

Reducing Poverty in Developing Countries —Some Basic Principles for Policy Design†

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International interest in poverty and welfare in developing countries has grown visibly in the past decade — as has research on these issues.¹ This growth is fueled in large part by a realization that world poverty continues to defeat the best efforts to reduce it. Over the past three decades neither direct poverty alleviation efforts nor economic growth has succeeded in stemming the rising numbers of poor in many countries. Progress has most certainly been made, but there is now a clear sense in the development community that “business as usual” is not going to better the lot of the world’s poor any time soon. This is, therefore, an opportune time to step back and review what we have learned from past attempts to reduce poverty.

The following sections take a pragmatic, policy-oriented look at efforts to reduce poverty and improve the living conditions of the poor. The focus is on extracting practical lessons from experiences of both developed and developing countries. The paper’s basic message is that policy-makers and researchers concerned with poverty programmes would do well to pay attention to what already is known:

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†The comments from the second discussant have not been received.

¹As examples of recent research on poverty and related issues see the World Bank’s Living Standards Measurement Study (LSMS) series; Cornia, Giovanni Andrea and others (eds) (1987) *Adjustment with a Human Face*. Oxford: Clarendon Press; Paul Glewwe and Jacques van der Gaag (1988) *Confronting Poverty in Developing Countries: Definitions, Information, and Policies*. Washington, D. C.: The World Bank. (LSMS Working Papers No. 48) John Iliffe (1987) *The African Poor*. Cambridge: Cambridge University Press; Michael Lipton (1983) *Demography and Poverty*. Washington, D. C.: The World Bank. (World Bank Staff Working Papers No. 623); Amartya Sen (1981) *Poverty and Famines*. Oxford: Clarendon Press; Dasputa Sugarta and others (eds) (1985) *Towards a Post-development Era: Essays in Poverty, Welfare and Development*. Delhi: Mittal; and the forthcoming 1990 *World Development Report* of the World Bank on poverty.

- About the consequences of bad economic policy on the poor;
- About the difficulty of targeting programmes specifically and only to the poor and the dangers of leakages to the non-poor;
- About institutional and infrastructural constraints and the danger of mounting overly ambitious programmes;
- About the difficulty – and cost – of getting income-generating programmes to the people most in need; and
- And about the need for simple, realistic, and persistent efforts to reach the poor with programmes that go beyond increasing their consumption in the short run to increasing their incomes in the long run.

The paper begins with a look at a currently topical issue: the effects of macro-economic stabilization and adjustment programmes on the poor. I start with this issue because it is important to understand the overall policy context within which poverty policies are operating, and because we need some sense of whether these programmes are going to make poverty reduction goals more or less difficult to achieve in the future.

The second section turns to programmes designed specifically for the poor. For such programmes, I consider the role that targeting can – and cannot – play in the design of efficient poverty-reduction policies, and then look at the distinction between programmes that reduce poverty through consumption transfers and those that do so through income-generating investments in the poor. The third section draws lessons from developed countries on the problems of measuring poverty, the difficulties in targeting poverty programmes, and the need to understand the behaviour of both the poor and the non-poor constituencies for poverty programmes. The fourth section turns to the experience of developing countries for lessons on the institutional and infrastructural limits to poverty programmes and on the leakages, particularly from transfer programmes, to non-poor beneficiaries. I conclude by summarizing what these lessons mean for the design of policies to improve the welfare of the poor.

I. MACROECONOMIC POLICIES AND THE POOR

While experience has shown that growth alone is not sufficient to improve the welfare of all the poor, experience has also shown that growth is absolutely essential to reducing poverty. A bad macroeconomic environment that reduces a country's ability to grow is without question the most serious danger to the poor. Further, it hurts the poor regardless of the government's social strategy. Tanzania and Sri Lanka, for example, were surely pro-poor in their overall policy stance. Yet unsustainable deficits, inefficient public sectors, and a myriad of market distortions in

the end made conditions worse for everyone, but especially for the poor.² The message is clear: no matter how well intentioned, policies that try to reduce poverty and improve welfare through fiscally unsustainable programmes inevitably harm those they are meant to help.

Understanding the causes of recent declines in welfare among the poor requires understanding of the distinction between policies aimed at stabilization and policies aimed at adjustment.³ Stabilization policies to dampen inflation from unsustainable fiscal deficits are inevitable – and the longer they are delayed, the more they hurt both the poor and the non-poor. Adjustment policies, by contrast, are intended to move economies from low to higher growth in the long run. Highly desirable but not necessarily inevitable, such policies can benefit the poor as much as the non-poor or even more. The distinction between stabilization and adjustment is blurred, however, because the term “adjustment” is often applied to both types of programmes.

It is easy to misread the message from recent efforts by many developing countries to promote sound macroeconomic management. One hears much these days about the costs the poor bear as economies shift from bad to good macroeconomic policies. UNICEF's famous treatise on Adjustment with a Human Face Cornia, Jolly, and Stewart (1987) suggests that adjustment policies adversely affect the well-being of the poor. I believe that the lesson from the 1980s is a little different.⁴ The poor are being hurt, but the culprit is not adjustment. Quite the contrary, the principal cause of declining living conditions for the poor in most countries is delayed adjustment.

The Inevitability of Stabilization

Recent work at the World Bank and elsewhere demonstrates clearly that the economic ills besetting many developing countries have their origins in stabilization or, more accurately, its absence.⁵ The need for stabilization has as its root cause

² On Tanzania, see Goran Hyden (1980) *Beyond Ujamaa in Tanzania: Underdevelopment and an Uncaptured Peasantry*. Berkeley; Sisira and Premachandra Athukorala (1987) *Macroeconomic Policies, Crisis and Growth in the Long Run: Sri Lanka*. Colombo: School of Economics, La Trobe University.

³ For a discussion, see Bela A. Balassa (1989) A Conceptual Framework for Adjustment Policies. Washington, D. C.: The World Bank. (Policy, Planning and Research Working Papers No. 139)

⁴ For a critique of Cornia's perspective, see Samuel Preston (1986) Review of Richard Jolly and Giovanni Andrea Cornia (eds) *The Impact of World Recession on Children*. *Journal of Development Economics*.

⁵ Two World Bank-sponsored comparative studies – one of the interrelationships among poverty, equity, and growth (The Political Economy of Poverty, Equity and Growth, RPO 673-73), and the other on macroeconomic policy during times of crisis (Macroeconomic Policies, Crisis and Growth in the Long Run, RPO 673-99) – both find that while the symptoms may differ, the underlying cause of economic crisis is often an unsustainable fiscal deficit.

bad macroeconomic management in the form of unsustainable deficits that lead to inflation. Price instability — inflation — is, of course, the main visible consequence of unsustainable internal and external imbalances. Stabilization programmes are designed to bring fiscal responsibility to the management of an economy by reducing fiscal deficits to sustainable levels.⁶

Although inflation is a complex phenomenon, and stopping it even more complex, it remains essentially a matter of too many dollars or rupees chasing too few goods and services. Curing inflation — stabilizing — requires one of two changes: restricting demand for goods and services, usually by cutting back on public sector activities, or increasing the flow of goods and services available for investment or consumption in the economy. In practice, demand-reducing policies have dominated, and it is these policies that have the greatest potential negative effect on the poor.

Fiscal deficits are created when governments spend more than they take in from taxes, from revenues from public sector activities, and from market borrowing. The gap between public expenditures and public receipts is covered back into balance, and thereby reduce inflation, governments must spend less (or, far rarer, raise more revenue). This reduction in government spending has two effects. First, where the public sector is a large part of the economy, as it is in most developing countries, reducing government expenditures tends to move the economy into recession. Wages and employment decline, and the poor are affected by “negative trickle-down”. Second, reducing government expenditures may reduce social services, which may in turn reduce the welfare of the poor.⁷

The poor suffer under stabilization because government services and the economic growth decline. The proximate cause of the decline in welfare among the poor may be the stabilization programme, but the need to stabilize grows out of past macroeconomic mismanagement. Such fine distinctions matter not at all to the poor, but they are important in drawing policy implications from the historical record: The only way to avoid the welfare-reducing effects of stabilization pro-

⁶A sustainable deficit is not necessarily a zero deficit. Many countries maintain permanent fiscal and trade deficits, some of them large, with no apparent short-term negative consequences. While the long-run consequences of these policies are much debated, it is clear that countries with good credit status — the United States, for example — can sustain large fiscal and trade deficits for considerable periods and still maintain reasonable price stability.

⁷I say “may” because several studies show that this story is only partly true. Welfare-related services provided by the public sector do not always benefit the poor to anything approaching planned levels. Often the principal beneficiaries of government-provided services are the working middle class — or lower middle class — who are formally not among the poor but who are politically visible and vocal. So stabilization-induced cuts in the provision of government services often do not affect the poor because they are seldom the primary beneficiaries of those services.

grammes is to keep one's fiscal house in order in the first place.

The Desirability of Adjustment

Although stabilization can be (and often is) postponed, in the final accounting governments, like the rest of us, must live within their means. However, in attempting to live beyond their means, countries often turn to policies that provide short-term relief but introduce distortions into the economy that reduce growth below its potential. Economic distortions, whether the result of inappropriate stabilization policies or not, also hurt the poor.

For example, it is now fairly widely held that growth strategies in many developing countries have been more capital-intensive than is economically defensible.⁸ Capital-intensive growth policies come about when the international community provides more lending than countries can reasonably absorb (such diverse examples as Brazil and Tanzania come immediately to mind) and when governments keep real interest rates artificially low. Making capital cheap relative to labour has a direct and negative consequence on the poor who, after all, have very little capital but a good deal of labour.

Having an overly capital-intensive development strategy is an adjustment problem, not a stabilization problem.⁹ It produces an economy that operates less efficiently than it might otherwise because economic agents, including the government, are not responding to true economic prices and incentives. Such economywide distortions come in many forms, most of them inherently anti-poor.¹⁰ Thus, while stabilization policies may hurt the poor because they reduce growth and government spending, structural adjustment programmes that remove distortions and make economies function more efficiently are often pro-poor.

There is theoretical and empirical evidence that adjustment is good for the poor.¹¹ In the long term, adjustment moves the economy onto a higher long-term

⁸ The World Bank's forthcoming 1990 *World Development Report* on poverty makes this point very clearly.

⁹ The cause of the domestic distortion in the capital market may, of course, be a lack of stabilization. Inflation drives real interest rates down — even to negative levels — when nominal rates are fixed, as they are in most developing countries.

¹⁰ The classic example is the suppression of agricultural prices, which serves as an implicit tax on export crops and a palliative for politically powerful urban consumers at the expense of rural areas where most poor reside. Similarly, credit and fertilizer subsidies in nearly every country in which they have been tried serve larger, better-off farmers, not the poor.

¹¹ See, for example, Martin Ravallion and Monika Huppi (1989) *Poverty and Undernutrition in Indonesia during the 1980s*. Washington, D. C.: The World Bank. (Policy, Planning and Research Working Papers No. 286); John Araka and others (1990) *Farmers Take on Structural Adjustment*. *African Farmer* 3: forthcoming. See also Kionel Demery and Tony Addison (1987) *The Alleviation of Poverty Under Structural Adjustment*. Washington, D. C.: The World Bank.

growth path, which may be more labour-intensive and agriculture-oriented than previous paths. Several studies have also demonstrated that even the short-term effects on the poor may be beneficial. Studies of Peru and the Ivory Coast show that removing price and other distortions helps the poor in general.¹² Any adjustment programme will involve winners and losers, but often the losers are not the poor.

Ironically, stabilization and adjustment policies would probably be more sustainable and politically palatable if the poor were the main losers. In fact, the history of unrest following the implementation of stabilization or adjustment programmes demonstrates graphically that the urban middle class, very much the non-poor (although by no means necessarily well-to-do), are the big losers. This is a politically powerful group, and its opposition has brought more than a few stabilization and adjustment programmes to a halt.

The importance for the poor of good macroeconomic policies cannot be overstated. Yet, history has made it clear that good economic policies alone may move the poor out of poverty only very slowly. Therefore I turn now from the macroeconomic world of stabilization and adjustment to policies and programmes directed specifically at the poor.

II. POLICIES FOR REDUCING POVERTY DIRECTLY: WHO? WHEN? HOW?

The best poverty-reduction programme is one that does precisely what it is intended to do, that is administratively efficient, and that has no or few economy-wide distortions. A programme that does exactly what it is meant to do is said to be perfectly targeted.¹³ An administratively efficient policy is one that delivers a dollar or rupee of resources to the poor at minimum cost. A policy that minimizes distortions is one which has as little effect as possible on consumption and produc-

¹² Paul Glewwe and Dennis de Tray (Forthcoming) *The Poor in Latin America During Adjustment: A Case Study of Brazil. Economic Development and Cultural Change*; Paul Glewwe and Dennis de Tray (Forthcoming) *The Poor During Structural Adjustment: A Case Study of the Cote d'Ivoire*. Forthcoming Proceedings volume, Division of Nutritional Sciences, Cornell University.

¹³ On the general principles of targeting see Timothy Besley and Ravi Kanbur (1988) *The Principles of Targeting*. Coventry, England: Development Economics Research Centre, University of Warwick. (Discussion Papers No. 85); Jean Dreze and others (1989) *Identifying and Reaching the Poor: Principles and Some Examples from a North Indian Village*. Background paper for the *World Development Report*, 1990. Processed; Paul Glewwe (1989) *Targeting Assistance to the Poor Using Household Survey Data*. Washington, D. C.: The World Bank; and Carolyn Winter (1989) *Target Efficiency in Health and Education: Developing Country Experience*. Public Economics Division, Country Economics Department. Washington, D. C.: The World Bank. Processed.

tion patterns outside those directly singled out for change. No policy achieves these objectives fully. Further, the more a policy excels in achieving one of these objectives, the more difficult it often is to achieve the other two. These criteria remain, however, the standards for judging poverty policies and programmes.

The Limits of Targeting

The issue of targeting is at the core of many recent efforts to improve the lot of the poor. In these times of increasing fiscal austerity and declining public sector budgets, targeted welfare programmes are viewed as a panacea — more poverty reduction for less money. Although targeting is essential to the design of economically viable poverty-reduction policies, it is equally important to recognize its limitations.

The extremes in the debate over the efficacy of targeting run something like the following.¹⁴ Proponents of targeting offer it as a solution to unsustainably expensive public sector transfer programmes that serve as many non-poor as they do poor. Opponents argue that, as a practical matter, targeting is infeasible and cannot, therefore, be the basis for general poverty-reducing policies. Both groups are correct because each is talking about a different issue. For the proponents of targeting, the issue is not perfect targeting of the poor but a movement away from programmes that are almost completely untargeted. Many “poverty” programmes are actually general consumption subsidies that benefit, if not everyone, at least a large fraction of the non-poor. These are the programmes that break the fiscal bank and whose removal can be the cause of painful civil unrest. They cannot be sustained from a fiscal standpoint and must, therefore, be better targeted. Such targeting is a far cry from the sort of perfect targeting that skeptics have in mind in which each programme dollar or rupee goes directly to the poor, with none reaching the non-poor and no poor being left out. The two notions are at the opposite end of the targeting spectrum, one calling for a move to at least some degree of exclusion, the other recognizing the impossibility of a case-by-case identification of the poor.

Difficulties of Measuring Income and Consumption. Designing a programme that reaches the poor and only the poor, whether in developed or developing countries, is generally impossible. Targeting a programme only at the poor will require accurate information on income, on consumption, and on other welfare-generating factors (access to government-provided services and their value, for example) for each poor and potentially poor individual or family in the country. Also needed is

¹⁴ See J. Price Gittinger (1988) *Targeted Programs for the Poor during Structural Adjustment: A Summary of a Symposium on Poverty and Adjustment*. Washington, D. C.: The World Bank for a general discussion of the pros and cons of targeting.

an administrative structure to supplement the income or consumption of each unit identified as poor. Information would have to be provided with very little lag between collection and access, and it would have to be updated regularly, perhaps as often as every six months. In this extreme form, targeting is beyond the financial and administrative scope of any government. But less extreme forms of targeting are both feasible and central to the current poverty debate.¹⁵

Proponents of targeting often claim that targeting can be effective for some subpopulations of the poor that are easy to identify: the aged, disabled, young children, lactating mothers. This is true but it misses the point that these easily observed characteristics are necessary but not sufficient for a well targeted programme. Many aged, disabled, young children, and lactating mothers are not poor and for a poverty programme to be truly efficient these non-poor groups must be excluded from the programme or made to pay. Such exclusions require either consumption or income information which is at the crux of the problem. Of course, should a society be able to afford to provide, say, social security to all its elderly citizens then income information may not be necessary. Few, however, can afford such largess.

Even targeting on groups rather than individuals gives rise to many difficulties that are at once well recognized in the literature and often overlooked in the design of policy. For example, any form of targeting requires some way to distinguish the poor from the non-poor. The choice is generally between an income-based measure, which emphasizes individual or household command over resources, or a consumption measure, which emphasizes shortfalls in meeting basic needs.¹⁶

Measuring either income or consumption is a resource-intensive, time-consuming task requiring great skill and dedication. There is ample evidence to suggest that it cannot be done well on a large scale or with great frequency. It is also a task that can be much more difficult in developing than developed countries.

Income is notoriously difficult to define, let alone measure. Definitions range from current money income to potential lifetime income, and the choice of defini-

¹⁵ See Charles C. Griffin (1989) Means Testing in Developing Countries. Paper prepared as a background document for the Rockefeller Foundation under the supervision of Nancy Birdsall. Processed; for a discussion relating to developed countries, see Martin S. Feldstein (1987) Should Social Security Benefits be Means Tested? *Journal of Political Economy* 95 : 468-84.

¹⁶ Even the choice of consumption or income is subject to debate between those who advocate consumer sovereignty and those who believe the public sector should act as a platonic guardian of the poor. On one side of this debate are those who champion the right of individuals, poor or not, to do as they wish with their incomes. On the other are those who want government to ensure a certain minimal level of consumption of basic needs (food, housing, clothing) whether the poor would themselves choose that level of consumption or not.

tion dramatically affects the targeting of poverty policies.¹⁷ Further, much income in developing countries, both urban and rural, does not pass through the market. This home-produced and nontraded income does not, therefore, come with a conveniently attached market-determined value, yet it looms quantitatively large as a source of real income for many poor families. If the relative importance of market versus nonmarket income remained constant over time and among families, non-market income would not be a serious measurement problem, no matter how large a fraction of total income it turned out to be. The opposite is much nearer the truth: the proportion of income that originates in nonmarket income is highly sensitive to economic circumstances and to changes in those circumstances.¹⁸

It is often argued that measuring consumption is easier than measuring income, but this is not so. Traditional households produce much of what they consume and consume what they produce. Even for households that do participate in the market, self-produced income and self-produced consumption are one and the same, and measuring either accurately is exceedingly difficult.

Implications for the Design of Programmes. The difficulties of measuring income and consumption have important implications for the design of poverty programmes in developing countries. They raise serious questions about the efficacy of programmes that require accurate measurement of either income or consumption *at the individual or household level*.¹⁹ Knowledge of household incomes or consumption is essential to programme design, but it is impractical and prohibitively expensive to try to use it as a basis for household-by-household targeting. If household income or consumption measures cannot be used to target poverty programmes for individual households, how should such measures be used? The answer: they should be used in ways that recognize the inherent and substantial difficulties statistical offices face in collecting these data. These difficulties imply a tradeoff between the accuracy of measurement and the extent of the sample covered. The international statistical landscape is littered with examples of failed programmes to collect detailed income or consumption data for large samples of households. Either use a large sample and keep it simple — or keep the sample small and collect meaningful income or consumption data.

Good income or consumption data, even for small samples of households, can tell us much about how to design poverty-reducing policies. Recent work in several

¹⁷ See Glewwe and van der Gaag, *op. cit.*

¹⁸ Anyone who has followed the economic woes of Africa over the last decade and who knows Africa "on the ground" will attest to the fact that measured GDP per capita has fluctuated much more than per capita welfare.

¹⁹ In other words, means-tested programmes for which individual household participation will depend on some measure of each household's income or consumption. For a country-specific cases of means testing and their shortcomings, see Charles Griffin *op. cit.*

countries shows that the poor are a heterogeneous lot, scattered both geographically and across most readily measurable characteristics. The poor are rarely concentrated in one or even a few socioeconomic groups.²⁰ Whether one is talking about income differences between blacks and whites in the United States²¹ or consumption differences among states in India²² the message is the same: eliminating all income differences *between* these groups would do very little to eliminate poverty or to improve the distribution of welfare so long as welfare differences *within* the groups remain unchanged. This finding contains a crucial message for the design of poverty projects. With rare exceptions, targeted poverty-reducing projects intended for groups selected on the basis of easily observed socioeconomic characteristics (including geographic location) will have substantial leakages to non-poor, will have little effect in reducing overall poverty, or both.²³

Consumption Now – or Income Later

Poverty and the programmes to reduce it (or offset its effects) have many dimensions. I find it useful to divide poverty issues and policies into two overlapping cells, each of which creates a distinct set of policy challenges: policies transferring consumption to poor people now, and policies that endow poor people with improved earning capacity for the future.

Transfer Programmes. Broadly speaking, we can divide transfer schemes into four overlapping categories: those designed to be temporary, those designed to be permanent, those that transfer goods and services in-kind, and those that transfer through price controls or subsidies.²⁴ These distinctions are important because in various combinations they serve different target population, produce different degrees of distortion, conflict more or less with other policy objectives, and sub-

²⁰Technically, as defined by easily observed socioeconomic characteristics (age, education, geographic location, for example), the variability of income, wealth, or consumption within a socioeconomic group almost always exceeds the variability of those measures between groups.

²¹James P. Smith and Finis R. Welch (1989) *Black Economic Progress after Myrdal*. *Journal of Economic Literature* 27 : 519 – 564.

²²Guarav Datt and Martin Ravallion (1990) *Regional Disparities, Targeting, and Poverty in India*. Washington, D. C.: The World Bank. (Policy, Research, and External Affairs Working Papers No. 375)

²³Leakages to the non-poor are, and should be, a serious concern in developing countries. Rich countries can afford such leakages, poor countries cannot. For poor countries with very serious public sector budgetary problems every non-poor person served by a poverty reduction programme is, in effect, one more poor person or household that is not served.

²⁴There is in principle a fifth cell: transfers of purchasing power, that is, income. These occur rarely in developing countries even though most economists would argue that they represent the most welfare-enhancing transfer.

stitute to greater or lesser extent for traditional forms of welfare.

The least pernicious transfer programme is a temporary one that distributes goods or services in-kind. These programmes are usually aimed at offsetting specific consumption shocks, such as a natural disaster, with the transfer of food, clothing, and shelter to affected populations. Such programmes are temporary by design and therefore not likely to create long-term distortions in the economy. They are also relatively easy to target.²⁵

Making in-kind transfer programmes permanent increases the risk of leakage and distortion. To the extent that the products delivered are nontransferable — for example, health care services — the problems generated by such programmes are less severe. For transferable or tradable commodities — basic staples, for example — leakages can and usually do grow over time. As leakages grow, so do the cost of the programme and its distortionary effect on other parts of the economy.

Permanent transfer programmes often operate through the price mechanism in the form of price ceilings and subsidies. This combination — permanency and the use of the price mechanism — carries with it two dangers, and their consequences can be found in many developing countries. Such policies are almost always distortionary. And very much related to this, they tend also to be expensive. There is ample evidence supporting the proposition that using the price mechanism to achieve redistributive goals is dangerous. When food prices are held artificially low — below their market-determined value — growers produce less than they otherwise would, increasing even further the gap between the administered price and the implicit market-determined price. Consumers shift consumption patterns to take advantage of the artificially low price, and subsidy or food import budgets are pushed ever higher.

The longer a transfer programme is in effect, the higher will be the leakage as non-poor consumers develop new and better ways of benefiting from the subsidized products. The middle class changes its consumption patterns; secondary markets develop. As this process goes on, a sense of entitlement begins to emerge. It then becomes increasingly difficult to remove the subsidy — not so much because the poor will be hurt, but because the middle class will not tolerate it. History is replete with cases of “entitlement” riots directed at preserving a subsidy that often has little to do with poverty reduction.

Income-generating Programmes. Welfare programmes that aim to reduce poverty permanently and broadly through transfers have not worked, and they will

²⁵ For such a successful temporary programme, see John D. Holm and Mark S. Cohen (1986) *Enhancing Equity in the Midst of Drought: the Botswana Approach. FAO Review on Agriculture and Development* 19 : 6 November-December 24–26; and Kelly McParland (1985) *Botswana: the Land the Rainmaker Failed to Reach. Action for Development* 135 : June 3, 6.

not. It is now increasingly accepted that the only long-term solution to poverty is economic growth, both national economic growth and individual economic growth.²⁶ In section I of this paper I discussed a set of issues related to improving a country's economic growth. Here, I examine policies that attempt to influence individual economic growth by increasing the capacity of the poor to earn income.

Policy-makers can increase the incomes of the poor through two avenues. They can increase the physical assets held by the poor, or they can increase the human capital held by the poor.²⁷ The initial reaction is often to favour the first avenue because it appears to have the most immediate effect on earnings and consumption. There are problems with this approach, however.

When one thinks of mechanisms for increasing the assets held by the poor and thereby increasing their command over income, one thinks first of increasing land or physical assets. Such schemes provide a quick fix in the sense that they have the potential for a more or less immediate impact, but they have not always provided a lasting solution. The reasons for their sometimes brief impact are still being debated by the development research profession, but the outcome is not all that surprising if one considers the context in which many land-redistribution schemes occur.

Many policies go wrong because they are not based on a firm understanding of the situation they are attempting to change. Land reform is no exception. Land distribution patterns in most countries are the result of a natural evolution. Social as well as economic factors have conspired to produce a pattern of land distribution characterized by relatively few large landholders and many landless. In a survival-of-the-fittest outcome, those best able to manage resources have accumulated them at the expense of the less able.

What does land reform do in this context? It disrupts this natural outcome by dealing with the symptom – the unequal distribution of land – but not the underlying disease – the inability of the poor to compete in an open market. While land reform may bring about an immediate improvement in that distribution, the odds are against the land reform's sticking if all else remains the same. Economists and policy-makers recognize this fact and have tried to counter the tendency of land reforms to unravel by supplying complementary inputs – increasing the access to credit and other essential agricultural supplies and sometimes providing extension programmes.

What these interventions cannot address is the key role of human capital in

²⁶See, for instance, Gustav F. Papanek (December 1989) *Growth, Poverty and Real Wages in Labor Abundant Countries*. Background Paper for the *World Development Report* 1990.

²⁷I do not consider here a third possibility, that of artificially increasing the price or value of assets or human capital already held by the poor. Just as with commodity prices this approach would be highly distortionary and therefore unsustainable unless based on underlying market forces.

agricultural production.²⁸ Unless an adequate investment in basic skills accompanies land reform, the outcome of placing previously landless farmers in competition with experienced large (ex)landholders may not be a permanent increase in income flows to the poor. Over time, more able farmers will once again drive out the less able, and the distribution of land will have a natural tendency to move back toward its old equilibrium.²⁹

There are many fewer examples of transferring ownership of other types of physical assets to the poor, but the problems are likely to be the same as with land. Without a solid base of complementary human capital investments, such transfers will not produce the lasting effects policy-makers hope for. That brings us to the role of human capital as a mechanism for permanently increasing the incomes of the poor.³⁰

Maldistributions of physical capital and land are symptoms of a more basic problem: the poor cannot compete especially in a modernizing world because they lack the human capital – the education and skills – to do so. Individuals with adequate human capital will be in a position to accumulate capital and land, unless policies or other distortions prevent them from doing so. But people lacking basic skills who are given capital and land may soon find themselves back where they started.

The increase in school attendance and literacy in the developing world has been nothing short of extraordinary over the past three decades.³¹ However, the next phase in this educational revolution – especially important to the poor – may be considerably more difficult than the just-completed phase. As they enter this next phase policy-makers and donors must recognize that those who have not been reached by education and literacy programmes to date may be very much more costly to reach than were those already served. Experience, especially in developing

²⁸ As documented in Dean T. Jamison and Lawrence Lau (1982) *Farmer Education and Farm Efficiency*. Baltimore and London: The Johns Hopkins University Press; and Marlaire Lockheed and others (1988) *Farmer Education and Farm Efficiency: A Survey. Economic Development and Cultural Change* 29 : 1 37–76.

²⁹ There are exceptions. Korea's land reform is often cited as one of the building blocks for its growth into an international economic power. But that reform worked for two reasons. First, the natural evolutionary forces that had produced the original distribution were virtually non-existent after the Korean War; second, Koreans built on a strong base of human capital.

³⁰ For an in-depth discussion see T. Paul Schultz (1988) *Education Investments and Returns. Handbook of Development Economics* Vol. I: 543–630. Amsterdam: Elsevier Science Publishers.

³¹ Marlaire Lockheed and others (1990) *Improving Primary Education in Developing Countries: A Review of Policy Options*. Washington, D. C.: The World Bank. See especially Chapter 2: Trends and Prospects in Primary Education Development.

countries, discussed below, underscores this conclusion.

In the following two sections this general discussion of poverty programmes and interventions gives way to more specific lessons from experience. I look first at the experience of developed countries, mainly the United States, in reducing poverty and its consequences, and then to an assessment of lessons from developing countries' efforts to improve the welfare of the poor.

III. LESSONS FROM DEVELOPED COUNTRIES

There are many more poor in the developing world than in the developed world, but experience with public policies to reduce poverty or protect the poor from the worst consequences of being poor is much more extensive in the developed world. The magnitude of the problem and the scarcity of resources in developing countries make it imperative that developing country policy-makers are aware of and benefit from the lessons of experience from developed countries. I review here some of the main messages as I see them that can be derived from developed countries' efforts to reduce poverty.

Levels versus Consequences

The experiences of most developed countries suggest that eliminating poverty in the sense of moving the poor out of poverty and making them independent of state support is an elusive goal. Most developed countries continue to have substantial numbers of households that do not earn enough to put them above the poverty line.³² The picture, however, is not all bad: several recent reviews show that public intervention has been quite good at mitigating the consequences of poverty, that is, at reducing the worst symptoms of poverty.³³

This picture of success in reducing the consequences of poverty while at the same time leaving large numbers of households below the poverty line arises in part from the tendency of analysts to use incomplete measures of welfare when categorizing households as poor. As traditionally measured, neither income nor consumption captures the welfare-enhancing effects of public health activities, improved food security, better infrastructure, and the like. Policies in these areas have changed dramatically the meaning of being poor, but this change is not easily monetized and therefore not easily summed up in income or consumption measures.

³² Poverty lines are almost always based on relative notions of poverty. Many of the poor in developed countries, the United States for example, earn incomes that would place them in the upper income brackets of many developing country income distributions. If poverty lines shift with economic development it is not clear that we can truly ever eliminate poverty.

³³ Jean Dreze and Amartya Sen (1990) *Hunger and Public Action*. Oxford: Clarendon Press. (Forthcoming)

Problems of Measuring Poverty

I have come to the conclusion that economists and statisticians have spent too much time on issues of measuring poverty and too little time developing and analyzing policies for reducing it.³⁴ This may seem like heresy coming from someone who spent a good part of his career developing a survey to measure the living standards of the poor, but I am convinced that it is true. Knowledge about the characteristics of the poor, including their likely behavioural responses to policy-induced changes, are critical to the design of poverty policies. Counts of the poor are not.

One problem with counting the poor is that we can seldom agree on who is poor and who is not.³⁵ For example, the United States, with all its data and intellectual resources, has 10 "official" measures of poverty. The proportion of families in poverty declines by one-third as one moves from the most restrictive cash-income measure to the most inclusive measure, which includes imputed income and benefits received in-kind. Bringing in the time dimension makes the situation even worse. For the United States, the official poverty estimate for 1984 found 11 percent of the population living in poverty. Yet 26 percent of the population registered as poor in at least one month of that year, and only 6 percent registered as poor in every month of that years. Sawhill³⁶ states that in 1986, 13.6 percent of the U.S. population was officially identified as poor but that less than 6 percent of the population probably was permanently poor. Obviously, poverty has an important time dimension that further complicates the measurement problems statisticians and analysts face in identifying the poor.

The great puzzle in my mind is why, given the inherent arbitrariness of any poverty measure, economists as a profession spend so much time debating measures of poverty. There is no such thing as an absolute poverty line, and even relative poverty is an elusive concept. Our best income or consumption measures in developed countries are probably off by 10 percent or more, especially for the poor. In developing countries, the measures are much worse (see below).

Sawhill's review of the U.S. experience offers two other lessons related to problems of identifying the poor that are relevant to – and borne out by – developing country experiences. The first has to do with means-tested targeting. I stated earlier in my general discussion of targeting that developing countries must pay

³⁴For an extensive discussion of poverty measurement issues see A. B. Atkinson (1987) On the Measurement of Poverty. *Econometrica* 55 : 749–64; William Birdsall (1984) The Value of the Official Poverty Statistics. Paper for the Association for Public Policy and Management, New Orleans.

³⁵This discussion is based on Isabel V. Sawhill (1988) Poverty in the U.S.: What Is It So Persistent? *Journal of Economic Literature* 26 : 1073–1119.

³⁶Isabel Sawhill (1988) *op. cit.*

attention to programme leakages — the poor not reached by the programme, and the non-poor who benefit from the programme. This appears to be especially important for means-tested programmes. According to Sawhill, only about half the means-tested cash assistance targeted for the poor in the United States in 1983 actually reached the poor.³⁷ This in a country with excellent household statistics and a large federal, state and local welfare bureaucracy.

The U.S. experience also offers a lesson on the efficiency of group targeting. Since the poor are a small fraction of the U.S. population, one might expect that they would be relatively homogeneous and easily identified. The popular image in the United States is of a poverty population made up of black urban slum dwellers. If true, this would have very important implications for programme targeting. But it is not. Sawhill, citing the U.S. Bureau of the Census, states that "only 7 percent of the entire poverty population lives in a low-income area...in a large city. While 70 percent of this group is black, blacks living in such areas comprise less than 5 percent of the black population and only 15 percent of the black poverty population" [Sawhill (1988), p. 1109]. This finding underscores the point that the poor are seldom to be found in neatly defined, easily targeted groups. They are widely dispersed, and programmes to reach them must recognize this. If this is true for the United States, with relatively few poor, think how much more likely it is to be true for most developing countries, with their much larger poverty populations.

Other Problems of Targeted Programmes

There are other lessons from the United States experience that policy-makers in developing countries would do well to note. The U.S. poor who are targeted by means-tested programmes have more than occasionally faced the highest tax rates on productive activities of any group in that society. There are well-documented cases of welfare households facing tax rates on earned income in excess of 100 percent.³⁸ For these households, a dollar earned resulted in a more-than-one-dollar loss in welfare benefits (food stamps, rent allowances, subsidized medical benefits). While this situation was certainly an unintended outcome of multiple welfare programmes that benefit the same individual households, it nonetheless had devastating incentive effects, trapping welfare recipients in programmes from which they might want to escape but, ironically, could not afford to.

³⁷ Technically, the United States spent \$31 billion on cash means-tested transfers in 1983. The poverty gap in that year was \$63 billion before the transfers and should therefore have been roughly \$32 billion after the transfers. In fact, it was \$47 billion, implying a net transfer of \$16 billion and a "leakage" of \$15 billion.

³⁸ Robert Haveman (ed) (1987) *Poverty Policy and Poverty Research: The Great Society and the Social Sciences*. Madison, WI: University of Wisconsin Press.

The lesson here goes beyond the need to recognize the dangers of a high implicit marginal tax rate. Each welfare or antipoverty programme (and the effects of any potential combination of programmes) must be weighed against the incentives it provides recipient households to change their behaviour. The better a programme is at providing for the poor, the less incentive there will be for poor households to find permanent nontransfer ways out of poverty. This is among the greatest dangers of consumption-transfer programmes. They may preserve precisely the poverty they are intended to alleviate. The U.S. experience with its Native American Indian population is a sad case in point.

Other Players in the Poverty Arena

There is a solution to the problem of a high implicit tax rate, and the U.S. experience with this problem will serve as my last lesson from developed countries. In the late 1960s and early 1970s, it looked as though welfare policy in the United States was about to take a dramatic turn. The concept of a negative income tax had surfaced in academic and political discussions.³⁹ A negative income tax builds on two principles. The first is that people will not work if the incentives to do so are sufficiently low, for example, if the implicit tax on their newly earned income is very high. This is a wholly uncontroversial idea, and one that is well documented in the economics literature for both poor and non-poor populations. The second principle is that poor households know how to improve their welfare better than the government does. In other words, a dollar in cash transfers is worth more than a dollar's equivalent in in-kind transfers.⁴⁰

Whereas most tax systems are discontinuous in the sense that zero is the minimum tax anyone pays, in a negative tax system tax payments can and do become negative, that is, become subsidies. When incomes fall below some predetermined level (the poverty line, for example) households are partly compensated for the loss. For example, if one's earnings fell \$ 100 below the designated minimum income line and the negative income tax rate were 50 percent, one would have a negative tax payment — a subsidy — of \$50. Conversely, someone below the poverty line who earned an additional dollar would be able to keep half of it rather than possibly losing the equivalent amount in reduced publicly provided benefits.

³⁹For a comprehensive discussion, see Alicia H. Munnell (ed) (1986) *Lessons from the Income Maintenance Experiments*. Proceedings of a Conference held in September 1986. Boston, MA: Federal Reserve Bank of Boston; James Tobin and Joseph A. Pechman (1967) *Is a Negative Income Tax Practical?* Washington, D. C.: Brookings Institution.

⁴⁰On average, a dollar of in-kind transfers will be worth less than its market value because it forces households off their preferred consumption path (the path they would have chosen had they been given money instead of goods or services).

The negative income tax was "perhaps the only major policy proposal of any type [in the United States] to command the enthusiastic support of a broad spectrum of economists ranging from Milton Friedman to James Tobin".⁴¹ In the first flush of enthusiasm for a negative income tax, very detailed administrative programmes were worked out, and large social experiments were carried out to assess its impact and costs. Yet today the term "negative income tax" is a quaint relic, no longer even on the periphery of the policy agenda.

Why did one of the most widely supported approaches for dealing with poverty in the United States drop so completely from the policy agenda? For two main reasons, both related to administration of the programme. A purported benefit of the negative income tax was that it would be much simpler to administer than other transfer programmes. There would be a single trigger for participation: income. Just as the non-poor were expected to report their incomes and earnings and to pay taxes on them, the poor would report their earnings and receive some part of the gap between their earnings and an agreed-on minimum income.

But rather than being met with enthusiasm, this focus on simplicity and a single trigger raised great fears among the keepers of poverty programmes – and therein lay the two reasons for the negative income tax's fall from grace. The first was that those who were able to work but who chose not to work would be eligible for benefits. Thus existing welfare programmes that relied on large bureaucracies to "filter" programme participants, thereby ensuring that only the deserving received benefits, were considered to be preferable, even though their administrative cost was substantially higher than any estimate of leakages to the non-poor from a negative income tax programme.

The second reason for the negative income tax's fall from grace was a corollary to the first: the proposed programme was a clear threat to the U.S. welfare bureaucracy. Its *raison d'être* was to simplify the system, to combine vast arrays of programmes into one, to reduce welfare programme overhead significantly. Jobs were on the line, and so in the end the idea died. The message: Even the best of ideas are not immune from the ravages of political pressures and rent-seeking behaviour. The politics of poverty are as much a force in shaping antipoverty programmes as is the desire to improve the welfare of the poor.

Although negative income tax programmes are not yet administratively feasible in most developing countries, what drove economists to develop these programmes – a concern for the disincentive effects of traditional welfare programmes – remains as important in developing countries as it does in developed countries. And the reasons for the failure of negative income tax programmes to capture political

⁴¹David T. Ellwood and Lawrence H. Summers (1986) *Is Welfare Really the Problem?* *Public Interest* 83 : Spring 57–78.

support serve as testimony to the importance of understanding who gains and who loses when designing and selling a new programme.

IV. LESSONS FROM DEVELOPING COUNTRIES

Many of the lessons from developing countries are variations on the themes discussed above, but their implications for the design of poverty programmes are more striking. When designing policies to reduce poverty in developing countries, four of the most obvious facts about such countries are four of the most important:

- The poor constitute a relatively high fraction of the total population;
- Most of the poor live in rural areas;
- Resources for reducing poverty are scarce in absolute terms and exceedingly scarce in relation to the population to be served; and
- Poverty, income fluctuations, and food insecurity have been ways of life for millennia, and traditional, nongovernment systems for dealing with these problems have had to develop to respond to these problems.

From these four facts we can derive two important principles for the design of poverty-reduction programmes. First, antipoverty programmes in developing countries that have the objective of raising current consumption should serve only the very poorest of the poor. Such programmes should be designed to deliver very basic "basic needs", probably at levels that are unattractive to the non-poor. Second, the bulk of antipoverty programmes should be directed toward increasing income, not consumption. That is, they should try to increase the poor's permanent command over resources, not just provide a temporary lift. These programmes must recognize the ever-shifting nature of economic development and must prepare the poor for entry into the modernizing world they will have to compete in.

As T.W. Schultz stressed many years ago, economic development is a process of change, and those who can adapt to change benefit at the expense of those who cannot. There is now ample evidence to support the contention that one of the best ways to prepare a population for change, perhaps the only way, is to educate them. Increased human capital does not in itself raise the welfare of the poor, but without it the scope for improving welfare is very limited. In a way, policy-makers face only two options if they want to improve the welfare of the poor. They can attempt to permanently protect the poor from the consequences of poverty or they can equip the poor to compete and so protect themselves. Permanently protecting the poor in the numbers found in developing countries cannot be done. The solution has to be to give the poor the wherewithal, in this case the human capital, to compete, to enable them to adapt to change, and so to win their share of the national welfare pie.

There are many other characteristics of developing countries that policy-makers – and researchers – ignore at their peril. One of these is the generally weak administrative infrastructure for serving the poor. I turn now to the importance of managerial capacity, administration, and infrastructure in the design of poverty policies.

The Managerial, Institutional, and Infrastructural Requirements

With considerable justification, economists are often accused of ignoring the context in which their theories and recommendations must work. Research and policy formulation in the area of poverty alleviation is no exception. As many of my research colleagues at the World Bank know, I have little patience for research relating to issues or policy options outside the range of administrative and institutional feasibility. Poverty research too often is supply-driven in the sense that the starting point is researchers' interests and available data, and only at the very end of their work do institutional and contextual considerations enter the analysis.

Let me be clear here about what I mean by "context". I do not mean that every country is a special case and that no generalizations apply. I mean that institutional considerations should be the starting point of policy-oriented research, not a tag-on at the end. Take, for example, the large amount of ongoing research on various issues of targeting.⁴² How much of this research is policy-relevant in the sense that it actually produces findings that will – or should – change policy stances? Much less than should be the case, given the pressing need for innovative policies to help the poor.

What are the institutional and administrative constraints that should form the starting point for policy-oriented research on poverty in developing countries? First, managerial skills are among the scarcest of resources in many developing

⁴² On the general principles of targeting see Timothy Besley and Ravi Kanbur (1988) *The Principles of Targeting*. Coventry, England: Development Economics Research Centre, University of Warwick. (Discussion Papers No. 85); Jean Dreze and others (1989) *Identifying and Reaching the Poor: Principles and Some Examples from a North Indian Village*. Background paper for the *World Development Report*, 1990. Processed; Paul Glewwe (1989) *Targeting Assistance to the Poor Using Household Survey Data*. Washington, D. C.: The World Bank; Carolyn Winter (1989) *Target Efficiency in Health and Education: Developing Country Experience*. Public Economics Division, Country Economics Department. Washington, D. C.: The World Bank. Processed; J. Price Gittinger (1988) *Targeted Programs for the Poor During Structural Adjustment: A Summary of a Symposium on Poverty and Adjustment*. Washington, D. C.: The World Bank; Charles C. Griffin (1989) *Means Testing in Developing Countries*. Paper prepared as a background document for the Rockefeller Foundation under the supervision of Nancy Birdsall. Processed; Martin S. Feldstein (1987) *Should Social Security Benefits be Means Tested?* *Journal of Political Economy* 95 : June 468–84.

countries. This is as true in the public sector as it is in the private sector. It means that programmes that demand heavy managerial inputs, day-to-day fine-tuning, or hands-on administration may in the end be self-defeating. Programmes to reduce poverty must be both administratively simple and administratively cheap. But they seldom are (for reasons that I will soon discuss).

Administrative capacity takes on added importance when we recognize that most of the poor in developing countries live in rural areas. The urban poor may be more visible and perhaps more vulnerable, but they often account for only a small fraction of a country's poverty population.⁴³ The problem is most serious, therefore, where the capacity to deal with it is weakest. This pushes us to face an unfortunate tradeoff: with the limited resource available for poverty-alleviation efforts, do we focus efforts on the easier-to-reach urban poor, or do we spread scarce resource thinly by trying to reach the much larger and more remote rural poor?

A clear example of this tradeoff can be found in the area of human capital and the delivery of education programmes. Many governments have devoted large segments of their public sector budgets to education,⁴⁴ but significant fractions of the population remain outside the formal education system or are only marginally educated. Because of the compositions of the populations already served and of those remaining to be served, the next steps along the road to universal literacy will be much more difficult than the ones already taken. In most settings, it will be much more expensive to serve the remaining populations — the rural poor — than it was to serve the more densely and centrally located urban populations. Few governments have the resources to provide all remaining underserved segments of their population with adequate access to education tomorrow, or within the next year, or even within the next 10 years. Choices will have to be made, and making them will require more knowledge than we now have about both the demand for and supply of education.

There is another tradeoff in the provision of education that many developing countries now face. With limited resources, educational systems are being forced to choose between the number of people who can receive education and the quality of that education. In many countries, especially in Africa, the demand for education far outstrips the ability of governments to provide it. The "solution" in too many countries has been to spread already stretched education resources among ever more students, seriously compromising the quality of education. True, there are economies

⁴³ Glewwe and de Tray, forthcoming. *op. cit.*

⁴⁴ There is, however, considerable concern over how efficiently these resources have been used. See, for example, World Bank (1988) *Education in Sub-Saharan Africa: Policies for Adjustment, Revitalization, and Expansion*. Washington, D. C.: The World Bank; and Lockheed, Marlaine and others, *op. cit.*

of scale in the production of education. But increasing the number of students in the system — while holding resources constant — eventually reduces the learning each student receives. Very visible at higher levels of education — at colleges and universities — this phenomenon exists at every level.

The laudable egalitarian approach that developing countries take toward educating their people can result in many having attended school but far fewer having received an education. The general lesson from this experience is among the most important for developing country policy-makers: policies that are unrealistic in their goals or that are not based on a firm understanding of financial and administrative constraints run the risk of falling far short of those goals. Policies that are realistic in their objectives may not sell as well politically but they are more likely to achieve what they set out to accomplish.⁴⁵

The experience of developing countries in the design and implementation of poverty programmes points very clearly to the need for focus and simplicity in these programmes. There is a tendency to think that because the need is so great and so immediate, we must attack the problem at every margin right now. Indeed, just the opposite is the case. No matter how well intentioned, the history of broadly based, administratively complex programmes shows that on average they serve no one well, except perhaps the administrators who manage them.

The Unintended Beneficiaries of Poverty Programmes

Poverty is a popular commodity in the international donor market. Its popularity means that many programmes having little to do with poverty reduction are being sold in the guise of poverty programmes. A recent example of this occurred in a much-heralded programme to soften the effect of structural adjustment on the poor in one of the many South American countries undergoing structural adjustment. The programme was billed by the international donor community as helping the poor during adjustment by providing them with temporary public employment. In principle, the programme was to offer a less-than-market wage so that it would attract only those unable to find regular employment. A recent interim evaluation shows that this is not quite what has happened. Wages in the new programme are sufficiently high to make them attractive to the already employed and to secondary workers in households above the poverty line. Most of the “new” employment, therefore, has gone to non-poor households. When asked about this apparent failure in the programme, a senior government official stated that there was no failure.

⁴⁵ This point comes through very clearly in a recent review by Judith Tendler of Ford Foundation efforts to reach the poor. See, Judith Tendler (1989) What Ever Happened to Poverty Alleviation? *World Development* 17 : 7 1033–1044.

The programme had never been intended to protect the poor. Its only objective was to pump new money into the economy as quickly as possible. The programme was a Keynesian demand-priming package disguised as a poverty-alleviation project.

Poverty projects seem to be more vulnerable to being captured by groups with other objectives than do other types of projects. Food-subsidy programmes are put forth as antipoverty efforts, but analysis often shows that the primary beneficiaries are the urban middle class.⁴⁶ Education and health programmes are nominally aimed at the welfare of the poor, but the rich receive the lion's share of the benefits. This diversion of the benefits of poverty projects to the non-poor is not surprising. In most countries, the poor remain unrepresented in the political process and so are seldom in a position to defend their programmes against attack. But since poverty programmes sell well, the mantle of poverty alleviation remains even as programmes characteristics are shaped to benefit the non-poor.

The problem of what I will call "middle-class capture" — the tendency for poverty programmes to end up serving others than the poor — is a difficult one to deal with in developing countries. The middle class generally is much better organized and much more politically powerful than the poor. But, equally important, members of the middle class are themselves often poor by international standards. So it becomes both politically and morally difficult to end the flow of benefits to the middle class, even when those benefits rightly belong to, and are needed by, the poor. Attempts to do so have been among the main sources of opposition to stabilization and adjustment programmes in many countries. The lesson here, not especially useful to those already facing the problem, is to avoid getting into the situation in the first place by limiting the benefits of poverty programmes to the poor.

V. A SUMMARY OF IMPLICATIONS FOR POVERTY-REDUCTION POLICIES

This tour d'horizon has covered much ground at a quick pace. I will close with a summary of what this material means for policies aimed at improving the welfare of the poor in developing countries.

Lesson 1: Investments in human capital are the key. Developing countries cannot solve their poverty problems through consumption transfers. They have neither the resources nor the administrative structures to do so. Poverty-alleviation efforts must be directed at increasing the income-generating potential of the poor,

⁴⁶For one discussion of such a programme see Karim Laraki (1989) *Food Subsidy Programs: A Case Study of Price Reform in Morocco*. Washington, D. C.: The World Bank. (LSMS Working Papers No. 50)

Comments on “Reducing Poverty in Developing Countries – Some Basic Principles for Policy Design”

The author starts with the claim that this paper takes a pragmatic policy-oriented look at previous efforts aimed at reducing poverty. According to the author, the basic message of the paper is that policy-makers and researchers failed to pay due attention to what was already known about the institutional and infrastructural constraints, leakages in the transfer programmes and the increasing cost of getting income-generating programmes for the poor operational because of difficulties in reaching the poor. The author also laments about the neglect or lack of search for simple feasible and persistent policy measures which would go beyond the objective of increasing consumption in the short run.

In the first section of the paper, the author underscores the importance of the macro-economic policies, in essence, the stabilization policy to arrest inflation from the existing high levels and check the unsustainable fiscal deficits. The author makes an effort to distinguish between stabilization policies and structural adjustment programmes. The author makes his belief explicit that one of the lessons from the 80s is that although the poor are being hurt, they suffer less than the non-poor and the principal cause of the decline in living standard of the poor is delayed adjustment not the stabilization *per se*. He however, concedes that the proximate cause of the decline in welfare among the poor could be the stabilization programme but the need to stabilise grows out of the history of economic mismanagement. After pointing out certain distortions he conjectures that the urban middle class is the one which emerges as the looser and being vocal, tends to oppose the stabilization policies.

While discussing the policies for reducing poverty, he details the problem faced in the identification of the poor because of measurement problems, variation in the life-time prospects and the problems faced in exclusive targeting. He is also cognizant of the fact that these limitations have a bearing upon the design of the programme. He makes a claim “that rare exceptions apart” targeted poverty reducing projects intended for groups selected on the basis of socio-economic characteristics will have very substantial leakages to the non-poor, and will have little effect in reducing overall poverty or both.

Regarding anti-poverty policies, the author divides poverty issues and policies

into two overlapping cells: (a) policies transferring consumption to the poor now and (b) policies that endow poor people with improved earning capacity in the future. Under the former category, he discusses transfer programmes. He makes a distinction between various transfer schemes on the basis of their permanence and temporariness, on the basis of transfer through goods and services in kind or through price controls and subsidies.

Frankly the central message of the paper is "put your houses in order" through stabilization policies. Although the poor may be hurt during the adjustment entailed by the stabilization package, the paper is reflective of the belief that they will emerge as gainers in the long run. The author has chosen not to discuss what factors to begin with are responsible for putting the house out of order and simultaneously having a large number of poor people. To what extent is a given country responsible for bad macro-economic management policies? Similarly, what is the mechanism which increases the number of the poor? The extent to which distributive pattern of assets and class structure is responsible not only needs to be quantified but also must be discussed in this respect. This paper totally ignores these questions.

Ironically enough, there is a pretence that welfare policies primarily aimed at poverty alleviation, are the subject of interest but the thrust is on the importance and need for stabilization programmes. Whatever anti-poverty policies are yielded grudgingly to me appear either general statements or inconsequential. The poverty alleviation efforts must be directed at increasing the potential of the poor and this should be done *mainly* by increasing human capital investment in the poor.

Firstly, under the stabilization programme, the author should have provided the data that whenever there are cuts in governmental expenditure, to what extent is the expenditure on social sectors like education and health affected, under austerity measures particularly if the governments fail to generate additional resources.

Secondly, the governments in order to recover cost are often advised to increase user charges. Raising the user charges particularly in the social sectors like education and health adversely affects the participation of the poor in these facilities. Finally, privatisation in the social sectors is encouraged both directly and indirectly in the regime of stabilization policies. Privatisation of the social sectors like health and education makes it difficult for the poor to participate because of high prices. All these measures tend to discourage the poor from participating in the education and health system. The adverse consequences of privatisation of these services for the poor are not very well quantified but in a variety of ways, the poor suffer the most. Similarly, the effect of human capital investment on distribution and poverty alleviation is based on the assumption regarding the operation of labour markets with respect to discrimination and segmentation. If the parental characteristics (not the characteristics of the individual such as age, and education and whatever comes

under the conventional earning function) emerges out to be the significant determinant of labour market outcome then the role of human capital investment is circumscribed. I am sure, Dennis de Tray is fully aware of these research studies and the filtering down mechanism experienced in the developing countries. This is not to deny the importance of human capital investment but to highlight its impact under different environments.

The paper under discussion presumably reflects the experience of the author in different capacities and is not a meticulous piece of research. Yet there is a need to document and substantiate general statements. It is imperative to assess the impact of stabilization policies under varying environments. In this context, the country and instrument-specific studies would prove very useful. For instance, the extent to which the worsening income inequality and rising level of poverty in Sri Lanka since 1978 can be attributed to the policies of liberalization needs to be determined prior to passing a judgement that stabilization policies are pro-poor or not anti-poor.

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