available at: <http://www.ipc-undp.org/pub/IPCOnePager22.pdf>

Inequality and the Education MDG for Latin America

by Eduardo Zepeda,
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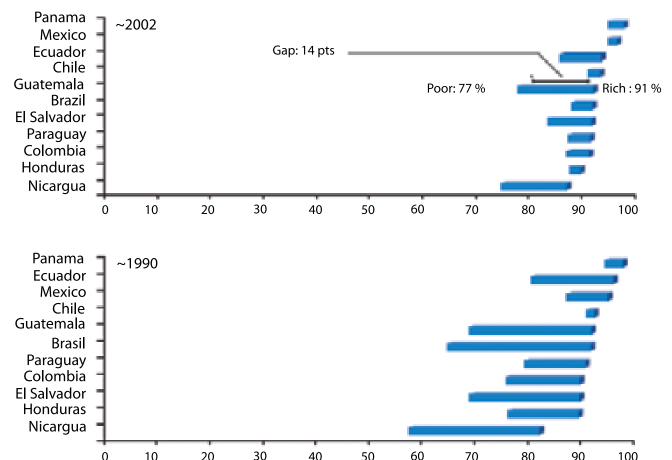
After the Millennium Declaration in 2000, eight comprehensive goals with specific quantitative targets to be met by 2015 were articulated as the Millennium Development Goals (MDGs). These include halving poverty and hunger, achieving universal primary education, eliminating gender disparities, improving child and maternal health, promoting sustainable development and constructing a global compact for development. In the year 2005, a comprehensive evaluation found uneven progress across the world. While many countries had experienced rapid progress towards several of the goals, a sizeable number had moved slowly and some had experienced reversals.

Key for development is the achievement of universal primary education, Goal 2. This goal is within reach for most regions—the exception is Sub-Saharan Africa. Latin America & the Caribbean (LAC) is performing well on this goal. The corresponding indicator, net enrolment in primary education, shows a 95% rate in 2004/2005. Progress in the region has been rapid, propelled by fast improvements by population groups with low attainment in the 1980s.

Using data derived from household surveys and displayed in the EQXIS system (http//:www.iadb.org/xindicators), one can visualise the speed of progress and the reduction in inequality. The graph shows the gap between the richest and the poorest fifth of the population in the 1990s and the 2000s for selected countries (bars indicate gaps; its left end gives the net attendance rate for the poorest fifth of the population, the right end gives that for the richest). Most countries experienced improvements in the national attendance rate and most also reduced the gap between the richest and the poorest quintile.[1] In some instances, such as Chile, Ecuador or Mexico, data for 2002 suggests that the difference in net attendance rates between these two groups is small.

But inequality is far from being eliminated. Looking closer and bringing in factors such as gender and ethnicity, one finds areas of concern. While no difference exists between the top and bottom quintiles for the *white* ethnic group in Brazil, both at 92%, the rate for afro descendents (*pretos*) in the poorest quintile is 86%. In El Salvador the interplay of income and gender shapes inequalities. While national attendance rates for males and females are the same, 88%, females in the poorest quintile have a low rate, 82%, while those in the richest have a 94% rate.

Net Attendance in Primary Education



LAC's inequality heritage might prevent it from achieving universal primary education by 2015. Current projections of net enrolment suggest that the region is on track to meet the target by 2015. However, projecting from the 1990s into the next 10-15 years assumes that the very rapid rate among the population groups that had a low educational attainment in the early 1990s will continue. But, it is easier to increase enrolment rates when initial levels are low. So now, with higher attainment, the speed of change is likely to slow down. ECLAC's MDG report (2005) confirms that inequality is a major problem.

Policy decisions guided by broad average figures can be seriously misleading. In order to achieve universal primary education, as well as other MDG goals and targets, policy making should be based, from the start, on analysis drawn from disaggregated data. While the region has been successful in narrowing large education gaps, the pace of future progress is likely to be slow. So policy efforts must be escalated. Support to deprived groups must be well designed since it will be more difficult to reach them. Success in increasing the number and proportion of people with primary education does not guarantee its quality; indeed, quality of education is clearly in need of improvement. Moreover, access to quality education must be egalitarian.

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One Pager number 23
Published: October, 2006
Available at: <http://www.ipc-undp.org/pub/IPCOnePager23.pdf>

Are Improving Terms of Trade Helping Reduce **Poverty in Africa?**

by Andrew Mold,
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Throughout the 1990s, the old slogan '*trade not aid*' aggressively pushed the idea that export performance and poverty reduction were intimately related. In recent years, however, there has been a growing realisation that links between the two are far from automatic and that serious mismatches can occur.

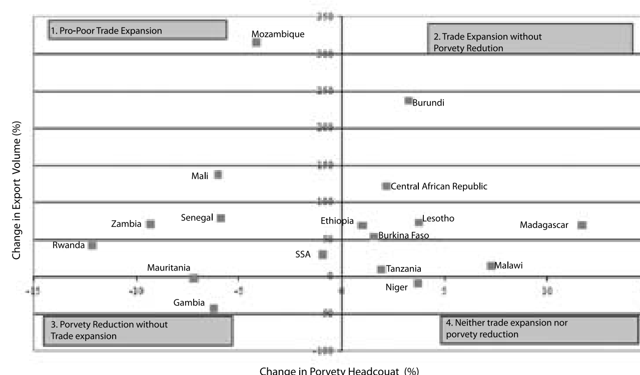
One illustration of this is the apparent mismatch in Africa between export performance and poverty reduction. Pessimistic assessments of African export performance abound. But these may not be totally merited. During 1996-2001 UNCTAD estimates of trade *volumes* (as opposed to trade *values*) show that some African LDCs achieved a very respectable increase in exports. Yet, this expansion was not accompanied in many cases by significant poverty reduction. For example, Madagascar and the Central African Republic expanded their exports by nearly 70% and 121% respectively over this period, yet their dollar-a-day poverty headcount *increased* by 12% and 2%. (See Graph). In Burundi, a 236% increase in export volumes resulted in a 3% *increase* in the poverty headcount.

In value terms many Africa's exports slumped over this period, as volume increases were not enough to offset collapsing real export prices, like those of coffee, palm oil, cocoa and cotton. In spite of small-holder farming still being predominant in Africa, exports of these commodities have not only failed to contribute to poverty reduction, but also have not prevented it from rising.

Recently reported record highs in commodity markets, driven by strong demand from China and India, do improve the terms of trade for commodity producers. However, major increases have been in minerals (commodities such as copper) and fuels, but agricultural commodities (or 'soft commodities'), the mainstay of African economies, have remained low.

Moreover, while the increase in fuel and mineral prices has had a favourable impact on some African countries, it has also caused a cleavage between exporters of hard and soft commodities. Countries such as Nigeria or Zambia are benefiting from their oil and copper exports, but others such as Uganda or Ethiopia, whose export earnings depend on soft commodities (and rely on the import of hard commodities, especially fuel), face an extremely difficult situation. The emergence of transcontinental value-chains dominated by Northern supermarkets and retail firms has added

Trade Expansion and Poverty Reduction, 1996-2001 for Selected African LDCs[1]



further complexity, raising problems of excessive market power on the part of buyers, and leading to a low and declining share of total value-added for African producers.[2]

The importance of agriculture for poverty reduction hardly needs emphasizing. Approximately 80% of the population of sub-Saharan Africa live in rural areas, and 70% depend on food production. Yet over the last two decades, policymakers in the North have generally turned a blind eye to the development problems caused by volatile commodity prices. Illustrations laid out here suggest that a new and more nuanced look be taken at the relationship between trade, economic growth and poverty reduction.

Clearly, for exporters of agricultural commodities, the first bit of long-term advice is to get out of commodities, and be careful about where they move into manufacturing production or services. But African policymakers are keenly aware that economists have typically been long on recommending diversification and short on practical advice about how to achieve this goal. Policies to reduce poverty must find mechanisms to reduce price volatility and improve the terms of trade for these 'soft' commodities. A completely free-market, non-interventionist stance on commodity markets has evidently failed the poorer developing countries.

Notes:

1. Own elaboration based on ECA's poverty estimates from country's household surveys and UNCTAD (2005), Statistical Yearbook (cd-rom).
2. See P. Gibbons and S. Ponte (2005), *Trading down: Africa, Value Chains, and the Global Economy*. Philadelphia: Temple University Press.

One Pager number 24
Published: November, 2006
Available at: <http://www.ipc-undp.org/pub/IPCOnePager24.pdf>

Old-Age Poverty and Social Pensions in Kenya

by Hyun H. Son and Nanak Kakwani,
International Poverty Centre

Protecting the elderly from the risk of poverty is a large challenge in any developing country. Although Kenya has a relatively small proportion of its current population over the age of 55, these individuals and the members of their households remain among the most vulnerable members of the society. The poverty rate among older persons is, by any of the standard measures, greater than that of the population at large. And the poverty rate of the elderly increased between 1994 and 1997 (the period for which there are household survey data available).

These poverty rates have various secondary consequences. There is a high rate of grandparents caring for children because of the HIV/AIDS epidemic. This exposes children to the consequences of old age poverty. A higher proportion of children living in elderly headed households are poorer than for the average.
Also, children living in these households have lower rates of school attendance than others.

The current pension system in Kenya is very limited: only about 3% of the elderly population report the receipt of any pension income. One of the potential alternative approaches to expansion of the pension system in Kenya would be the introduction of a non-contributory social pension that provided a benefit to all persons who attained a specified retirement age. These types of arrangements are generally seen as one of the few feasible alternatives in settings characterized by very high rates of poverty among the elderly and low rates of employment in the formal economy. Such factors limit the capacity of many formal retirement systems to achieve broad coverage even if participation is mandatory when people work.

There are a variety of key design parameters that dictate the nature and feasibility of any system of social pensions. The most important include the age of eligibility, the size of the benefit and the extent to which other eligibility criteria, such as means testing, are applied. The study by Kakwani, Son and Hinz (KSH hereafter) (2006) provides some initial observations on the feasibility of a non-contributory social pension. It offers preliminary assessments of the costs and potential poverty outcomes among the elderly in relation to the two main design parameters of benefit levels and age requirements.

The most basic questions regarding the feasibility and outcomes of a social pension system are the number of pension beneficiaries and the expected benefit level under alternative budget scenarios. The KSH study finds that if a pension program had been designed to reach elderly 55 years and older, there would have been more than 1.5 and 1.7 million beneficiaries in 1994 and 1997, respectively. Such a universal pension scheme would have cost 1.16% and 1.38% of GDP in 1994 and 1997, respectively.

Increasing the size of the benefit will increase the capacity of a social pension to alleviate poverty. But where to set the benefit level is primarily based on political economy and fiscal feasibility. One way to evaluate the alternatives is to estimate the 'efficiency' of expenditures. This is defined as the percentage change in poverty as a ratio to the total costs of a pension program. This enables one to focus resources on a specific target group, and would lead to a greater reduction in poverty.

KSH evaluates the cost efficiency of alternative pension programs in reducing national poverty in Kenya. It suggests that providing the benefit only to the poor elderly would result in the maximum reduction in poverty in relation to cost.

On the whole, the KSH study indicates that a non-contributory social pension could be implemented within a feasible range of costs. These could be as low as a little less than 1% of GDP, or could rise to about 3% of GDP if the benefit were increased to the equivalent of 50% of per capita national income. These expenditures need to be considered in the context of both the share of revenues that would be required for such a program and the poverty reduction that could be achieved.

Reference:
Kakwani, N., H. H. Son, and R. Hinz (2006) . "Old-Age Poverty and Social Pensions in Kenya", Working Paper No. 24, International Poverty Centre, Brazil.

One Pager number 25
Published: November, 2006
Available at: <http://www.ipc-undp.org/pub/IPCOnePager25.pdf>

What Is Poverty? Good Question.

by Terry McKinley, Acting Director
International Poverty Centre

The emergence of people-centred poverty measures in the late 1990s, first introduced by UNDP's *Human Development Report*, was a hopeful sign that poverty analysis would be re-aligned with the human development paradigm. But progress has been slowed by ambiguities. Moreover, some recent efforts have tried to redefine human poverty in income-poverty terms.

The inaugural 1990 *Human Development Report* defines human development as "a process of enlarging people's choices" and states that "income is a means [to], not an end" of human development (p. 10). However, in constructing the Human Development Index, the report included as one of its three indicators real GDP per person. This indicator was meant to denote "command over resources needed for a decent living" (p. 12). So what had been clarified as a means to human development (income) established itself thereafter as an indicator of the attainment of the end itself (human development). This has been a persistent source of confusion since then.

The Emergence of Capability Poverty

The 1996 and 1997 *Human Development Reports* broke new ground by defining measures of human deprivation in addition to human development. The path-breaking 1996 *HDR* developed the 'capability poverty measure', which was the first "multidimensional index of poverty focused on capabilities". The report stated that "unlike income, capabilities are ends, and they are reflected not in inputs, but in human outcomes—in the quality of people's lives" (p. 109).

The capability poverty measure was based on three *non-income* measures (related to health, literacy and reproduction), specifically "intended to complement income measures of poverty" (p. 27). Thus, this measure sought to maintain a clear distinction between means and ends. Otherwise, the same object—namely, deprivation—could be measured twice in the same index.

Reformulating capability poverty, the 1997 *HDR* produced the 'human poverty index', which was explicitly aligned with the three dimensions of the human development index. This led, however, to re-incorporating indicators for the lack of 'overall economic provisioning'. Instead of using income, as the HDI does, this new index used indicators for malnutrition and lack of access to health services and safe water. This was meant to incorporate measures of the lack of both private income (leading to hunger) and public income (leading to lack of public health services and water supply).

The income approach to poverty has difficulty in accounting for public income (e.g., public revenue that finances the provision of health and education). And income has little direct correlation with some basic capabilities, such as political freedom. So this approach cannot capture the full range of human deprivation.

The human poverty approach has difficulty in clearly defining some human capabilities. For example, is 'the command over material resources' a human capability? And if so, is the level of a person's income (including access to public income) an adequate proxy for this capability? But income is supposed to be a means to developing human capabilities, not an end in itself. This is a troubling ambiguity that underlies major recent problems.

'Capability-Based' Income Measures

In this regard, some poverty experts have recently concentrated their attention on developing a generalized income measure of capability poverty. One prominent example is Kakwani 2006 (IPC *One Pager* #22). This represents a well-intentioned effort to anchor income measures of poverty more firmly on a capability base. But its operationalization could reduce human poverty to income poverty and muddle the conceptual distinction between the two.

Note Kakwani's argument that "poverty is concerned only with the inadequacy of command over resources needed to generate socially determined basic capabilities". In other words, while people could be deprived of capabilities in various respects, they are poor only when they *lack adequate income* to support basic capabilities. Part of the debate relates to confusions (mostly unnecessary) about *basic* capabilities.

Kakwani's example of a millionaire (who obviously is not poor) having an incurable disease (being 'capability deprived') is not helpful since society is incapable, by definition, of guaranteeing freedom from such a disease. By contrast, society should ensure freedom from such *preventable* diseases as malaria, tuberculosis and HIV/AIDS—a major reason that such freedom should be regarded as a basic health capability. The same could be argued for freedom from hunger, for example.

But trying to formulate a 'capability-based' measure of income poverty has more serious flaws. Its main difference from traditional poverty measures appears to be its 'costing' of capabilities instead of basic food and non-food needs. But many capabilities are difficult to cost; and it is pointless to cost others, e.g., political freedom. Thus, this approach will most likely revert to the traditional method of costing the more easily defined commodity inputs into human needs, e.g., food, clothing and shelter. Thus, we will have come full circle back to traditional income-based poverty measures—an unfortunate legacy of underlying confusion in basic concepts.

Hopefully, this *One Pager*, along with IPC's December 2006 issue of *Poverty in Focus*, will stimulate a broader debate on this critical issue and lead to greater conceptual and operational clarity on 'what is poverty?'.

Reference:

Kakwani, Nanak, 'What Is Poverty?', *One Pager* #22, September 2006, International Poverty Centre, Brasilia.

UNDP, *Human Development Report*, 1990, 1996 & 1997, New York: UNDP.

One Pager number 26
Published: December, 2006
Available at: <http://www.ipc-undp.org/pub/IPCOnePager26.pdf>

Has There been any Social Mobility for **Non-Whites in Brazil?**[1]

by Rafael Guerreiro Osorio,
International Poverty Centre

Studies on social mobility often assume that as societies modernize, the socio-economic position of individuals will become attributable less to their *ascribed characteristics*, such as class, lineage, gender or race, and more to their own *individual achievements*, such as those based on ability, talent or effort. In other words, the characteristics of a child's family or other circumstances beyond his control will have increasingly less influence in determining his own eventual socio-economic status.

Such studies usually focus on individuals; they rarely examine *the mobility of groups*. It is possible that while individuals from disadvantaged backgrounds, such as non-whites, could enjoy greater social mobility, the relative position of the group to which they belong could change little. This could happen, for example, if individuals exchange positions exclusively with other members of their own group. Thus, a poorer non-white could achieve upward mobility at the same time that a richer non-white suffered from downward mobility. Alternatively, a poorer non-white could exchange positions with a slightly richer white but both would still have below-average incomes.

We test this proposition for racial groups in Brazil. Slavery was abolished in Brazil only in 1888. Until then, race was a powerful determinant of one's social position. At the top of society were Portuguese settlers and their offspring. In the middle were other white Brazilians of European descent and free people of mixed ethnicity. In the lower echelons were natives and enslaved Africans.

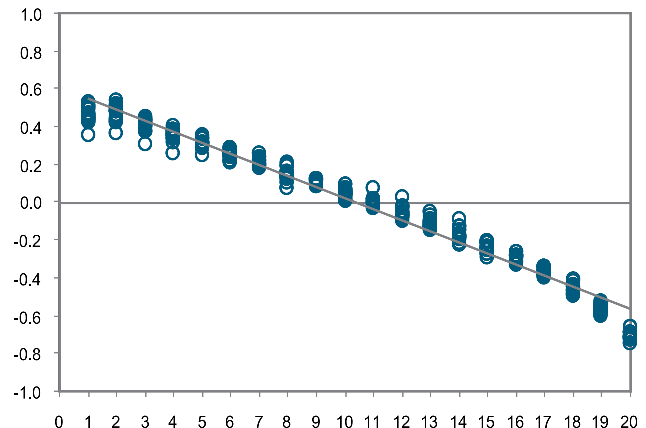
Although all the legal grounds for such stratification have now been eliminated in Brazil, people of African descent and other non- whites remain over-represented among the poor. Race remains a very important determinant of stratification, especially if the relative status of groups, not merely individuals, is examined.

In order to examine this claim, we choose the distribution of household income per person as a marker of social stratification. First, we divide the total population into twenty equal shares—vintiles—ranked from the poorest five per cent (first vintile) to the richest five per cent (twentieth vintile). We use Brazilian National Household Surveys as our data source for the period 1976 to 2005. However, we can compare income and race for only 19 out of the total of 26 survey rounds carried out during this period.

For each of these rounds, we calculate twenty 'odds-ratios', namely, the odds that a non-white person (either Afro-Brazilian or of mixed ethnicity) could be found in a particular vintile (such as the poorest 5 per cent) versus the overall odds that a person could be non-white. These ratios are normalized to range between -1 and +1. If the ratio is close to -1, the likelihood of finding such a non-white person in that vintile is very small; conversely, if the ratio is close to +1, there is a high likelihood of finding him there.

The results of this exercise are shown in the chart. For each vintile, denoted on the horizontal axis, there are 19 observations (although they overlap on the graph). For non-whites, the probabilities of being in the poorer vintiles over the course of 30 years are consistently positive, and for the richer vintiles consistently negative.

In other words, non-whites, *as a group*, have experienced very little social mobility. A simple regression, depicted by the line drawn through the data points, explains a remarkably high 97 per cent of all variance over the 30 years. This implies, for example, that no matter where a poverty line is set, non-whites would remain concentrated among the poor.



Our conclusion is that the socio-economic position of non-whites has remained remarkably stable and predictable over a long period of time. If race had not indeed remained an important determinant of socio-economic position, one would expect non-whites to have become more upwardly mobile, even if only slowly, over the last 30 years. But the available evidence suggests that there has been practically no upward mobility for this group.

Reference:
1. Rafael Guerreiro Osorio, *Race and Social Mobility in Brazil*. Paper presented at the Workshop "Equity and Social Mobility", IPC - DRCLAS, Brasilia, Brazil, January 2007.

One Pager number 27
Published: January, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager27.pdf>

MDGs: Misunderstood Targets?

by Jan Vandemoortele,
Currently UN Resident Coordinator in Pakistan; co-chair of
the UN inter-agency group that put the MDGs together in 2001

The Millennium Development Goals recently marked their fifth anniversary. They have generated tremendous support, globally and nationally. However, a common misunderstanding warrants a correction in the conventional view on the MDGs.

Origin – In 2000, the Millennium Summit synthesised previously agreed global goals and targets in a document called the 'Millennium Declaration'. Formulated as 8 goals and 18 targets, the 'MDGs' were endorsed by the UN General Assembly in late 2001. They were selected on the basis of available indicators and reliable data for documenting progress.

The MDGs aim to reduce hunger by one-half, infant and child mortality by two-thirds, and maternal mortality by three-quarters. The obvious question is: Why are these targets different? Why do they not call, for example, for a reduction by three-quarters across the board?

The simple answer is that most of the global targets are based on historical trends. They were set on the premise that progress observed at the global level over the previous 25 years would continue for the next 25 years—the period from 1990 to 2015. Thus, the MDGs are essentially an extrapolation of global trends of the 1970s and 1980s and projected forward till 2015.

Global vs. local targets – Thus, assessing whether progress is on track' for meeting the targets by 2015 can only be done at the global level. The quantitative targets were set in line with global trends, not on the basis of historical trends for any particular region or specific country. It is erroneous, for instance, to lament that sub-Saharan Africa will not meet the MDGs. These targets were not set specifically for that region.

The spirit of the Millennium Declaration was not to impose a one-size-fits-all benchmark for appraising and comparing country performance, regardless of differing historical background, natural endowments and particular challenges. Yet, it is common to misinterpret the MDGs as a uniform yardstick for human development. Statements such as '55 countries are off track to reach this target' or 'sub-Saharan Africa will reach that target by 2076' exemplify this misunderstanding.

It should not be surprising that many countries will miss several of the global MDGs because these targets were not set specifically for individual countries; they were based on aggregate global trends. It would be a tragic misunderstanding of the MDGs if all these countries were to be classified as 'failures' for the irrelevant reason that they will not meet artificial benchmarks set on the basis of past global trends.

The misinterpretation of the MDGs is not purely an academic matter. Being called a 'poor performer' when one is doing a perfectly respectable job is fundamentally disempowering. Interpreting the MDGs as a uniform yardstick will inevitably condemn more than half of the countries to the category of 'poor' performers —thereby undermining the support for the global targets among politicians and the public at large.

Making sense at the country level – Before dismissing the MDGs as targets that are 'easily set but never met', there are four practical steps that can be taken to make sense of the MDGs at the country level.

1. Global targets must be tailored to make them context-sensitive—essential for generating a sense of national ownership. They are meant to encourage countries to strive for accelerated progress. Their applicability, however, can only be tested and judged against what is realistically achievable under country-specific circumstances. No stigma should be associated with setting national targets that are less ambitious than the global MDGs. History shows that successful target setting critically depends on striking a judicious balance between ambition and realism.

2. Intermediate targets are essential for sustaining political commitment and ensuring accountability. The MDGs must be linked to the political agenda of today's government. Long-term goals, by themselves, are unlikely to help shape current policy reforms and action plan because the deadlines are too far in the future.

3. Actionable propositions and reforms must be formulated to make adequate progress towards agreed longer-term benchmarks. They will range from immunising children to iodising salt, training teachers and building schools, treating Aids patients and distributing bed nets, enforcing laws against gender discrimination, abolishing user fees for primary education and basic health care, and strengthening progressive taxation and re-allocating spending in favour of the poor.

4. Costing these actions and reforms will inform the national budget and aid allocations. National budget must adequately reflect the tailored and intermediate targets set under steps 1 & 2—a link that is often missing in practice. However, it would be ill advised to estimate the costs of the MDG targets over an extended period of time.[1] MDG costing will only yield results that have a reasonable degree of accuracy when done within a 2-3 year timeframe.

In short, global targets have their place but they have to be kept in their place. If the MDGs continue to be misinterpreted as a one-size-fits-all yardstick, a great silence is likely to befall them as the 2015 deadline draws closer.

Reference:
1. See Jan Vandemoortele & Rathin Roy, 2005, *Making Sense of MDG Costing*. Helsinki Process Magazine, Ministry of Foreign Affairs, Helsinki (Finland).

One Pager number 28
Published: January, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager28.pdf>

Why Not 'Front-load' ODA for HIV/Aids?

by John Serieux, Assistant Professor, Dept. of Economics, University of Manitoba and Terry McKinley, Acting Director International Poverty Centre

Global funds available to combat HIV/Aids are estimated to reach about US$ 9 billion in 2007. Although this amount will be only about half of what is needed, it is, nevertheless, substantial. Used effectively, such donor financing could help stem the pandemic's spread and mitigate its effects. In fact, disbursing the balance of such financing early on—'front-loading' it—should be a priority. But there is considerable resistance to doing so. Why is this the case?

Two major concerns predominate. Donors and recipient-country central banks worry about destabilizing the economies of countries. Recipient governments worry about the volatility of donor disbursement. So a gradual phasing in of ODA is often preferred, on all sides. But is this the approach best suited to confront a human development crisis of such magnitude? Moral imperatives aside, one can also make practical arguments that 'front-loading' would improve ODA's effectiveness.

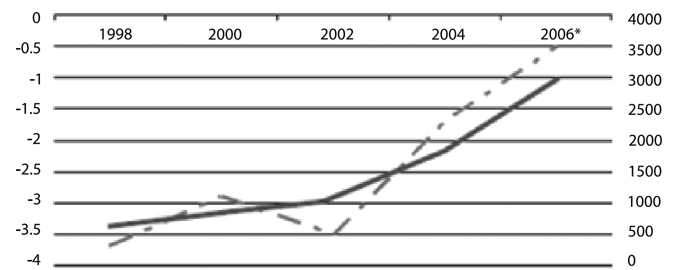
The effectiveness of ODA depends on three conditions:
(1) governments are able to use the ODA to increase spending aimed at combating the epidemic; (2) the foreign exchange provided through ODA is used to increase relevant imports; and (3) HIV/Aids spending reaches its intended target and is applied, quickly and effectively, to its intended objective.

However, recent trends in developing countries suggest that the first two of these imperatives are not being fulfilled. Governments are tightening up their budgets and thus not spending all available ODA. And central banks are stockpiling reserves instead of releasing them for needed imports. The Figure shows that in developing countries from 1998 to 2006 a) the fiscal balance of central governments moved from -3.7 per cent of GDP to only -0.5 per cent; and b) reserves rose from about US$ 691 billion to almost US$ 3 trillion.

In sub-Saharan Africa, the fiscal balance of central governments was projected to reach a surplus of 0.4 percent of GDP in 2006 (compared to -3.7 percent in 1998) while reserves were projected to reach about US$ 123 billion (compared to only about US$ 28 billion).

Governments have adopted an excessively cautious stance because of the numerous financial, debt and balance of payments crises of the 1990s. They are afraid, in particular, that more (ODA-related) spending will increase the prices of domestic goods and services. By causing wages to increase and the exchange to appreciate, such inflation would make the country's exports more expensive to produce and less competitive abroad. This is the so-called 'Dutch disease' effect. However, the evidence for this effect is weak. Moreover, if ODA is successful in mitigating some of the detrimental effects of HIV/Aids, it is likely to rule out such an effect by encouraging the use of excess capacity and improving all-round productivity. In this context, when governments spend the available ODA and central banks sell the corresponding foreign exchange, the related price and exchange rate effects are likely to be both moderate and transitory.

Fiscal Balance (% of GDP), dotted line
Reserves (US$ Billions), solid line



Source : IMF, world Economic Outlook 2006, Tables 18 & 35.* denotes projected.

ODA is urgently needed to treat the mounting number of people living with Aids and halt and reverse the deadly spread of the pandemic. In this fundamental sense, the sooner ODA is disbursed, the better. A maximal effort early on would also imply the need for less ODA in the future because fewer people would need to be treated and, by safeguarding human capabilities, higher future productivity would be assured. These are sufficient reasons for front-loading HIV/Aids financing.

However, there are other compelling reasons to adopt such a strategy. The effectiveness of government spending in combating the disease (i.e., whether expenditures are properly targeted and have their intended impact) depends on building up national capacities, in the form of extensive public investment in infrastructure, institutions and human resources. The sooner such capacities are created, the more effective ODA would be. This would imply that the marginal rate of return of even scaled-up future aid flows (the welfare impact per additional US dollar) would remain high.

The need to manage the volatility of ODA is further justification for front-loading ODA. Central banks should, indeed, have some latitude to accumulate international reserves (in combination with deferred spending by governments) early on so that they can smooth future expenditures if ODA drops. Having such a buffer is critical because once treatment of HIV/Aids is initiated, interruption (because of lack of funds) can be disastrous. But such a stance should not be confused with amassing reserves to protect the currency and short-circuiting the resulting monetary impact of government expenditures by 'sterilization' (which drives up interest rates). This latter approach contradicts the whole purpose of providing HIV/Aids financing and undermines its effectiveness.

Reference:

John Serieux. 2007. "Managing the Exchange Rate Consequences of Scaling up HIV/Aids Financing." Conference Paper for the international conference on "Gearing Macroeconomic Policies to Reverse the HIV/Aids Epidemic" jointly sponsored by IPC and the HIV/Aids Group of UNDP.

One Pager number 29
Published: February, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager29.pdf>

The Gross Inequities of Global Imbalances

by Terry McKinley, Acting Director, International Poverty Centre; and
Alex Izurieta, Visiting Scholar, Cambridge Endowment for Research in Finance

The huge size of current global economic imbalances is unprecedented. Such imbalances are both unsustainable and inequitable (see the IPC webpage on the State of the World Economy, e.g., Working Papers No.12 and No. 23).

A few rich countries are running large current account deficits. One in particular, the US, is running a deficit about 3.5 times larger than the deficits of all other OECD countries combined.

At the same time, a few rich and middle-income countries (Japan, Germany, China, Saudi Arabia and Russia) are running large current account surpluses. Prominent among these are big oil exporters and Asian exporters of low-cost manufactures, which deposit their surpluses in rich countries.

Why are these trends troubling? Do not all global surpluses and deficits balance out? Yes, in an accounting sense. While countries running large deficits have to borrow abroad to finance them, countries running large surpluses have correspondingly extra money to invest abroad. But in practical terms, the deficit countries can have problems in borrowing enough money abroad; and the surplus countries can have problems in obtaining a high enough rate of return on their investments.

The unhealthy US economy poses grave global risks: either the US dollar has to dramatically depreciate in order to reduce the country's trade deficit or US interest rates have to substantially rise to ensure attracting foreign investment. Or both.

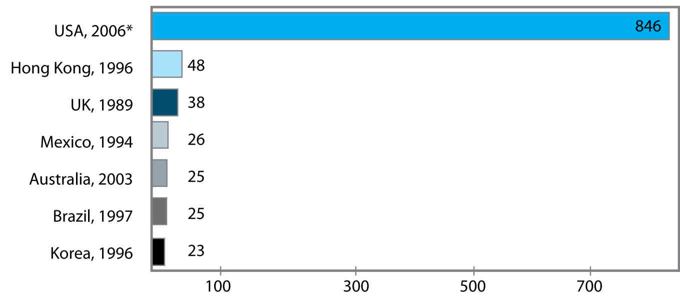
Normal exchange-rate and interest-rate movements might, under circumstances of small deficits and surpluses, be sufficient to correct global imbalances. But much more drastic movements, likely to destabilize global capital markets, would be needed to reduce the US current-account deficit—namely, about US$ 850 billion projected for 2006. This deficit is, by far, the largest ever recorded (see figure).

A positive solution to the US deficit will require international policy coordination. 'Market forces' will not solve the problem—unless they force an abrupt, devastating adjustment for all. The US's voracious demand for global goods and services is currently driving, for better or worse, the growth of many other economies. But this demand has to be slowed—preferably gradually—in order to rectify global imbalances. Absent a coordinated international response, the US economy could plunge into recession, destabilising the rest of the world.

Current global imbalances not only pose huge dangers; they also cause a grossly inequitable distribution of global resources. Capital is 'flowing uphill' to rich countries—overwhelmingly to one rich country, the US. A stark illustration of this inequity: the average US current account deficit in recent years has been one third *higher* than the total Gross Domestic Product of sub-Saharan Africa.

The money that many middle-income countries are now investing in the US could make a major contribution to development if it were redirected to poorer countries, or even kept within these middle-income countries. Because more goods and services would become available domestically, the population in such countries would enjoy a higher standard of living.

World's Largest Current Accont Deficits since 1970



*USA deficit for 2006 is an extrapolation of known figures over the first ten months of the year.

Currently, the US population is indulging in a standard of living that is six per cent higher than its own income, thanks to the mammoth and continuous inflow of capital from other countries. In global terms, the US is becoming a 'heavily indebted' country.

When a country runs an external deficit, major sectors of its economy must be spending more income than they receive. In the US, the most notable is the personal sector. Seduced by real estate appreciation and rising stock prices and encouraged by low interest rates, US households have hiked their net borrowing to over six per cent of national income in recent years. This profligacy cannot be sustained indefinitely.

Based, in effect, on borrowing money from other countries, US households have monopolized goods and services that could have a greater impact on global human welfare if they were consumed in poorer countries. Also, the US economy is enjoying a gargantuan inflow of financial resources that could be invested at a higher social rate of return by low-income and middle-income countries in their own development.

Since the US is enjoying the fruits of this inequitable imbalance in resource flows, it has limited motivation to correct it. An impending US economic collapse is probably the main factor that could impel national policymakers into action. An alternative solution, mutually beneficial to all, could be a coordinated effort by both developed and developing countries to stimulate domestic demand in regions other than the US.

Policies to stimulate domestic demand in Europe and Japan would help compensate for a slowdown in US demand. Substantially boosting demand, particularly domestic investment, in developing countries would be a priority for achieving an equitable resolution. For such countries, currently starved of development resources, such as for the MDGs, greater policy coordination is not an unrealistic ideal. It is an urgent necessity.

One Pager number 30
Published: February, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager30.pdf>

Privatising Basic Utilities in Africa: A Rejoinder

by John Nellis, International Analytics

In their IPC Policy Research Brief on "Privatising Basic Utilities in Sub-Saharan Africa: the MDG Consequences", Bayliss and McKinley are right to argue that (i) few private investors have taken much interest in water and electricity firms in Africa and of those that have, many have done a poor job; (ii) African governments were pushed into accepting private participation in basic infra structure by international financial institutions and donors; (iii) African governments still own and operate the bulk of the water and electricity sectors and public ownership in these crucial areas will continue for the foreseeable future; (iv) a larger percentage of the desperately needed capital to rehabilitate and expand these networks has to come from internal and 'official'—i.e., donor—sources; and (v) efforts to improve the operation of publicly-owned water and electricity firms have to be redoubled.

Since I agree with so much of their diagnosis, why do I still feel they have not offered the right prognosis and prescription? The reasons are three:

First, I believe the authors ***overestimate the ease of improving performance in state-owned firms***. In many African water and electricity utilities, reduction of system losses, improved maintenance, and network expansion were attempted for years prior to the privatization push. But under pure public management, the positive results, with or without donor assistance, were modest in the extreme. The problem in Africa is that: historically, publicly owned and managed utilities in these sectors, operating at less than cost-recovery tariffs, have delivered an inadequate quantity and poor quality of service; and they have delivered mainly to the better off segments of the urban population. What new and different methods of public management are being proposed to correct these failed past efforts? Perhaps they can be found in the longer study from which the Policy Research Brief is drawn; I find none here.

Second, they ***underestimate the amount of investment capital required in run-down African water and electricity sectors***. The financing needs are huge—much larger than any realistic increases in both internal revenue generation and donor funds. True, a number of past efforts to attract private investors have proven costly and counterproductive, but the fact remains that private capital must somehow be tapped if Africa is to repair and enlarge its basic infrastructure to meet ever-growing demand.

Third, ***the Policy Research Brief does not mention the promising 'hybrid' experiments that combine local African private management with public ownership***. For example, the Athi Water Services Commission (AWSC) is a hybrid mechanism to manage the water supply of the greater Nairobi area. The physical and financial performance of the traditional water department of the Nairobi City Council (NCC) had been disastrous. In 2000, donors recommended a lease contract to attract international private providers. The Kenyans rejected this advice and constructed the following: at the top, they created a new national water regulator (which will eventually set tariffs and monitor service quality, but does little right now). Next, the AWSC was created and its management procured from the Kenyan private sector—no non-Kenyans were allowed to bid. The team chosen basically consists of engineers who used to work in the city water department. They had to resign from government service to seek these new posts.

The AWSC is a corporation, a joint stock company. All of its shares are owned by the Nairobi City Council. AWSC was given a lease to manage the water production and distribution and the revenue collection in the area. It has to pay a small fixed percentage of its collections each month to the regulator and a much larger 'lease fee'—also a fixed percentage of revenues collected—to the NCC. It hires and supervises a water providing company, which is paid for its costs. As of 2006, all workers in the water providing company were former employees of the water department of the NCC. To reduce worker opposition to the scheme, this provider was not competitively procured; the former NCC employees were given the chance to prove themselves.

In its first 18 months of operation, AWSC succeeded in covering Operations and Maintenance costs due to much more rigorous collection efforts, even though the tariff had not changed, and even after subtracting the 15 per cent of revenues paid to the NCC and the regulator. Customer satisfaction is up considerably. Performance has definitely improved. But AWSC is covering only variable costs (though this in itself is an uncommon achievement). It has also inherited substantial debt that is not being serviced. AWSC is negotiating with the NCC and the central government to reduce this burden, attributable to the poor management of the past.

Depreciation of capital is not being covered, nor is there yet any surplus for crucially needed investments and expansion. The hope is that in the short term donors will meet these needs—the French have already contributed a modest amount and negotiations are planned with the World Bank.

To be sure, this is a first and partial step, with a number of problems still unresolved, chief among them the lack of a solution to the critical investment problem. But it is a promising combination of private management and public ownership that just may generate more private money. Similar schemes of this sort are in progress in several other African cities.

So, in a nutshell, the solution is not to eschew private investment, but rather find mechanisms to make it more politically acceptable, more socially responsible and more mutually beneficial.

Reference:
Kate Bayliss and Terry McKinley, "Privatising Basic Utilities in Sub-Saharan Africa: The MDG Impact", IPC Policy Research Brief No. 3, January 2007.

One Pager number 31
Published: April, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager31.pdf>

Debating the Provision of Basic Utilities in Sub-Saharan Africa: A Response to Nellis

by Kate Bayliss, Independent Consultant, Brighton, UK; and
Ben Fine, Professor of Economics, SOAS, University of London

Both delight and surprise are prompted by John Nellis' One Pager No. 31, a rejoinder to the Bayliss and McKinley IPC Policy Research Brief No. 3 on "Privatising Basic Utilities in Sub-Saharan Africa". The Brief reports on the book edited by Kate Bayliss and Ben Fine, *Privatization and Alternative Public Sector Reform in Sub-Saharan Africa: Delivering on Electricity and Water* (Basingstoke: Palgrave MacMillan).

The book inevitably goes beyond material covered in the Brief. It offers a swingeing and detailed critique of World Bank thinking and policy on privatisation, including a heavy dose of scepticism about the Bank's current *mea culpa*: "we were wrong; we privatised too much too soon and without preconditions in place". The Bank has partly come to its senses because, despite ample support for privatisation and exaggerated promises for its performance, it has performed miserably in sub-Saharan Africa.

The time is indeed ripe for a thorough 'rethink', which would involve giving the public sector a fair crack at the helm. Appearances to the contrary, this is not what the World Bank or Nellis is proposing. Their priority is to continue supporting the private sector whilst exhorting the state to build up capacity—but primarily to support private-sector, not public-sector, provision of utilities. The easiest privatisations are over; privatisation is now evidently floundering. So the state must work even harder, they argue, to make it a success. No assessment is given of what might be achieved by devoting the same resources and commitment to public sector provision. And this stance continues despite the admission, confirmed by Nellis, that the provision of electricity and water in sub-Saharan Africa will remain mostly the responsibility of the state.

Such is the context for Nellis' rejoinder. For twenty years his position on privatisation has reflected, even informed, that of the World Bank—starting with cautious endorsement of privatisation, followed by a full-scale embrace and, finally and most recently, culminating in implicit acceptance of its failings. His current five-point acceptance of our diagnosis is welcome. Delivering basic utilities in sub-Saharan Africa is no easy task. But the privatisation experiment has made it worse, by eroding state capacity or preventing it from being expanded.

Like the World Bank, Nellis is no longer committed dogmatically to a 'one size fits all' privatisation model. As mentioned, the priority of the new model is to get the state to support the private sector rather than simply leaving it to its own devices. This is apparent in his closing sentence: "So, in a nutshell, the solution is not to eschew private investment, but rather to find mechanisms to make it more politically acceptable, more socially responsible and more mutually beneficial".

To be fair, whilst accepting our diagnoses, Nellis does tax us on three points. The first is that we 'overestimate' state capacity in sub-Saharan Africa. He offers no evidence for this assertion, most likely because no estimate has been made. Our point is that the privatisation experiment has clearly over-estimated the capacity of the private sector. More importantly, Nellis accepts that public service provision will be predominant into the foreseeable future and, by implication, that it will have to be the focus of efforts at reform and capacity building—irrespective of its current failings.

Nellis reasonably questions how this might be done. This is a positive step over presuming that it cannot. He correctly anticipates that we address this crucial point in our book, putting forward the 'public sector system of provision' approach (pssop). This does not start from (private) market *versus* (public) state provision but from the specificities of each country and sector, in terms of practice and potential. For this approach, presumptions about under- or over-estimation of state capacity are beside the point: public service delivery must be addressed and evaluated as an option.

The second point relates to Nellis' assertion that we under-estimate the need for private capital to fill the huge investment gap in Africa. But private capital has already failed to fill the gap. This is why the new Bank model encourages ever increasing efforts by the state (as well as consumers) to absorb higher levels of risk to satisfy the guarantees now demanded by private investors. Crucially, private capital comes at a price, and one that is not necessarily cheaper than public finance. We are not precluding the participation of private capital, but we situate it within the economic and social functioning of a country as a whole and try seriously to weigh alternative forms of public and private financing of provision.

Nellis' third point relates to his positive example of the Athi Water Services Commission, billed as a hybrid of private management and public ownership (a project which was undertaken, not coincidentally, against donor advice). We give other examples of such initiatives in our book. Some work, some do not. This project, by Nellis' own account, is far from ideal. Most critically, it fails to address the lack of investment finance. What is significant, though, is that Nellis still assumes that private sector management can work but public sector management cannot. Such presumptions became self-fulfilling, in fact, during the era of privatisation when the capacity for public service provision was systematically undermined.

So, in a nutshell and as a counterpoint to Nellis, our solution is "not to eschew ***public investment***, but rather to find mechanisms to make it more politically acceptable, more socially responsible and more mutually beneficial".

One Pager number 32
Published: April, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager32.pdf>

MDG Targets:
Misunderstood or Misconceived?

by Hamid Tabatabai, Senior Economist International Programme on the Elimination of Child Labour (IPEC) International Labour Office, Geneva

In a recent One pager entitled "MDGs: Misunderstood Targets?", Jan Vandemoortele seeks to correct a "common misunderstanding… in the conventional view on the MDGs". He notes that "the MDGs are essentially an extrapolation of global trends of the 1970s and 1980s and projected forward till 2015… Thus, assessing whether progress is 'on track' for meeting the targets by 2015 can only be done at the global level… It is erroneous, for instance, to lament that sub-Saharan Africa will not meet the MDGs. These targets were not set specifically for that region." The same applies, a fortiori, at the country level as well. This One pager argues that if Vandemoortele were right, the MDGs are not so much misunderstood as misconceived.

Vandemoortele was the co-chair of the UN inter-agency group that put the MDGs together. His contention, therefore, could in principle be presumed to represent the 'official' view. It appears however to be at odds with numerous documents that suggest otherwise, at both regional and national levels. For example, the UN Millennium Project's main report is replete with statements such as "[t]he countries of East Asia have, as a group, moved closer toward achieving the Goals, but progress has been uneven within the region, within countries, and across the Goals. Some countries have already come close to achieving most of the Goals and have even committed themselves to more ambitious, MDG-plus targets, but others remain significantly off track for meeting the original Goals" (2005, p. 161).

More importantly, Vandemoortele's interpretation would rob the MDG framework of much of its force, if not of its very *raîson d'être*. There are several reasons. The first has to do with the MDG targets being merely extrapolations of historical trends. If that is all that one is aiming for, why bother at all? Ensuring that past trends would continue does not seem to call for all the fuss that surrounds the MDGs. A worthy justification for setting such targets would be to induce greater efforts to improve on past performance. The MDGs were presumably meant to accelerate trends through reforms in developing countries on the one hand, and increased flows of aid and investment from developed countries on the other.

Secondly, the fact that quantitative targets are based on *global* trends is not in and of itself a reason for not applying them at other levels, such as regional or national. Indeed the UN Millennium Project's Report explicitly interprets the MDGs as "country goals, since this is the spirit in which they are pursued the world over" (p. 3).

Thirdly, past trends are averages of diverse experiences. Some countries obviously lie below the average. One purpose of setting past trends as target could be to encourage weak performers to lift themselves up to the average level. This would also pull the average up. If this were the intention, the MDG targets would have to apply at the regional and national levels, not at the global level from which they are derived. It is not necessarily true that "[i]nterpreting the MDGs as a uniform yardstick will *inevitably* condemn more than half of the countries to the category of 'poor' performers…" (emphasis added). This would only be the case if past trends persisted, not when they accelerate. It is in principle possible for every country in a group to do better than the group average in the past.

Finally, if the MDGs were meant to be tracked only at the global level, why would so many countries try to reach the MDG targets at the national level? Clearly, many countries seem to find a conservative interpretation of the MDGs—that they apply only at the global level —inadequate and have adopted them on their own. Indeed, it is Vandemoortele's own organization, the UNDP, that is leading the MDG monitoring efforts and insisting on reporting at national level!

Vandemoortele however is surely right that "[i]t would be a tragic misunderstanding of the MDGs if …countries [missing the global targets] were to be classified as 'failures'… " There could indeed be any number of perfectly legitimate reasons why some countries might fall short of historical trends at the global level or any other quantitative targets, however set. The real yardstick for judging performance and effort is whether they have done the best they could under the circumstances.

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Vandemoortele, Jan. 2007. "MDGs: Misunderstood targets?". International Poverty Centre. One pager No. 28. January.

One Pager number 33
Published: April, 2007
Available at: <*http://www.ipc-undp.org/pub/IPCOnePager33.pdf*>

Why Is Africa Constrained from Spending ODA?

by Terry McKinley, Acting Director, International Poverty Centre

Attaining the MDGs in sub-Saharan Africa calls for a dramatic scaling up of Official Development Assistance. Yet governments have been constrained from spending the bulk of aid received in recent years. If aid cannot be spent, donors might ask: why give it? A better question is: what is preventing the spending?

A recent report by the Independent Evaluation Office of the IMF, "The IMF and Aid to Sub-Saharan Africa" supplies part of the answer. Governments in low-income countries bound by an IMF Poverty Reduction and Growth Facility (PRGF) spent, on average, only 28 per cent of their ODA receipts during 1999-2005. If their inflation rates exceeded five per cent, they spent, on average, only 15 per cent.

Inflation has been a preeminent concern for the IMF. A five per cent inflation threshold has been the trigger for its decisions about whether countries could spend aid or not. In other words, safeguarding macroeconomic stability—restrictively defined—has taken precedence over spending ODA.

What has been the IMF's justification? It has argued that ODA-financed government spending on domestic goods and services (not traded internationally) would outstrip their domestic supply. This would drive up the general price level and appreciate the country's exchange rate, damaging exports and economic growth.

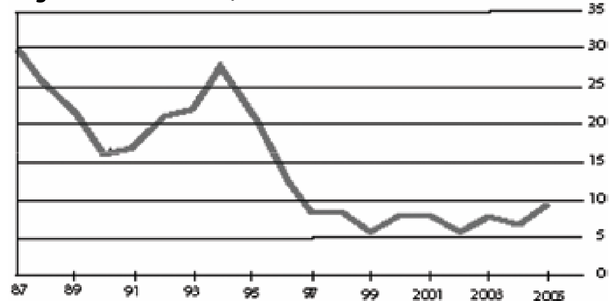
Yet, IMF's own research suggests that inflation rates of 5-10 per cent in Africa are not likely to harm growth. The IMF also now recognizes that adverse supply shocks (such as spikes in oil or food prices) could temporarily drive inflation above 10 per cent. Other credible research has found that the threshold below which inflation remains benign is 15 per cent, or even higher.

In contrast to the experience of some other regions, Africa has not experienced, on average, severe bouts of inflation. In the 1980s, its average inflation was below 25 per cent, and never exceeded 30 per cent. Beginning in 1994, its inflation plummeted, remaining anchored between five and 10 per cent during the PRGF years of 1999-2005 (See Graph). Similarly, its average fiscal deficit shrank rapidly: from about seven per cent of GDP in 1994 to almost two per cent in 1997. By 2005, it was a little less than two per cent.

When ODA to Africa began to increase in recent years, the IMF was not prepared to reverse gears on targeting such low inflation rates. Fiscal deficits (excluding grant financing) should have been increasing, not decreasing, in response to an upsurge of ODA. Instead, central banks channeled ODA into paying off domestic debt—including government debt held by central banks.

IMF practice has not kept pace with its own theory. In line with the logic of macroeconomic accounting, the IMF has recently asserted that the ideal scenario in response to a scaling up of ODA is that it be fully spent and 'absorbed'. In other words, not only should the government fully spend the domestic currency equivalent of ODA but also the central bank should eventually sell the corresponding ODA-supplied foreign exchange in order to facilitate greater imports (i.e., 'absorption'). Otherwise, ODA would not end up financing the transfer of additional real resources into the economy.

Average Inflation in Africa, 1987-2005



Source: *IMF Economic Outlook* database.

If ODA is not converted into payments for imports, it has to become a financial claim on foreign assets (either central bank foreign-exchange reserves or privately owned assets abroad). The same evaluation cited above finds that only 63 per cent of ODA was 'absorbed'; the remaining 37 per cent was used to accumulate foreign-exchange reserves or fuel private capital outflows. Just during 1999-2005, reserves in Africa increased from about three per cent of GDP to about 4.5 per cent. While using ODA to initially accumulate a modest cover of international reserves might make sense (especially in the face of future aid volatility), excessively stockpiling reserves implies that the central bank is undercutting the purpose of aid, namely, to transfer real resources into a country.

An overriding problem is that the monetary policy of central banks can often place tight restrictions on the scope of government fiscal policies. If central bank inflation targets are set below five per cent, governments are reluctant to spend ODA because of the fear of accelerating inflation above that threshold. They are also reluctant to widen fiscal deficits in order to increase MDG-related expenditures—even when such widening is financed by grants. And when the central bank does not sell reserves, it has to 'sterilize' the monetary impact of aid by selling government securities. This tends to drive up the real rate of interest and undercut fiscal expansion.

For ODA to have its full impact on expanding MDG-related expenditures, fiscal policies and monetary policies need to be coordinated. Fiscal policies should ensure that ODA is fully spent while monetary policies should ensure that ODA is fully absorbed. But under current policy regimes dominated by central banks, the role of fiscal policies has been no more glorified than containing deficits.

Such a regime has erected an imposing MDG roadblock. MDG-oriented development strategies clearly rely on more expansionary (ODA-financed) fiscal policies. Much of the increase in ODA will have to expand public investment to build more schools, health clinics, maternity wards, rural roads and irrigation systems. So, monetary policies should accommodate more expansionary fiscal policies. Instead, restrictive 'inflation-focused' monetary policies are currently blocking the fiscal expansion necessary for progress on the MDGs in Africa.

One Pager number 34
Published: May, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager34.pdf>

The IMF and Constraints on Spending Aid

by David Goldsbrough, Visiting Fellow, Center for Global Development (CGD)[1]

In a recent IPC One pager, Terry McKinley asks why Africa is being constrained in spending aid (IPC OP No. 34, 2007). He implicates "restrictive, inflation-focused monetary policies" sponsored by the IMF as the primary agent blocking fiscal expansion. I agree that the IMF has been overly conservative in formulating fiscal strategy in many programmes with low income countries. However, the core of the problem is not inflation targets. The main issue is the implicit assumptions the IMF makes—often without much supporting evidence—about how the real economy will respond to changes in fiscal deficits and public spending.

Our understanding of the links between macroeconomic policies and ultimate objectives such as growth and progress towards the MDGs is quite limited—much more so than the IMF, or its critics, often imply. In light of this uncertainty, humility is in order and choices on the utilization of additional aid should, to the maximum extent possible, be left to national political processes to decide. For example, following debt relief, the range of fiscal paths (for deficits, spending etc) that are feasible—in the sense of not risking renewed debt distress or macroeconomic instability—is greater than many IMF programmes would suggest.

A recent report by the Independent Evaluation Office (IEO) of the IMF, "*The IMF and Aid to Sub-Saharan Africa"* has triggered controversy about the IMF approach. The report suggests that IMF programmes target only 27 cents of each dollar of additional aid to be channelled to higher public spending. But results vary widely from country to country. The study, which used regressions to examine the relationship between *expected increases* in aid and programmed uses of that aid, allows for two important insights: i) results explain only a small part of the variation across programmes; and ii) they do indicate that the IMF programmes depend critically on a country's starting conditions. (Both results suggest the IMF is not pursuing a "one size fits all" approach).

If external reserves are low (less than 2 ½ months of imports), virtually *all* additional aid is programmed to be saved in higher reserves. If reserves are higher, but domestic macro-conditions fail a high test of stability—which the IEO proxied by inflation of 5 percent or lower— the vast bulk of extra aid (85 cents on the dollar) is channelled to reducing domestic debt. Only when reserves are high and domestic macro-conditions are highly "stable", most additional aid is programmed for higher fiscal spending.

These results suggest a very conservative policy stance. The IMF is right to take account of the level of reserves and domestic macro conditions when considering how additional aid should be used, but the *degree* to which these factors influence aid allocation seems excessive. Using part of any initial increases in aid to rebuild reserves is appropriate, but the share allocated to reserves should depend on how long the higher aid is expected to last. IMF programmes seem to assume that *all* aid increases will be temporary.

Unfortunately, the IEO results have been interpreted as implying that the level of inflation targeted in IMF programmes is the main issue. The IEO used the initial inflation rate, rather than a measure of domestic public debt, as the sole indicator of domestic macro stability because the internal database used by the IMF on performance under its programmes does not have good data on domestic debt. This lack is certainly shocking given the emphasis the IMF has placed on reducing such debt levels and makes it harder to tell what is really driving the fiscal design. However, both recent CGD work and earlier IEO evaluations suggest that the design of IMF fiscal programmes is heavily influenced by several implicit assumptions about how the economy will respond to fiscal expansion or tightening. In practice the country-specific empirical evidence is often quite limited:

- Programmes often assume that lower fiscal deficits, especially with domestic financing, will lead to higher private investment (through lower interest rates etc). In practice, the private sector response depends on many other policies and country-specific factors. IMF programmes have systematically overestimated the size and speed of such responses.
- The longer-term supply-side effects of higher public spending are, with some commendable recent exceptions, largely ignored in many macroeconomic frameworks. The main IMF focus is on the shorter term; programmes frequently lack concrete medium-term expenditure plans whose longer-term effects can be analysed. Yet, assessing the appropriate medium term fiscal path requires some judgment on the likely impact of higher public spending.
- Many programmes combine a conservative approach to initial projections of aid (to avoid programmes being underfinanced) with conditionality that calls for higher-than-expected aid to be saved and temporary aid shortfalls to be matched by spending cuts. Such an asymmetric approach reflects implicit assumptions about the duration of aid increases; it also tends to downplay the costs of temporary disruptions to spending, which can be high (e.g. in the health sector). Only recently have programmes begun to give greater emphasis to expenditure smoothing.

Addressing these three aspects of IMF programme design is, in my opinion, much more important than the concern about excessively low inflation targets. That is not to say that the IMF approach to inflation and monetary policy has always been right. It might well have given too much emphasis to achieving very low inflation in Africa. But reversing the recent gains on inflation is not going to yield higher growth, and might detract attention from other, more fundamental problems with the way IMF fiscal programmes are formulated.

Reference:

1. David Goldsbrough is chair of a CGD Working Group on IMF Programs and Health Spending.

One Pager number 35
Published: May, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager35.pdf>

Can all Cash Transfers Reduce Inequality?

by Sergei Soares, Institute of Applied Economic Research (IPEA); and
Eduardo Zepeda, International Poverty Centre

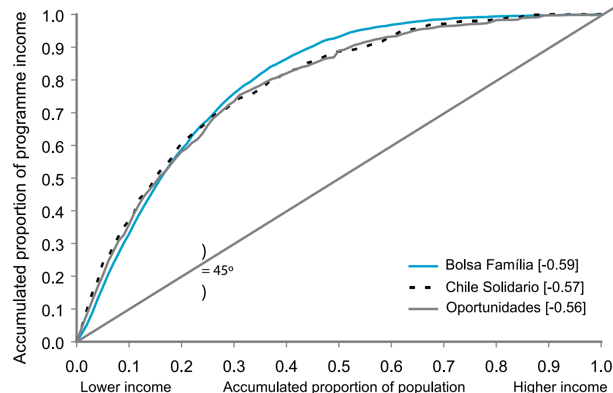
Over the last decade or so, Conditional Cash Transfer (CCT) programmes have proliferated in Latin America and beyond. CCTs are designed to reduce poverty, both in the short and the long term. These programmes usually provide a cash transfer to poor families, conditioned on children's school attendance and regular medical checks-ups of both children and pregnant women. CCTs are seen by many national governments and multilateral agencies as a cost-effective instrument to reduce poverty and provide the poor with opportunities. Overall, the sum of all transfers represents a very small share of national budgets and, obviously, even smaller fractions of national incomes. Still, CCTs *can* have a significant impact on poverty and inequality.

There is an extensive list of studies showing that CCTs reduce poverty, improve education and health outcomes, and alleviate various other sufferings of the poor, such as child labour and child mortality. There is also a heated debate on whether cash transfers should be conditional or not. However, not much has been discussed about their impact on the unacceptably high income inequality that has tormented Latin America for centuries. A recent paper examines the impact of such programmes on inequality in the three countries currently applying the best-known CCTs, i.e., Brazil's *Bolsa Família*, Chile's *Chile Solidario*, and Mexico's *Oportunidades*. These three countries also happen to have solid national statistical systems and household surveys covering periods of reference before and after implementation of their respective CCT programme, which allows good impact evaluation.

These programmes differ from one another in several ways. *Bolsa Família* and *Oportunidades* are both large programmes, covering respectively 11 and 5 million beneficiary households in 2004, but they diverge in the way targeting takes place. While *Bolsa Família* is a highly decentralised programme where targeting is the responsibility of municipal governments, *Oportunidades* undertakes massive surveys of poor areas to choose the target population through a much more centralised mechanism. By contrast, *Chile Solidario* is a small programme covering only about 225,000 households. It targets the extremely poor through a national system that registers beneficiaries on the basis of intense monitoring of families conducted by social workers.

The impact of CCTs on inequality can be gauged from the most widespread measure of income distribution, namely, the Gini coefficient. Total household income derives from several sources: labour, pensions, social security and CCT transfers, among others. Changes in the Gini coefficient can be broken down into changes in each income component. How much any given component actually contributes to the total change in inequality can in turn be indicated by the change in inequality of that component ("the concentration coefficient") and by the change in the component's share of total income.

Targeting Performance



All three CCTs examined show outstanding targeting results. Their concentration coefficients are close to –0.5, i.e. nearer the perfect pro-poor coefficient of -1 and far from the least pro-poor, +1. This can also be seen in the diagram, which shows concentration curves for the CCT component of total income in each country. For reference, the graph also shows the 45º degree line that assigns the same income to everyone in the population. Since all three concentration curves pass far above that line, the implication is that CCTs are transferring income to the poorest, thus reducing inequality. Remarkably, despite differences in the targeting mechanism, the effectiveness in reaching the poor is similarly high in the three programmes considered.

The reduction in inequality produced by *Chile Solidario* had only a small impact, changing a meagre 0.1 point in the Gini coefficient. Inequality in Mexico and Brazil, on the other hand, fell by 2.7 points. The key to understanding these results can be found in the share of total income that such transfers represent. The well-targeted income transfers of *Oportunidades* and *Bolsa Família* are sufficiently large to produce a significant reduction in inequality, even though they are small (close to 0.5%) in relation to total national household income in Brazil and Mexico. By contrast, the transfers of *Chile Solidario* are so small (less than 0.01% of total household income) that even with very good targeting they cannot make a dent in inequality.

Much remains to be discussed about CCTs, not least whether transfers should be targeted or universal and whether they should be conditional or unconditional. This brief analysis of three conditional cash transfer programmes and inequality suggests two particular issues for further discussion: (i) the choice among alternative ways to design an effective targeting mechanism; and ii) the optimal scale and income-targeting threshold that can ensure a meaningful impact on inequality.

Reference:

Sergei Soares, Rafael Guerreiro Osório, Fabio Veras Soares, Marcelo Medeiros and Eduardo Zepeda; "Conditional Cash Transfers in Brazil, Chile and Mexico: Impacts upon Inequality." IPC Working Paper No. 35. April 2007.

One Pager number 36
Published: May, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager36.pdf>

Using ODA to Accumulate Foreign Reserves in Sub-Saharan Africa

by Costas Lapavitsas, Reader in Economics, SOAS, University of London

Donors of foreign id expect it to boost investment and aggregate demand by transferring real resources to recipient countries. Such transfers are essential to sub-Saharan Africa (SSA). Furthermore, attaining the Millennium Development Goals (MDGs) calls for substantial increases in aid in order to strengthen domestic investment and welfare expenditures.

Yet, the IMF has been encouraging some of the poorest countries in SSA to adopt restrictive policies that prevent the transfer of real resources from abroad, including capital imports. A recent report by the Independent Evaluation Office of the IMF, *The IMF and Aid to Sub-Saharan Africa, 2007*, found that SSA countries with an IMF Poverty Reduction and Growth Facility (PRGF) spent an average of only 28 per cent of aid flows during 1999-2005.

This 'low spending' policy has aimed at avoiding increases in inflation above five per cent, the low threshold set by the IMF. However, this target is excessively restrictive, as has been argued in the One Pager '*Why is Africa Constrained from Spending ODA*'.

This One Pager on foreign reserves focuses, instead, on the lack of 'absorption' of ODA. According to the same IMF report, only 63 per cent of aid flows to sub-Saharan Africa were 'absorbed' during 1999-2005. The remaining 37 per cent were used to stockpile reserves. Countries with international reserves equivalent to less than 2.5 months of imports used aid almost exclusively to boost reserve levels, 'absorbing' next to none. Those above this threshold allowed much fuller 'absorption'. This practice is linked to the adoption of capital account liberalisation, which allows capital to flow freely out a country.

'Absorption' is a technical term referring to a widening of the current account deficit that corresponds to the transfer of real resources to an aid-recipient country. Absorption is controlled by the central bank since it can make aid-related foreign currency available to importers or keep it in reserves.

Using aid to build reserves can be a reasonable policy for a short period of time if aid is volatile and reserves are very low. But the policy of building reserves in SSA has continued for several years, and built up levels well beyond the 2.5 months threshold.

The table shows that aggregate reserve levels in SSA rose from 3.7 months of imports in 1997-2001 to 5.2 months in 2006, and are expected to reach 5.6 months in 2007. The increase has been driven by oil exporters, such as Nigeria, which are currently accumulating oil rents. But reserves have also risen well beyond 2.5 months of imports for many of the poorest countries, such as Guinea-Bissau, Mali and Sierra Leone.

Rising reserves in Africa are part of a general trend (encouraged by the IMF) of reserve accumulation among developing countries since the financial crises of the late 1990s. Developing-country reserves as a proportion of imports are now roughly three times

Reserves, Sub-Saharan Africa, (Months of imports)

	1997-2001	2002	2003	2004	2005	2006	2007e
Ghana	1.4	2.0	4.1	3.7	3.2	3.2	3.1
Guinea-Bissau	5.5	11.8	3.8	6.9	6.3	8.1	7.5
Kenya	2.8	3.8	4.2	3.3	3.1	3.6	3.7
Madagascar	2.6	4.2	2.8	2.9	2.9	4.0	4.1
Mali	4.1	6.7	7.8	6.4	5.6	5.6	6.1
Niger	1.7	3.1	4.6	3.6	2.8	4.3	3.5
Senegal	2.8	3.7	5.0	5.2	4.0	3.9	3.7
Sierra Leone	3.0	3.0	2.0	4.1	4.2	7.8	7.1
Zambia	1.3	4.1	1.7	1.7	2.5	3.0	3.2
SSA Total	3.7	3.8	3.4	4.2	4.6	5.2	5.6

Source: IMF, *Regional Economic Outlook: Sub-Saharan Africa, 2007*. 'e' means estimated.

those of developed countries. On average, they are estimated to be about 25 per cent of developing-country GDP. Most countries regard them as protection against sudden reversals in capital flows and ensuing financial panics, or continuous capital flight.

The policy of the excessive build-up of reserves is a response, in large measure, to capital account liberalisation and the free movement of capital that have made access of countries to liquidity essential. Since the late 1990s, moreover, developing countries have accumulated substantial short-term debt, for which rising reserves have functioned as liquid cover.

The costs and risks of such a policy are significant, however. A large proportion of reserves are held by central banks as low-yielding U.S. Treasury securities while the return on investment in productive assets would be much higher. There is also considerable risk because a fall in the value of the U.S. dollar could lead to losses in terms of the corresponding value of domestic currency.

It is misleading to call reserve accumulation 'self-insurance'. The policy was forced on developing countries by liberalised international capital flows and financial deregulation. There is thus a good case for actively managing the capital account, and thereby lessening the need for a large low-yield stock of reserves.

In sub-Saharan Africa reserve accumulation also represents a defence against aid volatility. Building up such a buffer would be unnecessary, however, if donors could provide more predictable flows. This problem is only compounded by the IMF's encouragement of 'low absorption' of ODA. Instead of financing real resource transfers into the economy, a sizeable proportion of aid money has been committed needlessly to securing greater liquidity.

Fiscal and monetary policies have become correspondingly conservative, choking off the prospects for greater public and private investment and more rapid growth. Hence, for many reasons, the current practice of excessive reserve accumulation acts as a substantial barrier to attaining the MDGs, especially the priority goal of halving extreme poverty in the low-income countries of sub-Saharan Africa.

One Pager number 37
Published: June, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager37.pdf>

Correcting Global Imbalances with Exchange Rate Realignment? No thanks!

by Francis Cripps; Alex Izurieta and Terry McKinley[1]

Global financial imbalances have recently been fading from the headlines. One reason might be the strong growth performance of the global economy, for both developed and developing countries, despite signs of a mild slowdown in the United States. Another reason might be optimism about self-regulating market mechanisms, best represented perhaps by the views of the International Monetary Fund in the latest *World Economic Outlook* (April 2007, pp. 106):

The analysis in this chapter of historical episodes of large and sustained imbalances and their reversal clearly suggests that a market-led realignment of real exchange rates can play an important complementary role to demand rebalancing across countries to facilitate a smooth unwinding of external imbalances.

We cannot share, however, this optimism, particularly about the effectiveness of exchange-rate realignment. Global imbalances are much larger than ever before. The last instance of a widening U.S. deficit, in the mid-1980s, could be sorted out amongst a small club of rich countries. Yet, its correction took nearly four years, required a 30 per cent dollar devaluation and triggered a recession.

This time the current account of the U.S. is twice as large as its peak deficit of the 1980s (as a per cent of GDP) despite a 17 per cent dollar devaluation over the last five years. The counterpart surpluses are widely distributed amongst both developed and developing economies. Moreover, the size of global capital markets is many-fold greater than in the 1980s, with the consequence that the required currency realignment could have a major impact on the distribution of global wealth as well as income.

Using the Cambridge-Alphametrics Model (CAM),[2] a World Macroeconomic Model, to explore various policy scenarios, we conclude that exchange rate realignment in the current state of the world economy is close to a 'beggar-thy-neighbour' recipe, favourable, at best, to the United States (assuming no retaliation from other countries).

A real depreciation of the U.S. dollar *vis-à-vis* the currency of its trading partners at a rate of around five per cent per year would cause a slowdown of the world economy from about five per cent per year in 2006 to around two per cent in 2015. The U.S. economy slows down only from a trend rate of growth of three per cent to 2.5 per cent by 2015. But its current account deficit is reduced from its trend by less than one percentage point of GDP. Meanwhile, the rate of growth elsewhere in the world is cut. For the developing world, the reduction is from seven per cent per annum to just above two per cent.

If real depreciation in the U.S. is accompanied by real appreciation in the Asian region alone (Japan, China and the rest of Asia), the turn-around of deficits and surpluses would be more significant. Japan's surplus would be reduced in 2015, while the surpluses of China and Asia would evaporate (Figure 1). However, Figure 2 shows that growth performance turns out to be much worse for Asia: there is recession in Japan, growth plunges to nearly zero in China and slows to about two per cent in the rest of Asia. However, the U.S. manages to regain its trend growth of about 3 per cent in about five year.

Figure 1: Current Account ($ Bn.)

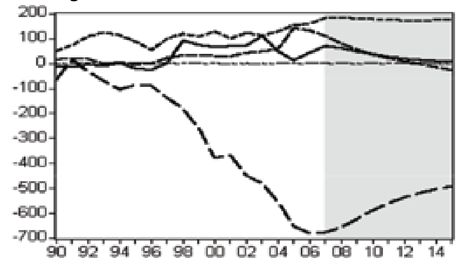
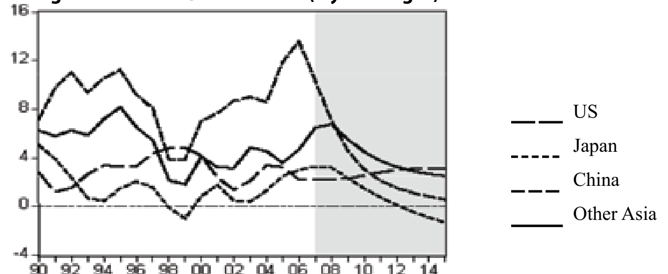


Figure 2: Annual Growth Rates (2 yr averages)



Of course, any model is only a rough approximation to a complex reality. So its results should be treated with caution. But it is not difficult to identify why there are likely to be such adverse outcomes from exchange-rate realignments. The reduction of net exports in the regions with appreciating exchange rates weakens their income growth; this effect reduces, in turn, their ability to import from the regions that experience exchange-rate depreciation. The net aggregate effect is that global income growth could be significantly slowed. The outcome could be worse if a corresponding disruption of capital markets causes volatility in investment.

Demand rebalancing, supported by the IMF as the complementary remedial measure, can in principle provide a more effective and mutually beneficial solution. The growth of domestic demand would have to slow in the U.S. while it increased in countries with current-account surpluses. But this would require a degree of coordinated international efforts that is unlikely to occur as long as international financial institutions continue to believe in the magic of market mechanisms. They cannot acknowledge the prospect that current mammoth global imbalances could result in an abrupt, drastic and mutually destructive correction.

References:

1. Director, Alphametrics Co., Ltd; Visiting Scholar, Cambridge Endowment for Research in Finance, University of Cambridge; Acting Director, International Poverty Centre, Brasilia.

2. The model has been developed by the Cambridge Endowment for Research in Finance and Alphametrics from an original version created by the Cambridge Economic Policy Group in the early 1980s. Its development has been supported by the International Poverty Centre, Brasilia. A detailed account of the model can be found in Cripps, Izurieta and McKinley (2007), 'Developing a global model for trade, finance and income distribution', *IPC Technical Paper No.1*, February. See IPC Research Programme, The State of the World Economy.

One Pager number 38
Published: June, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager38.pdf>

Raising Domestic Revenue for the MDGs: Why Wait until 2015?

by Terry McKinley, Acting Director, International Poverty Centre[1]

Financing MDG-based national strategies has focused, so far, on scaling up ODA. Mobilising domestic revenue, by contrast, has been neglected, despite being a better long-term option. There are various reasons: pessimism about raising revenue, a prevalent 'small-state' ideology and a preference for ODA-led solutions.

The development community seems content to emphasise mobilising domestic revenues after 2015. *Is such an* oversight justified? This One Pager believes not. It stresses domestic revenue mobilisation—starting now—as crucial to achieving the MDGs and any longer term development goals.

In order to highlight this issue, we examine trends in revenue mobilisation in a representative sample of 26 low-income countries in sub-Saharan Africa, comparing two periods, 1990-1995 and 2000-2005. The figure captures the major trends in total revenue and its two chief components, tax revenue and nontax revenue.

Total revenue increased by less than two percentage points of GDP, i.e., from 14.1 per cent to 15.9 per cent. This was driven by increases in tax revenue, with no discernable change in nontax revenue. Substantially more could have been achieved. The goal for 2006-2015 should be to double the average increase to four percentage points.

Even the modest increase achieved appears to be recouping an earlier loss of revenue. Total revenue for a representative sample of low-income countries in the early 1980s was 18-19 per cent of GDP. It dipped under 17 per cent in the 1990s and only recovered to 17-18 per cent in the early 2000s.

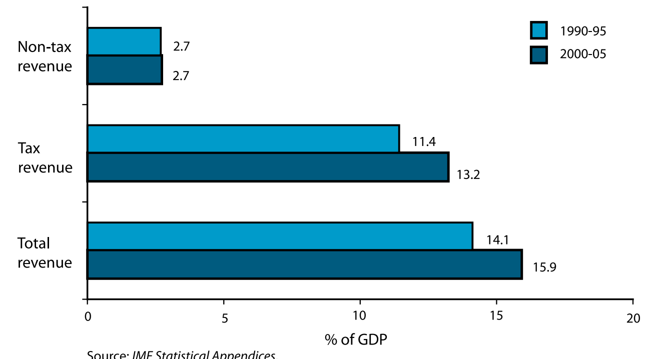
Recession or stagnant growth in many countries in the 1980s and 1990s is part of the explanation. The mistaken idea that governments in low-income countries were too big—and thus should be downsized—also partially explains the trend. And faulty tax advice from international financial institutions also played its part.

Governments had been advised to lower trade tariffs and institute, instead, a value added tax (VAT). They had also been advised to lower rates on direct taxes on personal income and corporate profits. As a result, trade taxes dropped markedly in sub-Saharan Africa from the early 1990s to the early 2000s, but the VAT recouped less than one third of the loss. Meanwhile, revenue from direct taxes languished.

Low-income countries in sub-Saharan Africa and elsewhere should adopt a more ambitious and diversified approach to revenue mobilisation if they hope to attain sizeable increases by 2015. Countries with a revenue/GDP ratio between 15 and 20 per cent should be supported to achieve the 20 per cent threshold. There are nine such countries in our sample of 26 (e.g., Benin, Cameroon and Malawi). Maximum efforts should focus on countries with a ratio lower than 15 per cent, assisting them to attain, at least, the minimal 15 per cent threshold. This applies to eleven countries in our sample (e.g., Burkina Faso, Mozambique and Tanzania).

The success of some countries in our sample (Ethiopia, Ghana, Mali, Mauritania, Rwanda and Uganda) in increasing their revenue/GDP ratio by four percentage points or more provides useful lessons.

Average Revenue Increase Sub-Saharan Africa



Source: *IMF Statistical Appendices.*

A common pattern among them: they did not necessarily follow standard advice, such as downplaying direct taxes or trade taxes. Instead, they often relied on multiple sources.

Ethiopia was able to raise its revenue/GDP ratio from 12 to 16 per cent over 12 years from direct taxes on income, profits and land-use and from import duties. Mali relied on taxes on personal income, corporate profits, a domestic VAT and a VAT on imports to boost its revenue/GDP ratio from about 14 per cent in 1993 to about 18 per cent in 2004.

During 1994-2004, Mauritania's increases in fishing royalties and indirect taxes accounted for most of its sizeable revenue increase of about eight percentage points, and helped raise its revenue/GDP ratio to 26 per cent. But countries with rising revenue based on natural resources—such as Mauritania (fishing) and Sudan (oil)—still face a major challenge to diversify their revenue sources.

From a dismally low 7.2 per cent revenue/GDP ratio in 1991/2, Uganda boosted revenue by 5.4 percentage points by 2003/4. It introduced a VAT, maintained rates on personal and corporate income, eliminated exemptions and began taxing small businesses. Starting from a low 9.1 per cent, Rwanda increased its revenue by 4.5 percentage points of GDP in 10 years, primarily through income and profit taxes, a VAT and elimination of exemptions.

Ghana had an extraordinary record, raising revenue from about 12 per cent of GDP in 1990 to almost 24 per cent in 2004. Direct taxes on both personal income and corporate profits accounted for about four percentage points. Another five points came from domestic indirect taxes, i.e., a VAT (mostly on imports), a petroleum tax and even a levy for national health insurance. Import taxes brought in an additional two percentage points.

These success stories underscore the need for more MDG-inspired ambition on raising domestic revenue in low-income countries. A major focus of ODA should be, in fact, to build up national capacities for revenue mobilisation. With revenue/GDP ratios four percentage points higher by 2015, some countries could begin graduating from ODA to domestic resources as the driving force of development.

Note:

1. Invaluable research assistance provided by Magali Solimano is gratefully acknowledged.

One Pager number 39
Published: July, 2007
Available at: <*http://www.ipc-undp.org/pub/IPCOnePager39.pdf*>

Should Khat Be Banned? The Development Impact

by Degol Hailu, Policy Specialist, UNDP, Caribbean

The global trade in *khat* is controversial. The United States and most countries in Europe have banned it, considering it a psychotropic substance. But it contributes significantly to farmers' livelihood in Eastern Africa (see the new book, Anderson et al. 2007). Though public officials in the region denounce its consumption, they benefit from the foreign exchange and tax revenues that it generates. So, how should this contradiction be resolved?

In Ethiopia, during 1990-2004 over US$ 413 million was earned from exporting 86,625 metric tons of *khat*. Accounting for up to 15 per cent of the total value of exports, it has become the second largest earner of foreign exchange. Two thirds of all *khat*, much of it exported, is produced in eastern Ethiopia (see the Figure). During 1980-2002, the Government collected 10.7 billion birr in revenue from taxing domestic and export trade in *khat*.

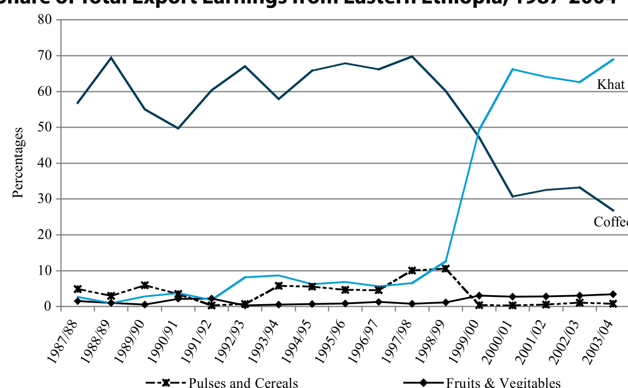
Why do Ethiopian farmers cultivate *khat*? Examining recent history provides an explanation. In the early 1990s, the Government introduced the strategy known as Agricultural Development-Led Industrialization (ADLI). It was designed to increase land productivity through various means, e.g., construction of rural roads, access to fertilizer, subsidized credit, improved seeds and water management. ADLI led to increased use of fertilizers and pesticides and an almost 50 per cent increase in cultivated area.

Production of major crops increased from 64 million kg before ADLI to 85 million kg afterwards. However, output prices have been falling in recent years. There have been several reasons: a slow process of urbanization, limited agro-processing activities and weak export markets. The terms of trade have moved against agriculture because input prices have grown faster than output prices. Consequently, while agricultural value added per worker in the non-*khat* sector was 310 birr in the 1980s, it declined to 266 birr during the period 1990/91-2002/03.

Earnings from coffee dropped from 2.1 billion birr in 1999 to 1.9 billion birr in 2004. Its price per pound declined from US$ 123.4 in 1995 to US$ 26.9 in 2002. Earnings from pulses and cereals have also declined while those from fruits and vegetables have remained low (see the Figure). While farmers accumulated debts during the years of high prices, they have struggled to repay them now that prices have collapsed.

In response, farmers have increased the cultivation of *khat*. The plant has many advantages: it is resistant to many crop diseases, grows in marginal land, requires low labour inputs and can produce up to four harvests per year. Thus, its net return per acre is often greater than that from coffee. While *khat* accounts for only 13 per cent of total cultivated land, it contributes 30–50 per cent of farmers' total cash income per year.

Share of Total Export Earnings from Eastern Ethiopia, 1987-2004



Source: Anderson et al. 2007.

Ethiopian farmers have responded to growing consumption of *khat*, which cuts across age, gender, religious, income and geographical boundaries. Mass consumerism is increasing in the neighbouring countries of Djibouti, Kenya and Somalia and as far away as Yemen and Uganda. Members of the Diaspora—Ethiopians, Somalis and Yemenis in Europe and North America—still consume *khat* and have become a major source of foreign exchange earnings.

However, few anti-khat campaigners acknowledge the importance of *khat* to the economies of Eastern Africa. The International Narcotics Control Board is leading the campaign to ban *khat*. In contrast, the World Health Organization has not yet found justification for restricting the availability and use of *khat*.

Since the evidence on the health consequences of *khat* remains inconclusive, a more feasible option than banning *khat* is to establish a system of regulating its production, distribution and consumption that takes into account its critical contribution to farmers' livelihoods. This option would involve licensing *khat* retailers, setting age limits for consumption and establishing a system of quality control for the product.

Prohibiting the cultivation of *khat*, by contrast, would threaten the livelihoods of many farmers and traders, and likely drive many of them deeper into illegal activity or into poverty. Criminalising those who have to rely on *khat* production for their survival is not the answer. The discussion of *khat* needs to be placed within a development framework instead of being dominated by a mindset that stresses illicit 'substance abuse'.

Reference:

Anderson, David, Susan Beckerleg, Degol Hailu and Axel Klein (2007). *The Khat Controversy, Stimulating the Debate on Drugs*, Oxford: Berg Publishers.

One Pager number 40
Published: July, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager40.pdf>

Job Creation versus Cash Transfers in Kenya

by Eduardo Zepeda, Senior Researcher, International Poverty Centre

After a long period of economic regression, the Kenyan economy has recently started to recover, raising hopes for reducing poverty. Buoyed by this recovery, the Economic Recovery Strategy of the Kenyan Government has the ambitious goal of creating 500,000 jobs per year. But if these jobs are going to be reasonably productive, Kenya will need to grow more rapidly than 6 per cent per year.

However, there is no guarantee that poor households will benefit from such projected growth or the jobs that it generates. So, targeted programmes will continue to play an essential role in the medium term in reducing poverty. This One Pager offers an initial assessment of the effectiveness of two such programmes—a job-creation programme and a cash-transfer programme based on child grants.[1]

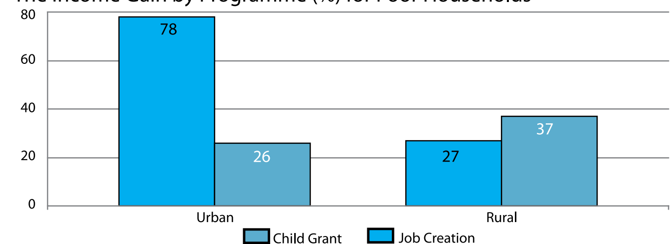
Targeted cash transfers are popular nowadays among governments and donor agencies. Often, they are based on the number of school-age children in a household and conditional on school attendance and health check-ups. Using data from Kenya's 1998/99 Labour Force Survey (LFS), we simulate such a transfer to all children aged 6 to 14 years in poor households. The cost is a mere four per cent of total household income. The result is a *six percentage point fall* in the incidence of poverty and *an eight percentage point reduction* in the depth of poverty.

What would be the impact of a job programme that is similarly financed? To answer this question, we simulate the effect of wages paid by such a programme to a group that includes both: 1) all unemployed workers from poor households and 2) all workers from such households whose labour earnings were lower than the level of wages paid by the programme. The wage level of such a programme is critical. We set the wage roughly equivalent to the poverty lines for rural and urban areas—*specifically,* the minimum wage of unskilled workers in rural agriculture and that of unskilled workers in all urban sectors other than Nairobi.

The overall percentage point decreases across the country in the incidence and depth of poverty are similar for the cash-transfer and job programmes. However, since the number of school-age children per household is larger in rural areas, the cash-transfer programme has a stronger impact there (providing a 37 per cent increase in household income—see Figure). However, in urban areas, where poor workers are relatively worse-off, the job programme has a stronger impact (boosting household income by 78 per cent).

An additional important finding is that the lower the capacity of a household to secure gainful employment, the larger the benefit of

The Income Gain by Programme (%) for Poor Households



Source: Own calculations based on Kenya's 1998/99 Labour Force Survey (LFS).

the job creation programme. The benefits of the job programme in urban areas are most pronounced for the poorest 10 per cent of households.

Both child-transfer and job programmes have a progressive regional impact, i.e., the increase in income is larger, the poorer the district. But the job programme tends to be more beneficial for the poorest households. In nine of the ten poorest urban districts, the job programme out-performs the child-transfer programme; and even in five of the ten poorest rural districts, the job programme is superior. The basic reason is that the job programme enables the poorest households to begin generating income.

Both child-transfer and job programmes help enhance the development of human capabilities, especially of children. The evidence suggests that increasing the income of poor households suffices—independently of conditionalities—to improve education and health. This assumes, of course, that there is an adequate supply of such services. But a job programme is likely to have a stronger multiplier impact than child grants by helping to build economic and social infrastructure. If such a programme builds health clinics and schools, for instance, it can help boost the supply of social services.

If enhancing the current productive capabilities of poor workers is an important objective, then a job programme is also likely to be better. Such a programme provides these workers with more productive employment and develops skills. One objection often lodged against job programmes is that they could distort labour markets, such as by raising minimum wages. However, under Kenya's low-wage, labour-surplus conditions, policymakers should be more concerned with creating economic dynamism than worrying about such imaginary impacts, which are more applicable to developed economies.

Note:

1. See Eduardo Zepeda (2007). 'Addressing the Employment-Poverty Nexus in Kenya', IPC Working Paper, forthcoming.

One Pager number 41
Published: August, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager41.pdf>

Why Have Tax Reforms Hampered MDG Financing?

by Terry McKinley, Acting Director, International Poverty Centre[1]

IPC One Pager No. 39 called for greater ambition in raising domestic revenue for MDG strategies in low-income countries in sub-Saharan Africa. It advocated boosting revenue by four percentage points of GDP by 2015. This One Pager examines why tax reforms achieved less than half this increase in these countries between the early 1990s and early 2000s.

A major reason: 'optimal' tax theory is apparently not optimal in low-income countries. An additional reason: the naïve assumption that lower rates on direct taxes could broaden their tax base. A third reason: the misguided belief that the VAT could replace trade taxes.

Our results suggest: 1) trade liberalisation limited the potential for increases in trade taxes—despite a marked rise in imports 2) lowering rates on direct taxes weakened vertical equity and had only a modest effect on broadening the tax base—despite economic recovery of the formal sector and 3) the VAT did expand tax revenue but not as grandiosely as advertised and not as an effective substitute for trade taxes.

Our results are based on a sample of 25 low-income African countries that have the disaggregated data needed for our analysis. Tax revenue increased in them from a low level of 11.6 per cent of GDP to only 13.2 per cent, a gain of a mere 1.6 percentage points in roughly ten years—well below the target of four percentage points.[2]

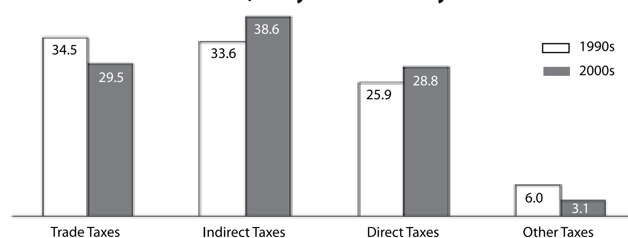
Trade taxes declined slightly as a per cent of GDP, i.e., from 4.0 per cent to 3.9 per cent. Direct taxes increased only about one quarter, namely, from 3.0 per cent to 3.8 per cent. Indirect taxes experienced the greatest increase, i.e., about 30 per cent, from 3.9 per cent to 5.1 per cent. The residual category, 'other taxes' (e.g., stamp duties, mining permits, airport duties), declined from 0.7 per cent to 0.4 per cent.

Consequently, as a share of total tax revenue, trade taxes dropped about five percentage points to a little below 30 per cent while indirect domestic taxes rose five percentage points to close to 39 per cent (see Figure). The modest three-percentage point rise in direct taxes (to about 29 per cent) was counter-balanced by a corresponding drop in 'other taxes'.

What happened to the two main components of direct taxes, personal income taxes and corporate profit taxes? A smaller sample of 18 countries that have relevant data shows that while personal income taxes accounted for two-thirds of the total increase in direct taxes, corporate profit taxes accounted for only one third. The remaining 10-11 per cent of total direct taxes, which include property taxes, did not change.

In order to compare the VAT and non-VAT components of indirect domestic taxes, we had to reduce our sample to the 10 countries in which the VAT was introduced between the early 1990s and the early 2000s. In these, the VAT rose to 3.7 per cent of GDP while non-VAT taxes dropped from 4.2 per cent to 2.1 per cent of GDP. This represented a net gain of 1.6 percentage points of GDP.

Share of Total Tax Revenue, early 1990s to early 2000s



Source: *IMF Statistical Appendices.*

Indirect domestic taxes could certainly achieve more—both for boosting revenue and enhancing equity. Reducing VAT exemptions and levying higher rates on luxury consumption items could help. Strengthening excise taxes on such items could also add revenue. Indirect domestic taxes should be able to contribute at least 2.0-2.5 percentage points to the targeted increase of four percentage points in tax revenue by 2015.

Direct taxes should be able to contribute at least another 1-1.5 percentage points, and more equity to the tax structure. But this would require ending tax holidays and exemptions for the corporate sector and halting the precipitous slide in its tax rates. The same logic applies to recent tax relief on personal income for the rich. Undertaking a minimally credible effort to enlarge property taxes, particularly on urban real estate, could also help.

Further tariff reductions in sub-Saharan Africa are not advisable until domestic indirect and direct taxes substantially boost total revenue. Recent increases in imports should be able to modestly increase tariff revenue, at least by 0.5 per cent of GDP.

Recent reforms, based on 'optimal tax theory', have weakened precisely the taxes (on imports and corporate profits) that are easiest to collect. Had trade liberalization been more extensive, as elsewhere in the developing world, tariff revenue would have fallen much further in sub-Saharan Africa. So why in low-income countries do we insist on making the mobilization of tax revenue—already a major challenge—even more difficult for national policymakers?

Notes:

1. Many thanks to Magali Solimano for invaluable research assistance on this One Pager.
2. Our aggregate results in this One Pager differ slightly from those in One Pager 39 because we had to drop one country, included additional data for others and took an average of three-years as our end-points.

One Pager number 42
Published: September, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager42.pdf>

The Fiscal Impact of Aid Flows: Evidence from Ethiopia

by Pedro M. G. Martins,
Visiting IPC Researcher, Institute for Development Studies, Sussex

Foreign aid flows to developing countries have increased considerably in the last decade. This trend is driven mostly by the need to meet the resource gap in countries committed to fight poverty and achieve the Millennium Development Goals (MDGs).

In sub-Saharan Africa, where aid inflows account for a significant share of GDP, the fiscal impact of aid is fundamental to assessing its effectiveness. This One Pager seeks to contribute to the debate on aid by presenting results from a traditional fiscal response model estimated for Ethiopia.

The model focuses on the impact of foreign aid on government expenditure, revenue and domestic borrowing. Fiscal data for 1964-2005 were obtained from the IMF's International Financial Statistics (IFS) database and complemented by secondary sources.

A summary of the results is presented in the table, with aid disaggregated into its two main components, grants and loans. The coefficients denote foreign aid's total impact on the remaining fiscal variables, over the period under consideration.

The results suggest that foreign aid to Ethiopia has had a positive impact on government capital expenditure, but not a significant effect on recurrent spending (the coefficients are virtually zero). Moreover, aid loans seem to have had a stronger impact on government expenditure than grants, particularly on capital spending (with a coefficient of 0.30 for loans versus 0.06 for grants).

These findings are not entirely surprising since aid flows (especially loans) are often earmarked to specific investment projects, while governments are likely to use domestic tax revenues to pay for most recurrent costs.

Interestingly, both aid grants and loans have had a strong negative effect on domestic borrowing. This suggests that aid and domestic financing are close substitutes. There are two possible interpretations for this relationship. Since domestic borrowing is often an expensive last resort to balance the budget, an increase in aid flows could be used to reduce such a burden. Conversely, it might also be the case that, facing a shortfall in aid flows, the government seeks domestic finance to keep expenditure levels stable.

The Fiscal Impact of Aid in Ethiopia, 1964-2005

	Capital Spending	Recurrent Spending	Domestic Revenue	Domestic Borrowing
Grants	0.06	0.00	-0.47	-0.44
Loans	0.30	0.03	-0.15	-0.46

Source: Martins (2007).[1]

The results also seem to support the hypothesis that aid displaces domestic revenue. Note the negative coefficient for loans (-0.15) but the even larger one for grants (-0.47). This raises concerns about how low-income countries, such as Ethiopia, can eventually overcome aid dependence.

However, these results might also be capturing some indirect effects, such as those due to aid conditionality. Aid flows to Ethiopia increased substantially from the early 1990s, roughly coinciding with the start of economic reforms that were designed to reduce public spending and reform the tax system (such as lowering rates). This might partly explain the apparent weak impact of aid on spending and the negative correlation with domestic revenue.

In conclusion, the results suggest that donors and recipients of aid should focus on ensuring greater 'aid additionality'. The priority should be on financing new capital spending, which can contribute not only to enhancing human development but also to expanding the economy's productive capacity.

While using foreign aid to pay off onerous domestic debt can serve a useful purpose at least in the short run, the medium-term purpose of aid should clearly be to expand MDG-related government spending.

Most troubling is the apparent displacement of domestic revenue by aid flows. One implication is that donors should channel more aid precisely into building up national capacities to mobilise domestic revenue. Otherwise, developing countries such as Ethiopia will have difficulty in graduating from heavy reliance on external aid.

Reference:
1. Martins, Pedro M. G. (2007). 'The Impact of Foreign Aid on the Government Sector: The Case of Ethiopia', forthcoming IPC Working Paper, Brasilia.

One Pager number 43
Published: September, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager43.pdf>

'Growing Pains': Key Challenges for New Conditional Cash Transfer Programmes in Latin America

by Fabio Veras Soares and Tatiana Britto*

Conditional Cash Transfer (CCT) programmes have been established in more than a dozen Latin American and Caribbean countries in the past 10 years. As the original models have become widely disseminated, new programmes have had to confront unresolved issues. Primary among them are graduation rules or, as some prefer to call them, 'exit-door' strategies.

Mexico's *Progresa* (now *Oportunidades*) has been the most important source of inspiration for CCT programmes in the region. It is known for focusing on the long-term objective of human-capital accumulation, such as ensuring that children attend school. This emphasis has led to a very low percentage of 'graduations', i.e., only 0.11 per cent of beneficiaries, from the programme since its start in 1997. The justification is that since the programme's success depends on breaking the intergenerational transmission of poverty, beneficiary children should receive continuous support throughout their educational cycles.

Chile Solidario does not have such a strong focus on human-capital outcomes. Instead, it concentrates on families in extreme deprivation and provides, through its *Puente* component, intensive psycho-social support for two years, in addition to providing families with cash transfers.

Many analysts have considered this programme a role model because this intensive support is regarded as an 'exit-door' out of deprivation, in contrast to the cash transfer, which such analysts regard as potentially generating dependency. However, even when families leave the *Puente* component after two years, they can still become eligible for other cash transfers from the broader network of social-protection services, such as the *Subsidio Único Familiar*.[1]

How have such older programmes influenced the more recent CCT programmes in the region? Paraguay's *Tekoporâ* and El Salvador's *Red Solidaria*[2] are illustrative of the challenges faced by smaller countries with lower financial and institutional capacities. Like Mexico's *Oportunidades*, both programmes place a strong emphasis on conditionalities that ensure human-capital accumulation. However, beneficiary families can stay in the programmes for only three years. Afterwards, the programme should re-assess their poverty *status* and undertake some phasing-out or exit-related measures.

This brief time limit highlights the tensions between the two major objectives of most CCTs—namely, short-run poverty alleviation (through transfers) and breaking the intergenerational transmission of poverty (through health and education conditionalities). Is it reasonable, for instance, to 'graduate' families before the completion of the educational cycle (or even the immunization cycle) of beneficiary children?

Paraguay's family support activities, which are inspired by *Chile Solidario*, are designed to enable families to 'graduate' from poverty within a three-year period. But this feature is not consistent with the programme's human-capital objectives, which require a much longer period of coverage.

The shortage of financial and institutional support for the programme partly explains its short duration. This is also why there has been a shift from a focus on human-capital outcomes towards 'complementary activities' that could boost the productive capacities of families so that they could overcome poverty within three years. Moreover, the programme's hiring of 'family guides' to provide the needed intensive support has implied additional administrative costs that inhibit broadening the coverage of the programme among extremely poor households.

In such a context, one of the major challenges for these programmes is to secure enough political support to guarantee their continuance beyond their first three-year cycle. In Colombia's *Familias en Acción,* for example, the initial three-year limit was effectively jettisoned as the longer-term demands of its human-capital objective grew stronger over time.

It remains to be seen whether the three-year limit will be strictly enforced in Paraguay and El Salvador. If their programmes do gain broader political support, they could evolve, hopefully, into permanent features of each country's social protection strategy.

This could enable them to access larger budgets and achieve wider coverage. If not, they would remain, unfortunately, one-off experiments that could benefit some extremely poor families for at least a short period of time. But they would achieve only a negligible longer-term impact on extreme poverty.

* Fabio Veras Soares, International Poverty Centre/IPEA and Tatiana Britto, Visiting Researcher, IPC.

References:

1. For more details see the interview with Andrés Toro - Coordinator of Territorial Management for the Social Protection System in Chile at <http://www.undp-povertycentre.org/publications/cct/Interview_Andres_Toros.pdf>.

2. See Soares and Britto (2007) 'Confronting Capacity Constraints on Conditional Cash Transfers in Latin America: The Cases of El Salvador and Paraguay.' IPC Working Paper No. 38.

One Pager number 44
Published: November, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager44.pdf>

Pro-Poor Growth: Though a Contested Marriage, Still a Premature Divorce

by Terry McKinley, Acting Director,
International Poverty Centre

Not so long ago, 'pro-poor growth' was ardently adopted as a premier development goal. But its twin objectives (both *faster* growth and *greater* equity) were always awkwardly aligned. A contested marriage, from the start, of divergent values. And for many, it appeared, the consummation of such a conjugal coupling proved exceedingly demanding.

Enthusiasm has more recently receded, as myriad adjectives jostle now to elbow 'pro-poor' aside. A parade of suitors, old and new: 'broad-based', 'shared' and 'inclusive'. But why now entertain divorce of equity and growth? Has 'pro-poor' failed to deliver on its promise? Is greater equity now passé?

Innumerable efforts were undertaken (to be sure) to define and measure 'pro-poor growth'. Some emphasized the role of growth in achieving *absolute* improvements. Others embraced equity, first and foremost—opting for narrowing differentials independently of absolute advance. This meant the poor should rise *relative* to the non-poor even if growth were slow, or negative. In fact, attaining greater equity across the total distribution was the encompassing intention.

However, pragmatism divined a 'third way': mixing *both* the means to *maximize* poverty's reduction. Growth was thus no longer 'pro-poor' or 'anti-poor', just poverty-reducing 'more' or 'less'.

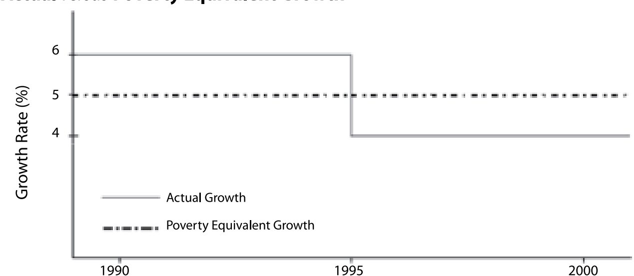
Equity advocates had entered such an analytical union with eyes widely shut. The goal, already pre-defined, had set the terms of the debate: poverty reduction as *absolute* uplift (moving people above a fixed poverty line). Greater equity was now merely *means* to such endeavour, no longer end in itself. And so the debate on 'pro-poor growth' had—without much pomp or circumstance—collapsed.

Pro-Poor Growth: Duelling Definitions?

1. The Kakwani, Khandker and Son Definition (2004):
   The Poverty Equivalent Growth Rate = the actual growth rate x (the total poverty elasticity/the poverty elasticity of growth).
   Where the 'total poverty elasticity' includes 1) the elasticity of poverty with respect to a change in inequality and 2) the poverty elasticity of growth. So, if poverty decreases as inequality is reduced, the ratio of the last expression rises and the Poverty Equivalent Growth Rate exceeds the actual growth rate.

2. The Ravallion Definition (2004):
   The Distribution-Corrected Growth Rate = the ordinary growth rate x (a constant x (1 – an inequality index)$^{\theta}$).
   Where an inequality index could be a measure such as a Gini coefficient. So, the distribution-corrected growth rate would rise as the Gini is reduced because the multiplicative term '(1-Gini)' would rise.

Actual *versus* **Poverty Equivalent Growth**



Some time before, differences had indeed seemed sharp. For instance, Nanak Kakwani had defined 'pro-poor growth' as a trend in which "the incomes of the poor grow faster than those of the non-poor". This standard, clearly relative, looked unequivocal.

In seeming contrast, Martin Ravallion had defined 'pro-poor' as a process of growth that was 'poverty-reducing'. Under such a banner, a rapidly growing economy, such as China's, could easily qualify—despite its rapidly rising inequality.

But such debated differences proved ephemeral. When one investigates the contestants' respective mathematics, such divergences disappear (Text Box).

From different starting-points, Kakwani and Ravallion had arrived at the same conclusion. The Figure illustrates their common challenge. Suppose that in Country X: 1) the actual growth rate during 1990-1995 was six per cent while the Poverty Equivalent Growth Rate (or the Distribution-Corrected Growth Rate) was five per cent and then 2) the actual growth rate during 1995-2000 declined to four per cent while the Poverty Equivalent Growth Rate remained at five per cent.

Which outcome is better? Faster growth but greater inequity in 1990-1995? Or slower growth but greater equity in 1995-2000? Poverty pragmatists could be indifferent (depending on the weight they place on inequality).

Growth champions might opt for 1990-1995 because of greater non-poor gains. Equity advocates might choose 1995-2000 because of lower inequality. Hopefully, growth's new wedding propositions—such as from the popular 'inclusive'—can help resolve such challenging disputes or clarify, at least, the central issues.

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One Pager number 45
Published: November, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager45.pdf>

Wage Cutting in Kenya Will Expand Poverty, Not Decent Jobs

by Robert Pollin, Mwangi we Githinji and James Heintz, Department of Economics and Political Economy Research Institute (PERI), University of Massachusetts-Amherst

Some economists blame excessive labour costs for the lack of growth of productive employment in low-income countries. For example, a 2005 paper by the World Bank, "Jobs in Kenya: Concept Note," gives primary emphasis to this explanation. But does this make sense? We think not, as we explain in our recent report, 'An Employment Targeted Economic Program for Kenya'.

Labour costs are considered excessive when the total compensation of workers exceeds their productive contribution. The two standard explanations are excessively high wages and rigid labour-market regulations, such as those due to unions or minimum wages. Let's start with the issue of high wages.

High Wages

We assume a goal of boosting private formal-sector jobs by 25 per cent (i.e., from 777,000 jobs to 960,000, an increase of 190,000 jobs).Using the 2005-6 Kenya Integrated Household Budget Survey (KIHBS), we simulate how much the wages of the average private formal-sector worker would have to be cut in order to achieve our goal.

If we assume a 'wage elasticity of employment' of -0.6 (based on elasticities estimated for similar countries), average private formal-sector wages would have to fall by 42 per cent to generate 190,000 new private formal-sector jobs. The resulting average wage would be Ksh 4,100 (Ksh 5,220 in urban areas and Ksh 2,784 in rural). This national average would be 15 per cent below the poverty level.

The average wage of urban workers would fall from 50 per cent above the poverty line to 10 per cent below and that of rural workers from 34 per cent above to 23 per cent below. About 1.7 million Kenyans would correspondingly suffer (the 770,000 workers plus their 900,000 dependants).

But 400,000 Kenyans would benefit, i.e., the 190,000 workers obtaining new formal-sector jobs and their 210,000 dependants. If we assume that these workers with new jobs graduate from informal-sector activities, their earnings would rise by an average of 60 per cent.

But these 400,000 Kenyans would still be living below the poverty line (10 per cent below in urban areas and 23 per cent below in rural). In addition, the total size of the private formal sector would remain very small, i.e., about seven per cent of the Kenyan labour force. So wage cutting is not a viable solution in a low-income country such as Kenya. While the depth of poverty might be reduced for some workers, the net effect would be to markedly broaden the incidence of poverty.

Labour Unions

What about problems with labour unions? The World Bank's "Jobs in Kenya: Concept Note" regards them as a major source of labour-market rigidities. But unions represent a small and diminishing share of Kenya's labour force. This is also the case in many other low-income countries that have undergone structural adjustment.

Between 1985 and 2000, for instance, union membership in Kenya fell from about 700,000 to about 436,000—a sharp decline of 38 per cent. Unions now represent only about four per cent of the total labour force. Moreover, a 2003 Kenya survey reported that about 94 per cent of firms reported zero days of work lost to strikes or labour unrest.

Union workers are often accused of enjoying wage premiums. But elite workers, who enjoy high premiums based on education or skill, usually do not join labour unions in Kenya. Unions are concentrated in the public sector, representing workers below the senior level. In the private sector, they tend to represent production-level workers who are not highly skilled. So, for these various reasons, unions are not a likely source of labour-market rigidities.

Minimum Wages

Do minimum wages hamper employment creation, especially among poorer workers, by making their unskilled labour too expensive? It is true that the confusing array of 45 separate minimum wage standards in Kenya needs simplification.

But drawing on data from the 2005-6 KIHBS, we find that almost three quarters of all workers paid on an hourly basis receive wages below the average level for the statutory minimum. For workers in the private sector paid on a daily or monthly basis (who are the overwhelming majority of all paid employees), wages are 43-50 per cent below the *lower range* of the statutory minimum wage. Being so low, minimum wages exert little influence on wage-setting.

Instead of accepting advice that reducing or eliminating minimum wages, weakening unions or cutting wages could create more jobs, the Government should concentrate on directly expanding decent employment through a comprehensive employment-targeted economic programme, including measures to raise worker productivity, broaden the availability of credit and enhance access to economic and social infrastructure.

One Pager number 46
Published: December, 2007
Available at: <http://www.ipc-undp.org/pub/IPCOnePager46.pdf>

Conditional Cash Transfers: Why Targeting and Conditionalities Could Fail

by Guy Standing, Professor of Economic Security, University of Bath, UK

IPC One Pager No. 44, "Growing Pains", argues that cash transfer programmes should become a permanent feature of social protection in developing countries. This One Pager takes that logic further, advocating a universal income grant as a foundation for basic economic security (see Standing 2007). Such an approach views targeting and conditionalities as both unnecessary and counter-productive.

Universal schemes are more necessary than ever as globalization and economic informalisation make economic insecurity more pervasive. Economic downturns and socio-economic disasters have become more numerous—whether due to economic forces or climatic conditions, and whether their impact is sudden (such as floods) or protracted (such as famines). The resultant costs can radically erode a household's capacity to sustain a viable livelihood base.

Cash Transfer Advantages

Are cash transfers an answer? Compared to alternatives such as food aid, they tend to be more effective. Commodity-based assistance is paternalistic: families have to accept what is presumed good for them, e.g., food, instead of making their own choices based on more income. Such assistance can also be market-distorting, as when it drives down prices for food grown locally or nationally. Moreover, such programmes strengthen a sense of charity rather than economic rights.

Can cash transfers do better? They can be distributed quickly, their administrative costs tend to be low, their selection of beneficiaries can be transparent and they provide freedom of choice in how the money can be spent. They can also contribute to rebuilding and sustaining livelihoods.

The 'Cash for Relief Programme' in Ethiopia, which was used to address crop failures, is an example. Its evaluation showed that cash grants were used to pay off debts, restore land productivity and help regenerate livelihoods. In contrast, food aid might have fostered only current consumption. The 'Cash for Herder' schemes in Mongolia were similar in their impact, reviving investment in assets, such as herds, that could regenerate livelihoods and the local economy.

Other such programmes have reduced the distress renting out of land or out-migration, helped households pool savings, and allowed farmers to sell their crops when prices are high and to buy seeds or livestock so that they could start work again.

Conditionalities

However, many cash transfer programmes have strategic weaknesses: they are neither universal nor non-conditional. They mix 'means-testing' with 'behaviour-testing' and often gravitate towards social therapy. Some of the most well-known schemes, such as Mexico's *Oportunidades*, have evolved into complex mechanisms of social engineering.

Operating a means-tested conditional programme, such as making grants to poor families based on their children's school attendance, requires considerable administrative capacity—which is often sorely lacking in many low-income countries. Such schemes are also inherently paternalistic even if they impose conditions, such as ensuring children's education, that are universally accepted.

They assume, in effect, that a poor family must be irrational or incapable of knowing what is in its long-term interests or lacks some kind of vital information. Moreover, in rural areas of Latin America and throughout regions such as sub-Saharan Africa, conditionalities related to health and education are likely to be ineffective because of a lack of schools, health clinics and transport.

Targeting creates additional problems. It implies maintaining a sophisticated and updated registration system. But such a system would have inherent problems with families that are economically insecure, since their incomes fluctuate unpredictably above and below any given poverty line.

Targeting

Targeting is often implemented primarily to gain political support from the non-poor. This is based on the dubious distinction between 'the deserving poor' (who often cannot work or are extremely deprived) and the 'undeserving poor' (who are capable of working and should not accept 'hand-outs', at least not for very long). There is little debate that children are 'deserving' but why should poor families with *pre-school* children or no children be excluded from receiving transfers?

But programmes that rely on targeting and conditionalities are invariably arbitrary, inequitable and inefficient. In contrast, universal security schemes are administratively simple, low-cost and affordable. They would also be non-stigmatising (based on a universal entitlement to transfers) as well as non-paternalistic. Most importantly, they would help strengthen social solidarity, contribute to households' freedom of choice and contribute to sustainable livelihoods and dignified work.

Reference:

Guy Standing (2007). 'How Cash Transfers Boost Work and Economic Security'. UNDESA Working Paper No. 58, October.

One Pager number 47
Published: December, 2007
Available at: <*http://www.ipc-undp.org/pub/IPCOnePager47.pdf*>

Is Financial Liberalization a Flop?

An Africa Assessment

by John Serieux, Assistant Professor of Economics, University of Manitoba; and Terry McKinley, Acting Director, International Poverty Centre

Sub-Saharan Africa's long-term development, including attainment of the MDGs and continued progress beyond 2015, depends on mobilizing domestic financial resources and channeling them to productive private and public investment. From roughly the mid 1980s to the mid 1990s, many of the countries in the region undertook financial liberalization in order to promote such an objective. This One Pager evaluates the outcomes by examining the experience of 19 countries that have liberalized (see Serieux 2008).

During 1965-1985, almost all African countries followed what orthodoxy now labels as policies of 'financial repression', i.e., maintaining (administered) low interest rates and directing cheap credit to certain enterprises and sectors in order to foster rapid growth.

Between 1986 and 1995, many of these countries underwent a process of domestic financial liberalization, instituting market-determined deposit and lending rates, eliminating directed credit, creating more competitive conditions and reducing the flow of credit to the public sector.

In our analysis, we explicitly compare the record of our sample of 19 countries for the period before liberalization (1965-1985) and that afterwards (1996-2005), using regression analysis to identify impacts on private (and public) savings, private investment, the liquidity ratio, credit to the private sector, and economic growth.

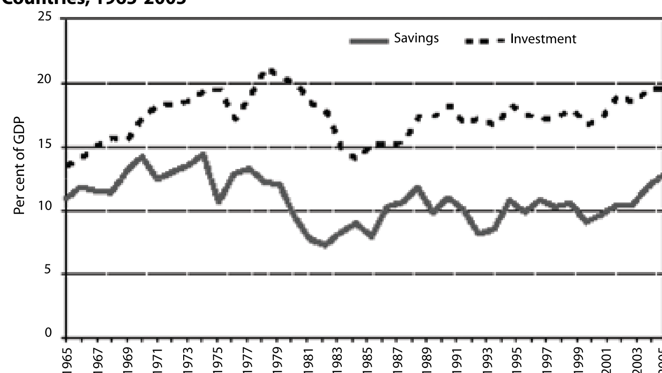
Private (and Public Savings): The Figure shows that total domestic savings for these countries peaked at 14 per cent of GDP in 1974 and declined to a nadir of just over seven per cent in 1982. It recovered modestly then stagnated at around 10 per cent through the 1990s, showing signs of a renewed rise only after 1999.

Thus, it is not surprising that our regression results suggest that neither liberalized nor 'repressed' financial regimes had a significant impact on private savings. Generally, factors such as terms-of-trade movements, the dependency ratio and inflation were the important determinants. Public savings were negatively related to private savings across both regimes, but were less so under liberalized finance.

Private Investment: Total Investment has followed a similar pattern to that of savings. But even a recent modest rise has not brought it back up to the peaks of the late 1970s, which exceeded 20 per cent. Nonetheless, our results show that 'repression' was negatively correlated with private investment while liberalization had no significant level effect. However, private credit did become more correlated with investment in the liberalized period.

The Liquidity Ratio: Under liberalized finance, the real rate of interest was the most important determinant of growth in liquidity

Gross Domestic Savings and Investment for 19 Sub-Saharan African Countries, 1965-2005



Note: Unweighted Averages.

whereas during financial 'repression', it was the level of income that mattered. However, overall, liberalization was correlated with slower growth in liquidity whereas 'repression' was correlated with faster growth.

Private-Sector Credit Growth: Under liberalization, public-sector credit expansion and the real interest rate had significant effects on the expansion of credit to the private sector. During 'repression', there were no such significant determinants. However, 'repression' was still associated, overall, with faster growth of such credit while liberalization was associated with slower growth.

Economic Growth: Neither 'repressed' nor liberalized finance was correlated with growth. In general, the rate of investment and growth in OECD countries were the important determinants.

In summary, liberalization has modestly reduced the substitutive relationship between public and private savings and increased the correlation between private credit and investment. But it has been negatively correlated with both liquidity and private-sector credit expansion and has had no effect on growth. In short, the overall effect of liberalization on resource mobilization has been ambiguous and marginal. So, though much heralded, liberalization must be judged a flop—at least by our empirical results.

Since the 'repression' period did not perform well either, our findings point to the need for deeper structural changes—probably beyond financial-sector policies—in order to substantially improve resource mobilization in sub-Saharan Africa.

Reference:

John Serieux (forthcoming 2008). 'Financial Liberalization and Domestic Resource Mobilization in Sub-Saharan Africa: An Assessment'. Draft Working Paper, Brasilia: International Poverty Centre.

One Pager number 48
Published: February, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager48.pdf>

Latin America's Progress on Gender Equality: Poor Women Workers Are Still Left Behind

by Eduardo Zepeda, Carnegie Endowment for International Peace[1]

The Millennium Development Goals seek to achieve gender equality by the year 2015 (see MDG No. 3). The set of indicators proposed to track progress towards this goal encompasses the social, political and economic spheres. We focus on an important economic indicator, i.e., the share of women in wage employment in the non-agricultural sector.

The Latin American and Caribbean region has shown notable progress on all indicators of gender equality. Official data from the United Nations show that, within the developing world, this region has had the best performance on women's economic progress. For instance, women hold 42 per cent of wage jobs in the non-agricultural sector.

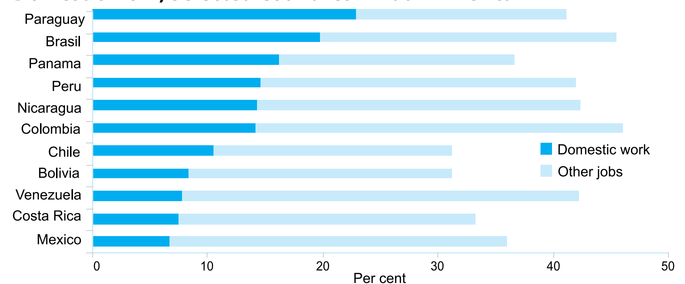
However, an assessment of the region's progress on gender equality cannot rely only on national averages. In the region in the world with the highest inequality, one should expect progress in gender equality to be inequitably distributed, and likely to be most limited for poor women.

We restrict our attention to *urban* areas, where this indicator is more relevant and data are more reliable. We then examine—by quintiles—the share of women in wage employment in the *urban* non-agricultural sector for 20 countries in Latin America (*circa* 2004). Data in EQxIS (www.iadb.org/xindicators) allow us to see that this share is 48 per cent for the richest fifth and 40 per cent for the poorest. Hence, the participation of poor women in such employment is eight percentage points lower, on average, across all countries. In countries such as Bolivia, Chile, Honduras and Panama, the difference can be as large as 15 percentage points.

But let us disaggregate our data in order to get closer to the real story. Often, the main wage work that poor women in urban areas can find is performing domestic chores for rich or middle-class households, e.g., cleaning, cooking and baby sitting. What if we exclude these jobs from our analysis since they are usually low paid, lack benefits and offer few opportunities—hardly a basis on which to demonstrate gender equality? If we do, the disparities between rich women and poor women become striking.

Excluding domestic work does not alter the share of rich women in urban wage work. But the share of poor women drops dramatically, by 12 percentage points, from 40 to 28 per cent! This suggests that more than one in four poor women workers (12/40) who are in urban wage employment are domestic workers. Moreover, the domestic chores that they perform for rich and middle-income

Share of Poor Women in Urban Paid Employment and in Urban Paid Domestic Work, Selected Countries in Latin America



Source: Author's calculations based on data from EQxIS.

households are likely to enable the women in these households to secure higher wage employment outside the household.

The importance of paid domestic work for poor women workers differs across countries in Latin America. For selected countries in this region, the Graph highlights: 1) the share of all poor women workers who are in urban paid employment and 2) the percentage of all poor women workers who are paid domestic workers.

The Graph allows us to gauge the share of poor women in urban paid employment who are domestic workers. This percentage is almost one half of all poor women in urban paid employment in Brazil, one third in Chile, a bit more than one fifth in Costa Rica and a little less than one fifth in Venezuela. Paraguay is an extreme case: more than half of poor women engaged in urban paid employment are domestic workers.

Thus, MDG-related policies aiming to reduce gender equality need to take into account the complexity of women's participation in labour markets, particularly in countries with high inequality such as those in Latin America. Access to non-agricultural wage employment, though important, does not necessarily expand significantly the economic opportunities of poor women.[2]

So indicators that focus solely on national averages might provide a misleading picture of progress in reducing gender equality. Disaggregating data, such as we have done for paid domestic work, should be an initial step in uncovering the real conditions of gender inequality.

Notes:

1. Former senior researcher at the International Poverty Centre and current staff member of the UNDP Poverty Group.
2. For a recent discussion of gender equality, see issue number No. 13 of IPC's *Poverty In Focus* magazine, published in January 2008.

One Pager number 49
Published: February, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager49.pdf>

The Urgent Need for Financial Reform to Mobilise Savings in Sub-Saharan Africa

by Sedat Aybar, Kadir Has University, Turkey and Costas Lapavitsas, School of Oriental and African Studies, University of London

In IPC Policy Research Brief No. 6, Pollin, Epstein and Heintz provide alternative proposals for monetary policy and financial-sector reform in sub-Saharan Africa, focusing on such issues as targeting short-term interest rates, instituting moderate exchange controls, proposing large-scale loan guarantee programmes and reviving state development banks (see also the directly related IPC Policy Research Brief No. 4).

This One Pager emphasises the importance of financial-sector reform for domestic resource mobilisation. The reason: savings mobilisation by liberalised financial systems in sub-Saharan Africa has been deeply unsatisfactory, severely constraining investment and making faster, sustainable growth unlikely.

Domestic savings collapsed in the 1980s, fell further in the 1990s and, despite partial recovery after 2000, have remained low and fluctuating. The Figure shows that savings performance in the region has been worse than in Latin America, and in complete contrast to that in East Asia.

External sources can partially plug this gap, but both FDI and workers' remittances are low compared to those in other regions. Substantial increases in ODA are required, but aid is volatile and often converted into flight capital, in large part due to liberalisation of the capital account. A longer-term solution requires stronger domestic resource mobilisation based on reform of the formal financial sector.

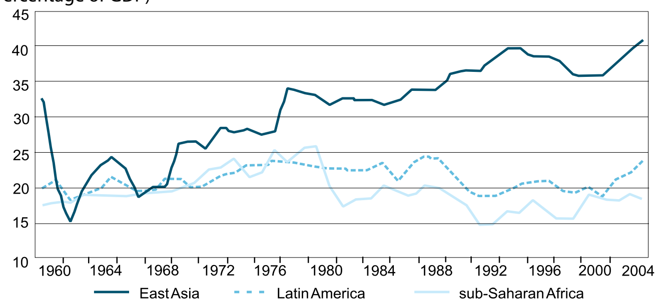
There is not, in fact, an absolute scarcity of savings in sub-Saharan Africa. Households hold substantial precautionary savings because of low and uncertain incomes. But their savings pattern is very irregular, and can involve as much dissaving as saving. Savings rates might rise as a result of higher economic growth, but the region's growth volatility adversely affects household capacity to save.

In this environment households require secure saving assets that allow for many small transactions—a service unlikely to be provided by the liberalised financial sector. Thus, a large part of savings goes into non-financial assets (livestock, real estate and jewellery) and into the informal financial sector, instead of financing productive investment.

African households save in non-financial assets partly in order to demonstrate status and wealth, but also because they typically face a risky financial environment. Informal financial assets are also favoured because they tend to involve small and frequently repeated deposits with institutions that operate in geographically and socially confined community settings.

The weakness of the formal system in mobilising savings has been exacerbated by financial liberalisation. The closure of state-owned banks with wide outreach was a significant factor. In addition, commercial banks limited their branch network, focusing on more profitable urban-based activities and reducing exposure in rural areas. Small depositors have also been discouraged by high minimum deposit and balance requirements as well as by the time and administrative effort required to complete transactions.

Gross Domestic Savings by Developing Regions, 1960-2004
(Percentage of GDP)



Source: World Development Indicators, 2007.

Savings with the formal financial system could increase provided that there were improvements in access, adequacy and reliability of financial assets. First, the semi-formal financial sector should be encouraged to provide further outlets for household savings.

Second, technological innovation should be promoted to ameliorate the problems of remoteness and costs of access to finance, including starting ATMs, mobile banks and, more significantly, mobile phone banking, particularly in rural areas.

Third, microfinance institutions could play a significant role in mobilising savings and pooling other financial resources in conjunction with the formal system. Sub-Saharan African banks should be encouraged to cooperate more with such institutions.

A more effective and radical measure, however, would be to use public mechanisms to mobilise savings, such as revitalised postal savings institutions and strengthened public pensions systems. Development finance institutions, more than 60 of which remain across the region, could also be rebuilt.

Public banking institutions in sub-Saharan Africa in the past have been associated with inefficiency and misuse of funds, and have often been subject to political pressure. Nonetheless, given the poor performance of liberalised formal finance, there seem to be few other viable alternatives if formal domestic savings mobilisation is to recover and sustain increased public and private investment.

One Pager number 50
Published: March, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager50.pdf>

Inflation-Targeting in Sub-Saharan Africa: **Why Now? Why at All?**

*by Terry McKinley, Director of the Centre for Development Policy and Research, School of Oriental and African Studies, London**

In May 2007, Ghana formally adopted an inflation targeting framework for its monetary policy. This meant that price stability had become the central bank's primary objective. Ghana is only the second country in sub-Saharan Africa, after South Africa, to adopt such a regime. Ghana's inflation target is five per cent while South Africa's is a 3-6 per cent band. Such low rates are common among countries in the region, even those without explicit targeting regimes.

Why choose such a policy regime? Especially when the global economy hovers on the brink of a significant slowdown (likely to be triggered by a U.S. recession)? This One Pager addresses these issues.

In 2002, the Bank of Ghana began moving toward inflation targeting but still continued to manage the exchange rate—a priority in countries subject to frequent external shocks. However, Ghana's new monetary regime requires focussing on the inflation rate, not the real exchange rate. Inflation targeting requires full exchange-rate flexibility.

Also, the Ministry of Finance has to restrain its fiscal policies in order to support the central bank's inflation target. The IMF has already encouraged Ghana to adopt a 'fiscal responsibility law' as a means to ensure strict budget discipline.

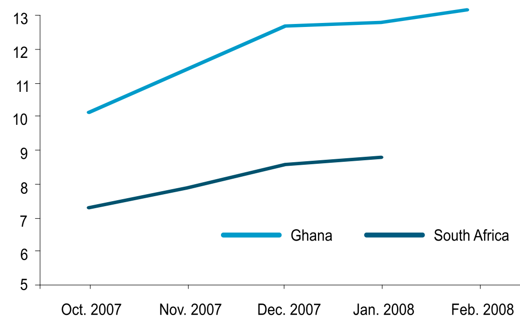
Will such a policy regime produce either price stability or growth? Not likely. Its chances look particularly bleak now. On March 18, 2008, the Central Bank announced an increase in its prime interest rate from 13.5 per cent to 14.25 per cent. Last November, it had hiked this rate a full percentage point, from 12.5 per cent. Why?

Inflation in Ghana has been on the rise since October 2007 (see Figure), driven by rising food and oil prices and increases in utility rates. The inflation rate rose to 13.2 per cent by the end of February—a 30 per cent increase over its October 2007 level and 2.6 times its five per cent target.

Is South Africa doing any better? In January 2008, its food prices were increasing by almost 14 per cent, with a markedly higher rate for imported food. Overall inflation had already exceeded its target range, rising to almost nine per cent, about one fifth higher than in October 2007 (see Figure), and the highest since 2003. The central bank governor pointed to increases in food and oil prices, combined with domestic capacity constraints (e.g., electricity shortages), as the motive forces.

The price increases faced by Ghana and South Africa—and many other countries in sub-Saharan Africa—are supply-side problems, mostly externally imposed. They cannot be blamed on excessive domestic aggregate demand. But policymakers in both countries must believe this to be the case when they resort to raising interest

Recent Increases in Inflation in Ghana and South Africa (CPI % change)



rates in order to squelch inflation. Such tightening of monetary policies is not advisable during the onset of a global slowdown. Ghana is a big exporter of cocoa and gold (whose prices are on the upswing), and expects to produce oil in a few years. However, it still runs very large trade deficits, covered fortunately by remittances and ODA. South Africa has also run consistently large trade deficits (e.g., over seven per cent of GDP in 2007), financed until now by private capital inflows. But a global slowdown (combined with high food and oil prices) could quickly widen such deficits and make financing them even more difficult.

Terms-of-trade shocks have been so frequent and severe in the region that inflation targeting is bound to fail, especially in economies becoming increasingly open. Recent price shocks are likely to depreciate exchange rates, which will, in turn, intensify inflationary pressures. The depreciation of the Ghanaian cedi already intensified in early 2008. The South African rand declined in value by 14 per cent for the first two months.

Rising food prices have already been battering the purchasing power of consumers in Ghana. And the recent jump in oil prices will surely slow growth in 2008 as well as hike inflation. Moreover, a U.S. recession will dampen, directly or indirectly, the growth of Ghana's primary commodity exports. The debilitating impact of these combined factors could sweep across many countries in the region.

Managing the exchange rate will become critical in responding to this imminent turmoil. Ghana should focus on stabilizing the real exchange rate and freeing fiscal policies to cushion domestic investment and consumption in the face of intensifying external shocks that will markedly worsen trade balances, growth prospects and mass poverty.

Note:
Published jointly by IPC as a One Pager and the Centre for Development Policy and Research as a Development Viewpoint <www.soas.ac.uk/cdpr>.

One Pager number 51
Published: April, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager51.pdf>

Are Estimates of Poverty in Latin America Reliable?

by Sanjay Reddy,
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What is the level sof income poverty in Latin America and has it been decreasing? Are current estimates reliable?

The most influential approach to gauging income poverty regionally as well as globally uses the World Bank's international poverty lines of 'one-dollar-a-day' and 'two-dollars-a-day' per person. The Bank uses 'purchasing power parity' (PPP) factors to translate these international lines into local currencies.

The Bank's estimates for Latin America suggest that 8.6 per cent of the region's population was in extreme poverty (living on less than one dollar a day) in 2004 while 22.2 per cent was in poverty (living on less than two dollars a day) (see Table). By comparison, extreme poverty affected 10.8 per cent of the region's population in 1981 and poverty affected 28.5 per cent.

The pace of poverty reduction in Latin America was thus slow—slower than in the entire world. The global percentage of the poor fell from 67 per cent in 1981 to 48 per cent in 2004, with extreme poverty falling from 40 per cent to 18 per cent.

Unfortunately, the Bank's method has serious problems. The most basic is the arbitrary nature of its approach to identifying the poor. In the United States, the reference country for setting the Bank's international poverty lines, even two-dollars-a-day does not reflect the real costs of meeting the basic requirements of a human being.

The 'thrifty food plan' of the U.S. Department of Agriculture estimates the costs just for food at a much higher level than $2 a day per person. PPP adjustments also distort the results since the costs of food items (which are internationally traded) are much higher in developing countries than this method (which gives great weight to the low cost of services there) suggests.

Thankfully, there is an alternative to the Bank's approach, i.e., the poverty estimates of the Economic Commission for Latin America and the Caribbean (ECLAC). While it has its own deficiencies, ECLAC's approach tries, at least, to use nutritionally anchored poverty lines that capture better the local cost of purchasing basic foodstuffs. It thus better captures the real requirements of human beings.

ECLAC poverty estimates for Latin America are invariably higher than those of the Bank. In 2005, the former suggest that almost

Share of the Population in Latin America in Extreme and Overall Poverty

World Bank Estimates	1981	2004
$1 a day line	10.8	8.6
$2 a day line	28.5	22.2
ECLAC Estimates	**1990**	**2005**
Lower Poverty Line	18.0	15.4
Upper Poverty Line	41.0	39.8

Source: Reddy and Pogge.

40 per cent of the population was poor (compared to about 22 per cent in 2004 for the Bank) and about 15 per cent was extremely poor (compared to 8.6 per cent for the Bank).

Unfortunately, the ECLAC method has its own flaws. It assumes, for instance, that all households have the same demographic composition. And it estimates non-food requirements in an *ad hoc* manner so that allowances for such requirements vary widely among countries. A third approach (Reddy and Pogge, forthcoming) seeks to improve on the ECLAC method.

This alternative approach would carefully construct poverty lines within each country based on a common underlying conception of the real requirements of human beings. This means that each national poverty line would reflect the local cost requirements of achieving a specific set of universal basic human capabilities. However, the resulting estimates would be comparable because the capabilities would be defined globally.

An example is provided by the ability to be adequately nourished. In this case, the poverty line would reflect the local cost of purchasing commodities with a certain nutritional content. While being locally relevant, such a poverty line would also have a common meaning across space and time.

Thus, it would be possible—especially in contrast to the World Bank method—to conduct meaningful and consistent inter-country comparisons. Such an approach eliminates the need for PPPs, which are invariably arbitrary. Rather, it strengthens and coordinates national poverty estimates, by applying a common and well-grounded conception of poverty in all countries.

Reference:

Sanjay G. Reddy and Thomas Pogge (forthcoming). 'How Not to Count the Poor', in J. Stiglitz, S. Anand and P. Segal (eds.) *Debates in the Measurement of Poverty*, Oxford: Oxford University Press. Available at <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=893159>.

One Pager number 52
Published: May, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager52.pdf>

Which Poverty Line? A Response to Reddy

by Martin Ravallion, Development Research Group of the World Bank

Some years ago a consensus emerged in the development community on the idea of an international poverty line of around $1 a day at purchasing power parity. This became the focus of the first Millennium Development Goal (MDG), which calls for halving the 1990 $1 a day poverty rate by 2015.

In a recent IPC One Pager, "Are Estimates of Poverty in Latin America Reliable?", Sanjay Reddy asserts that this poverty line is "arbitrary" and "unreliable." He feels that the line is too low to reflect well the Scost of not being considered poor in Latin America.

Reddy neglects to point out that the $1 a day line is not intended for measuring poverty in Latin America by the standards most Latin Americans would consider appropriate. The $1 a day line was explicitly designed to be representative of the poverty lines found in the poorest stratum of countries, none of which are in Latin America. While the latest available estimates indicate that about one fifth of the population of the developing world lives below $1 a day line, the figure is less than 10 per cent in Latin America (although that is still a lot of very poor people).

In measuring absolute income poverty in the world as a whole, there is a compelling case for treating any two people with the same real income the same way, even when they live in different countries. We need a common yardstick.

It is explicitly acknowledged by the World Bank that $1 a day is a frugal line. One could hardly argue that those people who are poor by the standards of the poorest countries are not in fact poor. This gives the $1 a day line a salience in focusing on the world's poorest that a higher line would not have. At the other extreme, suppose instead that one judged poverty in the poorest countries by (say) US standards. Learning that 95 per cent or more of the population is poor by this standard is unlikely to have much relevance in a poor country, given that US standards of living are not within most people's foreseeable reach.

Reddy claims there is a better approach, though he does not say much about the details. He refers to his paper with Thomas Pogge, which in turn cites Reddy et al. (2006), where one finds details on the preferred "capability approach." This entails calculating the cost of a country-specific food bundle for the poorest stratum of households in that country whose diets are deemed to be nutritionally adequate. To this food poverty line he adds an allowance for non-food spending consistent with the spending patterns of those near the food-poverty line. The key feature for Reddy is that a common nutritional cut-off point—he uses 2100 calories per person per day— should be used for all countries.

But hold on, this is sounding very similar to how most countries currently measure poverty. Indeed, it is the method used by 80 per cent of the country-specific poverty assessments summarized in Ravallion et al. (2008). The resulting national poverty measures are compiled in the World Bank's *World Development Indicators*, side-by-side with the international "$1 a day" numbers. It seems that Sanjay Reddy has reinvented the wheel.

Reddy also ignores an important problem: the purchasing power over commodities of the poverty lines generated by his preferred method is demonstrably not constant across countries. The reason is clearly not different nutritional cut offs, which do not vary much, but rather that there are multiple ways of reaching 2100 calories, implying very different standards of living. Unsurprisingly, people in richer countries tend to consume more expensive calories, and this is reflected in poverty lines. Across countries, the real income elasticity of the food poverty lines is 0.5; the elasticity of the non-food component of the poverty line is even higher, at 0.9 (Ravallion et al., 2008).

Thus two people with the same real income but living in different countries will not be treated the same way by Reddy's proposed method; typically the person living in the poorer country will be less likely to be deemed poor.

All this just brings us back to the key question: by which definition should we measure poverty in the world as a whole? The first MDG is implicitly saying that we should start with the definition found in the poorest countries, and give priority to bringing everyone in the world up to that standard. Once that is (hopefully) done, we can move to the task of bringing everyone up to the level of living needed to escape poverty in Latin America, by Latin American standards. We have a long way to go.

References:

Ravallion, Martin, Shaohua Chen and Prem Sangraula, 2008, "Dollar a Day Revisited," Policy Research Working Paper, World Bank, Washington DC. Available at <http://econ.worldbank.org/docsearch>.

Reddy, Sanjay G., Sujata Visaria and Muhammad Asali, 2006, "Inter-Country Comparisons of Income Poverty Based on a Capability Approach," Department of Economics, Barnard College. Available at <http://ssrn.com/abstract=915406>.

One Pager number 53
Published: May, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager53.pdf>

A Consistent Measure of Real Poverty:
A Reply to Ravallion

by Thomas Pogge,
Australian National University

In 1961, the United States Department of Agriculture published an Economy Food Plan carefully designed "as a nutritionally adequate diet for short-term or emergency use" for poor people. This diet was updated and later re-branded as the Thrifty Food Plan. The lowest cost stated for this minimal diet was $80.40 per person per month in 1999.

The relevant equivalent of the World Bank's $1 a day poverty line is $37.75 per person per month in 1999, and $49 today. This is clearly not enough to cover the basic nutritional and other needs of human beings in the US.

Is an equivalent to these amounts enough in poor countries? Obviously not, if "equivalent" means equally capable of meeting basic human needs. The $1 a day measure, however, relies on another notion of equivalence, which involves two conversions: converting any amount in local currency units (LCUs), via the national consumer price index (CPI), into its equivalent in some base year (currently 1993), and then converting the result, via 1993 purchasing power parities (PPPs), into 1993 US$s.

Imagine a simple world with three commodities: *necessaries*, *discretionaries*, and *services* (always in this order). If their prices do not move in lockstep, the CPI will reflect a weighted average of their price movements, based on the national spending pattern. By relying on the CPI, the $1 a day measure loses track of the price of necessaries. Falling prices of discretionaries (e.g., consumer electronics) may lead to a falling CPI even while rising biofuel demand is raising food prices. Poor people on constant incomes become poorer relative to what they need to buy, yet richer by the calculations of the $1 a day method.

Suppose the prices of the three commodities are LCU 5, 6 and 1 in some poor country and $3, $4 and $9 in the US. What is the PPP? Here again the answer depends on the spending pattern—in *both* countries. Suppose this pattern, in per cent, is 30, 50 and 20 in the poor country and 10, 50, and 40 in the US. This yields a PPP of 1.55; so the $1 a day measure will take each LCU to be equivalent to $1.55. But in reference only to necessaries, priced at LCU 5 and $3, each LCU is worth only 60 cents! Again, many who are very poor, relative to what they really need to buy, may not show up in the $1 a day statistics.

What is going wrong? Intuitively, income poverty (in the rock-bottom sense here at issue) is a function of what necessaries a person can buy. Through its reliance on CPI and PPP calculations, the $1 a day measure allows far too much influence to the prices of non-necessaries consumed in the same society. Through its reliance on PPPs, it also allows far too much influence to spending patterns in the US (and indeed in all other countries included in the PPP exercise). In our example, one LCU, though it buys only 60 cents worth of necessaries, is assigned much greater value because services are so expensive in the US ($9 versus LCU 1) and because US residents spend a lot on services. But should a poverty criterion be influenced so heavily by facts about prices and consumption of services that the poor do not need and do not consume?

Perhaps the best evidence one can have against any method is that its applications can deliver massively divergent results. The two notions of equivalence invoked in CPI and PPP calculations rely on very different (national and global) spending patterns. As a consequence, the comparison of two amounts in different years and countries varies with the base year chosen for the PPP conversion. One can use the CPIs of the two countries to convert into 1993 amounts and then compare via 1993 PPPs. Or one can use CPIs to convert into any other year and then do the comparison in PPPs of that year. One can get as many different results as there are PPP exercises.

The magnitude of the base-year effect is observable, because the Bank has actually worked with two base years. Before 2000, $1 a day was defined in terms of $31 PPP 1985, after 1999 as $32.74 PPP 1993. This switch of base year has caused large shifts in the relative position of national poverty lines. For example, using 1993 rather than 1985 as the base year raises all Chinese amounts—prices, incomes, consumption expenditures—in all years by 31 per cent relative to all Bangladeshi amounts in all years. And conversely, using 1985 rather than 1993 as the base year raises all Bangladeshi amounts in all years by 31 per cent relative to all Chinese amounts in all years. The $1 a day poverty assessment depends then on yet another irrelevancy: on the arbitrary choice of PPP base year.

Given the first Millennium Development Goal, millions of lives are at stake in counting the poor. Doing this requires a much more direct method than the $1 a day—a method that considers only the income a household has and the prices of the necessaries it might buy. A household is income-poor if it has no way of spending its money so that the basic needs of its members are fulfilled.

Ravallion is right; there are multiple ways of reaching 2100 calories. But this is irrelevant if the direct method focuses solely on the *cheapest* way each household has to get there.

Ravallion is also right to insist on a uniform criterion of income poverty, focused on the real income of the poor. Only the direct method achieves a consistent focus on what really matters: sufficiency for meeting basic human needs.

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Reddy, Sanjay G. and Pogge, Thomas (forthcoming). "How Not to Count the Poor", in J. Stiglitz, S. Anand and P. Segal (eds.) *Debates in the Measurement of Poverty*, Oxford: Oxford University Press. Available at <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=893159>.

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One Pager number 54
Published: December, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager54.pdf>

Equitable Access to Basic Services: **Who will Guarantee it?**

by Degol Hailu,
International Poverty Centre (IPC)

Current practice in utility provision involves the following. Governments retain ownership and pay for capital investments, while privatising the operations and management of the companies. Does this modality guarantee equitable access to water and electricity services?

Ensuring equitable access requires financing the initial outlays in infrastructure. Private companies seldom make these investments. More to the point, immediate profits are not assured. For instance, a British company walked out of a water-supply contract in Zimbabwe, claiming its customers were too poor to pay for its services. Water and electricity contracts are disputed, in some cases terminated, in many countries including Gambia, Kenya, Guinea, Mozambique, Nigeria and South Africa.

Public protests are common in response to exorbitant tariffs. A private electricity provider in Zambia submitted more than 10 applications for tariff revision. Consumers are expressing their discontent at three public hearings held by the Energy Regulation Board. Following the liberalisation of the sector in Nigeria, electricity prices increased by over 800 per cent. Recently, the country experienced widespread blackouts. In Guinea, water tariffs almost doubled after liberalising the sector. In Latin America, the cost of electricity connection reached 20 per cent of household income.

The expected efficiency gains are not always evident. Despite tariff increases only about a quarter of the total water connections were working in some countries. In other cases, wastage of water has remained at 40 per cent. In Cameroon and Burkina Faso, the electricity grid systems covered mainly the urban centres. Private management of utilities are linked to maintenance failures, cuts in water supply and electricity blackouts. The South African bill of rights guarantees water supply to poor households, but not all countries have such constitutional provision.

The deals offered to private contractors include purchase guarantees and tax holidays up to 30 years. Others obtained 100 per cent guarantee for the purchase of their output at fixed foreign exchange price. Indeed, there may be low investor interest and some enticement is necessary. However, the concessions result in heavy fiscal burdens, often diverting resources away from social spending.

Access to basic services in Sub-Saharan Africa (SSA) is extremely low. It is revealing to compare privatisation in the region with the United Kingdom and United States, where it had a better success. In the UK, water privatisation was proposed in 1984. The actual asset transfers took place over the period 1989-1990. Electricity privatisation started in 1989 with the split of the industry into many companies. Water privatisation intensified in the US beginning 1988.

Access to Essential Services

	Sub-Saharan Africa (2004)	UK (1980)	USA (1980)
Access to water (% of population)	56	100	100
Electric consumption (kWh per capita)	594	4,683	9,862

Source: World Development Indicators (April 2008).

When these countries privatised water provision, they had attained 100 per cent access. Electricity consumption of 4,683 kWh per capita in the UK and 9,862 kWh in the US was achieved. In contrast, by 2004, only 56 per cent of the population accessed clean water in SSA. About 83 per cent of the access was by urban dwellers. The 2004 electricity consumption in SSA was 6 per cent of the electricity consumption in the US in 1980 (see Table).

Clearly, discussions on privatisation in SSA must take its low access levels into account. Can the public sector do a better job? The record is not very telling. Publicly managed utilities are sometimes associated with poor maintenance, wastage, uncollected bills and uniform tariffs (irrespective of household income levels). There are success stories, however. Botswana's Water Utilities Corporation (WUC) increased the proportion of the population served by piped water. The restructured Namibian Water Corporation Ltd (NamWater) provides services adequately. Brazilian municipalities have been successful in supplying sanitation and water services equitably.

The lesson is this: the higher the level of access at the start of privatisation, the higher its success. Before embarking on full-scale privatisation, minimum targets on access must be achieved through restructured public provision. And when private provision is considered, it must be supported by adequate regulatory environments. These include the legal frameworks to enforce contracts and capacity to negotiate them in the interest of poor consumers.

Further Reading:

Bayliss, K. and Fine, B. (2007). *Privatization and Alternative Public Sector Reforms in Sub-Saharan Africa: Delivering on Electricity and Water* (eds.). London: Palgrave Macmillan.

One Pager number 55
Published: June, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager55.pdf>

Lessons from the **South African Electricity Crisis**

by Kate Bayliss, Centre for Development Policy and Research, SOAS

South Africa is suffering an electricity crisis. Blackouts have been widespread and the impact disastrous. Electricity supply is predicted to constrain growth for at least the next five years. How could this have occurred when until recently South Africa had a surplus of cheap electricity? This One Pager explores the causes.

The origins of the crisis stem from an ambitious electricity restructuring and privatisation programme started in the early 1990s. The process has been protracted, reforms have been difficult to implement and the private sector has failed to respond. Meanwhile, public investment has stalled; this is the main cause of the current crisis.

The focus of reform was on bringing market forces to bear on the electricity supply industry. Eskom, the state utility, was corporatised and in 2001, its core activities (the generation, transmission and distribution of electricity) were separated, with their finances ring-fenced.

The fragmented national distribution system was to be reorganized into six electricity distribution companies, owned by Eskom and the municipalities. Ultimately, the goal was competition and private sector participation in distribution. However, this process has involved complex legislation regarding the transfer of assets and has been painfully slow. By 2005, just one company had been created, only to be disbanded soon afterwards.

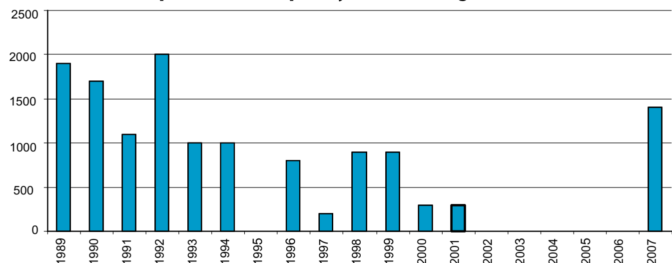
Crucially, policy uncertainty has contributed to a collapse in investment, in some cases falling to 1-2 per cent of the asset base rather than the desired level of 10 per cent. Lack of investment in the distribution infrastructure is a key factor in the crisis. There are now calls to drop the restructuring programme in favour of strengthening the existing structure.

In generation, the restructuring programme also aimed to create competition and bring in private sector participants. There was a moratorium on investment by Eskom in order to prevent crowding out of the private sector. In addition, public expenditure was steered away from investment to boost the economy following the removal of capital controls. There was, however, virtually no interest from the private sector: investment in new generating capacity dropped to zero between 2002 and 2006 (see Figure).

During the recent power cuts, a very high proportion of generation capacity was out of service. During January 2008, for example, this reached 23 per cent, mostly due to unplanned maintenance.

The Eskom plant is under severe strain due to factors such as poor coal quality, staff shortages and a high load on its capacity. A vicious circle has developed: a high proportion of plant is out of action, so further strain is placed on the existing plant, which becomes even more likely to break down.

Installed and Operational Capacity Added (Megawatts)



Source: UBS Investment Research.

Underlying the low level of plant availability in the longer term is the lack of investment in generation capacity, which has stemmed from unwarranted optimism in the willingness of the private sector to invest. The result has been a fall in Eskom's reserve margin (the ratio of peak-load unused capacity to total capacity) from more than 20 per cent to a precariously low eight per cent.

Because of this additional strain on the system, frequent outages are inevitable. Similar reform packages have been repeated in much of sub-Saharan Africa. But the 'unbundling' of the electricity supply industry to facilitate private sector participation has failed to elicit the critically needed investment (Bayliss and Fine 2008).

Across all developing countries, private sector investments in the power sector declined from US$ 47 billion in 1997 to US$ 14 billion in 2004. However, international advisors have continued to adhere to the orthodox package of restructuring policies, claiming that obtaining private sector investment is unavoidable because of a widening 'investment gap' in the power sector.

Meanwhile, a dramatic and rapid scaling up of financing is required in South Africa. Eskom plans to invest about US$ 44 billion over the next five years to raise capacity in the energy sector. This is projected to be financed by a combination of borrowing, price hikes and a government loan of US$ 7 billion. But the additional capacity will take several years to come on stream.

The electricity crisis of South Africa demonstrates that the widespread efforts across developing countries to encourage private sector investment in the electricity industry are unlikely to succeed. So the government and state utility must continue to scale up public investment in order to maintain and expand electricity capacity.

This article is published jointly with the Centre for Development Policy and Research.
See the Development Viewpoint series at <www.soas.ac.uk/cdpr>.

Reference:

Bayliss, Kate and Ben Fine, eds. (2008). *Privatization and Alternative Public Sector Reform in Sub-Saharan Africa*. London: Palgrave MacMillan.

One Pager number 56
Published: June, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager56.pdf>

Tariff Hikes with Low Investment: The Story of the Urban Water Sector in Zambia

by Hulya Dagdeviren, University of Hertfordshire and Degol Hailu, International Poverty Centre

According to current estimates, the Millennium Development Goal (MDG) of halving the 1.1 billion people without access to safe drinking water by 2015 will only be achieved by 2040, especially in Sub-Saharan Africa (SSA). Why will it take this long? Because tariffs are unaffordable and investments in infrastructure are extremely low.

The privatisation of water services has not helped reverse these trends. In many developing countries, privatisation has resulted in "spectacular failures", according to the UNDP's *Human Development Report 2006*. The failures spring from the absence of competitive market structures, ineffective regulation, and weak capacity to enforce and negotiate contracts.

The corporatisation of public companies and the commercialisation of water services are now common. These measures are often seen as intermediate steps towards "cost recovery" before full privatisation. An improvement in the performance of public utilities is welcome. But the current reforms are problematic in their excessive reliance on tariff rationalisation and their neglect of investment needs. The commercialisation of urban water services in Zambia is a good example.

Until the 1990s, Zambia's central government was responsible for the delivery of urban water services, except in the Copperbelt. Water tariffs were subsidised. Because of economic decline in the 1970s and 1980s, however, the government could not sustain the necessary investments and maintenance. The commercialisation of water started in the early 1990s, and by 2006 there were 10 commercial water companies in Zambia's urban centres.

Commercialisation led to tariff increases of up to seven-fold in real terms. Can the poor afford water tariffs in Zambia? The ratio of household spending on water to household income is the yardstick commonly used to assess affordability. The 5 per cent and 3 per cent benchmarks are often used. Our estimates indicate that, by both measures, low-cost water is unaffordable for about 40–60 per cent of urban dwellers in Lusaka and the Copperbelt, where most of the urban population lives. Using the 5 per cent benchmark, moreover, we found that water is unaffordable for all urban households in extreme and moderate poverty, except for those in the Southern Region.

It is unsurprising, therefore, that the proportion of the population with access to safe water declined from 72 per cent in 1992 to 57 per cent in 2002. The quality of access has also deteriorated: about 25 per cent of users lost their piped supply and became dependent on public taps, wells, boreholes, rivers, ponds and lakes (Table 1).

Because levels of access to water are low, utilities have to raise tariffs even higher to recover costs. Average cost recovery, however, was only 67 per cent. One reason is low revenue collection: 25 per cent of the billed amounts are never collected. The other is the high level of "unaccounted for water rate", which is the difference between the volume of water produced and the amount billed. This rate averaged about 50 per cent throughout the commercialisation period, largely because of poor infrastructure, lack of maintenance and wastage.

Table 1

The Population's Access to Water in Zambia (% of population)

	1992	2002
Total national access	72	57
Total urban access	93	90
Piped into residence	55	42
Public taps	34	38
Wells and boreholes	9	16
Rivers, ponds, lakes etc.	2	4

Table 2

Investment in the Water and Sanitation Sector, 1998–2002

	Actual government capital expenditure as a percentage of budgeted capital expenditure	Actual expenditure* as a percentage of required capital expenditure to maintain existing access rates
1998	3.1	2.4
1999	2.4	2.9
2000	3.0	1.8
2001	12.3	2.0
2002	8.8	2.2

* Including donor funds in the sector.

Are market-based solutions the answer to a lack of investment? The evidence indicates that investment did not increase after liberalisation. Not only has the government underinvested in the sector, but it has also failed to maintain its plans for capital expenditure. Total capital expenditure, including donor funds, has remained a minor fraction of the spending needed to maintain existing rates of access to water (Table 2).

The policy dilemma is how to fund capital investment without high tariffs restricting access. So far, Zambia's liberalisation strategy has emphasised tariff rationalisation. This has failed to ensure full cost recovery and has further constrained affordability and accessibility. The correct policy prescription is up-front public investment to renew and extend infrastructure. This approach would reduce unit costs in the sector, make tariffs affordable and improve the sustainability of cost-recovery efforts. Otherwise, Zambia is unlikely to meet the MDG on water for a very long time.

Further Reading:

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One Pager number 57
Published: June, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager57.pdf>

What Do We Mean by "**Feminization of Poverty**"?

by Marcelo Medeiros and Joana Costa, International Poverty Centre

The "feminization of poverty" is an idea that dates back to the 1970s. It was popularized at the start of the 1990s, not least in research by United Nation agencies. The concept has various meanings, some of which are not entirely consistent with its implicit notion of change. We propose a definition that is in line with many recent studies in the field: *the feminization of poverty is a change in poverty levels that is biased against women or female-headed households.*

More specifically, it is an increase in the difference in poverty levels between women and men, or between households headed by females on the one hand, and those headed by males or couples on the other. The term can also be used to mean an increase in poverty due to gender inequalities, though we prefer to call this the *feminization of the causes of poverty.*

The precise definition of the feminization of poverty depends on two subsidiary questions: what is *poverty*? and what is *feminization*? Poverty is a lack of resources, capabilities or freedoms that are commonly called the dimensions of poverty. The term "feminization" can be used to indicate a gender-biased change in any of these dimensions. Feminization is an action, a process of becoming more feminine. In this case, "feminine" means "more common or intense among women or female-headed households".

Because it implies change, the feminization of poverty should not be confused with the prevalence of higher levels of poverty among women or female-headed households. Feminization is a process, whereas a "higher level of poverty" is a state. Feminization is also a relative concept based on a comparison of women and men, including households headed by them. What is important here is the difference between women and men at each moment. Since the concept is relative, feminization does not necessarily imply an absolute worsening in poverty among women or female headed-households. If poverty is reduced sharply among men and only slightly among women, there would still be a feminization of poverty.

Relative changes in poverty levels can be measured in terms of poverty "among female-headed households" and "among women". These indicators, however, do not reflect the feminization of poverty. Both these and "feminization" capture a gender dimension of poverty, but in distinct ways. They differ by the unit of analysis and by the population included in each group, and obviously they have different meanings. There are reasons to consider both. The goal of headship-based indicators is to show what happens to specific vulnerable groups of women and their families, and thus their unit of analysis is the household. The population considered includes both men and women (and children) living in those households. It excludes women and men living in other household formations.

Indicators of poverty among females completely separate men and women as individuals, and include or exclude children as a gendered group in their aggregations. In determining the feminization of poverty, interpretation of results drawn from individual measures of poverty may not be accurate. Since poverty is usually measured at the household level, male poverty is intrinsically associated with female poverty and vice versa.

The feminization of poverty can also be defined as "an increase in the share of women or female-headed households among the poor". In contrast to our proposal, this definition focuses on changes in the profile of the poor and not on poverty levels within gender groups. Thus it has a potential disadvantage. It is difficult to interpret the results from this approach because measures of the feminization of poverty can be affected by changes in the demographic composition of the population. For instance, the impoverishment of female-headed households can be offset by a decline in the total number of such households, and thus the result in terms of feminization can be zero. The definition we propose gives rise to indicators that are not affected by these composition effects, which can be analyzed separately.

The feminization of poverty combines two morally unacceptable phenomena: poverty and gender inequalities. It thus deserves special attention from policymakers in determining the allocation of resources to pro-gender equity or anti-poverty measures. If poverty is not being feminized, resources can be redirected to other types of policies. Of course, whether or not the feminization of poverty is occurring in each country is a matter of empirical analysis. We propose a definition of the feminization of poverty that sees the phenomenon as a change in poverty levels that is biased against women or female-headed households. This definition provides a simple but effective tool for conducting policy analysis.

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One Pager number 58
Published: July, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager58.pdf>

Equitable Access to Financial Services: Is Microfinancing Sufficient?

by Degol Hailu,
International Poverty Centre

Access to the financial sector has numerous benefits. Savers and investors are matched, transactions costs are lowered and liquidity is created. But less than half of the households in developing countries have access to financial services, compared to over 70 per cent in the developed world.

By 2006, even in relatively successful countries such as Ghana and Tanzania, only about 6 per cent of the population had access to banking services. In Benin, there were only 35 bank branches serving a population of 7 million. Will microlending increase access to financial services?

Microfinance institutions (MFIs) serve the rural and urban poor, especially disadvantaged women. Often, commercial bank branches are far from towns and villages, and the transport costs needed to access them are unaffordable. The poor may even lack the minimum cash amounts required to open bank accounts. Unfamiliarity with the complex procedures and paperwork involved in withdrawing and depositing money can also constrain access.

Hence it is unsurprising that MFIs are attractive to the poor. They pool resources to spread risks for both borrower and lender. Traditional networks and peer reviews ensure creditworthiness. Loans are secured through joint liability. And savings cushion seasonal fluctuation in earnings or can be used to pay for social events and production inputs.

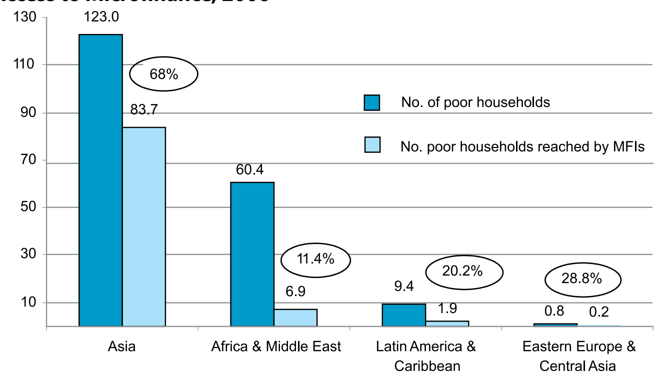
The 2006 Global Microcredit Summit pledged to provide microfinance to 175 million poor households by 2015. Governments and development agencies support the expansion of MFIs. For instance, the International Finance Corporation bought over US$ 1 million in shares in the Accion Micro Finance Company of Nigeria.

By 2006, there were 3,316 MFIs with more than 133 million members worldwide. Of these, 69.8 per cent were among the poor (defined as earning less than US$ 1 a day). Women accounted for 85 per cent of poor clients. In Sub-Saharan Africa, a total of 970 MFIs reported having 8.4 million clients.

As regards *households*, however, the figures tell a slightly different story. Of the 193.6 million poor families worldwide, only 47.8 per cent were within reach of MFIs. Of the 60.4 million poor households in Sub-Saharan Africa and the Middle East, only 11.4 per cent had access to microcredit. Asia fared better: 68 per cent of the region's 123 million poor households had access to microcredit (see Figure). Within Sub-Saharan Africa, a small number of countries are beneficiaries. About 1.4 million households in Ethiopia, 1 million in Nigeria and 688,199 in Burkina Faso participated in microfinancing schemes.

Even in Asia, the successes of MFIs have not been unqualified. Research shows that most poor clients are just below the poverty line—they are what is termed the "richest of the poor". MFIs were biased towards urban dwellers and were excessively dependent on external funding (Chandrasekhar, 2004).

Access to Microfinance, 2006



Source: Daley-Harris (2007). Circled figures indicate the share of poor households reached by MFIs.

What would enable MFIs to improve service delivery? One popular recommendation is to link them to commercial banks. Branch network-sharing, for example, benefits both the MFIs and the banks. It provides the latter with a wider client base and facilitates the extension of credit to MFI clients, especially among the owners of small enterprises (a development known as "the formalisation of the informal economy"). Linking MFIs to commercial banks, however, does not guarantee that enough of the poor will be reached. The effects of such endeavours are limited by the shortage of commercial banks, particularly in rural areas.

Ultimately, public policy will have to include direct lending to reach enough of the poor. In this regard, China's rural credit cooperatives and Vietnam's Bank for Social Policies are two examples worth considering. These countries provided selective interest rates, investment guarantees and export-promotion credit. Public policy focused on rural development through credit programs in labour-intensive sectors. Available information shows that half of the loans were provided to poor households, a third went to beneficiaries in remote areas, and more than a fifth was devoted to job creation. China and Vietnam experienced a dramatic fall in poverty levels. Their experience provides a lesson to be learned.

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One Pager number 59
Published: July, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager59.pdf>

New York's Brand-new Conditional Cash Transfer Programme: **What if it Succeeds?**

by Michelle Morais de Sa e Silva,
International Poverty Centre and Columbia University

In 2007, emulating the Mexican experience, Mayor Bloomberg decided that New York City should also have its own conditional cash transfer programme (CCT). He named the programme Opportunity NYC after the Mexican *Oportunidades*. Is Opportunity NYC just one more CCT in the plethora of existing programmes? Or will it influence the way educational reforms have been traditionally conceptualized?

Considering the frustration in the US with past education policies, there are reasons to believe that, if Opportunity NYC succeeds, it will influence future reforms. There will be a policy shift from improving teacher quality and accountability to enhancing demand by buying student motivation.

Opportunity NYC comprises three different sub-programmes: (1) Opportunity NYC Family Rewards; (2) Opportunity NYC Work; and (3) Opportunity NYC Spark. Family Rewards is a programme in which both parents and children can obtain cash rewards for activities related to health, education and parental involvement in school. Work rewards are for recipients of housing vouchers. It provides monetary incentives for finding paid employment and enrolling in professional training courses.

This *One Pager* looks at the Spark sub-programme, which is the educational component. Spark is solely focused on low-income students in 4th and 7th grade and gives them cash rewards in exchange for academic performance. The programme is separately managed by the City's Department of Education. The Spark's conditions and rewards are as follows: "students in the fourth grade will receive up to $25 for a perfect score on each of the 10 interim assessment tests taken throughout the year, up to a total of $250. Seventh graders can earn up to $50 per test for a maximum payment of $500 per year" (Seedco, 2007).

When compared to other CCT programmes around the world, Opportunity NYC stands out for making conditions for cash transfers that are mostly performance-based. The logic behind transfer conditionalities, in the case of the Mexican *Oportunidades* and the Brazilian *Bolsa Família,* is one of encouraging families to send their children to school as a way of breaking the intergenerational cycle of poverty. Their aim is to cope with the opportunity costs that children face to go to school. In contrast, Opportunity NYC focuses on improved academic performance as a condition for cash transfers. Despite not being the first CCT programme to go beyond school attendance, it is certainly the first to place grades at the heart of conditionalities (Mexico, Argentina and the City of Bogota have already made transfers conditional on grade completion).

Although the programme looks like it is imported from Mexico, it was completely designed by the American Inequality Lab, led by Professor Roland Fryer from Harvard University. Fryer argues that poor children lack the incentives to perform well. He often states that they do not have a close example of the returns to investing in education. In his view, cash incentives can provide the real motivation for poor children to do better in school. This argument goes against the human capital view of education, which sees it as an investment. It also neglects the potential role of education as an empowering and liberating experience.

Opportunity NYC Spark addresses educational performance as if it were exclusively about parental and student effort and the availability of cash incentives. It does not tackle the limits of what students can achieve (no matter how motivated they are) due to, for instance, lack of teacher qualifications, violence in schools and scarcity of educational resources.

What then would be the implications of a successful Opportunity NYC? First, success will mean that the provision of cash incentives will be given priority in educational reforms, leaving aside the traditional emphasis on teaching practices, school finance and governance structures. Longstanding debates and educational research will shift to determining the exact cash amount needed to produce the highest test results. Second, performance-based conditions may spread beyond New York City borders, "contaminating" not only other US cities and states, but also CCTs in developing countries.

Consequently, what is considered a pioneering South-North cooperation between Mexico and New York, may have a boomerang effect. The South may be compelled to follow-suit after the NYC experience. If so, we need to be alarmed—supply side issues and quality of education will be set aside, focusing too much on cash-based and demand-side incentives.

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One Pager number 60
Published: July, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager60.pdf>

Where Are the Jobs that Take People **Out of Poverty in Brazil?**

by Ana Flávia Machado, Centre for Development and Regional Planning, UFMG and Rafael Perez Ribas, International Poverty Centre

In Brazil's urban areas, job opportunities determine economic mobility and poverty. But not every job provides enough earnings to take families out of poverty. Jobs for poor workers are scarce in the formal sector. To improve their income, the poor resort to informal, unregistered jobs that are highly vulnerable. The contribution of informal jobs to poverty reduction should not be neglected.

In Brazil's metropolitan areas, about 70 per cent of those who are poor in a given month remain in poverty the following month. About 53 per cent of them are still in poverty after 12 months. These rates are slightly lower than those in developed countries. In the United States and the United Kingdom, for example, about 60 per cent of low-income groups remain in the same circumstance after a year. This suggests that Brazil's metropolitan labour markets have been more effective in promoting income mobility for poor workers. (Using Brazil's Monthly Employment Survey of 2004, we define poverty by per capita income in relation to the relative poverty line of 60 per cent of median income).

The links between job conditions and income mobility have not been adequately examined in many Latin American countries, including Brazil. To fill this gap we classify workers aged 18 to 60 into three groups. The first comprises formal sector workers (registered employees, employers, public servants and registered professionals). The second consists of informal sector workers (self-employed or non-registered employees). In the third group are the unemployed—those without a job but searching for one, according to the definition of the International Labour Organisation (ILO). Then, noting the initial labour condition, we identify the percentage of people who have moved from poverty to non-poverty.

As regards upward mobility, 3 per cent of poor workers in the informal sector move out of poverty the following month. For formal sector workers the rate is only 1 per cent, and thus poor workers in the formal sector are less likely to escape poverty. Additionally, about 85 per cent of informal workers who move out of poverty continue working in the informal sector and only 11 per cent move to a formal job (see the table). Hence these workers can escape poverty while remaining in the informal sector.

The unemployed move out of poverty at a higher rate of about 6 per cent. Some 51 per cent of them find work and thus improve their income. The most interesting result is that only 14 per cent of the unemployed experience upward mobility as a result of finding formal employment. This suggests that the formal sector has not helped people to escape poverty as much as the informal sector. Informal jobs account for 37 per cent of the upward mobility experienced by the unemployed. The upward mobility of the other half might be explained by the entry of other household members into the labour market—the "additional worker effect".

Workers Moving In and Out of Poverty in Brazilian Metropolitan Areas, 2004 (%)

Initial condition	Moving out of poverty	Condition the following month			
		Informal	Formal	Unemployed	Inactive
Informal	3	85	11	1	2
Formal	1	9	91	0	0
Unemployed	6	37	14	32	17
Initial condition	**Falling into poverty**	**Condition the following month**			
		Informal	Formal	Unemployed	Inactive
Informal	4	58	4	16	22
Formal	2	9	61	12	19
Unemployed	3	3	2	60	35

Source: authors' calculation based on the Brazilian Monthly Employment Survey, 2004.

Downward mobility figures show that 3 per cent of the unemployed and 4 per cent of informal workers who were not poor became poor after a month. For workers in the formal sector, the monthly rate of entry into poverty is only 2 per cent. Informal sector workers, therefore, are the most likely to fall into poverty because they may lack social protection during economic downturns.

Independently of their initial condition, about 60 per cent of the poor who fall into poverty retain the same labour status. That is, workers stay in their initial sector and the unemployed remain unemployed. But the percentage of workers who enter poverty because of unemployment is higher in the informal sector (16 per cent) than in the formal sector (12 per cent).

In conclusion, job opportunities are crucial to reducing urban poverty. Obviously, the formal sector provides the best conditions for workers, but in Brazil the poor have very limited access to this sector. Informality has been an alternative means of promoting upward mobility under low-income conditions, despite its greater vulnerability.

An effective policy should focus on creating formal jobs. This can be done by improving workers' skills and making formal employment more attractive. Expanding credit for small businesses would also help. Better safety nets that protect both formal and informal workers might be an effective policy alternative in the short run.

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One Pager number 61
Published: July, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager61.pdf>

The Global Benefits and Losses from
The U.S. Recession and Recovery Package

by Francis Cripps, Director of Alphametrics Ltd., and Terry McKinley, Director of the Centre for Development Policy and Research, SOAS

Until 2007, many people had believed that global economic growth, led by the U.S., could continue unabated for the foreseeable future. Mainstream commentators based their optimism on greater global economic integration and the adoption of market-driven patterns of development. They seemed little concerned that global current-account imbalances, especially the U.S. deficit, would remain huge.

Using such rosy assumptions, our macroeconomic model, *State of the World Economy*, made a baseline projection that by 2015 income per capita would increase by 15 per cent in the U.S. and by significantly more in other developed countries. Income in many middle-income countries, such as those in the CIS, the Middle East and Latin America, would grow more rapidly.

China and many other countries in Asia would do moderately well, achieving growth rates of 6-7 per cent. South Africa would grow by almost five per cent but the rest of sub-Saharan Africa would gain only negligibly. In fact, energy importers in the region would have zero growth from 2008 to 2015.

During the last year and a half, this optimistic scenario has looked increasingly irrelevant. Several factors have been important: big increases in the prices of oil and food, the end of the U.S. housing boom, increased fragility of the U.S.-led banking system, sharp depreciation of the dollar, ongoing conflict in the Middle East and increasing evidence of global warming.

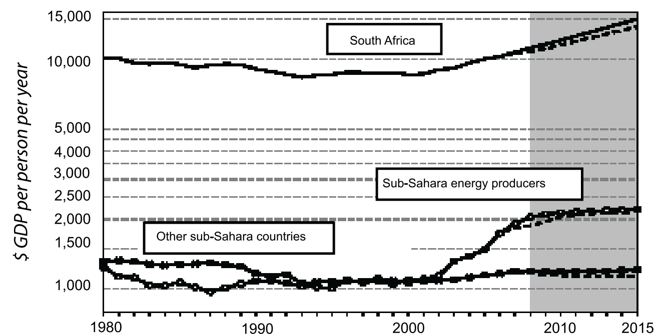
Assuming the combination of higher oil prices, U.S. recession and a falling dollar and no U.S. policy response, our macroeconomic model projected that the yearly growth of income per capita in the U.S. would have been -0.2 per cent between 2008 and 2015 and its level in 2015 would have been 15 per cent below the baseline projection.

But the Federal Reserve has moved swiftly to lower interest rates and inject credit into the financial system. And the Federal government has significantly increased spending and reduced taxes. While such measures are likely to improve spending in the U.S. and elsewhere, the disadvantage is that they are also likely to maintain high energy prices.

Under such conditions, our model projects that U.S. income per capita would improve slightly by 2015, ending up with a yearly growth rate of 0.5 per cent. But its level would still be 11 per cent below the baseline projection. Its long-term prospects would also be much bleaker. Income in Japan and Western Europe would be 8 and 12 per cent below the baseline, respectively. The U.S.'s mammoth current account deficit would worsen, in fact, from about 5.5 per cent of GDP to 5.9 per cent. Japan's surplus would continue at a little over four per cent of GDP.

The shortfalls in income (compared with the baseline) would be deepest in the middle-income countries in the CIS, the Middle East and Latin America (30, 22 and 17 per cent, respectively). While the current account surplus of the Middle East would drop markedly, that of the CIS (e.g., Russia) would increase.

Income Trends in Sub-Saharan Africa



The upper line for 2008-15 shows outcomes projected under the baseline scenario. The lower line (dotted) shows outcomes with a US recession and recovery package.

Growth in China would continue at only five per cent per year, in India at over three per cent and in the rest of developing Asia at less than three per cent. And the drops in their incomes, relative to the baseline, would be 8-11 per cent. China's current account surplus would drop substantially but India's deficit would be almost eliminated.

Our projection produces a more complex story in sub-Saharan Africa (see Figure). South Africa would do moderately well: it would grow at 3.7 per cent, lose only modestly relative to the baseline projection and gain a measurable decline in its huge current account deficit. Energy exporters in sub-Saharan Africa (such as Angola, Nigeria and Sudan) would grow at the same rate, 2.9 per cent, as under the baseline but their current account surpluses would decline below one per cent of GDP.

Energy importers in sub-Saharan Africa would fare the worst. Home to about 520 million people, i.e., almost two-thirds of the sub-Saharan total, these countries are overwhelmingly low-income. Though badly in need of rising incomes, they would experience a decline in income of 1.2 per cent per year. This compares with zero growth even under the optimistic baseline projection.

As a result of their domestic stagnation, their current account deficit, currently 7.4 per cent of GDP, would decline to five per cent in 2015. Heavily dependent on a few primary commodities for export revenue, they would still be subject to expensive oil imports since real oil prices would rise markedly.

Whether growth in the global economy increases or declines, it appears that these countries would still be stuck at the bottom of the ladder, in a 'poverty trap'. Their integration with the global economy is narrowly based and vulnerable. The results are asymmetric: they cannot gain from global upturns while they cannot escape the worst of global downturns. In future work with the model, we will analyze their condition more deeply and propose policy options.

One Pager number 62
Published: August, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager62.pdf>

A Global Realignment by 2020:
U.S. Decline, Emerging Economies Rise

by Francis Cripps, Director of Alphametrics Ltd., and Terry McKinley, Director of the Centre for Development Policy and Research, SOAS

In IPC's One Pager No. 62, we projected until 2015 the impact on the global economy of rising oil prices, a falling dollar and a U.S. recession, and then the additional effect of the monetary and fiscal stimulus that the U.S. Government implemented in response to the crisis. In the process, we discovered that the long-term prospects of the U.S. economy were projected to worsen after 2015.

So, for our current modelling, we: 1) project outcomes for 2020 instead of 2015 and 2) assume a sizeable yearly U.S. fiscal stimulus for 2008-2011 instead of just 2008. The total stimulus package—which amounts to 0.5 per cent of GDP each year in tax cuts, additional expenditures and credit incentives for private investment—should help the U.S. economy not only escape a severe recession but also fare better over the long term than originally projected.

Our focus in this One Pager is the resultant impact of such a scenario on the U.S. economy itself and on three large emerging economies, Brazil, China and India. Note that we hold constant, for now, the policy stance of these three countries.

We find that U.S. income per capita would begin falling after 2013, as the impact of our assumed four-year fiscal stimulus wore off. During the whole period 2008-2020, the projected growth of U.S. income per capita is only 0.5 per cent per annum, well below that of most other developed economies. If our assumed stimulus had not been applied, the projected outcome would have been much worse.

Why the U.S. Decline?

The principal determinants of U.S. decline are deep-seated structural problems, such as the persistence of a large current account deficit and an onerous external indebtedness. Despite the slowdown in U.S. growth, its current account deficit is projected to rise from -5.5 per cent of GDP in 2008 to -6.3 per cent in 2020.

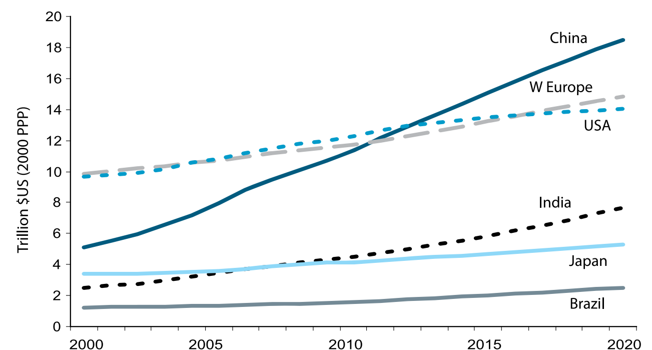
We make the critical assumption that dollar devaluation—which could play a supplementary role to fiscal policy—would cease in 2010. This would be necessary, we conclude, to contain mounting inflationary pressures (due to persistently high fuel and food prices) as well as mounting debt problems.

In contrast to U.S. stagnation and decline, China's income per capita is projected to grow by 4.7 per cent per annum during 2008-2020. This is a marked slowdown from its recent trend rate of growth of 7-8 per cent, but still high compared to the projected rates of other developing and developed countries.

Because of the global slowdown, especially U.S. stagnation, China's substantial current account surplus in 2008, namely, 6.8 per cent of GDP, would be cut by a full three percentage points by 2020. And it would face further challenges after 2020 from its increasing imports of manufactures, raw materials and high-cost energy.

India is projected to continue its current momentum of four per cent growth of per capita income through 2020 despite the global slowdown.

Size of the Main Economies in 2020



Since it is less dependent than China on imports, its current account would noticeably improve, progressing from a deficit of -2.4 per cent in 2008 to a small surplus of 0.5 per cent in 2020. This would be based on growing service income and increasing exports of manufactures.

Brazil's per capita income is slated to grow by a somewhat slower, but still credible, 3.4 per cent. It would benefit from sustained demand for its commodity exports and increased intra-regional trade and investment. But its conservative financial policies, which prop up the value of its currency, imply that its small current account deficit (i.e., a negative 0.3-0.4 per cent of GDP) would change little by 2020.

Global Realignment

Given the growth trends of all developed and developing countries, we project that by 2020 there would be a major realignment of the global economy, with the United States sinking significantly in importance and the three emerging economies assuming greater prominence.

In 2008, the size of China's economy (measured in purchasing power parity terms) was about 86 per cent of the U.S. economy's. By 2020, the corresponding percentage would be about 132 per cent (see Figure). Thus, China's economy would be the largest in the world, its size surpassing handily both those of the U.S. and Western Europe.

India's economy would enlarge from about 35 per cent of the U.S. economy in 2008 to about 55 per cent in 2020, and surpass the size of Japan's economy by about 45 per cent. From a much smaller starting point, Brazil would also acquire significantly more economic weight. For example, its economy would be about 38 per cent larger than Eastern Europe's total economy and be approaching one fifth of the U.S economy.

These results suggest that there would likely be seismic economic and political changes by 2020. These dynamics would be even more dramatic if the economic policies of China, India and Brazil were adjusted in order to enhance their long-term development prospects. This a topic to address in future papers.

This article is published jointly with the Centre for Development Policy and Research.
See the Development Viewpoint series at <www.soas.ac.uk/cdpr>.

One Pager number 63
Published: August, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager63.pdf>

Is the Conditionality Necessary in Conditional Cash Transfer Programmes? **Evidence from Mexico**

by Alan de Brauw and John Hoddinott, International Food Policy Research Institute

Conditional Cash Transfers (CCTs) are an increasingly popular tool for poverty alleviation. Drawing on lessons learned from programmes in a variety of countries—notably Mexico's *PROGRESA* programme—they are now found throughout the developing world. CCTs give cash transfers to households that meet specific conditions or undertake certain actions, such as ensuring that school-age children go to school or that pre-school children regularly see a nurse or doctor.

While empirical evidence demonstrates CCTs improve out comes related to health, nutrition and education, the desirability of imposing conditions on beneficiaries to attain those outcomes is a contentious issue.

Rationales for imposing conditions emerge from both public and private perspectives. From a public perspective, governments may perceive that they know the actions or behaviors that will benefit the poor better than do the poor themselves. Conditioning transfers then induces changes in behavior that leads to desirable outcomes. For example, governments may value female education more than families do. Conditioning may also help the government overcome information asymmetries. For instance, governments may understand the benefits of immunization, while individuals may be unaware of them. Conditioning transfers on immunization overcomes this informational asymmetry.

Finally, conditioning may have political economy benefits. Politicians and policy makers are often evaluated by performance indicators such as changes in school enrollment or health clinic use. By conditioning transfers on behaviors that increase these indicators, politicians and policy makers can provide useful evidence of accomplishments long before the desired outcome of poverty reduction occurs.

Conditionality can also provide private benefits. It can strengthen the bargaining position of women whose preferences are aligned with the government's preferences, but who lack bargaining power within the household. It may overcome stigma effects otherwise associated with welfare payments. Finally, recent work in behavioral economics finds that myopic households often undertake actions that can reduce their own long-term welfare. Conditionality offers a constraint that limits the adverse effects of this myopia.

Although there are several rationales for conditionality, some have raised concerns about its imposition. Conditionality is costly, and if the benefits of conditionality do not outweigh the additional costs, it may not be worthwhile. The primary public cost is associated with monitoring behavior, which would not be incurred without the conditions. Conditionality can create an opportunity for corruption, as individuals responsible for certifying that conditions have been met could demand payments for doing so. Conditionality can also impose costs on beneficiaries, and those costs may not be borne equally within the household. If the preferences of the poor do not align the conditions on their behavior, conditionality reduces welfare gains from participation.

Some households may find the conditions too difficult to meet; if such households are poor relative to other participants, imposing conditions may detract from the targeting of the CCT. Lastly, conditioning transfers can be perceived as demeaning to the poor, as one can argue that imposing conditions implies that the poor are either irrational or incapable of understanding their best interests.

Since conditionality is always part of a CCT programme, it is not clear whether its benefits actually outweigh the costs outlined above. To judge the benefits of conditionality, we considered the fact that some beneficiaries of Mexico's *PROGRESA* programme did not receive the forms needed to monitor the attendance of their children at school. Therefore their transfers were effectively unconditional.

Using administrative data on transfers in combination with data collected as part of *PROGRESA's* evaluation, we assessed the impact of imposing education-related conditions on school enrollment and attendance. Regardless of empirical technique, we find that on average children in households that did not receive the monitoring forms are 7.2 percentage points less likely to enroll in school. When children were making the transition to lower secondary school, the impact was even larger, while there was no measurable impact on children continuing in primary school. The impact is even more pronounced among households with illiterate heads.

Our results show that the benefits of conditionalities can be large. They could also be made much more efficient by calibrating the design of programmes based on the heterogeneity of the effect of the conditionality, they could be much more efficient.

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One Pager number 64
Published: August, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager64.pdf>

The New Global Poverty Estimates – **Digging Deeper into a Hole**

by Sanjay Reddy, Barnard College and School of International and Public Affairs, Columbia University

Recently, the World Bank released "updated" global poverty estimates. These new numbers are based on a new price survey and a new benchmark international poverty line of $1.25 in 2005 purchasing power parities (PPPs). The new figures purport to describe world poverty since 1981, and thus affect our understanding of the world over the last quarter century of globalization.

The new estimates also suggest that the number of poor is almost fifty per cent more than previously thought. Can the new estimates be trusted? Unfortunately, the numbers are based on the same methods used earlier and are undermined by the same problems as the earlier estimates.

The new international poverty line is too low to cover the cost of purchasing basic necessities. One could not live in the US on $1.25 a day in 2005, nor therefore on an equivalent amount elsewhere. One's daily income can be a great deal higher than $1.25 and still leave one unable to fulfill basic nutritional requirements. Since the international poverty line is defined in equivalent purchasing power units, this incoherence is not easy to overcome.

Another problem is using inappropriate PPPs to convert poverty lines across currencies. Consider the question of how many *rupiahs* are needed in Jakarta to possess the purchasing power of a dollar in Washington, DC. The question cannot be answered without first establishing the purpose to which the money is to be put. If the purpose is to purchase the goods needed to escape severe poverty (such as staple foodstuffs, which are internationally tradable and the prices of which tend more closely to reflect market exchange rates) the rate of equivalence may be different than if the purpose is to buy domestic services (which are relatively cheaper in poor countries as labour is less mobile). The PPPs calculated for each country also inappropriately reflect irrelevant information about the pattern of consumption in third countries other than the country in which the price level is being assessed and the base country with which prices are compared (the US). This is because the worldwide pattern of consumption determines the weights placed on different commodities when assessing the price level in each country.

The new poverty line is itself allegedly based on an average of poverty lines used in poor countries. However, many of these poverty lines have been defined by the Bank itself and they are translated into common units using the very PPPs the application of which is in question. The underlying source of the problems is the lack of a clear criterion for identifying the poor. We have no basis to conclude that the new set of PPPs generate poverty estimates which are closer to the "truth".

Even if the latest PPPs present a better picture of relative prices in 2005, that does not make them a better basis to judge poverty across countries in the previous years in which poverty must also be estimated to assess trends. The relative extent of poverty in different countries and years, and the estimated trend, is dependent on the base year chosen for the exercise and there is no convincing basis to pick the estimates corresponding to one base year over those corresponding to another.

PPPs reflect the relative costs for a worldwide pattern of consumption prevailing at only one moment in time, and this pattern is constantly changing. They merely present a snapshot of relative prices across countries at a point in time, which is no more authoritative than similar snapshots of the relative prices taken at other points in the time period being examined.

The use of national consumer price indices to identify the local equivalent of the international poverty line in years other than the base year further diminishes comparability across country-years. This is because each such index refers to the price of a basket of goods with a composition entirely different from the pattern of world consumption, which is used to calculate price differences across countries in the base year. The Bank implicitly admits this by substituting the new $1.25 international poverty line for the 2005 equivalent of its earlier $1.08 1993 poverty line as judged by the US CPI (which is close to $1.45 in 2005 prices).

The only region that appears to have had a faster rate of poverty reduction under the new estimates, regardless of whether the period is taken to begin in 1980 or in 1991, is Latin America. Moreover, if the final year of the comparison is moved backward by just three years to 2002, the rate of reduction of world poverty appears notably less favorable under the new estimates. The estimated reduction in poverty since may be due to misattribution of aggregate growth to the poor rather than to new information from surveys.

Two revisions have already been undertaken of the base year. The next global price survey is scheduled for 2011. The Bank can at that point choose between pulling the rug from underneath itself again by updating the PPPs used, continuing to use the same PPPs, or admitting that its method is wholly wrong.

There exist alternative methods. These involve careful coordination of household surveys and poverty line construction across countries, ensuring comparability from the first. Such an effort would be along the lines of the coordination of national accounts—a previous crowning achievement of the United Nations.

Reference:

Sanjay Reddy and Thomas Pogge (forthcoming). "How Not to Count the Poor", in Stiglitz, J., Anand, S. and Segal, P. ed., *Debates on the Measurement of Global Poverty*, Oxford University Press.

Click here to see the World Bank's New Poverty Estimates: <http://econ.worldbank.org/external/default/main?menuPK=469435&pagePK=64165236&piPK=64165141&theSitePK=469382>.

One Pager number 65
Published: September, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager65.pdf>

Global Poverty Reassessed: A Reply to Reddy

by Martin Ravallion,
Director of the Development Research Group, the World Bank

In "One Pager" No. 65, Sanjay Reddy says the World Bank is "digging (itself) deeper into a hole" in measuring global poverty. It seems we are in this hole (in Reddy's eyes) because we have not adopted his preferred method; I have tried to explain why we have not done so in past responses to Reddy (including Ravallion, 2008).

Nobody is stopping Reddy from doing his own calculations. Indeed, the Bank long ago made all the (now 670) household survey-based distributions we use publicly available on an interactive web site, *PovcalNet* (http://econ.worldbank.org/povcalnet), where users can try their own poverty lines. *PovcalNet* will soon be revised to include the results of the 2005 *International Comparison Program* (ICP). (The ICP is an international effort to collect prices from a large sample of outlets in each country.)

The 2005 round of the ICP is a quantum leap in our knowledge about the cost of living in the developing world. Nobody who bothers to look into the history of the ICP—from 1970 (crude price surveys for 10 countries) to 2005 (state of the art price surveys for 150 countries)—could disagree. Reddy dismisses these data improvements, but they have great relevance to measuring global poverty. Most importantly, the 2005 ICP did a much better job than prior ICP rounds in collecting prices. Doing reliable price surveys is difficult, particularly in poor countries where many goods (including those consumed by the poor) are not traded internationally. Far more detailed product descriptions introduced by the 2005 ICP helped to identify comparable goods, so that we do not make the mistake of judging people to be better off simply because they consume lower quality (and hence cheaper) goods.

Based on the new ICP we have updated our past "$1 a day" international poverty line to $1.25 in 2005 prices. This is the average poverty line found in the poorest 15 countries, based on data drawn from World Bank *Poverty Assessments* and governmental *Poverty Reduction Strategy Papers*. These national lines attain stipulated food energy requirements with allowances for essential non-food spending. Naturally, each national line accords with the prevailing concept of "poverty" in that country. (Nutritional requirements are similar, but the imputed expenditures for food and non-food needs vary greatly.) We estimate that one quarter of the population of the developing world in 2005 lived below $1.25 per day; one half lived below that line 25 years earlier.

As Reddy notes, $1.25 is lower than the value in the US of our old poverty line, which works out to be $1.45 in 2005 prices. This has nothing to do with Reddy's claimed faults in our methods, but stems from the revisions to the PPPs in the light of the better price data from the 2005 ICP; naturally, with higher PPPs in poor countries, the $US value of their national poverty lines falls.

Reddy thinks $1.25 a day is "…far too low to cover the cost of purchasing basic necessities," He asserts that: "A human being could not live in the US on $1.25 a day in 2005 (or $1.40 in 2008), nor therefore on an equivalent amount elsewhere, contrary to the Bank's claims." I have no idea how Reddy reconciles this view with the fact that one quarter of (say) India's population manages to live below the country's official poverty line, which is about $1.00 per day in 2005 prices—even lower than our international line.

Nonetheless, I agree with Reddy that the $1.25 line is frugal by international standards. That has never been at issue. In measuring global poverty against such a line, the Bank is explicitly measuring poverty in the world by a standard that would be judged far too low in many countries in the world. We are measuring poverty by the standards of the poorest countries, fully acknowledging that better off countries use higher standards for defining poverty.

Recognizing this point, the World Bank's global poverty measures have also used lines more representative of middle-income countries. Chen and Ravallion (2008) present results for $2.00 per day (the median poverty line amongst developing countries) and $2.50 a day (the median amongst all except the poorest 15 countries). Almost 60 per cent live below $2.50 per day.

At the other extreme, 95 per cent of the developing world's population lived below the average US poverty line of about $13 per day. But this is hardly a useful statistic for moving forward in the task of fighting absolute poverty in the world-hopefully starting with the poorest.

References:

Shaohua Chen and Martin Ravallion (2008) "The Developing World is Poorer than we Thought, but no Less Successful in the Fight Against Poverty," Policy Research Working Paper 4703, World Bank, Washington DC. Available at: <http://econ.worldbank.org/docsearch>.

Martin Ravallion (2008) "How Not to Count the Poor: Reply to Reddy and Pogge" in Sudhir Anand; Paul Segal; and Joseph Stiglitz (ed), *Debates on the Measurement of Poverty*, Oxford University Press.

One Pager number 66
Published: September, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager66.pdf>

The Macroeconomics of Scaling-Up Aid:
What We Know in Kenya, Malawi and Zambia

by Degol Hailu, International Poverty Centre

Last week at the United Nations, the MDG Africa Steering Group discussed the Gleneagles Scenario. The participants reiterated the need for scaled-up aid in order to support the attainment of the Millennium Development Goals (MDGs). At the same time, a report issued by the International Monetary Fund (IMF) assessed the macroeconomic implications of scaling-up aid in Benin, Niger and Togo. The report acknowledged that higher levels of aid will put moderate to sizable pressures on inflation and real exchange rates (IMF, 2008).

Concerns about such macroeconomic outcomes often constrain the full use of aid. Policies become too restrictive to allow full spending and absorption, even when aid is scaled-up. Countries are advised to maintain high interest rates, adopt inflation-targeting, and limit public expenditure. Macroeconomic policies have not been expansionary enough to increase MDG levels of spending.

To identify how concerns about macroeconomic instability have curtailed an effective response to MDG scale-up, we look at the cases of Kenya, Malawi and Zambia. These countries are confronting human development challenges and all of them receive resources to respond effectively, but they are not using those resources fully.

We compare spending and absorption *before* and *during* the aid surge periods to demonstrate the stance taken by the macroeconomic authorities in each country. Full absorption implies that the current account deficit was financed by an amount equal to or greater than the increase in the flow of aid. Full spending means expansion of the budget deficit before grants during the aid surge by an amount equal to the increase in aid.

The table shows that all of the aid was absorbed in Malawi, but only 59 per cent was spent through government fiscal expansion. Malawi had lower international reserves, mainly because of high absorption. Interestingly, the real exchange rate depreciated and the inflation rate fell by 15.4 percentage points. Hence full absorption of aid in Malawi did not result in macroeconomic instability.

In Zambia, 39 per cent of the aid was absorbed and only 6 per cent was spent. As expected, the level of international reserves increased. The inflation rate fell slightly. Surprisingly, the real exchange rate appreciated in the face of low absorption and spending of aid receipts. Despite the restrictive macroeconomic stance, Zambia experienced a less encouraging macroeconomic outcome.

Aid Absorption, Spending and Macroeconomic Outcomes, Averages

	Malawi		Zambia		Kenia	
	1999-02	2003-06	2001-03	2004-06	1995-99	2000-04
Aid absorbed (%)	-	100	-	39	-	33
Aid spent (%)	-	59	-	6	-	22
Inflation rate	28	12.6	21.7	18.1	6.4	4.5
Real exchange rate	103.2	75.5	108.2	139.6	69.9	72.6
Reserves ($US millions	213.3	182.2	322.1	373.3	735	1,244

Source: Serieux et al. (2008).

In Kenya, 33 per cent of the aid was absorbed and 22 per cent was spent. A significant portion of the aid was used to settle domestic debt and build-up reserves. The level of international reserves almost doubled. The inflation rate fell, but the real exchange rate also appreciated.

The above cases are classic examples of a pre-emptive macroeconomic policy driven by fears of a "Dutch disease" effect. What is often forgotten, however, is that short-term macroeconomic movements are normal and expected after resources are scaled up. Large and persistent changes in inflation and exchange rates indicate a lack of supply response. Despite these obvious facts, the low level of absorption and spending in these countries is a direct consequence of macroeconomic conservatism.

According to their Poverty Reduction Strategy Papers (PRSPs), fiscal policy in Malawi and Zambia focuses on keeping the overall balance at less than 1 per cent of GDP. The targets for inflation are set at less than 5 per cent. In Kenya, the inflation target for the period 2005–2007 was 3.5 per cent.

Earlier publications of the International Poverty Centre have emphasized the urgent need for large-scale programmes to meet the MDGs. We reiterate those recommendations. Fiscal and monetary policies have to be expansionary in order to scale-up resources in the interest of achieving the MDGs. Macroeconomic management must encourage full spending and absorption of aid.

References:

IMF (2008). *The Macroeconomics of Scaling Up Aid: The Cases of Benin, Niger and Togo*, Washington, DC, International Monetary Fund.

Serieux, J.; D. Hailu; M. Tumasyan; A. Papoyan; R. White; and M. Njelesani (2008). "Addressing the Macro-Micro Economic Implications of Financing MDG-Levels of HIV/and AIDS Expenditure", United Nations Development Programme (UNDP), HIV/AIDS Group (mimeo).

One Pager number 67
Published: September, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager67.pdf>

Can we Accurately Project MDG Indicators?

by Rafael Guerreiro Osorio, International Poverty Centre

The Millennium Development Goals (MDGs) are global, in the sense that they are to be reached by the whole world, not by countries individually. True commitment to MDGs has led many to ask the questions: will my country reach all or some of the MDG targets by 2015? Are we on track?

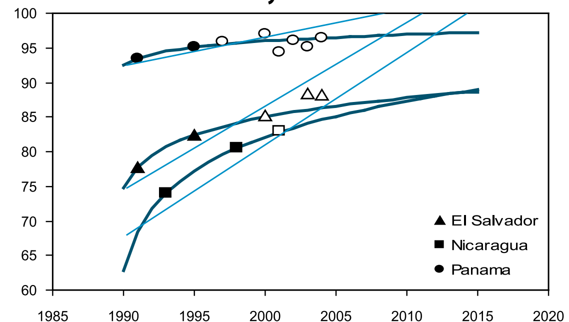
To answer the above questions we need projections of MDG indicators. Due to lack of data or technical skills, the answer to the above questions has frequently relied on simple linear projection of indicators for two or more points in time. However, the results obtained can be excessively optimistic because a linear projection implies the assumption that further improvements will be achieved at the same absolute rate as past improvements were. This is not a realistic assumption.

The case of primary education yields a fair illustration of the problem. The net attendance ratio is usually the share of the 6 to 11 years-old population attending primary school. There is a challenge that threatens the improvement of attendance: it is easy to increase it when departing from very low levels, but there is a level from which further improvements require great investments and much effort. Often, the expansion of primary schooling begins by, not surprisingly, reaching the easy to reach—then the growth pace of attendance is progressively reduced. Higher efforts and investments are needed to sustain growth as attendance increases. For example, some children not attending might live in remote areas, where there are neither schools nor teachers or not even roads. Enabling them to attend primary school will require much more effort than for children living in urban areas.

Projections should take this into account, but linear trends ignore it. The figure shows the net attendance ratio for three Central America countries for some points in time. A linear projection was made for each country considering just the two initial points. According to these projections, the three countries would reach a net attendance of a 100 per cent by 2015. However, the net attendance ratios of posterior years (the unfilled markers) show that the projection was rather optimistic. The net attendance ratio of Panama grew linearly in the next two periods, but then it started to float around 95 per cent. In El Salvador and Nicaragua, the observed value of the indicator is lower than the predictions of the linear projections. The dynamics of the indicator in those countries corroborates the axiom that further improvements are harder to achieve—particularly in Panama, where a high level of attendance had already been reached.

When dealing with "positive" indicators, those for which the more the better, concave functional forms, such as a logarithmic trend, would better represent the fact that the higher the level, the harder will be to reach further improvements. Logarithmic trends for each country based only on the two initial points in time were also plotted in the figure. According to these projections, none of the three countries would reach a net attendance ratio of a 100 per cent by 2015. In the cases of Panama and Nicaragua, it is obvious that the logarithmic trend predicted almost perfectly the dynamics of the indicator. For El Salvador the logarithmic trend resulted in a slightly pessimistic projection: its predictions for 2003 and 2004 are below the observed values. However, predictions are closer to the observed values than those of the linear trend.

Net Attendance Ratio in Primary Education



Source: Inter-American Development Bank, Equity and Social Indicators – EQxIS (www.iadb.or/xindicators).

Herein we showed a caveat of linear projection of MDG indicators. Often, simple projection techniques based solely on indicators for two or more points in time are all that can be done to assess whether a country is on track to achieve the MDGs. Even if this is the case, linear projections should be avoided. Elsewhere (Osorio, 2008) we present some simple alternatives to projecting MDG indicators in situations of scarcity of data. However, these should not replace more rigorous approaches to projection when there is availability of good data and technical expertise.

Projections are important because policy makers can make informed assumptions about countries, or groups within countries, whether they are on or off track in meeting the MDG targets. Therefore, projections must be as accurate as possible. But one should bear in mind that projections, no matter how complex, are not forecasts: they will give clues, but not definite answers on whether a country will reach the MDG targets by 2015.

Reference:

Osorio, R.G. (2008) "Alternatives for projecting MDG indicators", *Technical Paper Series*, No. 2. Brasilia, International Poverty Centre (IPC). Available at: <http://www.undp-povertycentre.org/pub/IPCTechnicalPaper2.pdf>.

One Pager number 68
Published: October, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager68.pdf>.

Where the Line is Drawn. *A Rejoinder to Ravallion*

by Thomas Pogge, Leitner Professor of Philosophy and International Affairs, Yale University

Martin Ravallion's "One Pager" No. 66

focuses on two key issues: the level of the World Bank's international poverty line (IPL) and its conversion to other currencies and years.

Having written on conversion before ("One Pager" No. 54), I can be brief. The purchasing power parities the Bank uses to convert its IPL into other currencies at best preserve purchasing power equivalence relative to the pattern of international household consumption. Similarly, the consumer price indices the Bank uses to convert the results to other years at best preserve purchasing power equivalence relative to each national household consumption basket. Such conversions are unsuitable within a poverty measurement exercise because the prices of necessaries play a much greater role in the lives of the poor than in general consumption expenditure.

IPL level in 2005-dollars	1990 baseline (millions of poor)	2015 target reduction of 27.5% (millions)	Annual reduction needed to reach target	Reduction needed to be "on track" in 2005 (millions)	Actual reduction achieved 1990-2005 (millions)	How are we doing in regard to MDG-1? (100% = exactly on track)
$1.00/day	1303.2	358.4	1.28%	228.7	424.2	185%; far ahead of schedule
$1.25/day	1817.5	499.8	1.28%	318.9	417.9	131%; ahead of schedule
$2.00/day	2753.6	757.2	1.28%	483.2	155.8	32%; far behind schedule
$2.50/day	3076.6	846.1	1.28%	539.9	-63.6	-12%; regressing

For example, the UN Food and Agriculture Organisation (FAO) reports that food prices have more than doubled since early 2006, with devastating effects on the poor. The IPL will not record these effects. It assesses a poor person's income against her country's general consumer price level (which has risen much less) rather than against the prices of what she absolutely needs to buy.

The political role of the Bank's IPL makes crucial where this line is drawn. At the 1996 World Food Summit (WFS) in Rome, 186 governments promised to halve, by 2015, the number of people in severe poverty. In the first UN Millennium Development Goal (MDG-1) they then promised to halve the "proportion of the world's people" living in poverty. Later reformulations of MDG-1 backdate its baseline from 2000 to 1990 and also replace "world's people" with the population of the developing countries.

So there were three successive targets: (1) the WFS target: to halve, over *19 years*, the *number* of poor worldwide, which implies a 3.58 per cent annual reduction in this number; (2) MDG-1 as adopted: to halve, over *15 years*, the *proportion* of poor in *world population*, which implies a 3.40 per cent annual reduction in the number of poor; and (3) MDG-1 as reformulated: to halve, over *25 years*, the *proportion* of poor in *the developing world*, which implies a 1.28 per cent annual reduction in the number of poor worldwide. The last and now official target is so much less ambitious because—thanks to 1990–2015 population growth of 45 per cent in the developing world —the number of poor needs to be reduced by only 27.5 per cent.

Are we on track to achieving at least this modest 27.5 per cent reduction over 25 years? The answer depends dramatically on how high or low the IPL is set. The Bank initially fixed its IPL at 1.02 1985-dollars, noting that the domestic poverty lines of eight poor countries were close to this amount. It later reset its IPL to 1.08 1993-dollars, noting that this was the median of the ten lowest domestic poverty lines. This August the Bank has reset its IPL again to 1.25 2005-dollars, noting that this is the mean of the domestic poverty lines of the 15 poorest countries. The rationale behind this variable "anchoring" of IPLs in domestic poverty lines (many of which are themselves fixed by the Bank) is obscure. Converted into 2008-dollars, the three IPLs come to $2.08, $1.63, and $1.40 respectively. If you live in the US and your consumption in all of 2008 costs more than $512, you are not poor by the World Bank's latest standard.

How about setting the IPL at a higher level? Chen and Ravallion (2008) give data—summarized in the table—for four different poverty lines. The data show how decisively the achievement of MDG-1 depends on where the IPL is fixed. The Bank's choice of $1.25 (2005) per day allows us to celebrate being 31 per cent ahead of schedule. Were the IPL set at $2.00 (2005) per day, we would be 68 per cent behind schedule.

If $1.25 is too low, Ravallion asks, how does much of India's population manage to survive on even less? Indeed, they "manage to live." But to count people as non-poor, more should be required: that they can afford sufficient food, clean water, basic health care, adequate clothing and shelter.

Adopting a more adequate IPL, could we still afford a commitment to eradicate poverty? If the Bank defined poverty in terms of $2 (2005) per day, it would count as poor 2.6 billion people whose 40 per cent average shortfall would amount to 1.3 per cent of global income (ibid., 23). Getting everyone to this very modest level—$819 per person per year in the US today—is not an extravagant goal when all it would take is a 1.3 per cent shift in the global income distribution. With its new IPL of $1.25 (2005), the Bank is counting as poor 1.4 billion people who, on average, live 30 per cent below this line. Their collective shortfall is 0.33 per cent of global income (ibid.). And we are grandly aiming to repair half of this problem over 25 years!

Reference:

Shaohua Chen and Martin Ravallion (2008). "The Developing World is Poorer than We Thought, but no Less Successful in the Fight against Poverty," World Bank Policy Research Working Paper WPS 4703. Available at <http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2008/08/26/000158349_20080826113239/Rendered/PDF/WPS4703.pdf>.

One Pager number 69
Published: October, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager69.pdf>

Are the Cheetahs Tracking the Tigers?

Probing High Growth Rates in Africa

by Degol Hailu, International Poverty Centre

African economies are growing. Between 2000 and 2007, GDP growth for the whole region averaged 4.4 per cent. Five countries managed to grow by more than 7 per cent. This magical number is often used as a benchmark for achievement of the Millennium Development Goals (MDGs). In another 14 countries, growth rates were at 5–6 per cent, even despite negative per capita growth for 12 of the 47 sub-Saharan countries. For instance, growth shrank by 5.6 per cent in Zimbabwe, by 2.2 in Cote d'Ivoire, by 3.3 per cent in Eritrea, and by 1.4 per cent in the Central African Republic.

These are fascinating figures by any standard. Some commentators have gone so far as to herald the advent of the African Cheetahs, following in the footsteps of the Asian Tigers.

Unfortunately, growth statistics alone tell us little about economic development. The right approach is to examine how growth is supported by tangible development outcomes. One of these is the extent to which high-growth economies have a vibrant manufacturing sector. The output shares of manufacturing in national income and exports are good indicators.

The table compares the high-growth periods for the African economies with those for the Asian Tigers. With the exception of Mozambique, the share of manufacturing value added (MVA) in the Tigers was four times higher than the share in the high- and medium-growth economies of the sub-Saharan region. Mozambique stands out: the country's manufacturing value added reached 15 per cent, almost three times the share in other countries of the region. But only 6.6 per cent of Mozambique's manufactured goods are exported.

On average, manufacturing's share of total merchandise exports was 83 per cent in the Tiger economies. This contrasts with a 1.7 per cent share for the high-growth countries and 9.7 per cent for the medium-growth economies in sub-Saharan Africa. More revealing is the individual performance of these economies. Manufacturing exports made up only 0.5 per cent and 1.9 per cent of total exports in Angola and Sierra Leone, respectively. In Sudan, fewer than 7.5 per cent of exports were manufactured goods.

It is starkly obvious that the high growth rates are driven by commodity exports. Oil is Equatorial Guinea's only export. Petroleum accounts for about 96 per cent of Angola's exports; diamonds make up the rest. Oil accounts for three-fourths of Chad's exports. About two-thirds of Sudan's exports consist of fuel. To cut a familiar story short, last week *The Economist* stated bluntly that "African trade has not changed much since the end of the colonial era. Unprocessed raw materials go out; finished goods come in." These may read as hasty judgements. Botswana, Cape Verde and Mauritius have performed remarkably. About 80 per cent of their exports are manufactured goods. As a share of GDP, however, manufacturing value added is only 5.5 per cent.

Growth Rates, Manufacturing Value Added and Exports

	GDP growth rate	GDP per capita grow rate	MVA (% GDP)	Manufacturing exports (% total exports)
High-growth energy exporters*	10.2	7.5	4.4	1.7
Mozambique	7.4	4.9	14.9	6.6
11 medium-growth economies	5.5	2.9	7.4	9.7
Manufacturing exporters**	5.2	3.0	5.5	80.0
The Tigers***	7.4	5.7	24.8	83.0

* Angola, Chad, Equatorial Guinea, Sierra Leone, Sudan.
** Botswana, Cape Verde, Mauritius.
*** South Korea, Hong Kong, Singapore.
Data years: Africa (2000–2006) and Asia (1980–1990).
Source: Calculated from the World Bank *World Development Indicators*, 2008.

The high-growth performances are encouraging, but there is little sign of expansion in manufacturing activities among the so-called Cheetahs. The dependence on primary commodities and the extractive industry is worrying, particularly in economies that are heavily dependent on imports and where domestic manufacturing may possibly provide substitutes. To repeat an age-old argument, long-term decline in the relative price of primary commodities is empirically demonstrated. This is explained by the low income elasticities of demand and limited scope for product development. The current global economic downturn is already having an impact on commodity prices. Between July and October, energy prices fell by 28.4 per cent. Non-energy commodity prices fell by 16.4 per cent.

Why manufacturing? It is well established that the sector is superior in productivity increases, economies of scale and spurring all-round linkages. The sector also demands and absorbs a mix of high- and low-skilled labour. This is what distinguishes the Tigers from the Cheetahs. The former reaped the benefits of industrial policy. For instance, the Tigers managed allocations of credit and coordinated its flow to the manufacturing sector. They relied more on the provision of credit-based than on equity-based financing. Manufacturers in South Korea were subsidised by as much as 75 per cent when obtaining credit.

Cheetahs run fast, but not for long. Learning the lessons of history may lead them to the Tigers' trail.

One Pager number 70
Published: November, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager70.pdf>

Cash Transfers and Child Labour:
An Intriguing Relationship

by Guilherme Issamu Hirata,
International Poverty Centre

Conditional Cash Transfer (CCT) programmes provide cash to poor households. In return, the households are expected to meet the conditionalities attached to schooling, among others. Several evaluations have found positive impacts on primary school attendance. One issue on which there is a heated debate is the impact of CCTs on child labour. Because the programmes affect children's time allocation, some impact on child labour is always expected. But it is not as evident as the impact associated with school attendance.

Besides the lack of child labour-related conditionalities in most CCT programmes, the impact, if any, depends on a variety of factors. These include the size of the transfers; the relative amount of child labour's monetary and non-monetary contributions; parents' preference for education; the type of education-related conditionalities attached to CCT programmes; and the way those conditionalities are enforced.

A recent impact evaluation of Paraguay's CCT pilot programme, *Tekoporã*, presents evidence that child labour is positively correlated to mothers' labour supply. This seems counterintuitive, since a frequently cited explanation for child labour is that poor households rely on it to secure a minimum level of income. Since a household's budget constraint decreases when the mother goes to work, it has been argued, the income generated by the child is less necessary.

Becker's "Rotten Kid Theorem" can provide one explanation for this counterintuitive correlation. Roughly speaking, suppose that the head of a household is altruistic, in the sense that he distributes the household income among all members instead of keeping the money for himself (in fact, the money is usually given to the mother because mothers are thought to be more altruistic than fathers). Then, according to the theorem, the other household members may be expected to increase their working activities in order to augment the household's income, and consequently their own. In other words, even children realise that engaging in income-generating activities would immediately increase their own well-being. This result is something that has received little attention so far— that a child has a stake in deciding whether or not to engage in working activities.

In this light, the child's preferences play a key role in determining child labour. Instead of assuming that parents send their children to work, one can think the incentive that drives the mother to work is the same that influences the child. For instance, a household might own a small business which, after some investments, demands a bigger labour force. Both mother and child may react in the same way by seeing an opportunity to earn income and going to work in order to meet this demand.

And what if the source of the aforementioned investment is a cash transfer? The CCT programme has an ambiguous impact on child labour. On the one hand, the increased opportunity cost of not attending school implies a reduction in child labour. On the other hand, there can be a somewhat contrary effect.

The persistence of child labour has different sources. For instance, it could be seen as a form of skills development. Alternatively, work might be valued more than schooling if children live in societies where there is a positive stigma attached to child labour. However, when the child's preferences highly determine whether he or she engages in labour activities, there is another issue to deal with: children's preferences could run counter to parents' preferences.

If so, the incentive provided by a cash transfer may not be sufficient to reduce child labour. Indeed, the evaluation of Paraguay's *Tekoporã* revealed that CCT programmes could indirectly stimulate child labour. Although more evidence needs to be gathered, there are indications that such a negative outcome might occur. The CCT programme would have to circumvent this situation.

Brazil's successful Child Labour Eradication Programme (PETI) targets working children. It demands that a child stop working in order for the household to receive benefits. If the objective of CCT programmes is to fight child labour, then proper targeting, child labour-related conditionalities, stronger incentives and improved surveillance are issues that have to be considered. These features of programme design could also lead to improvements on the supply side. For instance, more and better schools could be the result of a rising demand for services.

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One Pager number 71
Published: November, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager71.pdf>

Free Access to Primary Data Should Be a Right

by Rafael Guerreiro Osorio, International Poverty Centre

Few things are as important for development as the availability of data and unfettered access. Without data there can be no needs assessment. It will scarcely be possible to design effective policies or to implement, monitor and evaluate them. Data are not important only for governments. Democracy implies transparency of government actions and the accountability of governments to society. The availability of data from reliable sources is a step towards these goals.

Countries differ considerably in data production, as well as in their data dissemination policies. Both data production and dissemination influence countries' capacities to undertake development planning. The availability of data and free access also determine the extent to which the electorate can evaluate the performance of governments and their policies. Lack of capacity to produce data might have many excusable causes, but restrictive policies of data dissemination have none. As long as the anonymity of individuals and firms is guaranteed, all data should be available in the public domain.

Governments are usually the main producers of primary data. The most common primary data sources are administrative records, censuses and surveys. It is from such primary data that indicators are calculated. Many governments disseminate indicators, but not the primary data. Governments that withhold access to primary data impose restrictions in many ways. Some simply do not grant access at all; some grant access only to government officials; some grant access only when commissioning a consultancy or receiving something in exchange; some charge very high fees. By restricting access to primary data, governments ensure that their indicators will not be contested. Moreover, policy shortfalls that they do not want exposed are kept secret.

For a long time, there were technological limitations on the dissemination and use of data. Data dissemination was costly, as were analytical tools. In some cases, lack of technology and high costs may have been used as pretexts for restricting the availability of primary data. Technological progress has changed this, and today there are almost no limits on data dissemination. In most countries, cheap personal computers and internet access are becoming widespread, endowing individuals with processing power that once was associated with supercomputers.

Governments lose by restricting access to primary data. Worldwide, an increasing number of researchers are eager to acquire such data. Be it because academic competition requires them to publish papers, or because they want a say in decision-making, access to primary data allows them to test their hypotheses about development policy options. Each analysis becomes a potential free consultancy with particular views. So instead of commissioning a costly consultancy and receiving a single analysis, countries that disseminate primary data can acquire a full menu of policy options for free.

Fortunately, some governments have recognized the advantages of disseminating primary data and have begun to allow access to datasets. But it is not enough to make the data available if the information is not usable. Primary data dissemination packages must include data itself and metadata—the information on how the data were produced. The data must be disseminated in standard, non-proprietary file formats. Metadata should include descriptions of the data files, copies of the forms or questionnaires used in data collection, copies of the form-filling instructions or interview manuals and, in the case of surveys and censuses, comprehensive methodological documents.

There are many good examples of primary data dissemination. The outstanding one is that of the Demographic and Health Surveys (www.measuredhs.com). Statistics South Africa has done a remarkable job in making many of its surveys freely downloadable, with fair metadata (www.statssa.gov.za). The information technology department of Brazil's health ministry is a success story in the dissemination of primary data from administrative records (www.datasus.gov.br).

In Latin America, many statistical bureaus have started to offer free dataset downloads from household surveys: those of Bolivia, Ecuador, Honduras, Mexico, Peru and Uruguay, for instance, already do this. Some still have to work on the comprehensiveness of the metadata, particularly for older data, but these countries' initiative is commendable.

The more people have access to primary data, the more analyses it will generate; more ideas will emerge, and the quality of the debate on development options will improve. Democracy will benefit from the greater accountability of government actions and the increase in plural participation. Furthermore, primary data should not be seen as the property of governments, but as a societal asset. Free access to primary data should be seen as a fundamental right, not as a concession.

One Pager number 72
Published: November, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager72.pdf>

Eliminating Gender Inequalities **Reduces Poverty. How?**

by Joana Costa and Elydia Silva,
International Poverty Centre

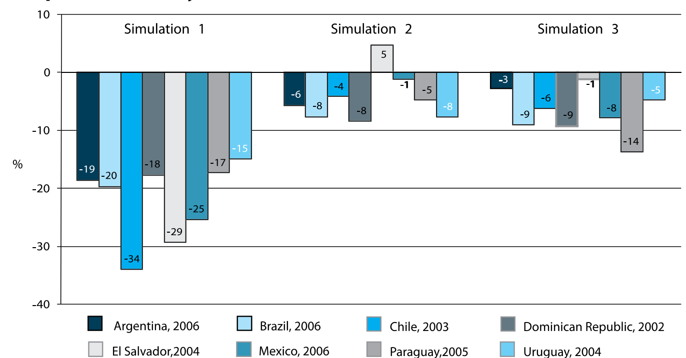
There are many ways in which gender inequalities are present in society. Those inequalities, like any other, are intrinsically unfair and should be fought against. In this One Pager, we show how gender inequalities in the labour market determine poverty levels. We answer the following question: which aspect of gender inequalities should be considered priority in the design of public policies that seek to reduce gender inequalities and poverty?

In order to understand the link between poverty and gender inequalities in Latin America, we look closely at eight countries: Argentina, Brazil, Chile, the Dominican Republic, El Salvador, Mexico, Paraguay and Uruguay. Three aspects of gender inequalities in the labour market are apparent in these countries. First, women have a markedly lower rate of economic activity than men. Second, rates of female informality and unemployment are usually higher than those for men. Third, women receive lower hourly remuneration. It could be argued that these observed inequalities are not produced by the labour market, and that they simply reflect differences in characteristics or endowments, such as education. In these countries, however, we find no gender gap in characteristics. Even controlling for characteristics, we find that women have a lower probability of participating in the labour market, a lower probability of being formal workers, and lower hourly wage remuneration.

To investigate the relationship between gender inequalities and poverty, we simulate counterfactual scenarios in which gender inequalities would be reduced. Their impacts on poverty levels are then estimated. In the first scenario, women and men with equal characteristics have the same probability of being economically active. In the second, women and men with similar characteristics have the same probability of being unemployed, formal workers or informal workers. In the third, women and men receive the same hourly remuneration for their characteristics.

The simulations are constructed independently and in a *ceteris paribus* context. This methodology is essentially a partial equilibrium exercise and, as such, it must be considered with some caveats. The results presented here do not consider all possible consequences regarding the simulations, and thus they do not represent a general equilibrium in the economies under study. Nevertheless, the results do correspond to a rough estimate of the possible costs of gender inequalities. Moreover, they do make possible an assessment of the relative importance of each aspect of gender inequalities in terms of how they affect poverty levels.

Impact on Poverty Levels



Source: Authors' calculations based on household surveys.

The figure presents the change in the poverty incidence that would happen in each scenario. The reduction of all three aspects of gender inequalities in the labour market would help reduce poverty. Moreover, the main aspect of gender inequalities to be fought against is the comparatively low rate of economic activity among women. First, if female participation or the labour force increases (simulation 1), the potential reduction of the incidence of poverty would be greatest in Chile (34 per cent) and least in Uruguay (15 per cent). Second, the potential decline in poverty that could be achieved by equalizing women's and men's probabilities of being unemployed, formal workers or informal workers (simulation 2) would not be higher than 8 per cent. It is interesting, however, to observe the effects in El Salvador. Since men have a higher unemployment rate, equalizing the probabilities increases the poverty level. This is a unique result in our simulation. Third, poverty declines by up to 14 per cent when female and male hourly remuneration is levelled (simulation 3).

Though it is important to eliminate others aspects of gender inequalities, we find that promoting women's participation in the labour market is the aspect with the greatest potential to promote pro-poor growth. Hence improving women's (particularly poor women's) access to the labour market is an essential element of public polices. Since caring for children increases the probability of women being economically inactive, one important means of increasing female participation might be to provide childcare facilities, especially to poor women.

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One Pager number 73
Published: December, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager73.pdf>

What Impact Does Inflation Targeting Have on **Unemployment?**

by Jose Angelo Divino, Catholic University of Brasilia

IPC One Pager No. 51 argued that inflation targeting has only slim prospects of success. This One Pager presents the findings of a recent empirical study of the impact of inflation targeting in a cross section of developing and emerging countries. The reasons usually given to justify adoption of this policy regime are transparency and credibility in monetary policy, the reduction of uncertainty, and implementation of the institutional and economic reforms required by the new regime. For developing and emerging countries, however, the economic benefits of inflation targeting are not yet well documented.

An inflation targeting regime uses the nominal interest rate as a policy instrument and aggregate demand is the transmission channel for monetary policy. On the real side of the economy, the consequences of this policy are twofold. On the one hand, adoption of a monetary policy regime might have undesirable effects on the labour market. Inflation might be brought close to the target rate, but at the cost of higher unemployment and lower economic growth. On the other hand, the price stability achieved might lessen uncertainty and create a favourable economic environment for consumption and investment. What does the empirical evidence reveal?

Here, we investigate the impact of inflation targeting on unemployment, economic growth, and the output gap (as measured by real GDP). We compare inflation targeters with non-targeters and use annual data for the period 1985–2005. The empirical research applied a difference-in-difference approach, accounting for both the regression to the mean problem and the potential effects of a poor economic performance in the first period (pre-targeting) on a country's decision to become an inflation targeter.

The main results are summarised in the table and they indicate that, on average, targeting countries were able to reduce the unemployment rate by about 5 per cent in the post-targeting period relative to non-targeters. But there was no significant difference in the volatility of unemployment between the two groups of countries or across the two periods, pre- and posttargeting. As regards economic growth, the results were less favourable for inflation targeting. The change in regime did not spur higher average economic growth or lessen the volatility of growth. For the output gap, however, the results provide some additional support for inflation targeting: targeters reduced the average output gap by about 1 per cent relative to non-targeters. Nonetheless, there was no significant difference in output gap volatility among targeters and non-targeters across the two periods.

Impact of Inflation Targeting on Selected Variables

Dependent variable	Change in unemployment	Change in output gap	Change in economic growth
Constant	3.29** (1.17)	-0.06 (0.13)	3.00*** (0.40)
IT dummy	-4.98* (2.78)	-1.05*** (0.33)	0.70 (1.07)
Initial mean	-0.34** (0.12)	-2.13*** (0.08)	-0.75*** (0.09)
IT*initial mean	0.82** (0.33)	?	-0.08 (0.27)
Heterosc. test	2.53 [0.1115]	1.89 [0.1692]	0.48 [0.4862]
R-squared	0.3521	0.9211	0.5910

Note: *, **, *** indicate statistical significance at the 10%, 5% and 1% level, respectively. Standard deviations are in parenthesis. Numbers in square brackets are p-values. Data Sources: For unemployment—Labour Statistics Database (Laborsta) of the International Labour Organisation. For economic growth, gross domestic product (GDP), and consumer price index (CPI) —World Bank. The output gap was computed as the percentage deviation of real GDP from potential output, as predicted by a linear trend. Up to 64 countries were included in the study.

A possible explanation for the mixed results is that several countries have moved to anti-inflation monetary policies based on interestrate rules, without announcing target values for inflation. Hence they are not formally classified as inflation targeters even though they are acting as such. Apart from the absence of a declared target for the inflation rate, the primary goal of their monetary policy is to stabilise inflation. This approach makes it difficult to identify changes in economic performance arising from the explicit adoption of an inflation targeting regime.

Despite this attribution problem, the empirical findings indicate that adoption of an inflation targeting regime did not exacerbate unemployment in developing and emerging countries. On the contrary, adoption of the regime reduced the average unemployment rate and narrowed the output gap. Hence there is no apparent reason to condemn these countries for adopting an inflation targeting regime for their monetary policies.

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The author thanks Degol Hailu and seminar participants at the IPC for comments and suggestions. All errors are the author's sole responsibility.

One Pager number 74
Published: February, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager74.pdf>

Why Aid Does Not Increase Savings Rates in **Sub-Saharan Africa?**

by John Serieux, University of Manitoba and Terry McKinley, CDPR, SOAS

Since the mid-1980s, sub-Saharan Africa has had the lowest savings and investment rates of any region in the world. It has also been the recipient of the highest levels of Official Development Assistance relative to output. Hence, many analysts have been concerned that ODA might be having a negative impact on domestic savings.

This would be the case if ODA mostly encouraged higher consumption rates, and did little to boost domestic investment. Has this been the case? This One Pager investigates this question (see Serieux, 2009).

Most previous analyses of this issue have presumed that aid could be used for either domestic consumption or investment. However, such analysis is incomplete since it also rests on the assumption that all ODA actually stays within the developing country.

Analyses have also fixated on the derived econometric relationship between ODA and domestic savings. This has been obtained by regressing the savings/GDP ratio on ODA/GDP (and other important explanatory variables, such as income per capita and the dependency ratio).

A resultant estimate of -1 for the coefficient for the ODA variable was presumed to indicate that ODA completely displaced domestic savings (and was, therefore, wholly consumed), while a coefficient of 0 would indicate that all aid was invested. Hence, an estimated coefficient that was negative and close -1 would help explain why both savings and investment rates remain so low in sub-Saharan Africa.

Displacing Savings

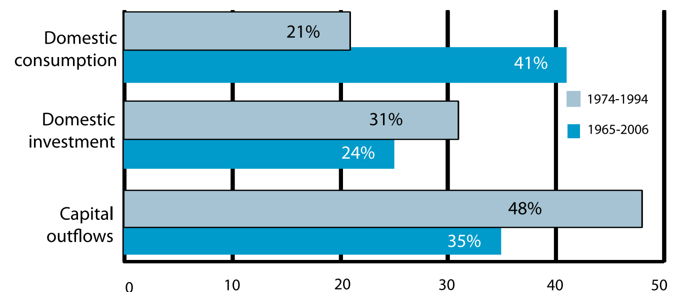
Most results have indicated that the coefficient ranges between -1 and 0 for the world as a whole and for most regions. But, curiously, the coefficient for ODA lies closer to 0 for sub-Saharan Africa than for other developing regions. This would appear to indicate that there is less displacement of savings by ODA in sub-Saharan Africa, and thus most aid is invested. But if this is true, why do domestic savings and investment remain so low in sub-Saharan Africa?

What such analyses ignore is that a significant part of ODA might be flowing back out of the country, without having had any impact on either domestic consumption or investment. In other words, the ODA-savings regressions have largely been misinterpreted. They have ignored reverse flows altogether – the third option for an outlet for ODA.

The reverse outflow of ODA could assume various forms. It could be used to reduce foreign liabilities, namely, by paying interest on foreign debt and principal payments on non-concessional debt. It could take the form of net acquisition of foreign assets by the private sector (capital flight) or by the public sector (reserve accumulation).

What does such a tripartite analysis (consumption, investment or capital outflow) reveal for sub-Saharan Africa? What share of ODA finances each of the three? To answer this question, we used panel data on relevant regression variables for 29 sub-Saharan African countries for the period 1965 to 2006. We regressed savings on total ODA/GDP as well as its two major components, Grants/ODA and Concessional Loans/GDP (together with other relevant variables).

ODA Results



Capital Outflows

We found that, at the margin, 35 per cent of ODA simply financed capital outflow. And only 24 per cent financed domestic investment. The remaining 41 per cent financed domestic consumption (see for the year 1965-2006). Grants had a significant coefficient of about -0.5 but loans were insignificant.

We then narrowed our period to 1974 to 1994, when ODA was almost continuously increasing, to see whether the trend of increasing ODA made a difference to those estimates. The percentage of ODA used to finance capital outflows jumped to 48 per cent while the percentage boosting domestic consumption dropped to 21 per cent. The record of financing domestic investment looked moderately better since the percentage rose to 31 per cent.

However, the overall results do not paint an encouraging picture. It is true that during the period in which ODA continuously increased, the share that financed domestic investment rose. However, this could be explained by the rising share of concessional lending vis-a-vis grants since the former had a positive impact on savings.

Most troubling was the rise in the share of capital outflows, namely, from 35 per cent (for the whole period) to 48 per cent (during the period of rising ODA).

The most likely outflows, especially during the late 1980s and early 1990s, were debt service payments. During the more recent period, accumulating foreign-exchange reserves may have become more important. But determining the composition of capital outflows is a topic for more in-depth research.

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This article is published jointly with the Centre for Development Policy and Research.
See the Development Viewpoint at <www.soas.ac.uk/cdpr>.

South-South Cooperation
in Times of Global Economic Crisis

by Michelle Morais de Sá e Silva,
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For South-South cooperation, the current moment of global economic downturn is one of anxiety. South-South cooperation was born with the Non-Aligned Movement. It went through a latent period, but re-emerged in the 1990s and early 2000s. The momentum gathered when a handful of middle-income countries such as Brazil, India, Mexico and South Africa were set to improve their position as global players. They had developed some relatively successful social programmes, which they sought to share with other developing countries. Considering that conventional North-South cooperation had turned out to be of limited effectiveness, South-South cooperation gained further impetus.

As countries of the South start facing the domino effect of financial and economic crises in the North, one may reasonably ask: what will become of South-South cooperation? Will it be put on the back burner? Will it become stronger? This One Pager discusses some scenarios and argues that the very principle of South-South learning is likely to survive.

One of the possible scenarios is that of doom. As economies shrink and costs have to be cut, it is very likely that developed countries will reduce their official development assistance (ODA). For instance, Japan, Finland, Sweden and Norway significantly reduced their ODA immediately after their economies faced turmoil in the early 1990s. Norway cut its ODA by 10 per cent, Sweden by 17 per cent and Finland by 62 per cent (see Roodam, 2008).

Why would South-South cooperation suffer from falls in ODA? Is the cooperation not between countries of the South? In theory, yes. In practice, South-South cooperation projects have been increasingly funded by so-called triangulation initiatives. Under triangulation, a developed country funds cooperation projects between two or more developing countries. Japan, for instance, has led the developed world in funding triangulation. Another example is the United Kingdom's support to a cooperation programme on social development between African and Latin American countries.

The distribution of ODA among different sectors may also change. ODA will go to temper the damage done to economies as a result of reduced consumption in the North. Social sectors will most likely be at the end of the priority list. The resources allocated for triangulation by developed countries are also likely to be reduced.

Political variables will also enter into the analysis of future scenarios. The revitalisation of regional integration initiatives such as the Southern Common Market (Mercosur), and the creation of new ones like the Union of South American Nations (Unasur), are an indication of commitment to further cooperation. Many Latin America countries, however, are facing presidential elections in the near future. Will the fate of South-South cooperation be determined by political expediencies? On the one hand, for example, Brazil's current administration has greatly expanded South-South cooperation initiatives towards Africa and Latin America, particularly in the fields of social protection, HIV/AIDS and agriculture. Other political parties might have their own motivations to promote South-South cooperation, such as gaining international influence and legitimising their own policies at home. Thus, in the event of political re-orientations, South-South cooperation efforts may well survive.

There is another reason for hope. Chile and Uruguay, for instance, are examples of countries that have not been affected by the crisis to the same extent as their neighbours, Brazil and Argentina. According to data on real GDP growth from the International Monetary Fund (IMF), in 2008 the Argentine and Brazilian economies grew by 6.5 and 5.2 percentage points respectively, but that growth is likely to slow to 3.6 and 3.5 per cent in 2009. Chile and Uruguay will not lose more than 1 percentage point in economic growth this year. These countries may possibly enhance their involvement in South-South cooperation.

Another possibility is that even those countries that have been hit by the crisis may engineer some creative solutions to share with their peers. For instance, recent government figures indicate that Brazil lost 654,000 jobs in December 2008 alone. In Brazil, creative social programmes such as *Bolsa Família* and the national HIV/AIDS initiative indicate the country's accumulated human capital and institutional capacity. The current crisis may pave the way for new solutions, which later could be shared with other countries of the South.

Regardless of which scenario prevails, the bottom line is that developing countries have learned that they can turn to each other for assistance and mutual learning. That cannot be erased by the current crisis. If anything, it will be reinforced, since industrialised nations will be too busy fixing their own problems and developing countries may be left on their own. If that holds true, South-South cooperation is here to stay.

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One Pager number 76
Published: February, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager76.pdf>

Is the South Ready for **South-South Cooperation?**

by Melissa Andrade,
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There are high expectations that South-South cooperation will bring many benefits. But are governments in the South really prepared to cooperate? Do they have the capacity to do so? Doubtless they do in trade policies, for instance, but many gaps persist in the field of social development.

North-South cooperation has been built on a complex institutional architecture. Over the years, multilateral and bilateral cooperation agencies have developed an underpinning for cooperation, with financing guidelines, specialists, lines of research, regional offices and logistical arrangements. In the South, this management expertise is not always present to facilitate the exchange of best policy practices.

Adapting policies from one context to another calls for much experience, planning, knowledge of the foreign context and dialogue based on mutual expectations. Apart from the ministries working on foreign policy, developing countries still lack the means to engage in effective cooperation. High level politicians have the vision of ensuring that all countries are better placed in the global arena, but line ministries still lag behind the top vision.

Consider some of the challenges ahead. In the South there is little systematic capacity development to enable countries to deliver cooperation, and little investment in expanding governments' capacity to cooperate (Andrade, 2009). Staff shortages are common and international cooperation is subordinated in the face of so many domestic demands. The institutional arrangements are inadequate to sustain effective and timely cooperation with new partners. For example, the Mercosur Social Institute, which aims to promote South-South cooperation on social development, was created only at the end of last year.

Communication is also a hurdle. China is very much Chinese, just as Brazil is very Brazilian and India very Indian. This is not to say that each country should not celebrate its own culture and national identity, but there is a fundamental need to relate to the experiences of others—not only to transmit one's own experience, but also to learn. Usually there are language barriers. Understanding a country's legislation may also be challenging for someone from elsewhere. There is also a need to improve the flow of information on successful policies in the South. A visit to the websites of ministries of social development in countries of the South reveals that little information is available except in the national language, mainly dedicated to domestic issues. Governments are not thinking globally; their audience remains national.

Cooperation benefits from a two-way process in order to avoid repeating the North-South dialogue. This means learning not only from middle-income countries but also from low-income ones. Such an approach is opening new possibilities of learning beyond intraregional experiences. There is now more exchange than ever before between Latin America and Africa, and between Asia and Africa.

What does the future hold? This process of learning about other countries in the South will become crucial. Why do cash transfer schemes work so well in Brazil and South Africa but are having difficulties expanding in other low-income countries? How could Chile develop an integrated database for targeting the beneficiaries of social policies, while in other countries the flow of information remains so problematic? These issues, explained in IPC's *Poverty in Focus* publication on cash transfers, will have to be addressed in preparing the global players in the South.

As new donors emerge there will be a greater need for accountability and public opinion will become increasingly important. Just as British and Swedish citizens are concerned about how their money is spent in recipient countries, so Brazilian, Chinese and South African citizens will want to know the same. Where is all the effort on cooperation going? What results are being achieved? Questions such as these will inevitably arise in the rapidly industrializing countries.

Cooperation in the South will have to develop its own body of knowledge, including the design, implementation and evaluation of cooperation programmes. It will also have to articulate a coherent message and accelerate programme implementation as noted by the UN General Assembly in 2007.

Given the global appetite for promoting South-South cooperation, the current and future challenges are becoming more evident. Until Southern countries develop the capacity to address these constraints, triangulation will still be needed to help build links. What is needed is more investment, not only in the technical part of cooperation but also, and especially, in building the capacity of developing countries to cooperate and transfer knowledge in areas beyond "hard policies". Building a multipolar setting has its costs, and it is crucial to create a new institutional architecture to back up these emerging South-South partnerships.

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One Pager number 77
Published: February, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager77.pdf>

The Rich Expand, the Poor Contract. The Paradox of Macroeconomic Policy in Ethiopia

by Degol Hailu,
International Policy Centre for Inclusive Growth

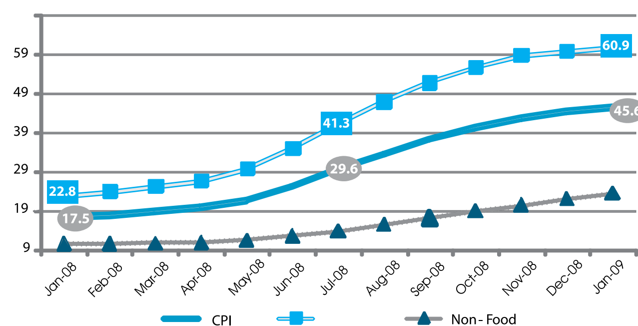
Rich countries have earmarked about $7 trillion to reverse the current global economic slump. The United States allotted $700 million to rescue ailing banks. About $180 billion was used to rescue just one insurer (AIG). A $787 billion stimulus package is also in place. The United Kingdom set aside $692 billion. The Chinese announced a $586 billion fiscal stimulus. Monetary policy has also become expansionary. The US and the UK cut interest rates to zero per cent and 0.5 per cent, respectively. Can low-income countries embark on such expansionary fiscal and monetary policies? Unfortunately not, as the case of Ethiopia demonstrates.

The government of Ethiopia and the International Monetary Fund (IMF) recently agreed on austere macroeconomic package. It included tight fiscal policy, with government domestic borrowing targeted at zero—down from 2.7 per cent of GDP in the previous fiscal year (2007/2008). Domestic borrowing by public enterprises is to be kept to 1.1–2.2 per cent of GDP, down from 4.4 per cent. Tight monetary policy will limit broad money growth to less than 20 per cent, down from 23 per cent growth in the previous fiscal year. The reserve requirement of commercial banks was also increased from 5 per cent to 15 per cent. The birr was depreciated by 10 per cent against the US dollar (see IMF, 2009)

Why is Ethiopia deflating while inflating is the order of the day? The answer lies with recent trends in inflation. The figure shows that the consumer price index (CPI) jumped from 17.5 per cent in January 2008 to 45.6 per cent in January 2009. In the same period, food inflation almost tripled from 22.8 per cent to 60.9 per cent. Non-food prices more than doubled to 23.4 per cent from 10.5 per cent.

Import prices have fuelled inflation. Data from the National Bank of Ethiopia indicate that food and petroleum imports, as a share of merchandise imports, account for about 21.5 per cent and 12 per cent, respectively. Between 2006 and 2008, the price of petroleum imports rose by 74.6 per cent. The entire import bill has risen by 50 per cent.

If exogenous shocks pushed up prices, then low global demand—combined with lower commodity and energy prices—is likely to drive down prices in the coming months. If so, is the austere macroeconomic stance justified? Contractions of this magnitude seem an overreaction. Public expenditure cuts often fall on investment rather than consumption. In the face of exogenous shocks, fiscal expansion is incorrectly seen as adding to demand, which leads to the prescription of austerity to a least-developed country. Macroeconomic tightening is a cruel medicine. The short-term contractions can have devastating long-term consequences, including a reduction in investments related to attainment of the Millennium Development Goals (MDGs).



Sources: The Ethiopian Central Statistical Agency (CSA) and the National Bank of Ethiopia (NBA), online databases.

What is the alternative policy stance? The Ethiopian economy, beyond external factors, is suffering from a failure to stimulate the supply side, mainly agricultural productivity. The strategy pursued in the last 18 years was successful in providing inputs and raising output levels, but it has failed to lift farmers out of the subsistence quagmire. Harvests rely heavily on rain, with only 2.5 per cent of the crop land irrigated and three tractors used per 100 hectares of arable land. Fertiliser and machinery are costly and crop prices do not grow as much in boom years. Farmers often face unfavourable terms of trade. The extent of the market is limited by the low (14 per cent) level of urbanisation. Access to existing markets is impeded by the lack of infrastructure and market institutions (see Anderson et al., 2007).

Credit expansion, to both the public and private sector, can be directed to investments in urban developments, irrigation, rural infrastructure, agricultural research and market developments. The establishment of the Ethiopian Commodities Exchange (ECX) in 2008 is one step forward. The ECX aims to efficiently link buyers and sellers of farm produce through secure payment systems, grading of produce and the provision of reliable information on prices. Such institutional innovations and investments cannot be realised by the tightening of fiscal and monetary policies.

Whereas trillions are earmarked for the various stimulus packages and bank bailouts in the rich countries, the poor are condemned to the settle for a new brand of the Washington Consensus.

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One Pager number 78
Published: March, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager78.pdf>

Impact Is Not Enough: Image and CCT Sustainability in Nicaragua

by Charity Moore,
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The significance of conditional cash transfer programmes (CCTs) has grown in recent years, particularly in Latin America. Nicaragua's CCT, the *Red de Protección Social* (RPS), had a short life span (2000–2006). Nonetheless, the programme received international acclaim for its achievements. The RPS regularly directed funds to female household heads conditional on the households' fulfilment of certain co-responsibilities (or conditionalities, as they were known until recently). These included children's school attendance, medical check-ups at local health centres and mothers' participation in educational sessions.

Evaluation of RPS's first phase found that it had significantly increased school enrolment and other education indicators (Maluccio and Flores, 2005). Perhaps more impressively, it had reduced stunting by 5 percentage points in treatment communities, an unexpectedly large result (IFPRI, 2005). These outcomes, combined with other positive assessments of its performance, made RPS something of a model CCT. To the surprise of many members of the international community, however, the Nicaraguan government voluntarily discontinued the programme. What happened?

The downfall of RPS came not from its lack of impact, but partly because of its failure to establish and maintain a positive image for itself within Nicaragua. The experience highlights the need for CCTs to garner national support and foster domestic understanding of their objectives and policies. This is particularly true of CCTs that depend on external funding, which may be absorbed in meeting the demands of the organisations providing the finance.

RPS would have benefited from a campaign that increased internal support from both government officials and the non-beneficiary populace. Sentiments in Nicaragua about RPS tended to be polarised and uninformed. Some common opinions were misleading, and RPS officials grappled with domestic opposition arising from a lack of understanding of the programme's objectives and procedures.

Domestic pessimism and misperceptions ranged from the programme's purpose to policies and impacts. There was a persistent belief that RPS was not concerned with alleviating long-term poverty, but rather that it was perpetuating poverty by giving cash transfers to the poor. In reality, RPS was noteworthy for its focus on using conditional transfers as a mechanism to initiate behavioural changes and increase investment in long-term human capital accumulation. The programme's educational components and co-responsibilities, while central to RPS, were not well known or understood among domestic critics.

Another complaint was that the programme was inefficient and too expensive. RPS might have received greater support if government officials had understood all the services the programme provided—why RPS managed these services rather than others, and the long-term savings the current expenses were expected to generate. If the programme's positive impacts had been clearly and consistently communicated, some of these accusations might have been tempered.

Rather than addressing these attacks, RPS officials focused on satisfying the requirements of the programme's loans in order to ensure that it could continue to receive funding for future phases. They were also unduly concerned with responding to external criticisms that might endanger its funding. This approach, while not unreasonable, neglected important domestic constituencies whose negative opinions and misperceptions ultimately contributed to the programme's demise.

The lack of domestic understanding ultimately overwhelmed the programme. Nicaraguan support could not be maintained, and RPS's autonomy was eventually eroded. Officials were forced to share RPS resources with other groups, to the detriment of the programme's own efforts. The mission was diluted. Officials and resources were spread too thinly, and efficiency and enthusiasm were damaged. Eventually, RPS was discontinued, to the surprise of many within the international community, who understood the programme's purpose and impacts better than domestic constituents.

The end of the Nicaraguan experience with RPS is disappointing in light of the programme's achievements, but it provides relevant lessons to policymakers working with CCTs, particularly those receiving external funding. Even if a programme is deemed successful to the international community, domestic constituents must still approve of it. The support of both the non-beneficiary populace and government officials is important. Key domestic officials may change over time, and support cannot be provided solely by a few officials who may not remain in their positions. Frequent communication of a programme's purposes, policies and results is important to gaining and maintaining support. Without steady domestic approval, even an excellent programme may lose support and eventually be discontinued. With such support, the programme is more likely to continue to function, improve and enjoy greater backing and influence.

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One Pager number 79
Published: March, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager79.pdf>

Confronting Crises: Learning From Labour Markets in the Past

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The current economic crisis is spreading to the developing world. Even solid emerging economies are affected. **IPC Working Paper No. 51** reviews labour markets in three Latin American countries over the past two decades and suggests how recessions affect the working poor. This One Pager looks at experiences that might guide policy options to confront the crisis. It examines two large, export-dependent countries, Chile and Mexico, and reviews two kinds of economic period: slow growth (Chile, 2000–2003; and Mexico, 2000–2004); and decline (Mexico's 1995 tequila crisis).

In each of these periods, poor workers (the 20 per cent with the lowest labour income) performed relatively better than in non-recession years. In the two slow-growth periods, poor workers' income rose by about 0.7 percentage points more than the increase for the average worker, which was 0.2 per cent in Chile and 1.9 per cent in Mexico. During Mexico's contraction, poor workers' labour income fell by 3.6 percentage points less than the 15.1 per cent drop in mean incomes. Since the supply of unskilled workers is much larger, one assumes that poor workers have less bargaining power when demand is slack, and thus the improvement in their relative income might be surprising. But the fact is that wages at the bottom of the distribution are already so low that there is little room for further cuts.

We offer insights into these income patterns by distinguishing those that stem from adjustments in workers' socio-demographic characteristics from those arising from changes in the returns to those characteristics: sex, age, education, place of residence, employment sector and contract type. The change in returns is the main factor in overall changes in earnings. Some of the most relevant changes in returns are summarised below.

In Chile, during 2000–2003, a 2.4 per cent fall in the returns to full-time (against part-time workers) was the most important factor in the change in relative earnings. This change gave poor workers—who do more part-time work than the average worker—a 0.8 percentage point edge, explaining most of their improvement in earnings. All other changes were smaller and they worsened poor workers' relative income, albeit by a small margin. The table lists four of the main changes.

Mexico's slow-growth period of 2000–2004 was different. The main change was the fall in returns to urban workers relative to rural workers, spurring a 1 percentage point improvement in poor workers' relative income. The 0.9 per cent increase in the returns to informal employees, relative to the self-employed, improved the poor's relative income position by about a third of a percentage point (though this was partially offset by a -0.6 per cent relative loss from the increase in the return to formal employees against the self-employed). Since men are better paid, the 0.7 per cent fall in the relative returns of male workers also improved the poor's relative incomes. This implies that women make up a larger proportion of the poor.

The most striking changes came during the tequila crisis. Two-thirds of the poor's relative income "gain" stemmed from two changes: a 3.7 per cent fall in the returns to urban (against rural) workers and a 2.4 per cent fall in the return to services (relative to agriculture). A drop of 2.4 per cent in the returns to male workers added to the poor's relative income, albeit modestly. But not all factors favoured the poor. Their relative incomes worsened with the 2.6 per cent increase in the relative return to full-time workers.

This review suggests that periods of slow growth and recession in Mexico and Chile improved the poor's relative income. That their labour income does not fall as much as others' during crises may offer comfort, but even a small decline can exact a heavy toll. Safety nets and emergency assistance help protect minimum consumption levels, but policies to confront economic crises should not be mere mitigation strategies. They should include interventions to strengthen human capacity and improve the poor's main asset: labour.

Changes in Mean Labour Earnings and Relative Returns to Workers' Characteristics. Annual Percentage Changes

Chile 2000–2003, slow growth		
	mean	20% (df)
Actual earnings per worker	0.19	0.64
40+/-39 hours	-2.37	0.76
Secondary/no education	0.96	-0.16
Urban/rural	0.42	-0.05
Male/female	0.32	-0.06
Mexico 2000–2004, slow growth		
Actual earnings per worker	1.88	0.65
Urban/rural	-2.62	1.02
Informal/self-employed	0.89	0.27
Male/female	-0.66	0.17
Formal/self-employed	0.64	-0.57
Mexico 1994–1996, recession		
Actual earnings per worker	-15.11	3.54
Urban/rural	-3.69	1.45
40+/-39 hours	2.63	-0.88
Male/female	-2.45	0.55
Services/agriculture	-2.42	1.07

Source: Zepeda et al. (2009).
Note: (df)= difference between the mean change for the bottom 20 per cent of the earnings distribution and the mean change for the entire sample

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One Pager number 80
Published: March, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager80.pdf>

How Does the **Financial Crisis Affect** Developing Countries?

by Diana Alarcon, Poverty Practice, Bureau for Development Policy, UNDP; , Columbia University; and José Antonio Ocampo, Columbia University

The global economy is in crisis as a result of inadequate regulation and supervision of banks and financial markets. The prudential regulation and supervision recommended to developing countries was largely ignored in the developed nations. No country, however, is spared from the consequences of the downturn. The impact on developing countries is even greater.

The crisis is driven by the reversal of the three factors that fuelled the economic boom of 2003–2007. This period saw exceptional levels of financing (private flows to some countries and overseas development assistance to others), high commodity prices and large flows of remittances. The continuing decline in capital flows and exports is hurting the developing countries, despite their having adhered to stringent macroeconomic frameworks.

The accumulation of international reserves and lower levels of external debt allow some developing countries to protect themselves from the rapid deterioration of capital flows. But the contraction of credit, its high cost and the volatility of portfolio investments have already led to a contraction of financial flows. Bank lending to emerging markets fell from a peak of US$410 billion in 2007 to US$167 billion in 2008, and is projected to fall to US$60 billion in 2009 (Griffith-Jones and Ocampo, 2009).

Lower trade volumes will be the main channel of transmission to exporters of manufactures and services (including tourism). The volatility of commodity prices will also affect exporters of primary goods. In countries like Congo, Equatorial Guinea, Gabon and Nigeria, oil provides more than 50 per cent of government revenues from commodity exports. In Côte d'Ivoire and Guinea, cocoa and minerals account for a fifth of revenues. Cotton and aluminium exports provide a fifth of tax revenues in Tajikistan. In Trinidad and Tobago, and in Bolivia, commodities account for 22 and 12 percent of GDP, respectively. The prospects for commodity prices remain poor. Recent projections by the World Bank forecast a 25 per cent reduction in energy prices in 2009 and a 23 per cent fall in non-energy commodity prices (World Bank, 2009).

Remittances often provide a safety net in recipient countries. Income from migrant workers helps stabilise consumption levels when recipient economies contract. But remittances have been falling since 2008 in the range of -1 per cent to -6 per cent. The decline in remittances will be devastating to countries that largely depend on them. For instance, remittances make up 45 per cent of Tajikistan's GDP. Guyana relies on remittances for a quarter of its income (see table).

Remittances as a Proportion of GDP

Country	% of GDP
Tajikistan	45
Moldova	38
Tonga	35
Lesotho	29
Honduras	25
Lebanon	24
Guyana	24

Source: World Bank (2009).

What should be done to mitigate the impact of the crisis? In most developing countries, macroeconomic indicators, including the accumulation of reserves, have improved in the last five years.

Those countries are much better placed to adopt expansionary fiscal and monetary policies. Infrastructure investments and social spending on nutrition, basic education and health care are essential. There is also an opportunity to expand non-traditional exports through a mix of exchange rate policies and sectoral incentives.

Concerted international action is also needed. A new system of financial regulation should be built upon two broad principles: the need to incorporate counter-cyclical mechanisms in order to correct for the boom-bust nature of financial markets; and effective regulation whereby the domain of the regulator is the same as the domain of the market to be regulated, which is global in nature.

Reforms are needed in three areas. First is the creation of a meaningful and truly global reserve currency with a substantial expansion of resources to provide counter-cyclical liquidity to developing countries. Second, with greater voice given to developing countries, the International Monetary Fund (IMF) can be instrumental in coordinating global macroeconomic policy. Third, IMF lending has to come without the overly burdensome conditionality of the past. It must have quick-disbursing facilities for countries with strong economic policies facing temporary liquidity problems.

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One Pager number 81
Published: April, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager81 .pdf>

Is the Washington Consensus Dead?

by Degol Hailu, International Policy Centre for Inclusive Growth

The recent G20 meeting in London elevated the International Monetary Fund (IMF) to a new level. Its lending capacity was tripled to US$750 billion. In the aftermath of World War II, the IMF was established to deal with declining commodity prices and deteriorating international trade. During the oil price shocks of the 1970s the IMF became lender of last resort, mainly to countries with balance of payments problems. The debt crisis of the early 1980s in Latin America gave the Fund further impetus. By the mid 1980s the IMF and the World Bank had become policy architects in low-income countries. The 1998 Asian financial crisis brought the IMF to the forefront of crisis management. In 2009, we are again at another milestone–the Fund is back with even greater influence.

The IMF's past lending practices, however, do not make good reading. The Fund has shoved the Washington Consensus down the throats of low- and middle-income countries, often with heavy conditionalities. Williamson (2000, p. 251) stated, "I invented the term 'Washington Consensus' to refer to the lowest common denominator of policy advice being addressed by the Washington-based institutions to Latin American countries". The advice included fiscal discipline; cutting tax rates; interest rate liberalisation; competitive exchange rates; trade liberalisation; liberalisation of capital flows; privatisation; and deregulation of prices and markets.

The IMF argued that its conditionalities were designed to prevent moral hazard and adverse selection; to provide credibility to reforms; and to show commitment to policy change. It applied the principal-agent problem to development finance. In private financial markets there is an asymmetry of information. Adverse selection blurs the distinction between a viable borrower and a potential defaulter. Moral hazard provides the wrong incentive for the borrower to engage in risky actions. Similarly, the IMF argues, concessionary lending may be an incentive for borrowers to deliberately seek balance of payments crises in order to acquire funding, and hence the need for conditionalities.

Will the IMF provide the new resources under a post-Washington Consensus arrangement? Will the financing be free of conditionalities? The answer is no. Washington Consensus polices and the associated conditionalities are alive and well. As of today, the policy prescriptions are the same as those listed by Williamson. If history is a guide to the future, they are unlikely to change soon.

In 2008 alone there were 224 types of conditionalities imposed on 15 countries. The table lists just eight of them. The highest conditionality is in the area of fiscal reforms, followed by financial liberalisation, privatisation, trade reforms, exchange rate adjustments and price liberalisation. Conditionalities are also highest in the least developed countries.

IMF Policy Prescriptions and Conditionalities Imposed in 2008

Country	Prescription
Djibouti	Introduce law to set single-rate VAT at 7 per cent by 2009.
Honduras	Adjust tariffs in the electricity sector in line with cost recovery. Raise interest rate by 25 basis points.
Mali	Eliminate all customs exemptions.
Niger	Reduce the rate of profit tax from 35 to 30 per cent.
Pakistan	Eliminate electricity tariff subsidies.
Republic	Introduce commercialisation and phase out fuel price of Congo subsidies by 2011.
Ukraine	Prohibit multiple currency practices. Achieve a fiscal balance of zero.
Zambia	Adjust tariffs in the electricity sector in line with cost recovery.

Source: IMF MONA online database.

The simple truth is that conditionalities are paternalistic. They are meant to alter behaviour and induce changes in economic, political and social structures. They also serve as a sort of collateral; in some cases they are a form of coercion to ensure adoption of otherwise unpalatable reforms. Conditionalities trigger conflicts between the recipient country's objectives and those of the lender. The lender enjoys bargaining power over financially dependent recipients through control of credit tranches. The outcome is usually in favour of the lender, whose catalytic function and seal of approval give it powerful leverage. For this reason alone, conditional lending erodes ownership of reforms.

Developing countries are in critical need of capital flows. Besides the impact of the current global recession, they still need external finance to supplement domestic savings. Aid and multilateral credit have been disappointing. As Mayo (2009) argues, what low-income countries require are portfolio finance. These types of capital flows require high credit ratings. The IMF could create mechanisms for the development of bond markets. It would act as the underwriter, providing sovereign guarantee schemes to protect the bondholders against possible default. This would lay the foundations for the much needed aid exit strategy, instead of perpetuating a failed consensus along with gratuitous and punitive conditional lending practices.

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One Pager number 82
Published: April, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager82.pdf>

HIV and Income Inequality: If There Is a Link, What Does It Tell Us?

by Göran Holmqvist, Institute for Futures Studies, Stockholm and Nordic Africa Institute, Uppsala by Göran Holmqvist, Institute for Futures Studies, Stockholm and Nordic Africa Institute, Uppsala

The global HIV prevalence map reveals striking contrasts between high- and low-prevalence countries. Africa is the most affected continent, but within Africa there is a distinct geographical pattern. A handful of Southern African countries have prevalence indicators in the range of 15–35 per cent, while rates in West African countries are in the range of 1–5 per cent and those in East African countries are somewhere in between. What explains this variation in HIV prevalence rates? The answer could offer some clues about the HIV epidemic and how to counteract it. More generally, it may also teach us something about why certain societies are more vulnerable than others to an infectious disease such as HIV.

The question has been addressed by a number of studies that apply some form of regression technique using indicators available at cross-country level. As always, cross-country regression results should be interpreted with care. There are several caveats, such as measurement problems, omission of relevant variables and uncertain directions of causality. With indicators of sexual behaviour, such issues are particularly acute. Statistical relations are not always causal and causal relations do not necessarily indicate what the most relevant intervention should be.

Cross-country studies reveal a significant link between income inequality, normally measured by the Gini coefficient, and HIV prevalence (other significant variables being the percentage of the population that is Muslim, male circumcision and regional dummies). The link between income inequality and HIV prevalence persists when one controls for various other indicators of poverty, economic development, gender inequality and urbanisation (Tsafack Temah, 2008). The same result is yielded by a global sample, one for Sub-Saharan Africa alone, and a global sample excluding Sub-Saharan Africa. The same link has also been revealed in national studies based on states/provinces in the United States and China; for an overview of regression results, see Holmqvist (2009). While HIV/AIDS is often termed a disease of poverty, these results indicate that it could more justifiably be described as a disease of inequality.

While this connection between income inequality and HIV has relatively strong empirical support, its interpretation is an open issue. Why should there be such a link between the distribution of incomes in a society and the spread of HIV? The link echoes the more general discussion on the relation between income inequality and public health, wherein the same statistical association has been established for a number of diseases.

One possible interpretation would be grounded in a theory of the economics of sexual behaviour. Essentially, the adverse future life chances of people living in poverty are likely to increase their readiness to take risks today. On the other hand, high income levels make it more affordable to engage in multiple partnerships. High income inequality would stimulate both these behaviours. This theory could easily be combined with the now influential view that the phenomenon of multiple and concurrent partnerships is a key factor behind the spread of HIV. Another interpretation of the income inequality-HIV link would take a sociological perspective, emphasising the role of social capital and social cohesion. Income inequality is assumed to undermine social cohesion, thereby making it difficult to establish norms, communicate with trust and mobilise collective resources in the pursuit of joint goals or to control risk. A third interpretation could be that the link is spurious—purely statistical and driven by a third factor related to both income inequality and HIV.

What does this imply for policy? First, the empirical support for a link between income inequality and HIV prevalence is another illustration of how unequal societies with large social divides pay a price in terms of public health. HIV and AIDS are far from being the only diseases to fall into this category. A key issue is to establish a clearer understanding, based on empirical evidence, of the pathways that lead from income inequality to HIV. It is an area in which more research efforts are needed.

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One Pager number 83
Published: April, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager83.pdf>

The 2015 Debt Crisis

by Paul Ladd, Poverty Practice,
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At the London G20 Summit, participants reaffirmed their commitment to the Millennium Development Goals (MDGs) and to increasing official development assistance (ODA). This aid will be important in helping the poorest countries meet the MDGs that were agreed before the crisis, but it will probably be insufficient to tackle the additional problems caused by the current economic downturn.

Hence a lot of attention has focused on the US$1.1 trillion of new financing that the G20 pledged to make available. Although this will be helpful for many developing countries facing liquidity or budget problems, the fact that this support will come mostly in the form of loans rather than grants may pose future problems for debt sustainability. This One Pager argues that the international community should move now to put in place an international mechanism for sovereign debt restructuring so that future debt crises do not have to be resolved through ad hoc rounds of debt relief.

Developing countries are being hit on all sides by the crisis. Their growth is projected to slip to 1.6 per cent in 2009, down from 8.3 per cent in 2007 (IMF, 2009). Slower domestic growth means lower tax collection and less investment in growth, jobs and the MDGs. And a slowing global economy means that communities are receiving fewer remittances from family members working overseas.

Exports are falling because of lower international demand and reduced trade finance. And international credit markets are frozen, imperilling not only future investment but also the ability to roll over existing loans. The World Bank has estimated that some 98 developing countries could face a financing gap of between US$268 billion and US$700 billion in 2009 (World Bank, 2009).

Like their counterparts in the North, developing-country governments have to balance their books and improve the standard of living of their electorates. With other financial flows drying up, it will be tempting to take advantage of the expanded loans available through the development banks and the International Monetary Fund (IMF). This may be a necessity for some countries, even if unwelcome loan conditions remain in place.

External public debt levels are therefore likely to rise again, but this is not necessarily a bad thing. Countries and their populations have a right to borrow, to invest in jobs and growth for the future and also to smooth good and bad times. But we may soon see warning lights flashing again. The last three decades have brought a cycle of sovereign indebtedness that has been costly not only financially but also in terms of human opportunity. The oil boom in the late 1970s led to a world in which excess liquidity washed down to the world's poorest countries. By the late 1980s and early 1990s, an unfavourable external environment, coupled with irresponsible creditor and debtor government behaviour, left citizens in many developing countries saddled with high levels of debt.

The international community slowly recognised that many poor countries were caught in a debt trap and, facing mounting pressure from civil society, creditors put in place a series of debt relief schemes such as the Highly-Indebted Poor Countries (HIPC) programme and the Multilateral Debt Relief Initiative (MDRI). These schemes have contributed significantly to reducing the debt burden of some 24 eligible countries. While another 17 could receive irrevocable debt relief once they meet eligibility criteria, many other ineligible countries still hold high levels of debt.

If developing-country debt problems come to a head once again—including because of how the international community is responding to the current economic crisis—we will need a new way of addressing the problem. A second round of debt relief schemes based on creditor largesse will lack credibility. The scene is set once again for an idea that almost reached fruition in 2003, albeit in an imperfect form. An international mechanism for sovereign debt restructuring, which includes provisions for temporary moratoria on debt servicing, could provide a better means of restructuring unpayable debts in a way that is fairer, more transparent and more efficient for the creditors, the indebted country, and its population.

To be effective and comprehensive, however, any such arbitration mechanism would need to cover the claims of the World Bank and IMF. These are not covered by the recent introduction of "collective action clauses" in sovereign bonds.

The time to put in place such a mechanism is before a new debt crisis emerges, not when the waters start to get choppier. Otherwise, 2015 may be remembered as the year that a new debt crisis emerged, rather than the year in which we celebrate achieving the MDGs.

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One Pager number 84
Published: May, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager84.pdf>

What Is the Impact of Cash Transfers on Labour Supply?

by Clarissa Gondim Teixeira,
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Since the 1990s, Latin American governments have implemented various conditional cash transfer programmes (CCTs). The objective of CCTs is to alleviate poverty in the short run and create conditions for upward social mobility in the long run through human capital investments. CCTs target families living below the poverty lines, focusing on children and school-age adolescents.

This One Pager investigates the impact of the Brazilian CCT, the Programa Bolsa Família (PBF), on beneficiaries' decision to supply their labour. The theoretical departure is this: households have a time-allocation strategy between housework activities and paid work. Income shocks, such as cash transfers, alter such time-allocation preferences. In other words, they change the relative value of time. Let us assume that paid work hours do not generate any additional well-being to households, except for increases in income. As cash transfers increase income, paid time loses value relative to unpaid time. Therefore, the expected behaviour is a reduction in the supply of paid work hours and an increase in housework or leisure hours.

Using data from the Brazilian annual household survey (PNAD-2006), Teixeira (2008) conducted an empirical analysis to determine if the above effects hold or not. PBF targets two groups of families. The first comprises poor families whose monthly per capita income was between R$50.00 and R$100.00 in 2006. This group received variable transfers of R$15.00 per child or breastfeeding mother, up to a maximum of three people. The second group comprises families below the extreme poverty line whose monthly per capita income was less than R$50.00. In addition to variable transfers, this second group received a R$50.00 fixed transfer.

Teixeira (2008) finds a marginal reduction in labour hours supplied in response to PBF's transfers. The reduction was statistically significant but not large. The variation is between 0.5 and 3.5 hours per week for working adults. The effect is greater depending on the share of the transfer in households' income. Those below the extreme poverty line reduce their supply of labour more than those below the poverty line. Additionally, households in which there is only one child or those who receive R$15.00, R$50.00 or R$65.00 reduce their labour supply to paid work more than those with larger families.

Both the transfer's value and its value relative to household income are relevant. However, analysing the transfer share over household income enables a better identification of the most affected individuals than does analysis of whether or not the household receives the transfer.

Moreover, the change in the supply of work hours varies according to gender and sectors. Women are more sensitive to budget shocks, as expected, because of intra-household work divisions. For instance, women usually contribute more to domestic activities and childcare. Since women tend to be low-paid, the cash transfer more easily changes their time-allocation preferences. This is in line with Becker's (1965) Time Allocation Theory, which suggests there is a substitution between paid work hours and time allocated for housework activities.

The empirical evidence suggests that PBF increases housework by an average of 1.1 hours per week. Hence PBF marginally reduces labour hours supplied by the households in our sample, but it also increases the time that women allocate to housework. This latter impact actually implies greater household well-being. The evidence does not suggest a perfect substitution between hours of paid work and housework activities. Thus we cannot affirm that women's work hours are completely replaced by leisure hours as might be the case with men, since men contribute relatively little to housework.

Formal work is the least elastic and self-employment is found to have the greatest elasticity. This means workers in the formal sector are less likely to reduce their labour supply in response to the cash transfer. In most cases, formal work involves a fixed number of working hours. Besides that, the value of work hours devoted to formal work constitutes a payment with the added value of workers' rights and benefits. On the other hand, informal and self-employment activities do not offer any of these benefits. Thus they offer greater flexibility in terms of time spent at work. Labour market weaknesses, such as informality, exacerbate the marginal adverse effects of the reduction in adults' labour supply.

The evidence shows that the beneficiaries have different behavioural responses to the income shock—that is, the PBF transfers. We find a marginal change in labour hours supplied by the households in the sample. Future improvements in the PBF must take account of this effect and strategies must be designed to counter them. Similarly, parallel initiatives focused on training and empowering informal and self-employed workers are desirable in order to minimise the programme's adverse effects on hours supplied for paid work.

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One Pager number 85
Published: June, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager85.pdf>

The Indonesian Response to the Financial and Economic Crisis: **Is the Developmental State Back?**

by Degol Hailu, International Policy Centre for Inclusive Growth (IPC-IG)

The current economic slowdown is jeopardising efforts to achieve the Millennium Development Goals. Poverty is worsening and jobs have been lost. The Asian Development Bank estimates that by 2010, about 100 million people in Asia will fall into poverty.

The slump is affecting Indonesia mainly through declines in its exports and capital flows. The prices of its major export commodities are falling. The stock market has plummeted in the last six months. The markets for Indonesian Government Securities and Indonesian Certificates (SBIs) showed a deficit of US$2.2 billion in the first four months of 2009. Added to the crisis is food-driven inflationary pressure. In 2008 the consumer price index (CPI) reached 12 per cent, up from 6.6 per cent in 2007. Food prices account for 49 per cent of the rise in inflation. The CPI weight for food is 36 per cent. How is the Indonesian government responding to the financial and economic crisis?

In the first quarter of 2009, rubber exports fell by 32 per cent. Farmers have suffered most. In some provinces tapping has completely ceased. The policy response was to cut shipments of rubber exports by 700,000 tons, a cartelist measure that was taken in concert with Thailand and Malaysia. The hope is to keep prices high and maintain constant income levels, just as the Organisation of Petroleum Exporting Countries (OPEC) does.

The price of tin, another major Indonesian export, fell from US$23,595 per ton in July 2008 to US$12,355 in April 2009. The government suspended the quota system that set minimum limits on tin exports. When prices were high, provinces such as Bangka Belitung and the Riau Islands were required to export at least 90,000 and 15,000 tons of tin, respectively. By suspending the minimum quota, the government is encouraging producers to cut their output and keep prices stable in the face of slow global demand. As a result, tin production fell from an average of 120,000 tons between 2005 and 2007 to 80,000 tons in 2008.

The footwear and textile sector is also suffering from sluggish global demand. Currently, 60 per cent of production is exported, while 40 per cent is consumed locally. Like other Asian countries, notably China, the government is openly discussing the shift in its development strategy. The new focus is on expanding domestic markets. In fact, the target for the footwear and textile industry is to switch the above percentages: 60 per cent for domestic consumption and 40 per cent for exports. As part of its stimulus package, the government is providing direct subsidies for the purchase of machinery under the Machinery Revitalisation Programme. Recently, the footwear industry received a cash subsidy of US$5.17 billion, and US$22.1 billion was provided to the textile industry.

The drive to boost domestic consumption is also accompanied by an import-substitution strategy. For instance, Indonesia produces about 24,000 tons of cotton annually. But estimates suggest that domestic cotton production satisfies only 4 per cent of demand. The balance is imported, mainly from Egypt and the United States. Again, the government stepped in and launched a scheme to increase cotton output to 48,000 tons in the next few years, and to double the area under cultivation to 40,000 hectares. The provision of subsidised seeds and farm inputs has already started in Gunung Kidul, Yogyakarta, Pati, Kudus, Blora, East Java, and South Sulawesi provinces.

The government's response to the crisis has also included macroeconomic policy changes. The interest rate was cut to 7.8 per cent in 2009 from 9.5 per cent in 2008. A fiscal stimulus of US$7 billion, or 1.4 per cent of GDP, has also been announced. The stimulus comes in the form of tax cuts (76.5 per cent of it), infrastructure expenditure (16.8 per cent) and direct subsidies (6.7 per cent). Fortunately, 2009 started with a fiscal deficit of 1.2 per cent of GDP, which gave the government room for deficit financing.

Cartelist stances in the supply of commodity exports, direct industrial subsidies, import-substitution measures and a Keynesian fiscal stimulus have been the hallmark of the Indonesian response to the crisis. Until now these heterodox measures have been anathema to the neoliberal consensus. We are witnessing the resurgence of the developmental state, given the crisis of legitimacy faced by that consensus.

Note:
This article is based on consultations held during the author's recent visit to Indonesia under a UNDP research project. Sincere thanks go to the many people who generously provided their insights.

One Pager number 86
Published: June, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager86.pdf>

Towards an MDG-Consistent Debt Sustainability Concept

by Bernhard G. Gunter,
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Many pledges to increase official development assistance (ODA) remain unfulfilled, and the current economic crisis may constrain such capital flows even further. Can increased debt financing by countries that make progress towards achieving the Millennium Development Goals (MDGs) be justified?

In the spring of 2005, the International Monetary Fund (IMF) and the World Bank implemented a new debt sustainability framework for low-income countries. This policy-based framework seeks to tackle the debt sustainability challenge. According to the framework, countries eligible under the Multilateral Debt Relief Initiative (MDRI) are not supposed to accumulate new debt, even if their debt levels are below the thresholds established in the framework.

Low-income countries are concerned that the framework may lock them into a "low debt-low growth" scenario. Hence the Report of the Secretary-General of the United Nations (UN, 2005: 18) proposed to "redefine debt sustainability as the level of debt that allows a country to achieve the MDGs and reach 2015 without an increase in debt ratios." Following the Secretary-General's proposal, the United Nations has requested suggestions for a conception of debt sustainability that is more consistent with attainment of the MDGs.

Debt cancellation, followed by grant financing for required MDG expenditures, would be the first-best solution. In donor countries, however, there are considerable political constraints on increasing the necessary grant financing. Most of the aid pledged (including the promises made at the G-20 summit in January 2009) is still in the form of loans. While it is not possible to increase the debt financing of development strategies without also increasing indebtedness, it makes sense to provide more loans to countries that can bear more debt.

Gunter, Rahman and Shi (2009) recently provided empirical evidence of a robust relationship between achieving the MDGs and having a greater capacity to bear debt. The study used the same probit regressions used to justify the framework introduced by the Bretton Woods institutions. The finding is that the capacity to bear debt is related to progress made in social development. Even after controlling for good policies and institutions, the capacity to bear debt shows a statistically significant positive relationship with social development.

This allows for the adoption of a new, MDG-consistent debt sustainability framework, which could either add an MDG-progress indicator to the current framework or replace the policy-based indicator with an MDG-progress indicator. The exact composition of the indicator, as well as the next steps to be taken, need further discussion. Our argument is that the new framework has clear advantages.

It should be pointed out that the MDG-consistent debt sustainability concept has some limitations. It will not remove the debt overhang of poor countries that are not eligible for the MDRI and the Heavily Indebted Poor Countries debt relief initiative. The concept is of little use to countries that do not make progress towards achieving the MDGs. Indebting these countries does not provide any solution, since increased debt financing could easily create a debt overhang. This MDG-based concept is not suggested as a mechanism to determine which countries are deserving and undeserving aid recipients. Debt sustainability frameworks and aid allocation frameworks are two different concepts.

Given the above caveats, an MDG-consistent debt sustainability framework has at least four policy implications. First, having a framework with an MDG-progress indicator could increase the nominal amount of total aid provided by donors. This is because increasing aid through loans has lower real costs for donors than providing the same nominal amount of aid in the form of grants. The main policy implication for donors is that they could provide concessional lending beyond the current loan limits.

Second, the proposed new framework would allow countries that make progress towards achieving the MDGs to increase their concessional debt financing. It would also allow them to avoid the costly alternatives of non-concessional financing from domestic and external sources. Third, debt sustainability will be directly linked to the financing of the MDGs, not just good policies and institutions alone. Finally, achievement of the MDGs is measurable more objectively than the policy-based framework introduced by the IMF and the World Bank. All in all, the adoption of an MDG-consistent debt sustainability concept is a win-win solution.

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One Pager number 87
Published: July, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager87.pdf>

Age and Gender Bias in Workloads During the Lifecycle: **Evidence from Rural Ghana**

by Raquel Tsukada and Elydia Silva, International Policy Centre for Inclusive Growth

This One Pager discusses how age and gender affect workloads during the lifecycle of women and men in rural Ghana. We argue that the division of labour seems to sustain gender-income differences and intergenerational poverty. The workload is disproportionately carried by women, while children enter the labour force prematurely and the elderly work beyond retirement.

According to economic theories, individuals consume a constant percentage of the present value of their lifetime income, which is based on their forward-looking expectations. Savings are made during the economically productive period, and dissaving happens during childhood and retirement. Low-income individuals have a high average propensity to consume. Time constraints, especially during the productive ages, hamper their ability to increase expected permanent income. Consequently, individuals in low-income households tend to extend their working life from childhood to old age in an attempt to increase their consumption level.

Using data from the Ghana Living Standards Survey, we find that children aged 10 and below spend significant hours a week working. A 60 year-old woman still works about 50 hours a week (figure a). The high dependency ratio, lack of formal employment, weak social protection and absence of pension schemes for most rural households extend the heavy workload until the very last years of life.

The data also reveal an unambiguous gender bias in time use. On average, women work disproportionably longer hours than men during their lifetimes. The high intensity of domestic unpaid work restricts their time availability to perform remunerated activities. Women therefore tend to have a reduced savings capacity. Their peak workload reaches 80 hours a week during their most productive age (around 30), while men, peaking around the same age, work about 50 hours a week.

Disaggregating total work into domestic (unpaid) and market (paid) work, we uncover another interesting fact. The disproportionate work burden on women coincides with the period when they bear their first children and take on the traditional demanding female role in parenthood. Men's lifelong workload peaks in the same age range as does women's, but this is because men spend longer hours at paid work (figure b). Men are thus able to substantially increase their permanent income during their most productive age.

The gender bias starts at school age (7–14). There is no significant difference between the proportion of boys and girls attending school, but the time use of children reveals an important story that is masked by the gender-unbiased enrolment rates. School-age girls work increasingly longer hours than boys. They have less time available for homework and self-study. Most of the workload consists of unpaid domestic chores (figure c). Hence the ability of women to earn income seems to be gender-biased from childhood, when girls' accumulation of human capital is neglected and the potential for higher income is foreclosed. The upshot is lower female intra-household bargaining power, which points towards persistent female time poverty and further income poverty (see also Costa et al., 2009).

In the context of slow cultural change in intra-household gender roles, policies to empower women should primarily address alternatives for reducing domestic work. Lessening the burden of domestic work on women requires improving access to basic infrastructure and making childcare facilities available. Excluding children from the labour market and investing in human capital at an early age help their savings capacity and protection during old age.

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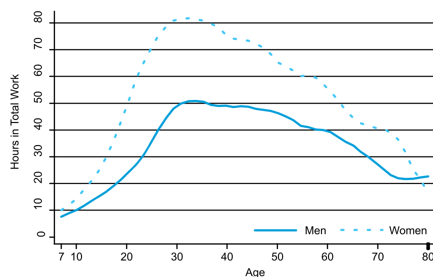
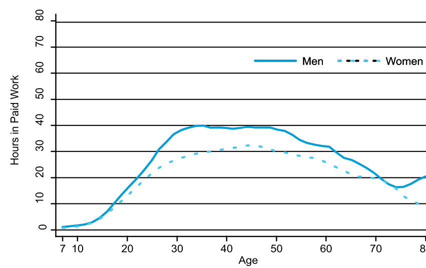
Workload During the Lifecycle of Women and Men in Rural Ghana

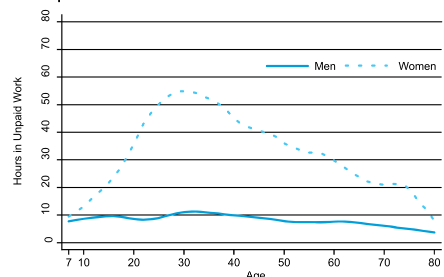
a. Total Work



b. Paid Work



c. Unpaid Work



Note: Non-linear estimations using Ghana Living Standards Survey 4 (1998–1999).

One Pager number 88
Published: July, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager88.pdf>

What Explains the Decline in Brazil's Inequality?

by Degol Hailu, International Policy Centre for Inclusive Growth (IPC-IG) and Sergei Soares, Institute for Applied Economic Research (IPEA)

The economics profession has long debated whether there is a trade-off between growth and equity. Countries that pursued inequality-reducing strategies have been warned that growth will be affected, and hence that poverty increases. The harbingers of doom advocated a growth-focused strategy. Their assumption was that the income of the poor rises in direct proportion to economic growth. The truth is more like this: economies with more equal income distribution are likely to achieve higher rates of poverty reduction than very unequal countries. In this One Pager we consider if this is the case in Brazil.

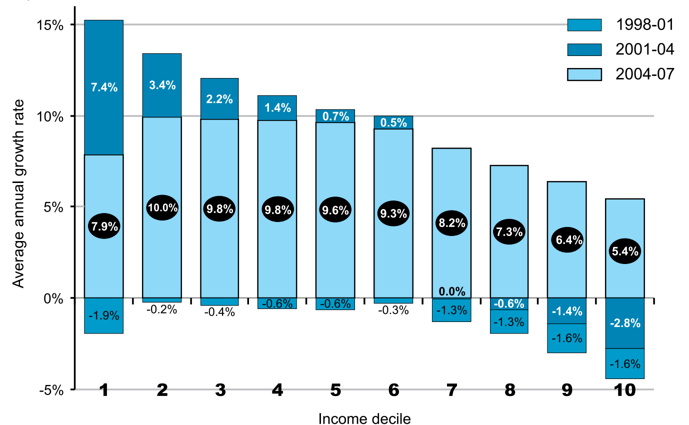
Inequality in Brazil, as measured by the Gini coefficient, fell from 0.59 in 2001 to 0.53 in 2007. Much remains unknown about why inequality has fallen, but two sets of known causes stand out. The first consists of improvements in education. In the early and mid 1990s, for example, the workforce gained more equal accessto education. This is because of universal admission to primary schooling and lower repetition rates.

In conjunction with other demographic trends, such as a decline in family size and improvements in family dependency ratios, access to education helped reduce inequality. We estimate that the impact of improved access to education on primary income distribution was 0.2 Gini points per year from 1995 onwards.

The second set of factors that reduce inequality are direct cash transfers from the state to families and individuals. These transfers improve secondary income distribution. For instance, a rise in the minimum wage leads to an increase in various transfers, such as the lowest level of the contributory pension system, partially contributory rural pensions, and non-contributory income substitution for those who are unable to work and who live in poor families. At the same time, conditional cash transfers, such as Bolsa Família, deliver substantial amounts directly to the poorest families. Together, these changes lead to reductions in inequality of another 0.2 Gini points per year.

These two well-documented causes of inequality reduction explain about two-thirds of the fall in the Gini coefficient since 2001 (see Veras et al., 2006). For the remaining third the evidence is somewhat unclear, but we can plainly see knock-on effects of better income distribution. As the figure shows, the income of the bottom six deciles in Brazil has been rising since 2001, while the income of the top four deciles has risen only since 2004. For the period 2001–2007, the bottom six deciles, which account for only 18 per cent of income, accounted for 40 per cent of total income growth. These numbers cannot be explained solely by education policy, demographic trends or social protection.

Average Annual Growth Rate in Per Capita Incomes By Deciles for Three Periods between 1998 and 2007



Source: National Household Sample Surveys (PNAD).

Structuralists have long argued that under-consumption could be tackled through egalitarian income distribution. This in turn would trigger efficient capacity utilisation and encourage new investments. We can safely argue that well designed and targeted social policies stimulate aggregate demand and consumption. The transmission mechanism is straightforward. A virtuous cycle of increases in the income of poorer families, together with wage growth, has enlarged the domestic market. Greater consumption of mass-market goods has led to growing labour demand for these same families, spurring further increases in their income and purchasing power. For instance, unemployment fell by 22 per cent between 2004 and 2007.

Brazil still has a high level of inequality and progress in being made towards lowering it. It is too early to say with certainty, but one reason why the financial and economic crisis did not hit Brazil as hard as other countries may be the growing domestic market and changes in the structure of demand created in the last decade. These, in turn were spurred by this virtuous pattern of improved income distribution.

Reference:

Veras, F., S. Soares, M. Medeiros and R. Osorio (2006). Cash Transfer Programmes in Brazil: Impacts on Inequality and Poverty. Working Paper # 21. IPC-IG.

One Pager number 89
Published: July, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager89.pdf>

Do CCT Programmes Work in Low-Income Countries?

by Simone Cecchini, Economic Commission for Latin America and the Caribbean (ECLAC)

Conditional Cash Transfer (CCT) programmes have worked fairly well in large upper middle-income countries such as Brazil and Mexico. But this does not mean that the CCT model can be exported to all countries, especially the poorest. As the table shows, programmes in low-income countries are reaching a much smaller share of their population and of the extremely poor. The number of beneficiaries of CCT programmes in Brazil and Mexico is larger than the number of the extremely poor, whereas in Nicaragua the beneficiaries are equivalent to 7.8 per cent of the extremely poor population. Low-income countries also have a much more limited capacity to spend on these programmes. For instance, Mexico invests 0.44 per cent of its GDP and 4.3 per cent of total social spending in CCTs, while Honduras invests 0.02 per cent of GDP and 0.2 per cent of social spending.

Coverage and Investment of Selected CCT Programmes

Country (programme), year	Coverage		Investment in CCT	
	% of total population	% of extremely poor[a]	% of GDP	% of social spending
Brazil (Bolsa Família), 2006	22.7	> 100.0	0.43	2.0
Mexico (Oportunidades), 2006	23.8	> 100.0	0.44	4.3
Guatemala (MFP), 2008	13.6	46.7	0.06	0.8
Honduras (PRAF), 2006	6.8	14.9	0.02	0.2
Nicaragua (RPS), 2006	2.5	7.8	0.04	0.4

Note: a Does not consider exclusion or inclusion errors.
Source: Cecchini et al. (2009) and ECLAC, calculated on the basis of official figures.

A recent paper on Guatemala, Honduras and Nicaragua reveals the challenges that CCT programmes face in small, low-income countries with weak institutional settings (Cecchini et al., 2009). First, because of their multidimensional approach to poverty reduction, CCT programmes require coordination among the different sectors and territorial units of the state. In the Central American countries cited above, however, state institutions are quite fragile and coordination is far from effective.

In Honduras, an attempt is being made to coordinate efforts to fight poverty by means of the Red Solidaria. But there is still an overlap of actions between the Programa de Asignación Familiar (PRAF), which is the nationally financed cash transfer programme, and the pilot programme funded by the Inter-American Development Bank (IDB). Guatemala has no Ministry of Social Development and its CCT programme, Mi Familia Progresa (MFP), was launched in 2008 without sufficient coordination with the education and health sectors.

Second, successful and sustainable programmes must endure over time and be considered as a state policy that is not subject to governmental change. This entails setting up state-based funding mechanisms, not simply depending on foreign donors. In Nicaragua, the Red de Protección Social (RPS), financed by an IDB loan, was reasonably successful, but the present government replaced it with other poverty reduction initiatives such as Hambre Cero and Usura Cero.

Third, CCT programmes require an ability to implement and manage sound and transparent beneficiary information and payment systems. Low-income countries, however, often have weak statistical capacity and fragile banking systems. Guatemala lacks an information management system to register beneficiaries. Payments are made in cash at mass events often attended by the first lady. In Nicaragua, the RPS cash transfers were distributed by security companies hired for that purpose.

In Guatemala, Honduras and Nicaragua, which are marked by widespread poverty, geographical or other categorical targeting for poverty reduction programmes may be sufficient. Second-level targeting based on complex proxy means tests may lead to the exclusion of potential beneficiaries, as well as to tensions and feelings of discrimination. Similarly, conditioning cash transfers on school attendance or health check-ups is somewhat inappropriate in areas where these services are either absent or of dismal quality. It is equally unsuitable to announce the imposition of conditionalities when the proper information systems are lacking.

It is thus quite evident that in low-income countries funds should be devoted not only to increasing the demand for social services but also to expanding their supply. Efforts in that direction were made with RPS in Nicaragua and are under way as part of the PRAF in Honduras. These CCT programmes include cash transfers for the provision of education and health services in order to meet the increased demand that they generate.

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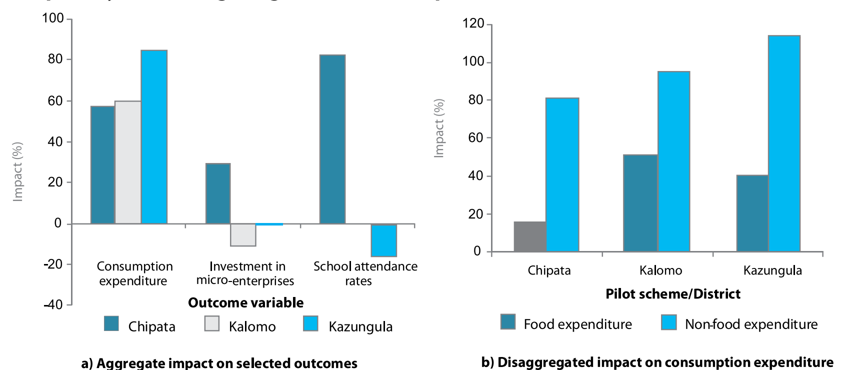
One Pager number 90
Published: July, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager90.pdf>

Social Cash Transfers in Zambia: What Is Their Impact?

by Gelson Tembo, University of Zambia and
Nicholas Freeland, MASDAR International Consultants, United Kingdom

Social Cash Transfers (SCTs) have become increasingly popular in Sub-Saharan Africa, because growth-centred development policies have failed to reduce poverty. SCTs support the consumption of the poorest, and allow them to invest in human and other forms of capital that reduce the intergenerational transmission of poverty.

Propensity Score Weighting Estimates of Impact on Selected Outcomes



a) Aggregate impact on selected outcomes

b) Disaggregated impact on consumption expenditure

In Zambia, pilot SCT schemes aim to reduce extreme poverty among the most labour-constrained of the ultra-poor, representing some 10 per cent of the population. This One Pager reports the relative impact of three spatially separated pilot SCT schemes with variations in design: Chipata (urban), Kalomo (periurban to rural) and Kazungula (rural, remote). Target households are characterised by high dependency ratios and high incidences of household heads who are elderly, orphaned, female or widowed. The Kazungula scheme has the poorest target group: household income is about a third of that in Chipata, and children have only half the daily number of meals taken by their counterparts in Chipata and Kalomo.

Impact was estimated using propensity score weighting (see Hirano, Imbens and Ridder, 2003). Principal components analysis was used to estimate an asset wealth index, which allowed disaggregation of the SCT impact estimates by wealth status. The results show that the SCTs do have positive and significant effects on consumption expenditure (for complete results see Tembo and Freeland, 2008).

The impact of SCTs on selected outcomes and disaggregated consumption effects are presented as percentages of the levels the outcome variables would have been if the beneficiaries had not participated in the schemes. In Kazungula, the poorest district, the impact on consumption is one and a half times as much as in other districts (Figure a). The SCTs are especially effective at raising non-food consumption. Impact on food expenditure is significant only in the two rural districts (Figure b).

Though not a primary objective of the analysis, there is also evidence of investment effects. The types of investment effects differ depending on where the scheme is located and the available opportunities. All things being equal, in Chipata, the urban pilot, beneficiary households are 30 per cent more likely to invest in microenterprises than they would if they did not participate in the scheme. Such effects are absent in the two rural pilots of Kalomo and Kazungula. Instead, beneficiary households in these districts own three times more small livestock than they would if they had not been beneficiaries of SCTs (not included in the figure).

School attendance rates have improved in the urban scheme (Chipata), the only one of the three to have an educational premium and a "soft" condition of school attendance attached to it. There is no evidence of impact on enrolment rates in any of the three schemes.

Impact is not homogeneous across household wealth categories. The relatively less poor are able to accumulate assets when they participate in the SCT programme, but the same cannot be said of the asset poor. Such threshold effects seem to suggest that poorer households may require higher transfer levels than their less poor counterparts. In the rural, remote scheme of Kazungula, similar threshold effects are evident with respect to school attendance.

In conclusion, SCTs are effective tools of basic social protection. As with most things, however, a "one-size-fits-all" approach is inappropriate. Expectations about impact need to be moulded by programme design and initial conditions, and vice versa.

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One Pager number 91
Published: August, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager91.pdf>

Can Low-Income Countries **Adopt Counter-Cyclical Policies?**

by Degol Hailu, International Policy Centre for Inclusive Growth and John Weeks, SOAS, University of London

The current global recession reconfirms low-income countries' vulnerability to external shocks. The exposure is a direct result of integration into the world economy. Declines in export earnings, remittances, tourism and capital flows are some of the transmission mechanisms. The developed and middle-income countries have responded with a series of stimulus packages. More to the point, they are able to adopt counter-cyclical policies. Can low-income economies do the same?

In this One Pager we argue it is possible. What is needed is a rejection of the price-determined economy framework in macroeconomic policy analysis, and in its place the adoption of the demand-determined economy framework. The theoretical distinctions between the two frameworks imply fundamental policy differences.

Price-Determined Economies

A price-determined economy is either in a unique full employment general equilibrium, or prevented from achieving it by price "distortions". All markets clear instantaneously. Any action by private or public agents to inhibit market adjustment in prices will result in an outcome below full employment. This implies that fiscal and monetary policy should be "neutral" and "passive".

Fiscal policy would be "neutral" in that: (i) taxes should not affect the decision of private agents between income/consumption and leisure; (ii) neither taxes nor expenditures should affect the relative profitability of commodities; (iii) government should not distort capital markets by competing with private agents; and (iv) the inherently distorting operations of the public sector should be minimised: taxes should be levied on a uniform basis and fiscal deficits should be minimised.

The theoretical basis for the price-determined framework is weak. It cannot be demonstrated that the full employment price set is unique, which calls into question the concept of "distortions". If there is more than one non-distorted outcome, one cannot be sure that the prices in an economy with public sector interventions are substantially different from non-distorted outcomes.

Consider this apparently simple statement: "tariffs distort profitability between importables and exportables". The validity of this statement requires the prior demonstration of the existence of a unique full employment general equilibrium. Since this cannot be demonstrated generally, even in theory, the correct statement would be, "tariffs alter profitability between importables and exportables". This is the core of the policy debate. If public sector actions distort the economy, that results in inefficiency, then such actions should be avoided or minimised. If the actions alter the economy, then a subjective policy assessment is required to determine whether the alteration is beneficial to society.

Demand-Determined Economies

An economy is demand-determined when its level of output is limited by one or all of the components of aggregate demand: consumption, private investment, government expenditure, or exports. In this framework, relative prices change as the level of aggregate demand rises and falls. Hence relative prices are not "signals" to producers and consumers, but result from their production and consumption decisions. Since prices do not determine quantity choices by consumers and producers, they are derived from them; they are not pointers of efficient allocation. Public sector interventions, therefore, should be judged on a pragmatic basis in terms of social cost and social benefit. The criterion for judgement should be whether taxes and expenditures achieve the goals set by society; when those goals conflict, an empirical analysis of trade-offs is required.

If one moves from the ethereal world of the abstract to the characteristics of low-income economies, it should be obvious that the price-determined framework is not applicable. First, most of these economies, such as those in Sub-Saharan Africa, are still advised to constrain demand through high real interest rates and fiscal austerity, and in some cases by heavy debt burdens. Second, as the current crisis reveals, many of the economies are suffering from transmission of shock through contraction in external demand. Third, major prices are not primarily market-determined. It is obvious that the nominal interest rate is an administered price if the monetary authorities practice inflation targeting. In addition, aid flows and debt servicing represent a substantial portion of the balance of payments, and neither is directly sensitive to the exchange rate. As a result, the value of a "floating" exchange rate is determined by non-market flows.

The current global recession is a demand constraint. The need to adopt counter-cyclical policies to unlock this constraint requires interventions to be "distortionary". In the short and medium run this involves counter-cyclical policies, and in the long run public investment that increases aggregate supply.

A country-specific policy package that recognises economies to be demand-determined would have the following components: (i) an expansionary fiscal budget, consistent with the rule that the overall deficit not exceed public investment; (ii) an accommodating monetary policy that tolerates moderate inflation in order to achieve higher growth by providing subsidised credit for poverty reduction programmes (the target could be that the real interest rate equals the sustainable growth rate of per capita income—the Golden Rule); and (iii) a managed exchange rate regime that seeks to promote exports and alter the relative price of tradeables and non-tradeables without causing unmanageable inflation spirals.

One Pager number 92
Published: August, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager92.pdf>

One Instrument, Many Targets:

Timor-Leste's Macroeconomic Policy Challenge

by Rui A. Gomes, UNDP Timor-Leste and Degol Hailu, International Policy Centre for Inclusive Growth

It is difficult to be sanguine about Timor-Leste's progress towards achieving the localized Millennium Development Goals (MDGs). The share of people living under the national poverty line increased from 36 per cent in 2001 to 50 per cent in 2007. The maternal mortality ratio remains unacceptably high. About half of the children are underweight. In Dili, the capital, 58 per cent of the youth have no jobs (Government of Timor Leste and UN, 2009). Can Timor-Leste scale-up MDG-related investments?

The good news is that the country has been blessed by offshore oil and gas fields. Resource revenues rose from US$29.5 million in 2002 to US$993.1 million in 2006. The government followed the Norwegian model and set up a Petroleum Fund. The proceeds are invested in safe US government bonds at a 5–6 per cent return. As of June 2009, US$4.8 billion was accumulated in the fund and part of it was invested. The fund is expected to total US$8 billion by 2012.

The government withdraws roughly 3–6 per cent a year from the Petroleum Fund. This strategy ensures that temporary gains spread into future benefits, especially in the event of a fall in oil prices.

In 2008, US$396 million was withdrawn. The government estimates that by the end of 2009 it will be able to withdraw US$589 million. The projections are based on oil prices of between US$40 and US$60 until the petroleum deposits are depleted a decade and half from now.

Essentially, the Petroleum Fund is what makes up government spending. Oil and gas revenues constitute 98 per cent of total government budget and nearly fivefold the value of GDP. Domestic revenue has been more or less constant since 2002. The table shows that without oil and gas revenues, the overall fiscal balance will drop to a deficit of 97 per cent of GDP. The not-so-good news is that the non-oil economy remains dangerously small and the country is dependent on a highly volatile and finite revenue source. The oil sector is an enclave that has virtually no linkages to the rest of the economy. It creates no employment for the domestic work force.

Our focus here, however, is on the macroeconomic challenges. Timor-Leste has adopted the US dollar as its official currency.[1] The absence of a national currency has constrained monetary and exchange rate policies. There is neither interest rate policy, nor broad money management, nor reserve ratio requirements.

Fiscal policy is the only effective instrument available to moderate inflationary pressures and expand MDG-related investments. According to the Banking and Payments Authority (BPA), yet to be transformed into a full central bank, food prices increased by 14 per cent in 2008. The inflation rate rose to 12.4 in July of the same year from 1.3 per cent in February, and averaged 9.2 per cent for the year. The consumer price

Central Government Budget as Percentage of Non-Oil GDP

	2002	2003	2004	2005	2006	2007	2008
Oil and gas revenues	10	14	46	107	195	330	481
Domestic revenues	7	10	10	11	10	11	9
Expenditure	23	21	20	26	32	59	106
Non-oil fiscal balance	-5	0	1	-5	-21	-46	-97
Overall balance	5	14	46	102	174	284	384

Source: IMF (2008). *Country Report* 08/203 and *Country Report* No. 09/219. International Monetary Fund (Washington, D.C.). Found on IMF website <http://www.imf.org/>.

index weight for food is 57 per cent. Public expenditure has more than doubled since 2002 but the government is planning major cutbacks in spending because of fears of further increases in inflation. The latest IMF Press Release stated that its staff "welcome the authorities' intention to reduce the spending envelope in the 2010 budget … and support the maintenance of the current monetary and exchange rate regime to preserve macroeconomic stability" (IMF, 2009). The argument is that oil and gas revenues, unlike tax revenues, do not reduce private sector income. Hence the expenditure is seen as adding to aggregate demand.

If macroeconomic stability is the overriding objective of fiscal policy, how is the MDG challenge to be tackled? A zealous anti-inflation policy will be socially counterproductive. The answer may lie in adopting monetary policy, which implies Timor-Leste having its own currency. This might resolve the trade-off between macroeconomic stability and poverty reduction. Subsequently, greater coordination of expansionary monetary and fiscal policies with exchange rate policy is required.

Fiscal policy could be used to scale-up public investment in rural infrastructure and increasing productive capacity to stimulate food supply as well as crowd-in private investment. In the short run, labour-intensive public work programmes can be effective. Monetary policy, through interest rates, can be used to crowd in private investment by improving access to credit. While the financial sector matures, the central bank could play the role of a development bank and an intermediary of last resort. A managed exchange rate could be used as an inflationary anchor and to create incentives for diversifying into non-oil activities. A coordinated macroeconomic policy would tackle the inflationary pressures without resorting to contractionary measures.

Note:

1. The government introduced coins that have equivalent values to US cents. The coins are issued for convenience rather than for their impact on monetary variables.

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Government of the Democratic Republic of Timor-Leste and United Nations (2009). The Millennium Development Goals, Timor-Leste, MDG Report. UNDP Timor-Leste website, <*http://www.tl.undp.org/MDGs/MDGs_File/UNDP_MDGReport_Final.pdf*>.

One Pager number 93
Published: August, 2008
Available at: <http://www.ipc-undp.org/pub/IPCOnePager93.pdf>

Conservation and Ecotourism in Brazil and Mexico: **The Development Impact**

by David Ivan Fleischer, International Policy Centre for Inclusive Growth

Conservation projects alter local productive modes and have an impact on livelihoods. For example, sea turtle conservation projects affect fishing communities through hunting restrictions. It is not painless for communities to improve fishing technology in order to prevent the accidental capture of sea turtles. The inability to adapt to environmental requirements forces fishermen to abandon traditional livelihoods. A combination of environmental conservation and ecotourism development can provide the solution.

Sea turtle hunting has been banned in most Latin American countries. Brazil banned it in 1980 and Mexico in 1992. Before the bans, older fishermen in Mazunte, Mexico, and Praia do Forte, Brazil, taught younger ones the traditional knowledge of: (i) capturing turtles at sea; (ii) collecting eggs at local beaches; (iii) slaughtering adult turtles; and (iv) preparing meals from turtle meat or eggs. As with any traditional knowledge, this one demanded learning and practice before the fishermen became fully adept. The ban on sea turtle hunting meant cessation of a generational activity.

Then came the conservation and ecotourism projects: the Centro Mexicano de la Tortuga and Brazil's Projeto Tamar. These were implemented to recover the sea turtle population through education programmes and alternative livelihoods. Fishing boats with nets were replaced by those with sea turtle exclusion systems. Fishermen were hired to help find sea turtle nests and transfer them to incubation areas. In helping to recover nests, the fishermen began to earn a living. As a result, the projects gained important conservation allies.

But did the conservation and ecotourism projects reduce poverty? In the case of the communities in Mazunte and Praia do Forte, the answer is yes. The table shows changes in key social indicators in both towns by comparing the periods before and after the conservation and ecotourism projects. Before the projects, households had virtually no potable water or electricity, nor access to health facilities and schools. The projects significantly improved household welfare.

Average family income increased by 17 per cent in Mazunte and by more than twofold in Praia do Forte. Universal access to piped water was achieved in Mazunte. A hospital was opened in Praia do Forte. Three schools were opened in each town. Food and nutritional intake also improved because of the availability of more options and variety. Before the conservation projects, the main staple food in both towns included sea turtles, corn, rice and beans. Beef, fruits, poultry and vegetables are now commonly consumed and form the basis of a modern diet.

Changes in Key Social and Economic Indicators

Mazunte, Mexico (population, 2,000)

	Family income	Piped water	Electricity	Health	Schools
Before conservation (1999)	US$600	0 homes	0 homes	0	0
After conservation (2008)	US$700	1,000 homes (100%)	1,000 homes (100%)	1 clinic	3 (K-12)

Mazunte, Mexico (population, 2,000)

	Family income	Piped water & sewage	Electricity	Health	Schools
Before conservation(1999)	US$300	0 homes	0 homes	0	0
After conservation (2007)	US$900	1,900 homes (95%)	2,000 homes (100%)	1 hospital	3 (K-12)

Source: Data collected by author; and Comisión Federal de Electricidad (CFE) and Department of the Municipality of Santa Maria Tonameca, for Mazunte; and Companhia de Eletricidade da Bahia (Coelba) and Empresa de Agua e Saneamento da Bahia (Embasa), for Praia do Forte.

The value of rentable spaces and land plots increased significantly.[1] For example, a commercial space of 60m2 in Praia do Forte could be rented for about US$600 in 1999, whereas by 2007 the same space would rent for US$3,000. In Mazunte, a 2,000m2 plot of land would sell for about US$4,000 in 1999, while by 2008 a lot of the same size would sell for about US$21,000 (not in table). Members of the communities have also integrated themselves into ecotourism by offering lodging, dining and entertainment.

Before the conservation and ecotourism projects, both Mazunte and Praia do Forte were geographically isolated and they relied on sea turtle hunting and the cultivation of one or two crops. The experience of these towns shows that well designed initiatives can reduce poverty. Fishing is less profitable now, but it no longer threatens sea turtles and still guarantees additional income and food supplements. Through training and capacity-building, local communities were able to move from a subsistence-based economy to a successful, service- oriented one.

Note:

1. Reliable data for land price and rent are only available since 2000, as the ecotourism boom in both towns only started around 1999.

Reference:

Fleischer, David I. R. (2009). 'Ecotourism, Sea Turtles and Livelihoods: Adaptation and Resistance to Development and Conservation in Mexico and Brazil'. Dissertation, University at Albany, Department of Anthropology.

One Pager number 94
Published: September, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager94.pdf>

The Global Economic Crisis Hampers Human Development. **How?**

by Degol Hailu,
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For developing economies the current crisis means reduced demand for their exports, a decline in capital inflows and lower income from tourism. This One Pager discusses the transmission of the crisis from changes in aggregate variables to its impact on progress towards human development. The focus is on African economies.

According to the International Monetary Fund (IMF), in 2008 the volume of world trade declined by 3.9 per cent over the figure for 2007. It is forecast to decline by a further 7.7 per cent in 2009. This fall in demand entails a cost of about US$251 billion to African economies. The loss comes from drops in commodity prices. Between April and December 2008, the price of beverages and food fell by 24 per cent. Prices for minerals, ores and metals dropped by 51 per cent. Prices of vegetable oil seeds fell by 47 per cent. Prices of agricultural raw materials dropped by 35 per cent. Crude oil prices plunged from a high of US$127 per barrel in July 2008 to US$39.93 in January 2009. Ten countries in the region rely on oil exports as a major source of income.

For the region as a whole, foreign direct investment as a share of national income is predicted to drop by 16 per cent in 2009 from its 2007 value. The World Bank has reported that remittances to Africa will fall by 8.3 per cent in 2009. Early reports indicate that Ireland, Italy and Latvia have already cut their foreign aid by 10 per cent, 65 per cent and 100 per cent, respectively. Africa's share of tourist visits declined from 20 per cent of total world visits in 2007 to 4 per cent in 2008.

How, then, does the crisis affect human development outcomes? The UN estimates that up to 103 million more people will fall into poverty or fail to escape poverty because of the crisis. According to the International Labour Organisation (ILO), the unemployment rate is expected to increase by 0.6 per cent in 2009. About 45,000 jobs have already been lost in South Africa. In the Democratic Republic of Congo, 100,000 workers were made redundant because of smelter closures. In the Central African Republic, half of the workforce has been laid off from the Société d'Exploitation Forestière en Centrafrique (SEFCA). In the Zambian mining sector, 6,000 people lost their jobs in November 2008.

Conceição et al. (2009, p. 5) note that "less skilled and poorer workers are often more likely to be laid off at the beginning of an economic downturn. Lack of education and transferrable skills implies that the group is likely to be the last to get employed after the economy bounces back." Formal sector job losses also increase the informalisation of labour. Job safety and legal protection are compromised. Excess labour supply caused by reverse migration is likely to worsen poverty through added unemployment in the returnees' home towns and villages, further lowering wage rates.

A fall in remittances jeopardises the capability of households, which use the funds as effective social insurance and to smooth out income and consumption levels. Families may sell their productive assets such as land, livestock and beasts of burden, making them even more vulnerable and destitute.

Reduced household consumption is likely to increase malnutrition, especially among children. This hinders child growth, affecting learning and cognitive abilities. The World Bank has reported that infant deaths in developing countries may be 200,000 to 400,000 per year higher on average between 2009 and the Millennium Development Goal (MDG) target year of 2015. Friedman and Schady (2009) estimate that the current crisis will lead to between 30,000 and 50,000 excess infant deaths.

Because of income shocks, poor households may withdraw their children (often girls) from school so that they can complement household income by working in the informal labour market. This perpetuates the intergenerational transmission of poverty and reduces future income during adulthood.

The crisis can worsen income distribution. It is likely that high-income groups can withstand shocks by drawing down savings or by using banking facilities. Low-income groups often lack savings or access to financial services in order to achieve inter-temporal adjustments in their income.

What should be the immediate response? The crisis disproportionately affects the poor, who have weak coping mechanisms in the first place. Subsidies that protect vital consumption items such as food and cooking fuel are useful anti-crisis measures. Existing social assistance programmes such as labour-intensive public works and cash transfers can be scaled-up to protect jobs and incomes. Social and infrastructure spending needs to be ring-fenced. These measures require financing and policy space to adopt counter-cyclical macroeconomic policies.

What should be the long-term response? National policies and institutions determine the course of development. But the vulnerability of economies to crisis is largely determined by their position in the production and distribution hierarchy of the global economy. What is needed is a strategy for the transformation of economic and social structures.

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Conceição, Pedro, Namsuk Kim and Yanchun Zhang (2009). "Economic Shocks and Human Development: A Review of Empirical Findings". UNDP/ODS Working Paper. New York, United Nations Development Programme.

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One Pager number 95
Published: September, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager95.pdf>

Do CCTs Lessen the Impact of the Current Economic Crisis? **Yes, but...**

by Fábio Veras Soares,
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The recent financial and economic crisis has sparked a debate on whether conditional cash transfer (CCT) programmes make families less vulnerable to that crisis. This link between the crisis and CCTs was made because countries like Brazil, which have large CCT programmes, were enduring the impacts better than most others.

CCTs can help families to sustain their food consumption levels. That in turn reduces any negative impact on the nutritional intake of children; it also keeps them in school and away from work. If the spillover effects documented in the literature are to be believed, the flow of income into communities can also help alleviate the fall in overall economic activity. CCTs that can expand during a crisis help to mitigate the effects of the crisis. They work as local-level automatic stabilizers, similar to how unemployment benefits do in the developed world. They can both avert the short-term impact of the crisis and attenuate its long-term negative effects on human development outcomes.

Nonetheless, it is one thing to say that countries with CCT-like programmes are sheltering the more vulnerable from the worst consequences of the crisis, and another to recommend that CCT programmes be designed and implemented during a crisis. It is not easy to design and implement CCTs. Several steps are involved, political will is required, and funds must be committed. In Brazil, the number of beneficiaries of Bolsa Família has increased, as has the value of the benefit as an anti-crisis measure. In Mexico, a new stipend designed to compensate for the rise in food prices has been included into the grant components of Oportunidades. These changes were only possible because the programmes are well established and have been working smoothly for some time.

It can be even more challenging to implement CCTs in low-income countries. In most such programmes in Africa, the conditionalities have been much less strict than in some Latin American countries, and community targeting has been widely used. It can be costly in terms of funds and time to establish targeting and monitoring mechanisms. Moreover, it might not be feasible to provide financing during a crisis period, when government revenues are falling. Authorities should be cautious about relying on donor funds to implement these programmes, since sustainability becomes an issue.

Even assuming that it is possible to design and implement CCTs fairly quickly, a well-crafted strategy has to be thought through with commitment from both donors and recipient countries. This is particularly true as regards the question of how to phase-in and phase-out external aid, so that programmes do not lose political support and face being discontinued.

Policies and programmes can only be effective if they are implemented under a sustainable social protection strategy. Such a strategy should enable better coordination among programmes, between the central and local levels, and among the different international players in order to avoid duplication of effort and waste of resources.

In relatively successful cases, such as Chile Solidario and Bolsa Família, policy integration has been facilitated by the presence of registries of potential beneficiaries for CCTs and other social programmes. Such databases enable the authorities to build an array of indicators on families' socioeconomic conditions. This makes them powerful tools in mapping the different needs of various communities, and they could be used to guide other policies. They can be useful not only to line ministers whose work is closely related to the conditionalities or complimentary programmes, but also to providers of basic utilities such as water and electricity. Registries enhance monitoring of the poorest families' access to social services and infrastructure in a more calibrated way than household surveys. The latter, though they are nationally representative, are often based on small samples that do not facilitate sound analysis for local-level interventions. This knowledge base allows rapid crisis response when programmes may need to expand in order to cover a larger proportion of those that fall into poverty.

Some CCTs have proven strong enough to avoid becoming isolated elements of a minimal saf ety net and have developed into more inclusive social policies (Bastagli, 2009). They have reached that stage through trial and error that is finally paying off, though many challenges still lie ahead.

In sum, CCTs are not panaceas to strengthen the (emergency) resilience of families and states. But they have features that can be used to lessen the impact of a crisis as long as they are integrated in a broader social protection strategy whose goal is not solely to work as a minimal and temporary safety net.

Reference:

Bastagli, Francesca (2009) "From Social Safety Net to Social Policy? The Role of Conditional Cash Transfers in Welfare State Development in Latin America" (forthcoming). IPC-IG Working Paper. Brasilia, International Policy Centre for Inclusive Growth.

One Pager number 96
Published: September, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager96.pdf>

Do Poorer Countries Have Less Capacity for Redistribution?

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The government of a rich country will be disinclined to give its aid to a country that has internal capacity to tackle poverty through redistribution from people at a similar standard of living to taxpayers in that rich country. Yet we do not have tools for measuring the capacity for redistribution that reflect this property. Indeed, past measures imply heavy tax burdens on people who would be considered poor in rich countries.

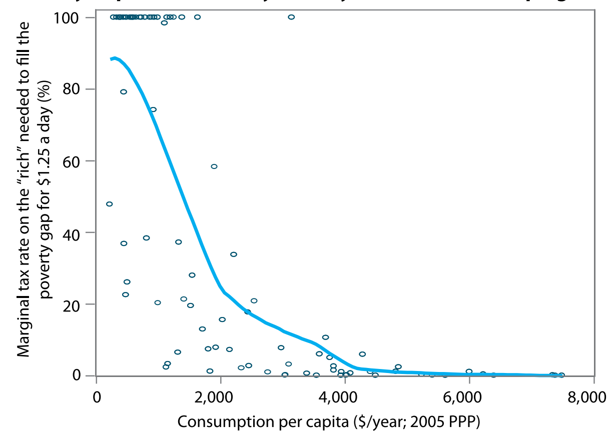
The issue of country capacity for redistribution also arises in discussions of development policy within developing countries. It is often argued that "sustained poverty reduction is impossible without sustained growth." To accept this claim one must essentially reject its corollary: "sustained poverty reduction is impossible through income redistribution." Is that right?

New and better measures of the capacity for redistribution can be devised and implemented with currently available data (Ravallion, 2009). These measures make a more appealing assumption about how the required tax burden is to be allocated amongst those living above the poverty line: the burden is set to zero until one reaches a standard of living that would not constitute poverty in a representative rich country, and then rises as a share of income in excess of the rich-country line.

On implementing these measures using data for 90 developing countries, I find that developing countries fall into two distinct groups. The first appears to have little or no scope for making a serious impact on the problem of extreme absolute poverty through internal redistribution from those who are not poor by US standards. The second group appears to have far more scope for such redistribution. Most of the poorest countries in terms of mean consumption fall into the first group. The marginal tax rates (MTRs) needed to fill the poverty gap for the international poverty line of $1.25 a day are clearly prohibitive (marginal tax rates of over 50 per cent and many of 100 per cent or higher) for the majority of countries with consumption per capita under $2,000 per year at 2005 purchasing power parity. Even covering half the poverty gap would require prohibitive MTRs in the majority of poor countries. Yet amongst better-off developing countries—over $4,000 per year (say)—the marginal tax rates needed for significant pro-poor redistribution are actually very small—less than 1 per cent on average, and under 6 per cent in all cases (see Figure.)

Basic-income schemes (guaranteeing the poverty-line income to everyone, whether poor or not) financed by progressive income taxes would also require prohibitive marginal tax rates in the poorest half of developing countries. If the tax burden is confined to those who are not poor by developed-country standards, providing a basic income of $1.25 a day would call for marginal tax rates of 100 per cent or more for three-quarters of countries. Even for middle-income developing countries, this type of redistribution only starts to look feasible in terms of the implied marginal tax rates if one allows for a basic income appreciably less than $1.25 a day and/or significant tax burdens on the middle class.

MTR on those Living above the US Poverty Line Needed to Cover the Poverty Gap for $1.25 a Day Poverty Line for 90 Developing Countries



The emphasis often given to the role of economic growth for poverty reduction in poor countries can claim support from this new evidence on the capacity for redistribution in poor countries. The poorest countries appear to have weak capacity for attacking poverty through income redistribution, given the sheer weight of poverty and thinness of the rich strata in their starting distribution. But with sufficient economic growth the tax rates on the rich required for covering the poverty gap start to fall rapidly. Thus it makes sense that the poorest countries focus on growth, and rely more on aid, but that redistribution starts to emerge as a viable strategy for fighting poverty at higher income levels.

These new measures and data suggest an affirmative answer to the question posed in the title of this One Pager. However, that support comes with qualifications. The capacity for redistribution varies amongst countries at any given level of mean income. And the variance is highest amongst the poorest countries; there are even a few poor countries where a substantial dent on poverty could be made with seemingly light taxation of the rich. These differences bear little relationship to a standard measure of inequality, but reflect the deeper parameters of the distribution of income in each country that have generated lower poverty to start with.

Reference:

Ravallion, Martin (2009) "Do Poorer Countries have less Capacity for Redistribution?" Policy Research Working Paper 5046, World Bank (Washington, DC).<http://econ.worldbank.org/docsearch>.

One Pager number 97
Published: September, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager97.pdf>

Do CCT Programmes Have a Pro-Poor Spillover Effect?

by Christian Lehmann,
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Conditional Cash Transfer programmes (CCTs), such as Progresa in Mexico or Bolsa Família in Brazil, have been compared to a "magic golden bullet in development". A plethora of rigorous evaluations of such programmes points to a significant increase in food consumption among cash-recipient households. A topic that has not received much attention yet is the impact of cash transfer programmes on the food consumption of households that do not receive the transfer (programme-ineligible households) but that are in the same village as cash recipients.

Why should we care about programme-ineligible households? In many cases, funding for a CCT is limited. Hence governments and non-governmental organisations often allocate transfers to the most vulnerable groups of a population. But the vast majority of those deemed ineligible for the programme are far from what we would consider "well-off". For example, the monetary value of ineligibles' daily per capita food consumption in Mexico's Progresa was less than US$1.0 when the programme started in 1997. Poverty therefore persists even among ineligible households. If a CCT has a positive food consumption spillover on ineligible households, the overall impact on poverty is much greater than previously recorded.

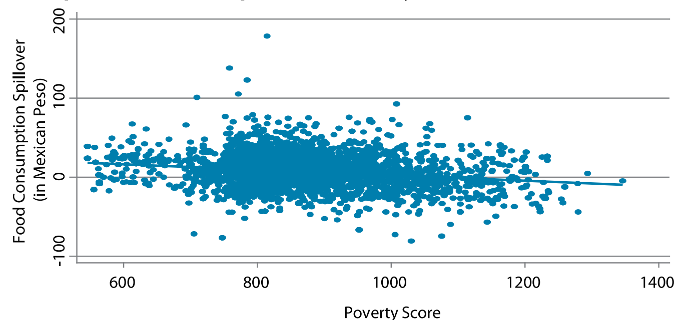
Why would programme-ineligible households increase their food consumption, even though they do not receive the cash transfer? First, transfers increase the recipient households' demand for goods and services. This in turn changes prices and labour demand in the community. If a programme-ineligible individual is a labourer, the increase in demand for goods and services leads to more employment opportunities, and thus additional income. If programme-ineligible households are engaged in small business activities they benefit from increasing prices (higher profits).

Second, the liquidity induced by a CCT improves credit markets (Angelucci and De Giorgi, 2009). The consequent increase in access to loans can be used to scale-up domestic agriculture, livestock production and other small business activities.

Third, a CCT may lead to increases in informal food gifts from programme participants to programme-ineligible households. In the anthropology literature, this phenomenon is often referred to as "solidarity". The economic literature emphasises the importance of in-kind sharing as a means of informal insurance against shocks (illness, crop failures and so on). Households have an incentive to share food with other households in order to receive help when they themselves fall into precarious situations (the principle of "reciprocity"). These and other important channels through which a CCT affects ineligibles' consumption are discussed in depth in Lehmann (forthcoming).

Is the food consumption spillover pro-poor? Using data from Mexico's Progresa we analyse if poorer ineligible households or the "better-off" ineligible households benefit from the food consumption spillover. We compare the average monthly per capita food consumption of ineligible households in villages where households receive cash transfers to that of ineligible households in villages where there is no CCT. Our results suggest that the increase in food consumption is greater for poorer ineligible households than for "better-off" ineligible households. In general, the poorer the village as a whole, the greater the spillover on ineligible households. The food consumption spillover, therefore, benefits the very poor.

Per Capita Food Consumption and Poverty



The figure visualises the relationship between the increase in ineligible households' monthly per capita food consumption and their level of pre-programme poverty. The latter is represented by a wealth multidimensional index. The lower the index, the higher the level of poverty. Each dot represents the increase in food consumption for a programme-ineligible household in our sample (i.e., non-recipients of transfers) due to the existence of a cash transfer programme in the village. The downward-sloping line shows the trend. We see that poorer ineligible households benefit more from the existence of a CCT in their village. Their increase in food consumption is, on average, higher than that of "better-off" ineligible households in the same village.

What are the implications? Evaluations of CCTs that focus entirely on programme participants do not capture the overall community impact on poverty. Poorer, programme-ineligible households indirectly benefit from the programme through higher food consumption, and thus the impact on poverty is greater than previously recorded.

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One Pager number 98
Published: September, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager98.pdf>

Raindrops for Education: How To Improve Water Access in Schools?

by Acácio Lourete, Christian Lehmann and Raquel Tsukada
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In many countries, efforts to achieve the Millennium Development Goal (MDG) of universal primary education have led to a rise in the number of schools built. The fact that more children may have the opportunity to attend school is a necessary but not sufficient condition to guarantee proper primary education. Complementary inputs such as the number and quality of teachers are also important. Here we focus on the adequate provision of water as one of the key determinants for pupils to acquire a proper education that meets international standards.

A major obstacle to learning is the lack of physical capacity to absorb what is being taught. Without a minimum calorie intake, the development of cognitive abilities is impaired. And a high incidence of poverty is usually accompanied by striking levels of poor nutrition: in developing countries, about 32.5 per cent of children are malnourished. Malnutrition also contributes to the 10.9 million child deaths each year globally. Apart from these dysfunctions, other symptoms are more clearly evident. After long walks to school many children arrive hungry and thirsty, with little energy left to pay attention.

A promising complementary infrastructure to school construction is Rainwater Harvesting (RWH). This is a low-cost technology to catch and store runoff rainwater. Sufficient rooftop area in schools allows a large amount of water to be collected during monsoon seasons, diverted from gutters into a closed storage tanks (also called cisterns).

How can RWH contribute directly to the attainment of universal primary education? First, RWH increases the effective time children spend in classrooms. In many primary schools in developing countries, particularly in remote arid and semi-arid zones, pupils must bring water to prepare school meals or to drink. These children spend a significant proportion of their time collecting water, often from distant sources. RWH reduces the demand for water from such sources. The time children save is then spent in a greater number of effective classroom hours. There is also a gender consideration: schoolgirls usually skip classes if adequate sanitation facilities and water are not provided. The annual cost for girls is estimated to be equivalent to a full month of lost classes.

Second, RWH improves children's health. Studies have shown that hand washing with soap may halve the incidence of diarrhoea, the second leading cause of under-five child mortality (Curtis and Cairncross, 2003). Bacterial diseases are frequent corollaries. A third of the 1.2 billion people infected or at risk of being infected by soil-transmitted helminthiasis are children. Rainwater, when properly stored, removes the risk of infection by water-borne and water-washed diseases. If potable water is made available, kitchen gardens can be cultivated. The fruits and vegetables that can be grown potentially increase pupils' calorific intake, directly improving their learning capacity and general health.

Third, RWH relaxes the budget constraint on schools. For instance, if a school buys water to satisfy a certain share of its demand, RWH reduces water bills. The money saved can be invested in teacher salaries and other infrastructure improvements.

Finally, RWH at the school level has positive spillovers. Programmes in India have shown that the construction of rainwater technology, especially when community members are stakeholders (either co-financing the cistern or taking charge of its equitable usage) has a knowledge spillover on the community. Children are often "ambassadors" of knowledge for their households. They easily adopt new practices and thus are open to learning about water management, the importance of hygiene, the consequences of consumption from unsafe water sources, and the advantages of having a cistern at their own home.

RWH is a promising complementary activity and is relatively accessible at little cost (the average material cost for a 16m3 ferrocement cistern in developing countries is about US$950). But its take-up remains a challenge to budget-constrained schools. Innovative and community-driven financing strategies, such as "merry-go-around" schemes, are needed to increase rainwater harvesting practices (see Lehmann and Tsukada, forthcoming).

Hence, in order to keep making steady progress towards the education MDGs, more than physical shelters need to be built. Students who are likely to drop out of school require additional incentives to attend classes. Water security seems to be a strong incentive because of its several associated benefits. Where access to utility provision is somewhat scant, RWH provides a cheap, promising and environmental-friendly solution. Funding and the exchange of best practices for upgrading the technology are what seem to be missing.

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One Pager number 99
Published: September, 2009
Available at: <http://www.ipc-undp.org/pub/IPCOnePager99.pdf>

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Printed in Brazil

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ISBN 858820104-6
9 788588 201040