The quality of growth and poverty reduction

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Introduction

The relationship between growth and poverty reduction has been widely researched over the past decade or so and a number of generally accepted findings have emerged. Hence, the necessity of growth for poverty reduction is generally acknowledged but at the same time growth is characterized as not sufficient as both the distributional impact of growth as well as social policies – that ensure the participation of all segments of society in such growth – influence the poverty reduction impact of any given expansion path of an economy. Further, recent work has especially focused on how the pattern of economic growth impacts on material poverty reduction – e.g., whether the growth engines of economic upswings are found in sectors that are employment intensive and lead to real wage increases, especially for households located at the lower end of the income distribution.

The extensive discussions about the relationship between the growth process and poverty reduction led to an examination of the quality of growth. The term ‘quality of growth’ emphasizes that quantitative growth processes have to be evaluated in terms of their qualitative outcomes in “improving peoples’ lives and expanding their ability to shape their own futures” (Thomas et al, 2000, p. XXIII). Such quality aspects of growth include the sustained ability to reduce material poverty, improve health and education outcomes, create job opportunities, reduce vulnerabilities and risks, protect the environment, and to lead to higher participation and voice in more equitable institutions. From a developmental perspective, growth becomes an instrument for achieving welfare improvements of people and growth does not represent an end in itself. Hence, the focus on how the quality of growth can best contribute to sustained improvements in such outcomes.

In this short presentation, I would like to present some empirical examples as to the relationship between growth and a few outcomes indicator in Latin America and then focus on the growth versus material poverty reduction experience in Argentina in recent years which might provide some interesting leads as to what important elements of public policies to support the quality of growth are. The data presented originate in a number of empirical studies carried out by (or for) the World Bank’s office in Buenos Aires. Based on that discussion, I would like to elaborate on public policies for skills building and equity as key elements to foster quality growth.

Cross-country tabulations

With the introduction of the term quality come normative values as to what growth should lead to – and it will be hard to come up with an exhaustive list. The reduction of poverty, in its multiple dimensions, is arguably the most important goal of development, also adopted by the...
world community in the specification of its millennium development goals.

Figures one to four show mappings between average real economic per capita growth and four poverty indicators. First, material (or monetary) poverty measured by the annual percentage decline in the headcount rate (Figure 1). Second, the decline in the under-5 and infant mortality rates in the period between 1995 and 2003 (Figures 2 and 3). Third, the increase in the net primary school enrolment rate (Figure 4). The latter is probably a meaningful indicator of progress in lower- and lower-middle income countries in Latin America but not very insightful in the middle and higher-middle income countries where universal education has been achieved. Hence, the graph includes only a few data points.

The cross-tabulations support the findings of many similar exercises – improvements in poverty and social indicators are, on average, associated with positive economic growth but important variations exist across countries. For example, a significant number of countries in Latin America experienced periods of increases in monetary poverty in the presence of positive per capita economic growth (Figure 1) – due to increasing inequalities which more than offset the growth effect. Argentina is an example in case which showed increases in poverty during a good part of the 1990s while economic growth was robust and sustained. Similarly, almost all countries in Latin America achieved declines in the infant and under-5 mortality rates between 1995 and 2003, including many of the countries that went through economic recessions and contractions in economic output, like, for example, Uruguay and Paraguay (Figures 2 and 3). Nevertheless, improvements tended to be lower in countries with lower growth rates than those with higher growth rates. Finally, the few (meaningful) data points included in Figure 4 show that changes in net enrolment rates show a similar dispersion when mapped against economic growth rates.

**Growth and Monetary Poverty in Argentina, 1992-2004**

I would now like to examine the relationship between growth and one of the above indicators, monetary poverty reduction, in more depth in the case of Argentina. For that purpose, I am using the compilation and analysis of household survey data conducted by CEDLAS (2005) for the World Bank. Figure 5 shows growth incidence curves for a number of different time periods in Argentina from 1992 to 2004. Such curves map the percentage change in real income for each percentile of the entire income distribution for different periods with households ordered from poor to rich on the horizontal axes. Hence, if in a given time period we find the entire growth incidence curve to be negative, it implies that all households – regardless of their position in the income distribution – experienced a decline in real incomes. If the curve is upward sloping, it implies that the better off households achieved higher income growth than the poorer households.\(^3\)

Different time periods of growth and recession in Argentina impacted in very different ways on the poor and non-poor. First, growth in Argentina from 1992 to 1998 was clearly anti-poor: real incomes of poor households declined while real incomes of better-off households

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\(^3\) Different definitions as to what constitutes pro-poor growth can be illustrated with such growth incidence curves. According to Kakwani and Pernia (2001) and Klasen (2003), pro-poor growth would imply that the percentage increase in real incomes of the poor is higher than of the non-poor, i.e., generally speaking only if income inequality decreases can pro-poor growth occur. Ravallion (2004) defines pro-poor growth in the absolute sphere with any growth being pro-poor that benefits the poor. For Ravallion, the matter of interest than becomes how pro-poor a given growth is with the pro-poor bias of growth being enhanced through an improved income distribution.
increased. Consequently, the growth incidence curve in Figure 5 has a positive slope. Second, during the recession and crisis period, from 1998 to 2002, all population groups lost and real incomes of all households across the income distribution declined. However, even for this period we can observe an, almost more moderate, anti-poor bias as the percentage decrease in real incomes was higher for the poorest than for the better-off. Hence, income inequality in Argentina also increased during the slump and crisis period. Thirdly, a very different picture emerges when we look at the recovery period (the exact period covered through the household surveys corresponds to May 2002 till the end of 2004 and hence covers well the economic rebound). Here, we find that all households gained as the corresponding growth-incidence curve is distinctly positive. Further, this time around the curve shows a downward slope, signaling that the rebound had a pro-poor bias as the percentage increase in the income of the poor was higher than then percentage increase of the income of the better off. This positive development in the last years, however, could not compensate for the negative and anti-poor bias of the earlier growth periods, leading the overall net effect of changes in household incomes over the entire period (1992 to 2004) to be negative and the resulting growth incidence curve to be upward sloping.

Bertranou and Kharmis (2005) further disentangle the poverty and inequality changes in the 2002 to 2004 period and identify different ‘drivers’ causing the positive distributional and poverty impacts witnessed above. In the first year (May 2002 to May 2003), the recovery of real incomes occurred almost exclusively for the bottom of the income distribution and was in large part driven by the massive income transfer programs that had been introducing in 2002, especially the Heads of Household Program. The Heads of Household Program was Argentina’s main response to the social and economic crisis and reached up to 2 million households at its peak. The program provides US$50 equivalent per month to individuals who are the head of a household; are unemployed; live in a household w/ minors, disabled or pregnant women, and work 4 hours a day or take training or education classes. Galasso and Ravallion (2003) show that the net incidence (hence taking into account forgone other income of the participants) of the program in 2002 (as well as in 2003) was strongly pro-poor (see Figure 6) as around 80 percent of program payments benefited the bottom two income quintiles.

In the first year of recuperation, hence, the distributional and poverty impact of transfer payment was clearly more important than real wage and employment effects. Bertranou and Khamis (2005) find that job creation between May 2002 and May 2003 did play a role but that about half of additional occupations were due to the public works program of the Heads of Household Program. Of the other half, newly created informal sector jobs (either as self-employed or employees) accounted for about two thirds of total new employment. However, real wages remained depressed (in the public sector) or even continued to decline, especially in the informal sector (by almost 20 percent between May 2002 and May 2003) so that the combined employment/wage impact on real income growth of households was minor. Figure 7, reproduced from Bertranou and Khamis (2005), shows growth incidence curves with and without Government transfer payments and it emerges that the almost the entire pro-poor distributional change between 2002 and 2003 can be attributed to transfer payments.

Quite a different picture emerges when examining the May 2003 to end 2004 period. Figure 8 shows that real household incomes increased across the entire income distribution spectrum and, in addition, in a distinctly pro-poor way. But in contrast to the earlier period, this was not due to the expansion of transfer payments but rather to three factors. First, additional
employment generation occurred in industries and sectors important for the poor (high poverty rate and high number of poor obtaining income from these sectors): manufacturing, construction and retail sectors. Second, the very same sectors showed a significant employment elasticity of growth for lower-skilled labor. Third, the rebound translated into increased real wages: overall, real wages increased by 15 percent from May 2003 to December 2004 and the increase was stronger for informal sector workers (18 percent).

The pattern of growth during the rebound in Argentina, especially between mid-2003 and end-2004, hence showed a pattern favorable to the poor. In part, such pattern was supported through a markedly different set of relative prices than before the collapse, most importantly a strongly devalued real exchange rate (stimulating internal, import-substituting demand) as well as favorable international prices for primary commodities, especially soy beans. An important question is to what degree the current pattern of economic expansion offers sustainable growth perspectives – a key ingredient for a quality growth path.

Public Policies for Skill Building and Equity to Foster the Quality of Growth

The empirical examples above show that a discussion about the qualitative outcome effects of growth have to lead to a discussion of public policies that support the pace and pattern of economic growth, how poorer households can be supported to share the benefits of such growth, and how public policies lead to improvements in opportunities and outcomes across different welfare dimensions. This field is extremely wide and would include discussions of macro-economic policies in general (stability and the avoidance of crisis which tend to affect the poor the most), exchange rate and financial sector policies (as they determine key variables determining international competitiveness), policies for equality and equity (both of incomes and assets), policies that foster the creation of good and secure jobs in the growth process (in which the social protection system plays a crucial role), policies that preserve the environment in the long-run as otherwise short-term gains in income cannot be maintained if the natural capital is depleted, and policies that enable the poor to acquire the needed skills to participate in such growth. I want to briefly focus here only on two such aspects – the importance of skills building for the poor and the importance of equity enhancing policies.

My first point concerns the necessity for public policies for quality growth to focus on long-term skill building in a strategic way. In the above discussion of the post-crisis Argentine growth pattern, we had observed that the pro-poor pattern of growth between 2003 and 2004 was derived from employment creation and real wage recovery in sectors of importance to the poor – relatively low-skilled sectors. For the pattern of growth to have a similar positive impact on reducing material poverty in the future, however, it will be important to achieve sustained productivity increases. Sustainable growth in the longer run will depend on such productivity improvements which both render industries competitive internationally and translate into better paid jobs. Key for such productivity increases are policies that help the poor to acquire needed skills. Put differently, the very fact that a pattern of growth is intensive in the use of low-skilled labor is good in the short-run but not sufficient for sustainable quality growth and poverty reduction in the longer-run.

Francois Bourguignon refers to the crucial role of skill building, education and training when he talks about the necessary supply response of labor to growth potentials in open economies (2005). Without such policies, not only can growth opportunities not be realized (and hence economic growth would falter at some point) but also the fruits of such growth would not be
spread equitably. The potential for redistribution through the growth process itself would be considerably lower.

Closely linked to the necessity of public policies to support skill-building of the most disadvantaged so that they can participate in a longer-run growth pattern in competitive sectors based on technological change and productivity increases, are public policies that tackle underlying inequities in the distribution of assets. In the above empirical example from Argentina, we focused mainly on the direct distributional effects of redistribution policies (the Heads of Household Program) and the distribution effects of the pattern of growth. However, while doubtlessly important, redistribution policies through expenditure policies will only be able to achieve changes in the distribution of labor incomes to a certain degree. In order to achieve a more equitable growth from the outset will depend on the distribution of assets which determine opportunities of households to participate in economic growth in the first place.

The recently released World Development Report (2005) on equity and development makes two arguments why reducing the inequity of assets matter immensely for development – and therefore also for the quality of growth. First, with imperfect markets, inequalities in power and wealth translate into unequal opportunities, leading to wasted productive potential and to an inefficient allocation of resources. Examples from imperfection of markets are abundant – spanning credit markets (where the poor, even if they have equal investment opportunities, often lack collateral to obtain credits), human capital markets (as the expected returns on education are known to be influenced by location, contacts or discrimination on grounds of gender, caste, religion or race), and land markets (lack of titling and imperfect rental markets). In the presence of such imperfections, a highly skewed distribution of assets limits the opportunities for the poor to participate in economic development and improve their living conditions, thereby, in turn, reducing the development potential of societies overall.

The second channel of influence between the distribution of assets and development pointed out by the WDR derives from economic and political inequalities being associated with impaired institutional development. Unequal power – which is often linked to highly unequal asset distributions in the first place – leads to the formation of institutions that perpetuate inequalities in power, status and wealth. And such institutions, the WDR argues, are typically also bad for fostering innovation, risk taking and investment necessary for long-term growth.

If an improved distribution of assets leads to an improved distribution of income in societies, the direct link to material poverty reduction is clear: for any given economic growth rate, the lower the income inequality, the higher the material poverty-reducing effect of that growth. But many of the other dimensions of quality growth mentioned above are also likely to be positively influenced by policies for equity: higher equity can lead to better opportunities for children from poorer families to obtain a good education, less conflict and risk, higher political stabilities which in turn can reduce the risk of crises, fairer institutions – and, to close the circle, a higher degree of consensus for society to support public policies that seek to widen opportunities for the most marginalized population groups.

**Bibliography**


**Figure 1: Growth and Monetary Poverty Reduction**

![Graph showing growth and monetary poverty reduction](image)

Source: Calculations based on World Development Indicators (2005) and data from World Bank Poverty Assessments
Figure 2: Growth and Decrease of Under-5 Mortality Rate, LAC, 1995-2003

Average GDP per capita growth rate (annual)

Mortality rate decrease, under-5 (per 1,000 live births)

Source: Calculations based on World Development Indicators (2005)
Figure 3: Growth and Decrease of Infant Mortality Rate, LAC, 1995-2003

Source: Calculations based on World Development Indicators (2005)
Figure 4: Growth and Increase of Primary School Enrolment, LAC, 1998-2002

Source: Calculations based on World Development Indicators (2005)
Figure 5: Argentina: Growth-Incidence Curves

Source: CEDLAS (2005)

Figure 6: Argentina: Net Incidence of the Heads of Household Program, by population quintile, 2002 and 2003

Source: Galasso and Ravallion (2004) and World Bank estimates
Figure 7: Argentina: Growth Incidence Curves, 2001-2003, with and without transfers

Source: Bertranou and Khamis (2005)

Figure 8: Argentina: Growth Incidence Curves, 2003-2004, with and without transfers

Source: Bertranou and Khamis (2005)