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Overcoming Poverty in the Developing: World Lessons of Experience

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ABSTRACT

This paper classifies all state interventions for poverty reduction into five broad categories. By comparing the performance in poverty reduction and the components of the strategies for the reduction of poverty in different developing regions and country groups, it tries to identify the interventions that are most effective in reducing poverty. The most effective interventions for the reduction of poverty are the policies that generate efficient and labor-absorbing growth; the redistribution of assets and the widening of access to resources in favor of the poor entrepreneurs, and the improved human capital endowment of the poor. In comparison, interventions in the labor market, and the regulation of prices, public distribution and subsidies are not effective methods of reducing poverty except in very limited cases.

RESUMEN

Este trabajo clasifica en cinco amplias categorías las estrategias gubernamentales para la reducción de la pobreza. Por otro lado, intenta identificar las intervenciones más efectivas para el alivio de la pobreza por medio de un análisis comparativo de los distintos componentes de cada estrategia y su efecto sobre la reducción de la pobreza en diferentes regiones y grupos de países en vías de desarrollo. Las políticas más efectivas son las que generan un crecimiento eficiente que incluyen la necesidad de fuentes de trabajo, redistribución de bienes y ampliación del acceso a recursos en favor de los empresarios pobres, así como el mejoramiento de la dotación de capital humano a los pobres. En comparación, las intervenciones en los mercados de trabajo, el control de precios, los subsidios y la distribución pública no son métodos efectivos para la reducción de la pobreza, salvo en contadas excepciones.

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I. Introduction

ERADICATION of poverty has gradually become established as a goal of development policy over the last three decades. Commitment to this goal has come to be nearly universally shared by the developing and developed nations and the international development agencies. Today national development programs rarely exclude the consideration of their effects on the poor. The donor nations cite the alleviation of poverty as a major objective of their programs for international assistance. The World Bank now makes poverty assessments -- consisting of the measurement of the incidence of poverty, the preparation of the profiles of the poor, the identification of the poverty groups and the formulation of programs and policies for the alleviation of poverty -- of the borrowing member countries at regular intervals, and their country strategies are required to consider poverty reduction as one of their major objectives.

The focus is on the reduction of the incidence of *absolute* poverty, i.e., the number of persons below some minimum acceptable standard of living. This is to be distinguished from the objective of increased equality in the distribution of income, which is neither necessary nor sufficient for the reduction of absolute poverty. Consensus about the need to improve the living standard of those who fall below a minimum acceptable level is far greater than the consensus about the need to reduce the inequality of any given distribution of income.

Measuring the incidence of absolute world poverty, by counting the population below a given absolute standard all over the world, is a very difficult task.[1] The World Bank, in the World Development Report 1990, used an upper poverty threshold of $370 and a lower poverty threshold of $275 per person per year at (constant 1985) purchasing power parity (PPP) prices to estimate the incidence of absolute poverty in the developing world. It found that in 1985 1.115 billion persons (33 percent of the population of the developing countries) were poor (below an annual per capita income of $370) and 633 million persons (18 percent of the population) were extremely poor (below an annual per capita income of $275). These estimates are at best rough approximations. A constant level of income at PPP prices does not ensure the same level of attributes that are often used as the criteria for the identification of absolute poverty (e.g., inadequate intake of nutritional energy) across countries. Moreover, estimates of income at PPP are subject to different degrees of error in different countries. Furthermore, one would suspect that the conversion of income distribution in individual countries at PPP prices involves a good deal of error.

It is simply not possible to establish the trend over time of even this oversimplified and imperfect index. From available country-level estimates, the best guess that one can make about the trend in absolute poverty in the developing world, over the last quarter century or so, is that it has been falling as a proportion of population but rising in absolute number.

The incidence of absolute poverty varies a good deal from one developing region to another. The World Bank estimates of extreme poverty may be used to illustrate the point.[2] Thirty percent of the popu-

1 This kind of headcount index is one of several measures that are necessary to get a reasonable idea of the dimensions of poverty in judging the effectiveness of public policy. Other indices relate to poverty gap (resources necessary to bring all the poor barely up to the poverty threshold as a proportion of total income necessary to support the entire population at the poverty threshold income) and distributionally weighted poverty gap (which estimates the poverty gap by attaching higher weight to the gap between actual income and the poverty threshold income the greater the poverty of the person concerned). For a discussion of these measures, see Martin Ravallion, *Poverty Comparisons: A Guide to Concepts and Methods* (Washington, D.C.: World Bank, 1992). For our present purpose a distinction among these measures seems unnecessary.

2 This paper, focused on broad trends and patterns, will not provide detailed statistical evidence. Estimates of

lation of Sub-Saharan Africa were in extreme poverty in 1985. The proportion was 29 percent in South Asia, 21 percent in the Middle East and North Africa, 12 percent in Latin America, 9 percent in East and South-East Asia, and 4 percent in the former centrally planned economies of Eastern Europe. An interesting point to note is that the ranks of these regions in terms of per capita income are not correlated with their ranks in terms of the incidence of poverty. Thus the Middle East, North Africa, and Latin America have far higher per capita incomes than East and South-East Asia.[3] The incidence of absolute poverty is, however, far lower in East and South-East Asia than in these other regions.

Information on trends in the incidence of regional poverty is rudimentary. It is nevertheless possible to surmise certain broad features of trends in the incidence of regional poverty over the last quarter century with reasonable certainty. Poverty has declined dramatically in East and South-East Asia, both as a proportion of population and in absolute number. This trend has been particularly pronounced in the Republic of Korea, Taiwan, Hong Kong, Singapore, Malaysia, Indonesia, China, and, to a lesser extent, Thailand. In South Asia the proportion of population in poverty has declined over time, although the number of the poor has increased. In Sub-Saharan Africa the incidence of absolute poverty has increased as a proportion of population. The former centrally planned economies of Eastern Europe and Central Asia had succeeded in reducing the incidence of absolute poverty in their societies to very low levels. But during the transition to a market economy that has been going on in these countries since the late 1980s, the incidence of absolute poverty has been increasing sharply. The trend for Latin America over the long period is hard to establish.[4]

IFAD estimates show that in most Latin American countries the proportion of rural population in absolute poverty increased between the years 1965 and 1988.[5] Numerous country studies by the World Bank suggest that over the decade of the 1980s the proportion of Latin Americans in absolute poverty has increased significantly. The experience of the Middle East and North Africa appears to be something close to the experience of Latin America. IFAD estimates suggest that the proportion of rural population in poverty increased in many countries of this region between 1965 and 1988. During the 1980s the problem of absolute poverty appears to have become aggravated in most of them.

This paper will try to identify the components of a successful strategy of poverty reduction by comparing the experience of poverty strategies in different regions and country groups. Section II of the paper enumerates the main types of interventions to reduce poverty. Section III compares the components of the poverty reduction strategies pursued in different developing regions. The concluding section analyzes the effectiveness of specific interventions

the incidence of poverty and trends in the incidence of poverty are drawn from: World Bank, *The World Development Report 1990* (New York: Oxford University Press, 1990); International Fund for Agricultural Development (IFAD), *The State of World Rural Poverty,* by I. Jazairy, M. Alamgir, and T. Panuccio (New York: New York University Press, for IFAD, 1992); or individual country studies usually made by, or reported in, World Bank documents.

3 This is the case for per capita income measured both in current dollars and in PPP dollars. In current dollars per capita income in East and South-East Asia in 1985 was 30 percent of that in Latin America and less than half of that in the Middle East and North Africa. Regional averages of per capita incomes in PPP dollars are not available, but a comparison of country-level estimates leads one to expect that their differences were in the same direction and very substantial. Latin America includes the Caribbean.

4 The present writer feels least certain about the circumstances and trends in Latin America. He would like to note that Latin America is the only region in which he did not have an opportunity of direct field experience.

5 International Fund for Agricultural Development (IFAD), op. cit.

by comparing the performances of the regional strategies.

II. Interventions to Reduce Poverty

The view that poverty reduction is the natural outcome of economic growth in a market economy is based on the expectation that growth helps transfer labor from low-productivity subsistence activities to activities with higher productivity. Initially, the expansion of productive employment at constant wages helps alleviate poverty. Once "surplus" labor in the subsistence sector is exhausted (i.e., the so-called Lewis transition is completed), real wages rise, thereby accelerating the process of poverty reduction.

It is easy to see why this process may fail to obtain in reality. Initial resource endowment, in the absence of intervention, may not permit high enough a rate of accumulation to absorb the increment in labor force. This might be designated the case of increasing impoverishment due to inadequate capacity for growth. Another possibility is the highly concentrated distribution of scarce productive assets -- land, physical capital, and human capital. The scarcity of productive assets would dictate a very high and increasing share of income for them. Thus a very high, and continuously increasing, share of income would have a highly, and increasingly, unequal distribution. In this case growth might induce poverty.

Public intervention to reduce poverty in these cases could take a variety of forms. Most policy interventions for the reduction of poverty could be classified under one or the other of the following five sets of policies.

1. *Provide the poor with productive and remunerative employment by promoting efficient, labor-absorbing growth.* This calls for a comprehensive strategy encompassing incentives for accumulation and attraction of capital from abroad; promotion of investment productivity; and incentives for a high elasticity of labor demand.

2. *Convert the poor into productive entrepreneurs.* Focusing on growth alone may often be an inadequate strategy for poverty reduction even though the growth elasticity of employment is reasonably high. This would be the case, discussed above, if productive assets are scarce and distributed very unequally. A small, and decreasing, proportion of income would in this case be shared among workers. Consequently, real earnings of the poor workers might decline.

An effective way to reduce poverty in this case is to provide the poor with productive assets to convert them into productive entrepreneurs. Since most poor societies are predominantly agrarian, and since most of the poor in a typical developing country are located in the agrarian sector, the redistribution of land is a powerful method of granting the poor access to productive assets. Other methods are the provision of credit for nonfarm microenterprise and granting access to education and training that would make the poor more productive as entrepreneurs.

3. *Increase the productivity of the poor workers both in wage employment and in self-employment.* Increased productivity leads to an increased demand for wage labor, which is translated into increased employment or wages or both. Increased productivity of the self-employed workers directly raises their income. Increased productivity can therefore provide the labor-dependent households with the means to escape poverty. The principal policy to enhance the productivity of the poor is to endow them with greater human capital, education, and health.

4. *Guaranteeing the poor security of employment at a living wage.* Policy makers have often felt that in a market economy the workers are at a serious disadvantage relative to the employers in terms of the security of both employment and earnings. They have therefore often adopted policies for employment security at regulated wages. In practice, these policies have ranged from an expansion of public employment at administered wages to leg-

islations of minimum wages, conditions of work, and rules for termination of employment for the private sector. Public works programs would also belong to this set of policies.

5. *Income redistribution through the regulation of prices, public distribution, and subsidies.* Policy makers in developing countries have made widespread use of price control, public distribution, and subsidies as methods of protecting vulnerable groups of population from poverty. Thus "essential goods" have often been distributed through the public rationing system at low cost. Goods and services used by the poor for consumption and production have been kept cheap through direct and indirect subsidies. It has been argued that these policies make the real incomes of the poor higher than they would otherwise be, and hence they constitute a powerful weapon for the reduction of poverty. Direct income subsidies and poverty relief in cash and kind would also belong to this group of policies.

Each poverty reduction strategy represents a specific combination of these five groups of policy interventions. Different strategies combine individual policy interventions in different proportions.

III. A Comparison of Poverty Reduction Strategies

In the introductory section we noted that the success in poverty reduction varies from one region and country group to another. To what extent has this variation been due to the different poverty reduction strategies that they adopted? What does this tell us about the effectiveness of different forms of public intervention for the reduction of poverty?

East and South-East Asia. Let us first consider East and South-East Asia. One could make a distinction between China, on the one hand, and the remaining seven countries (South Korea, Taiwan, Hong Kong, Singapore, Indonesia, Thailand and Malaysia) in the group, on the other.[6]

South Korea, Taiwan, Hong Kong, and Singapore have for the last thirty years or more followed an "outward looking" development strategy. In more recent years Indonesia, Thailand, and Malaysia have also gradually moved towards a similar strategy. The strategy is based on the rejection of the system of arbitrary protection of production for the home market and discrimination against exports that the strategy for import-substituting industrialization fosters. In the remainder of this paper we shall use the term ESEA countries (for East and South East Asian) to designate these seven.

There have been differences among the poverty reduction strategies pursued by individual ESEA countries. But there are certain elements that have featured in most of their strategies. Broadly speaking, poverty reduction strategies in these countries have emphasized the first three of the five groups of interventions listed in the preceding section.

All of these countries succeeded in achieving high rates of growth with an emphasis on the efficiency of resource use. The demand for labor increased rapidly in these countries, resulting in the steady growth in real wages.

Most of these countries strongly emphasized the redistribution of assets and other methods to promote productive entrepreneurship among the poor. South Korea and Taiwan started out by implementing highly egalitarian land reforms. Singapore and Hong Kong, being city-

6 Apart from the former Indo-Chinese countries (for which the turbulent history of the recent past and the absence of information act as major reasons for their exclusion from the present analysis) this list excludes one other major country of the region, the Philippines. Both development strategy and poverty outcome in the Philippines have been very different from what they have been in the countries of East and South-East Asia listed above.

states, avoided the need for land reforms. These countries, however, went for an egalitarian distribution of what is perhaps the most important asset in these societies -- housing -- through public housing programs. Malaysia also resorted to considerable redistribution of assets, although the emphasis was on the disadvantaged ethnic groups. Indonesia's agriculture was characterized by peasant landownership with limited inequality. Thailand avoided land reform. But Thailand also had a relative abundance of land.[7]

Taiwan's development strategy is an outstanding example of the promotion of small-scale enterprises. Elsewhere in the region small-scale enterprises received very considerable support. By and large, these countries avoided the disincentive that small-scale enterprises are subjected to, relative to the large-scale enterprises, in a typical import-substituting industrialization strategy.

The ESEA countries have achieved remarkable success in improving the endowment of human capital. Sustained public investment in human development and the encouragement of private investment have resulted in the achievement of a high level of literacy, extensive schooling, and a high standard of public health. The ESEA countries have steadily made their labor force better educated and healthier over the years with rapidly increasing productivity and real earnings.

The ESEA countries have generally avoided using the last two groups of interventions discussed in the preceding section. In these countries the share of the public sector in total employment has generally been small, and employment and wages in the public sector have not been far divorced from market rules. There has been little attempt to regulate the conditions of employment and its termination in the private sector. Minimum-wage legislations have either been nonexistent or set at a sufficiently low level so that their effect was to protect the very vulnerable groups of workers rather than to affect the overall level and structure of wages. The regulation of prices and public distribution have also been generally avoided.

China's record in the reduction of poverty has been remarkable during both the pre-reform period and the post-reform period. There are, however, certain differences in the components of the strategies during the two periods. The emphasis on efficient growth, as a mechanism for the rapid expansion of productive and remunerative employment, has been far greater in the post-reform period than during the pre-reform period. Emphasis on guaranteeing poor peasants access to land was strong during both periods. Maoist China started its economic development strategy by implementing an egalitarian land reform. Chinese reforms at the end of the 1970s similarly started with an egalitarian redistribution of access to the hitherto communally held land. During the post-reform period the emphasis on the access that small entrepreneurs have to productive resources was extended to nonagricultural sectors as well. During both periods, the emphasis on human capital investment was very strong. Maoist China made extensive use of guaranteed employment at regulated wages, regulated prices, and public distribution as instruments for the protection of the poor. These are gradually being dismantled during the post-reform period, although very considerable remnants continue to be in place.

South Asia. The major countries that make up South Asia are India, Pakistan, Bangladesh, Sri Lanka, Nepal, Burma, and Afghanistan. The principal development strategy adop-ted by these countries was industrialization of the import-substituting variety, Afghanistan and Burma having ex-

7 Also, Thailand's record with respect to the *change in inequality* in the distribution of income is the worst among the countries in the group.

perienced little industrialization of any kind. The rates of growth experienced by the region have varied among countries and have ranged from low to moderate. The efficiency of resource use has likewise been low. The growth that took place was not characterized by a high elasticity of labor demand. South Asia's record in the redistribution of land and other assets for the promotion of productive entrepreneurship among the poor has been very weak. Comprehensive land reforms have been unknown. The record of these countries in promoting human capital endowment has also been far poorer than that of ESEA countries.[8]

South Asia made extensive use of the last two sets of interventions listed in section II: regulation of the labor market and the use of price control, public distribution, and subsidies. It has been alleged that the region's failure to achieve higher growth and faster poverty reduction can be substantially traced to these interventions. Regulations of conditions of employment, the termination of private employment, and the level and structure of wages were effective only in the modern sector of the economy. These measures at best succeeded in creating small islands of protected high-cost employment and generally contributed to the low elasticity of labor demand. Price control, rationing, and subsidies created severe distortions which reduced the efficiency of resource use. Moreover, there was little control over the targeting of the benefits of the complex system of direct and indirect subsidies. A substantial portion of the benefits were appropriated by the nonpoor.

Sub-Saharan Africa. Sub-Saharan Africa appears to have failed to effectively implement any of the first three sets of interventions. Its growth performance has been very poor. It did little by way of the redistribution of assets. It had little success in improving the human capital endowment of the poor. Interventions with the labor market, prices, and distribution have been pervasive but with even less focus on the protection of the poor than in the case of South Asia.

Former Centrally Planned Economies. Russia and the former centrally planned economies of Eastern Europe and Central Asia (FCPEs, former centrally planned economies, for short) are now categorized as middle-income developing countries. These countries had achieved very substantial success in reducing poverty before their system of central planning came to be overthrown. Their poverty reduction strategy was based on the last three of the five sets of interventions listed in section II: extensive investment in human capital, guaranteed employment in public enterprises at administered wages, and the widespread regulation of prices and distribution. Although human capital was highly developed, the system does not appear to have made particularly efficient use of this resource, an outcome that was closely related to the policy of guaranteed employment and wages that were administered and not related to productivity or skill. The efficiency of the use of other resources was also low. This too was very closely related to the strategy of regulating prices and distribution to the point that the overall system of incentives was a very poor guide to efficient allocation of resources. One would conclude that the success in poverty eradication was bought at the cost of forgoing economic efficiency, growth, and prosperity.

Unlike Chinese reforms, the reform process in these countries have been accompanied by a severe increase in the incidence of absolute poverty. This is because the inefficient interventions for the protection of the poor -- e.g., regulated prices, public distribution of essential

8 United Nations Development Programme, *Human Development Report 1993* (New York: Oxford University Press, 1993).

goods, and subsidies -- have been substantially removed without any offsetting interventions for the protection of the poor. Unlike post-reform China, in the FCPE countries, the reform process witnessed a sharp deceleration in the already low rate of growth of their economies. Almost without exception, these economies experienced large annual declines in their national products. Also unlike China, there was little by way of granting the poor access to productive resources. The FCPE countries lack a coherent strategy for the protection of the poor. Economic reform requires the dismantling of the past system of inefficient egalitarianism. To do this without aggravating poverty, it would be necessary to implement some of the efficient poverty-alleviating policies in the list outlined in section II, principally the generation of efficient growth leading to higher productivity and remuneration of the workers.

Unfortunately the reform program has failed not only to promote higher growth but also to prevent a precipitate decline in output and income. Together the decline in aggregate output and the increase in inequality due to the dismantling of inefficient egalitarianism led to a sharp rise in the incidence of poverty. Since an increase in the incidence of poverty beyond a point was not politically tolerable, the process of dismantling the system of inefficient egalitarianism was halted. Thus, for example, the old system of guaranteed employment was granted a further lease on life. Despite a decline in national output by a quarter to a third, the level of employment in these economies showed insignificant decline until very recently. The failure to deal with the problem of rising poverty has therefore effectively put a halt to the reform process itself.

Latin America. Latin America's growth performance was very good until the end of the 1970s, although the efficiency of resource use was not high, given that import-substituting industrialization was the dominant development strategy. The elasticity of demand for employment was not high enough to avoid a high and often rising rate of unemployment. During the 1980s the growth performance of Latin America worsened a great deal as GNP growth rates in these countries fell below the rates of growth of their population. The Latin American countries generally have a poor record of redistribution of assets and promotion of entrepreneurship among the poor through an expansion of their access to productive resources. Their record in endowing the poor with human capital is also mixed: it is rather poor for Brazil, the largest country in the region, but good to moderate for Costa Rica, Uruguay, Chile, Argentina, and Mexico. The region made extensive use of the last two of the five sets of interventions discussed in section II -- public intervention in the labor market and the regulation of prices, distribution and subsidies.

North Africa and the Middle East. The growth performance of North Afri-ca and the Middle East was very good until the end of the 1970s and disastrous during the 1980s. The efficiency of resource use in these countries is unlikely to have been high. The growth in employment in the major countries, such as Egypt, has been highly inadequate. Several countries in the region, notably Egypt, resorted to land reform and other redistributive measures. But, by and large, the development strategies failed to ensure widespread promotion of entrepreneurship among the poor through an expansion of their access to other productive resources. Compared to their levels of income per capita, these countries have generally had very low levels of human development, a fact that is illustrated by the lower ranks of these countries in terms of human development than in terms of per capita income.[9] It is reasonable to surmise that the

9 Ibid.

human capital endowment of the poor in these countries has been rather low. Most countries in this group have made extensive interventions in the labor market and in the direct regulation of prices and distribution and the use of public subsidies as measures to redistribute income and reduce poverty. Only very recently have some of these countries started to move away from an extreme dependence on these interventions.

IV. Some Lessons

A simple juxtaposition of the performance in poverty reduction against the composition of poverty reduction strategies for the different regions/country groups points to the conclusion that the first three sets of interventions are far more effective than the last two in alleviating poverty.

Efficient growth leading to a rapid expansion in productive employment at steadily rising real rates of remuneration has been the single most important source of poverty reduction in ESEA countries and probably in post-reform China. The great attraction of this source of poverty reduction is that it is sustainable. It does not create a fiscal burden for the state. The ESEA experience also underlines that it is a delusion to believe that the market, left to itself and free from distortions created by arbitrary public intervention, will lead to this kind of growth. The ESEA experience clearly brings out the indispensable role of the state in actively and imaginatively promoting this kind of growth.[10] Among the interventions necessary for this to happen are the provision of infrastructure, both physical and social, and the creation of a system of incentives that encourages accumulation, the direction of investment to socially productive activities, and the prevalence of a technology that makes adequate use of labor. Obsessive preoccupation with allocative efficiency is not conducive to the kind of imaginative activism that is necessary for the state to effectively fulfill this role. The essence of the ESEA experience is that the point is not to avoid intervention with the market but to make interventions that are purposeful and consistent with efficient growth. What must be avoided are policies and distortions that are inconsistent with efficient growth, such as discrimination against exports, protection of industries selling in the domestic market by insulating them from external competition, and overt distortion of factor and product prices that restricts the use of labor and other abundant factors.

Redistributive policies to grant the poor access to productive assets can be a powerful instrument for the alleviation of poverty, especially when this is done in the context of an overall strategy of efficient growth. This can become an indispensable component of the poverty reduction strategy if the initial resource endowment is characterized by very low land/labor and asset/labor ratios. Unless assets are redistributed in favor of the poor, "efficient" growth in the market could easily result in a highly skewed distribution of income in favor of the few owners of scarce assets.

Human capital endowment should be seen as an extension of the strategy of redistributing assets. Productivity of human capital is very high, and its initial endowment in a poor country is rather low. An increase in the human capital endowment of the poor therefore assures an increase in the poor's income entitlement. That the ESEA countries -- notably South Korea -- were able to achieve a steady and rapid rise in real wages long before the completion of the Lewis transition must be explained by a rise in labor productivity across the entire economy, triggered by a rise in human capital endowment per member of the labor force.

Labor market interventions -- the provision of employment security in the public sector to increasing numbers of workers,

10 World Bank, *The East Asian Miracle* (New York: Oxford University Press, 1993).

regulation of security and condition of employment in the private sector, and minimum-wage legislation -- are almost always ineffective as instruments for poverty reduction. In a typical developing country the government is incapable of implementing these measures outside the small modern sector. These policies inevitably lead to a rise in the cost of labor and thereby reduce the growth of productive employment in the modern sector. They also adversely affect the efficiency of technology and the flexibility of industries to restructure in response to external shocks.

This should not mean complete absence of state intervention in the labor market. The need for one very important form of intervention -- investment for the improvement of the human capital endowment of the members of the labor force -- has already been emphasized. Workers, especially the vulnerable groups, must also be protected from the monopoly power of the employers. To that extent there may be a strictly limited role for measures such as minimum-wage legislation, although these measures must not be used to exert an overt upward pressure on the average level of wages or distort the structure of wages. Another kind of labor market intervention that may have a favorable effect on poverty reduction is public works programs. Such programs should, however, be organized for the purpose of productive capital construction based, as far as possible, on market rules and not as relief programs merely to supplement the consumption of the poor.

Regulation of prices, distribution, and subsidies are usually highly ineffective as poverty reduction measures. Typical programs -- subsidized food and housing, for example -- have serious adverse effects on production incentives. Targeting these direct and indirect subsidies to the poor is a virtually impossible task given the poor state of information about the location of the poor and the limited administrative capability in reaching them. In reality, these difficulties are exacerbated by the manipulation of the powerful groups that almost always succeed in redistributing these benefits in their favor. Even in socialist China the aggregate of all subsidies makes the distribution of income more unequal than would be the case in the absence of subsidies.[11] The argument that direct and indirect subsidies are a substitute for the redistribution of assets, and are feasible while redistribution of assets is not, is patently false. The political forces that make a redistribution of assets impossible can be trusted to successfully bid for these subsidies as well.

Once again, not all subsidies are ineffective in protecting the poor. A means-and-needs-tested income subsidy for the very poor would be extremely useful to eradicate poverty among those groups (such as households with unfavorable labor endowment) who cannot benefit from employment and production opportunities. It is, however, important to make sure that the government has the ability to implement these subsidies and to prevent their degeneration into unfocused programs whose benefits are appropriated by the nonpoor. It is a good general rule that the access of the poor to a resource is best ensured by avoiding its underpricing. The powerless poor can never successfully compete with the powerful rich for the scarcity premia that exist in an economy.[12]

11 A.R. Khan, K. Griffin, C. Riskin, and Zhao Renwei, "Household Income and Its Distribution in China," *The China Quarterly*, December 1992.

12 The Grameen Bank in Bangladesh provides credit to the landless workers engaged in nonfarm activities at a rate of interest that is higher than the interest charged by other institutional sources of credit. The present writer has argued that one of the principal reasons why the poor have been the beneficiaries of the Grameen Bank program is that its credit has not been underpriced. For an analysis of many novel features of this program, see Mahahub Hossain, *Credit for the Rural Poor: The Experiences of the Grameen Bank in Bangladesh* (Dhaka: Bangladesh Institute of Development Studes, 1984).