

Poverty in Asia

Executive Summary

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I. Introduction

1. The World Bank policy paper "Poverty and Hunger: Issues and Options for Food Security in Developing Countries" (1986), makes an important point for a general discussion of the poverty question in Asia -- i.e. that the hunger/poverty problem is not essentially a food production issue, but a problem of food and income distribution. The argument is as follows.

- * The world has enough food to meet its nutritional needs and all indications suggest that production will continue to outpace population growth globally. Except for Africa, this is probably true of most individual developing countries as well.
- * The hunger problem, then, is in lack of access to adequate diets (food distribution) and not food supply per se.
- * Generally, it would take a relatively small shift in the distribution pattern of food in LDCs to fill the nutritional gap of the poor -- in most cases less than 5 percent of national food supply.
- * Population growth rates and the rate of economic growth are the major determinants of the incidence of poverty (i.e. through effects on the growth of employment and, therefore, on the ability to purchase food). Those economies which experienced the fastest growth experienced the greatest decline in poverty. The study's projected increase in poverty in the eighties is based on assumptions of a general decline in economic growth rates relative to population growth.
- * One important fact about the incidence of hunger in LDCs is that it varies considerably from year to year with prices and food production. In fact, the

welfare of individual families or regions varies much more widely than the national averages, which are fairly stable. This is easily understood when we recognize that the average annual variation in international prices for rice is 20 percent and 35 percent for wheat. Variation in LDC grain production ranges from 8 percent for rice to 18 percent for wheat. The fact that prices do not fully reflect variation in supply is due to the impact of government policies -- both buyers and sellers. Several important observations flow from these data: (a) The welfare of the poor in LDCs is directly affected by conditions in international agricultural markets, including interventions by the developed countries that have contributed to price variability; (b) It is directly affected by the national policy environment in individual LDCs; (c) In consequence, both redistribution and stabilization of grain markets are presented as viable options for dealing with the hunger problem.

- * In this context, LDC governments give high political priority to stabilization efforts. Unfortunately, many of the measures they take to protect themselves from variations in production at home and price variation abroad are detrimental to the efficient allocation of resources and to growth.

The World Bank paper makes a number of valuable contributions to the discussion of Asian poverty. First, it emphasizes the critical importance of income, hence employment, in the hunger equation. Second, in stressing the variability of income/nutritional levels across countries and income groups, the paper suggests that globally, across a wide variety of economies, nothing succeeds in reducing the overall incidence of poverty like rapid growth. Third, the fact that poverty levels vary considerably with changes in growth rates and market conditions suggests the primary importance of structural and policy reforms in a long term attack on the problem since these can favorably affect both the pace and pattern of economic growth. Fourth, the trade regime of the LDC and the state of international markets appear to be vital components of the equation. Fifth,

the paper suggests the origin of many of the interventionist policies of LDCs in the political requirement to stabilize food prices and supplies.

The weakness of the World Bank paper as the foundation for a general discussion of poverty lies in its narrow emphasis on market interventions and public management of food markets and its neglect of the evident need to liberalize LDC markets generally. Properly applied, the IBRD strategy is consistent with a broad reform effort. In fact, targeting is an attempt to provide security in the context of a less interventionist general strategy. But it should not set the agenda for a general discussion of the poverty problem. In particular, it is important that any system of targeted food distribution be tied to specific growth and structural reform objectives, be limited in time (e.g., tied to the horizon of structural adjustment programs), and not create a permanent institutional lobby for a perpetual distribution program -- we do not wish to recreate the Elizabethan Poor Laws.

2. The Numbers:

The World Bank study estimates that the population which is more than 10 percent below established FAO nutritional standards is 14 percent in East Asia and 50 percent in S. Asia. The average for all developing countries is 34 percent. Of the 730 million population (1980) in this category in developing countries, 510 million are in the Asian region.

The incidence of poverty declined 6 percentage points over the decade of the seventies, although in absolute terms, the number increased 10 percent. Thus population growth continues to detract from the employment potential of even the dramatic production gains of the green revolution. Not surprisingly, the declines in poverty were most dramatic in the Middle East and East Asia, which grew the fastest.

II. The Past Two Decades - Successes and Shortcomings

1. Summary:

The two-pronged development strategy for Asia that has focused on the interactions between a structural transformation of agriculture on the one hand and an active private sector to stimulate off-farm employment on the other, has been in some respects quite successful. The agricultural sector-- particularly food production-- has grown dramatically in response to the green revolution and countries such as India and Indonesia which were major food importers twenty years ago now have modest surpluses. In the green revolution areas, employment has increased significantly (both on-farm and off-farm) and the incidence of poverty has been significantly reduced. However, in many countries the rapidity of that growth has slowed. The non-farm sector has not grown rapidly enough to absorb the increased population and, more recently, agricultural growth rates appear to be declining. Overall, the advances have been diminished or overcome by population growth.

For purposes of making a large and durable impact on poverty, it is necessary now to emphasize policy and structural reform to promote sustainable growth -- to increase the productivity of investments, strengthen market institutions, stimulate entrepreneurship, encourage resource mobilization, and energize the interactions between agriculture and industry. This is the surest way of generating rapid increases in productive employment and sustainable declines in the incidence of poverty.

2. A Strategy: For over two decades the development community has operated with a substantial consensus on the major elements of a viable growth strategy/model for the Asian region.

* A strategy in which the leading edge was a structural transformation of agriculture based on a combination of irrigation, new high-yielding seed, and fertilizer, directed mainly at foodgrain production.

- * This was to be complemented by a rapid growth in labor-intensive small and medium scale enterprises, which would provide jobs for the burgeoning population.

The complementarity between the two components rested in the assumption that a thriving agriculture would produce:

- * the food surplus essential to supply the off-farm workforce at less cost,
- * a large and growing domestic market for the products or services produced by labor-intensive firms would flow from rising rural incomes,
- * a wage structure that would stimulate exports and encourage foreign investment.

It was also a strategy that built on the resource endowments and large domestic markets of these developing Asian economies. In both the agricultural and off-farm sectors the strategy built upon abundant labor and economized on scarce capital. In both sectors, the driving force was to be the initiative and energy of the individual entrepreneur.

The last three points are interdependent. With a very high income elasticity of demand for food, characteristic of most low income countries, any increase in income, from whatever source, would stimulate significant increases in the demand for food. This, in turn, would push up the prices of basic foodgrains, with two effects -- higher wage bills and, frequently, political unrest. A dynamic agricultural sector which kept food prices (and wages) low was, therefore, essential to exploiting the large labor surplus in these countries. A broad-based growth in agriculture, on the other hand, would produce an enormous demand for simple consumer goods and services in the rural sector that, in the right policy environment, would stimulate the rapid growth of labor-intensive enterprises. This, in turn, would provide a growing outlet for surplus rural labor. It is important to point out that the "broad based" character of agricultural growth was essential to the model. Agricultural growth confined to a few highly favored areas, no matter how fast, would not provide the aggregate demand essential to stimulate a dynamic

off-farm sector. Thus, both growth and equity depended on a rapid increase in productivity in the agricultural sector in combination with the rapid growth of employment off farm.

3. A Success Story: The success and credibility of the agricultural leg of this strategy has, on the whole, been remarkable.

* Throughout the region, the agriculture sector has experienced rapid growth and we are approaching a food surplus situation in several countries (in terms of effective demand). Furthermore, the evidence appears to indicate that the strategy (if not the local institutions) has been neutral to scale (i.e. has not been biased against the smaller farmer), has stimulated the growth of agro-business and agro-service firms (with associated employment gains), and appears to be sustainable (if at somewhat reduced growth rates than in the initial years). Clearly rapid agricultural growth has effectively reduced rural poverty in the green revolution areas.

4. Limitations and Problems: Over the past decade we have, however, experienced some disappointment with the results of this model.

a) Approaching the Technology's Productive Limits:

The green revolution technologies spread very rapidly in the irrigated areas to which they were well suited. Production and productivity of basic cereals grew rapidly, as did rural incomes and employment. More recently, however, we see evidence of slowing agricultural growth rates (though certainly not stopping). This is not surprising, as we begin to consolidate the immediate gains from the original green revolution technology. However, should structural reform succeed, we can expect a significant increase in employment and hence in

income and in the demand for food. Additional gains, to meet this increased demand, will require significant new efforts in both the irrigated and rainfed areas.

Opportunities for further gains do exist. Fertilizer use on many (non-green revolution) crops and in non-irrigated areas is still quite low, for example. In several countries productivity of both land and labor is well below the known potential. In the irrigated areas there is considerable potential for more efficient use of water and the maintenance of infrastructure has been universally poor. This makes it imperative that we not lose sight of the high recurrent costs associated with O&M in the irrigated areas. In several countries the policy environment has impacted negatively on the intensivity of both land and labor use, reducing the contribution of the agricultural sector to growth. There is still much to do in agriculture, and the relative size of the agricultural sector and of the rural population makes further growth highly dependent on what happens in agriculture. But we probably will not see the high rates of growth and job creation in agriculture, particularly food production, over the next two decades that we experienced in the previous twenty years. In fact, it may require considerable effort simply to sustain the 3-4 percent annual growth rates characteristic of the past decade.

b) Marginal and/or Rainfed Agricultural Areas:

In most of Asia there are substantial rural areas which have so far reaped little direct benefit from the green revolution. The reasons vary -- e.g. lack of supporting infrastructure (roads, irrigation, rural electrification), lack of appropriate biological material, or policies that favor the irrigated crops. Equity concerns have shifted our focus from the intensively cultivated (and populated) irrigated areas to the relatively depressed conditions of the marginal and rainfed regions (testimony to the success of strategy). Since the seventies there has been pressure to deal with poverty in these regions directly by redirecting

agricultural research efforts and rural investment to the problems of these areas. Some rainfed areas have high production potential and should have high priority in many cases, of development strategies. In contrast, it should be recognized that in developing more marginal lands, the cost may considerably exceed the benefit in either economic returns or employment, even where production improvements are technically feasible. This limits the opportunities for expanding employment and making a major impact on poverty in such marginal areas.

c) Off-farm Employment:

Unfortunately, in several of the countries of the Asia region the growth of the industrial and non-farm sector has been disappointing. The reasons are clear enough. The mobilization of large amounts of capital into inefficient public enterprises, restrictive regulatory and licensing policies which discourage efficient trade patterns and rational investment decisions, public subsidies which distort commodity markets, overvalued exchange rates and negative interest rates that bias both public and private choices, are distressingly common. The damaging effects on both growth and equity have become all the more evident in the context of the debt crisis.

These growth-inhibiting distortions have been less prevalent in Asia than in other regions, but have still served to retard growth in both South and East Asia. The Philippines provides one example of reasonably satisfactory growth in agriculture, including achievement of self-sufficiency in rice, but very poor performance in industry from both efficiency and equity standpoints. Unsound policies led to an inefficient capital- and import-intensive industrial sector. This not only led to economic growth along unsustainable patterns, but also engendered disappointing performance in terms of employment growth and poverty alleviation. The South Asian economies have frequently placed excessive emphasis on public sector interventions in industry -- both direct production by the public sector and excessive regulation of investment, trade, and production. This has retarded growth in employment, with deleterious effects on both efficiency and equity. Where output markets have been sheltered from market forces, labor markets have often been

characterized by above market wages for the labor "elite" and inefficient use of labor. In India, for example, inefficient use of capital and high wage bills induced by organized labor have increased the cost of manufactured goods to the rural sector, slowing down both demand and job creation.

In these countries the interactions between the agricultural sector growth and the off-farm sector have been far less than their potential. The consequence is that off-farm employment has not kept pace with labor force growth, the demand for agricultural products is depressed, and the take-off engendered by the "green revolution" is stifled.

It should also be noted that these same policy distortions and investment patterns that have inhibited off-farm employment have also slowed the expansion of the agricultural sector, limiting employment potential there as well. Structural reforms can be expected to benefit the agriculture sector by reversing biases in incentives that have penalized agriculture.

d) Growing Importance of Trade

The development model of the past two decades, outlined above, attempted to economize on capital requirements and to exploit the labor surpluses characteristic of the Asian region especially South Asia. It was an "Asian" model, driven by the large internal markets of the densely populated Asian countries. International trade and private equity investment played a modest role in the model, although there are clear examples in Asia where trade was a significant factor in the growth performance. To the extent that there were external capital requirements, it was assumed that there would be a steady expansion of official aid on a government to government basis and that low interest rates which would permit public borrowing by LDCs. Clearly these assumptions are no longer valid. In the future, the LDCs will have to rely on the expansion of trade (hopefully in a liberal international trade regime), careful management of exchange rates and international debt, and attractive investment climate for foreign capital to meet a growing share of their external capital requirements.

It is also the case that the distortions in LDC trade regimes have frequently contributed to development patterns biased against agriculture, against the poor, and against efficient growth generally. Overvalued exchange rates have discouraged exports and encouraged both food and capital imports, to the detriment of agriculture and higher employment. Protectionism has encouraged inefficient sectors/industries by distorting prices and by insulating them from competition. This absorbed capital that might have been more productively used in agriculture or labor-intensive industries.

In this context, however, we must also focus on the emerging protectionist tendencies in the trade policies of the developed countries and the impact they have on the promotion of trade liberalization strategies in LDCs.

III. The Next Decade

1. Growth and Poverty: At this stage we are faced with the question of what represents a viable strategy for dealing with poverty in the Asia region and what role is appropriate for the donor community in general and the U.S. in particular in such a strategy.

- a) Growth, Structural Reform, and Poverty

No attack on poverty can succeed without sustained annual growth rates at least 2.5% to 5% above population growth rates (depending on institutional environment, initial income distribution patterns, the pattern of growth etc.). Historical experience, particularly in East and Southeast Asia, indicates that rapid growth along the lines outlined in this paper can be confidently expected to reduce poverty significantly. It is also fairly clear that any strategy which relies on distributive or redistributive policies in the absence of growth rates at this level will not be viable and will not prevent the continued expansion of poverty.*

* Sri Lanka provides an example of a relatively low incidence of poverty without remarkable progress in terms of per capita income growth. The assumption of this paper is that it is more feasible to achieve rapid, sustainable growth than to achieve (not to mention sustain) the sort of political and social order that accounts for Sri Lanka's success.

Historically, in the fastest growing economies of the region, off-farm employment has expanded rapidly with the growth of the industrial and service sectors. Malaysia, Thailand, Korea, Taiwan all followed this pattern. The economic literature generally supports the basic assumptions of our growth strategy that a rapid growth in the off-farm sector in combination with a structural transformation of agriculture will result in substantial gains in employment and comparable reduction in poverty.

Policy/structural reform efforts that eliminate the policy biases that have clearly restrained growth in output and employment both in agriculture and non-agricultural activities, have the greatest potential for achieving big increments of growth and employment in the next few years. Properly conceived and executed, such reforms will improve economic incentives, increase the efficiency of resource use, and mobilize additional resources for investment. This, in turn, will encourage an expansion of the economy and with it jobs. With increased competition, productivity of resources should increase and with it incentives for technological innovation. Demand for agricultural products should rise while at the same time prices and production costs should fall.

We now understand fairly well how macro-policies can bias the economy against the agricultural sector. Controlled food prices, export taxes, overvalued exchange rates (which cheapen food imports but also favor heavily capitalized industries) all depress the rural sector generally.

But even in a policy environment generally "supportive" to agriculture, policies may well work to the detriment of the poor if they do not operate to stimulate efficient decisions. For example, if the irrigated areas are able to offset their rising production costs by input subsidies (fertilizer, credit, water) there will be little incentive for farmers to seek cost-reducing efficiencies. One effect of this situation could be that the rainfed areas, which generally have lower production costs (per unit of product), will not be able to take advantage of the rising cost structure for irrigated crops to enter the

national markets competitively. The poor will suffer both from a slower growth of food supplies and from the reduced rural employment opportunities.

Without structural reform, policies will persist which weaken incentives for entrepreneurs to take advantage of an Asian LDC's greatest source of comparative advantage -- its abundant labor. If capital remains in highly inefficient enterprises (public or private), and restrictive regulatory environments persist, smaller, labor-intensive enterprises will not emerge in sufficient numbers or grow. Again, the poor suffer from slower growth and fewer jobs.

These efforts at policy and structural reform are made both more urgent and more feasible by the financial crises which many of these regimes confront in the face of high international debt levels, deteriorating balance of payments situations, and large budget deficits with concomitant reductions in national development expenditures. Structural reform efforts must succeed if we hope to create an environment for an expanding private sector. A significant liberalization of LDC economies is required to provide incentives for efficient use of resources and to mobilize the entrepreneurial talent which exists in the private sector. Only in this way can we hope to expand employment fast enough to make a dent on burgeoning poverty.

To the extent that growth, employment, and poverty are concerns which drive our programs, we must give highest priority to these policy and structural questions. This is not a departure from the development strategy of the seventies. Rather, it focuses our attention on the key gap or constraint in our implementation of that strategy -- the growth of the off-farm sector and the structure of the policy environment.

In the short and medium terms, the donors and multilateral banks can assist the design and implementation of the adjustment efforts, help to fill resource gaps, and mitigate the costs and disruptions of the transition period. It is essential that stabilization efforts be combined with longer term efforts to liberalize these

economies, stimulate international trade, and encourage appropriate public and private investment. We should aim for reform efforts that are oriented towards growth, and not merely stabilization.

These adjustment programs inherently entail large shifts in the structure of incentives and rewards within an economy. Therefore, more than any other aspect of the development process, structural reform is a matter of political will. The political obstacles are significant.

b) Agriculture

There are still considerable gains to be had in agriculture and these should be energetically pursued. New technical opportunities occasioned by bio-technical research, improvements in research and extension system, infrastructure investments in the rainfed areas, and the privatization of input and commodity marketing systems all have high priority and promise significant increments of growth. Even maintaining recent growth rates will require considerable investment in improved efficiency in irrigated areas.

In a period of economic crisis it is important that stabilization and liberalization programs do not disrupt critical public investments in agriculture. Continued food surpluses are critical to the growth process. At the same time we must also assure that policies supposedly supportive of agriculture but which distort markets (e.g. input subsidies, protectionism, etc.) and excessively increase budget deficits are brought under control. In a period of slowing growth, all investments, including those for rural and agricultural development, must be examined critically for their impact on overall growth.

First priority in agriculture must be given to developing or maintaining the national research system and training institutions on which future long-term growth depends. Current market surpluses should not lull us into assuming that the battle is over. Successful structural reform efforts should engender an expanding economy, higher employment, and increasing demand for

food. Furthermore, falling prices will necessitate further technical innovations to reduce production costs and intensify production or the agricultural sector will begin to lag. A response from the agricultural sector will depend on the state of its basic institutional capacity for technical innovation.

c) Trade and Investment

We must jointly create an environment which encourages LDCs to liberalize further their international trade regimes, free up their exchange rates, and generally improve the investment climate for foreign private capital. This is essential for two reasons. First, the distortions and inefficiencies engendered in the domestic economy by inappropriate international policies, such as overvalued exchange rates and protectionism, have proven extremely costly to over time, both to efficiency and equity. Second, it will be increasingly difficult for these countries to fill their external resource gap through official borrowing or official aid. They will have to rely increasingly on private capital.

d) Human Capital and Population

We have recognized that one of the most effective ways to promote growth and assist the poor is to invest in people -- education, health, family planning. Basic literacy and numeracy and improved health significantly increase the productivity of labor in every sector, increasing earning capacity. It is also clear that improved literacy (especially among women) and increased child survival has a dramatic impact on fertility patterns. Family planning, of course, has a direct impact on the denominator of LDC population growth rates, which have dissipated many of the gains of the past three decades.

Protection of the vulnerable elements of the society in the face of instability of food supplies and income or from the transitional impact of adjustment programs is also of considerable importance to a stable growth path. Food security not only reduces the level of human suffering associated with the transition period

but also helps maintain the productivity of the labor force. A more stable food regime also reduces the political risk/costs of many development decisions.

Nevertheless, we should exercise caution in recommending a strategy of targeted food programs. Such programs can easily degenerate into permanent "doles" and, as we have seen historically, have a tendency to expand over time. It is often exceedingly costly and difficult to target efficiently. The result can be a heavy drain on government budgets and the creation of a large institutional lobby which perpetuates such programs.

The key is to tie such programs directly to specific growth and reform objectives. For example, high-potential rainfed areas which can make a significant contribution to overall national growth may require extensive infrastructure investments that can be constructed through food for work programs. Food programs designed specifically to support structural adjustment programs can similarly have a clear development focus and be limited to the duration of the transition. Nutritional programs linked to child survival programs can make a direct contribution to the overall quality of the workforce in the next generation and permit a reasonable focus of effort. Growth is the best solution to poverty and all of our resources, including food, should be directed to high payoff and high priority investments. Food should be used to mobilize the poor into a productive and efficient economy, not to create a permanent "poorhouse".

Finally, it is evident that the process of transition to modernity is one of high risk (also great opportunity) for the poorest elements of the community. They have few assets save their own labor. Bad weather, erratic markets, poor health all threaten the survival of family. Our investments in human capital -- education, health, food security, family planning -- all contribute to reducing these risks and raising the returns to their labor.

IV. Implications and Opportunities for AID:

AID's development strategy for the remainder of the eighties should be to alleviate poverty on a sustainable basis by emphasizing the following components:

- * Structural Reform: Active support for policy reform and structural adjustment to assure the conditions exist for the evolution of effective markets with an emphasis on those public sector investments which are essential to a thriving market economy.
- * Private Sector: The active promotion of private sector expansion in a competitive market setting with an emphasis on the rapid growth of small and medium sized private sector firms which can stimulate off-farm employment, and the establishment of basic market institutions.
- * Food Security: Special attention should be given to focused interventions to protect those poorer segments of the population who may be adversely affected during the adjustment process. (For example, targeted Title II programs to protect the poor disadvantaged further by stabilization efforts.) However, every effort must be made to assure that these programs be used to integrate the poor into a productive economy and to stimulate rapid growth, and not to create a class which is excluded from development through a permanent "dole".
- * Agriculture: As agriculture continues to represent a large portion of GDP and employment within the Asia region, we will continue to stress technological advance leading to greater efficiency. However, growing grain surpluses declining trends in grain prices and growing international integration of agricultural markets, will necessitate greater attention to diversification, comparative advantage, economic desirability, etc. in the selection of projects. Regionally focused poverty programs need to be weighed carefully against competing uses for the same resources, the implications of continuing to sustain heavy public investment budgets, and the danger of diverting attention from the critical need for policy and structural reform.
- * Human Capital: Nationally, and in the marginal and rainfed rural areas particularly, emphasis should be given to population programs to reduce the pressure on available resources and to permit significant improvements in the human capital base. Concomitant

with this are focused and quick payoff improvements in the health of the community such as child survival efforts and immunization campaigns. In the long term, improvements in human capital may well be the most significant investment we can make in marginal areas .

- * Trade: Among structural reforms, we must make a special effort to liberalize the trade policies and investment climate for foreign capital in LDCs. We will also seek ways to encourage non-traditional exports and to promote trade and investment agreements between U.S. and LDC firms directly.

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