

## The Relationship between Economic Growth and Poverty Reduction

In the preceding section, we reviewed the relevance of democracy and good governance to poverty reduction, and how their relationship might be deepened. In this section, we ask ourselves: in achieving poverty reduction, will it be enough to focus on GDP growth? An answer to this question carries significant implications for the kind of support that the international community should offer in combating poverty.

Jagdish Bhagwati of Columbia University sets out three central reasons in support of his belief that growth is the key to poverty reduction:

- It creates jobs that ‘pull up’ the poor into gainful employment by providing greater economic opportunity;
- It provides the revenues with which to build more schools and provide more health facilities for the poor;
- It creates the incentives that enable the poor to access these facilities and also for the advancement of progressive social agendas generally (Bhagwati, 2001).

Bhagwati is not alone in stressing the importance of growth in poverty reduction. His views are very much in line with the Washington Consensus (see Annex D) which, as Joseph Stiglitz says, paid little attention to issues of distribution or fairness: ‘If pressed, many of the proponents [of the Washington Consensus] would argue that the best way to help the poor is to make the economy grow’ (Stiglitz, 2002, p. 78). This is the trickle down view of poverty reduction.

Is this valid? While there is significant evidence that, over time, differences in growth across countries account for much of the variation in income poverty, there can also be large variation in poverty reduction in situations where there is the same growth rate in per capita consumption. It is generally the case that growth which reduces inequality reduces poverty more quickly than that which is accompanied by rises in inequality. For example, according to the World Bank, in Uganda growth with declining inequality delivered strong poverty reduction, while in Bangladesh rising inequality tempered poverty reduction from growth. On the whole, growth leads to less poverty reduction in unequal societies where wealth and opportunity are concentrated than in egalitarian societies. The Bank finds that the sensitivity of poverty to growth depends a great deal on initial equality in poor people’s access to opportunities to share growth.

There is now growing evidence that policies that enhance the capabilities and opportunities of the poor to take part in growth have the double advantage of reducing

poverty while enhancing growth. Policies that improve the education and health of, and confer property rights on, the poor and reduce gender disparities have such double benefits.

While this may be broadly acceptable to many, investment in pro-poor sectors like education and health may take time to yield productivity benefits, so that the dynamic effects of investment on growth may show up only given sufficient time. It could be argued that in the longer run an economy might achieve higher GDP growth through early attention to pro-poor human development. Some scholars have, for example, argued that China's recent high growth rate has been made possible partly by the earlier investment in the education and health of its people, though its economic policies immediately after the revolution – for example the collectivisation of agriculture and the so-called 'great leap forward' – were disastrous. In judging the robustness of pro-poor policies, one therefore needs to take the sequencing of policy and productivity lags into account.

Economic policy, then, could produce a range of outcomes: growth may have differential outcomes in terms of poverty reduction. Pro-poor growth need not detract from overall performance.

It is also necessary to distinguish between strategies that seek to attack poverty through pro-poor growth policies like investment in education and health, and straightforward transfers of income or assets. Much of the uneasiness about pro-poor policies among the followers of the Washington Consensus and others arises because of doubts about the efficacy of the transfers route for reducing poverty in a sustainable way. What worries many is that transfers to the poor might mean that investment, including in sectors like education and health, might suffer, with the result that the capacity of the economy to provide employment and higher wages in the future might suffer.

We believe this is a genuine dilemma in many societies and that several remarks are in order. Firstly, transfers *per se* might be necessary in times of distress, such as famines, financial crises, sudden loss of employment and chronic hunger. An absence of state policy that responds to distress and hunger, apart from violating a sense of humanity, risks the danger of social upheaval and political instability – and that is bad for growth. Secondly, adequate nutrition is productivity enhancing – people cannot work without food in their stomachs; there might thus be a positive link between transfers to the poor and economic performance. And the staying power that the poor acquire through consumption subsidies such as price subsidy schemes for cereals and other essential articles of consumption may alter the wage bargaining and other aspects of market power dynamic that may be necessary for democracy to work well. It is also widely recognised that the redistribution of land in societies where ownership is highly concentrated has beneficial effects on account of both equity and growth, as the experience of Korea, Taiwan and others shows.

While subsidies may thus have a place, clearly there is a limit to them and the ques-

tion is how to get the level right, so that incentives to work and to ensure growth in the economy grow are not damaged. The dilemma is that in many poor countries, the situation may be so fragile that there is no alternative but to provide support for the poor even if it is damaging to growth in the long run, unless international assistance comes to the rescue in providing a cushion.

Overall we are driven to conclude, as Joseph Stiglitz does, that notwithstanding the correlation between growth and poverty reduction across countries:

... the statistics show that some countries have grown without reducing poverty, and some countries have been much more successful in reducing poverty, at any given growth rate, than others. The issue is not whether one is in favour of or against growth. ...

The question has to do with the impact of *particular policies*. Some policies promote growth but have little effect on poverty; some promote growth but actually increase poverty; and some promote growth and reduce poverty at the same time. The last are called pro-poor growth strategies. Stiglitz (2002), p. 82