

2

INEQUALITY AND HUMAN DEVELOPMENT

**“There are only two families in the world, as my grandmother used to say: the haves and the have-nots.”**

**Sancho Panza in *Don Quixote de la Mancha*, Miguel de Cervantes**

Across many of the MDGs poor people are being left behind

“What is it that impels the powerful and vocal lobby to press for greater equality?” asked Margaret Thatcher, then UK prime minister, in 1975. She offered her own answer: “Often the reason boils down to an undistinguished combination of envy and bourgeois guilt.”<sup>1</sup> Plato took a different view. Writing in the fifth century BC he warned Athenian lawmakers of the threat posed by extreme inequality. “There should exist among the citizens neither extreme poverty nor again excessive wealth”, he wrote, “for both are productive of great evil.”<sup>2</sup>

Two contrasting views on a question that retains a powerful relevance today: does inequality matter? If so, why? In this chapter we argue that inequality matters because it is a fundamental issue for human development. Extreme inequalities in opportunity and life chance have a direct bearing on what people can be and what they can do—that is, on human capabilities. Children facing a higher risk of death because they are born into a low-income or indigenous household or because they are female, for example, clearly have less opportunity to realize their potential. Inherited disadvantage in opportunity is wrong for intrinsic reasons: it violates basic precepts of social justice. There are also strong instrumental reasons for a concern with inequality. Deep disparities based on wealth, region, gender and ethnicity are bad for growth, bad for democracy and bad for social cohesion.

They are also bad for the Millennium Development Goals (MDGs). The MDGs do not directly address inequality. In this sense they are distribution neutral. Progress is measured by aggregating and averaging change at a national level. In theory, the MDGs could be met even if, say, households with low incomes were falling behind on the income poverty and health targets, or if the rate of reduction in child deaths among boys was sufficient to compensate for a slower rate of reduction among girls.

The distributional blind spot of the MDGs is a weakness on two counts. First, the MDGs themselves are rooted in ideas about global justice and human rights. They are universal entitlements, not optional or discretionary allowances. It follows that progress should be for all, regardless of economic status, gender, parents' wealth or location in a country. Yet the MDGs do not remind governments that success in advancing towards the MDGs should be measured for all of society, and not just in the aggregate. The opportunities that shape the distribution of income, education, health and wider life chances in any society are not randomly distributed. As we show in this chapter, the disparities hampering progress towards the MDGs are systemic. They reflect complex hierarchies of advantage and disadvantage that are transmitted across generations—and they reflect public policy choices.

The second reason for a focus on inequality relates to progress within the MDG framework. Across many of the MDGs poor people are being left behind. As we show in this chapter, a recurring theme in data from a large group of countries is that progress among the poorest 20% of the population is far below the national average. Apart from being unjust, this is sub-optimal from the perspective of MDG attainment. People who are poor account for a far

The idea that people should be consigned to an early death, illiteracy or second-class citizenship because of inherited attributes beyond their control violates most people's sense of what is fair

larger share of deprivation than people who are not. It follows that accelerated progress among poor people is one of the most effective routes to faster national progress. Put differently, current patterns of progress are slowing the overall advance because the smallest gains are being registered among the households that account for the biggest part of the problem.

These considerations have important implications for the design of MDG strategies. For many of the MDGs the jury is now in, with the evidence that a “trickle down” approach to reducing disparities and maintaining overall progress will not work. The MDGs set quantifiable targets that lend themselves to policy responses rooted in technical and financial terms. Ultimately, however, the real barriers to progress are social and political. They are rooted in unequal access to resources and distribution of power within and

among countries. Unless these inequalities are corrected, the first principles of the Millennium Declaration—commitment to social justice, equity and human rights—from which the MDGs are derived will not be translated into progress in human development at the required rate. The appropriate response is to ensure that inequality and the measures to overcome disparities in life chances figure more prominently in the design of poverty reduction strategies.

This chapter sets out the reasons why inequality matters. It then looks at different dimensions of inequality and shows how interlocking inequalities in income, health and education disadvantage the poor. It concludes by showing how even modest moves towards greater distributional equity could advance human development and accelerate progress towards the MDGs.

## Why inequality matters

Ideas about inequality, like ideas about fairness and social justice, are rooted in values. As Amartya Sen has argued, virtually everybody today believes in equality of something: equal rights before the law, equal civil liberties, equality of opportunity and so on.<sup>3</sup> Similarly, most people would accept that not all inequalities are unjust. Inequality in income is an inevitable product of any functioning market economy, though there are questions about the justifiable extent of income inequality. At the same time, few people would accept in principle that inequalities in opportunity are tolerable when based on gender, inherited wealth, ethnicity or other accidents of birth over which individuals have no control. The idea that people should be consigned to an early death, illiteracy or second-class citizenship because of inherited attributes beyond their control violates most people's sense of what is fair.<sup>4</sup>

From a human development perspective there are a range of mutually reinforcing

intrinsic and instrumental reasons why inequality matters. These can be broadly summarized under five headings.

### Social justice and morality

The view that there are limits to tolerable deprivation is fundamental to most societies and value systems. Adam Smith powerfully expressed the basic concept: “No society can be flourishing and happy”, he wrote, “of which the far greater part of members are poor and miserable.”<sup>5</sup> It was Smith who went on to elaborate the idea of relative poverty, arguing that all members of society should have an income sufficient to enable them to appear in public “without shame”. All major religions express concerns with equity and place obligations on their adherents to address extreme deprivation as a moral duty. Public ideas reflect wider normative concerns. Opinion surveys show that more than 80% of the public in (very unequal)

Latin America believe that the gap between rich and poor is too large, with only a slightly smaller share echoing this concern in the (less unequal) United Kingdom.<sup>6</sup> While few of the respondents to these surveys might be able to indicate what an acceptable level of inequality would be, the surveys point clearly to an underlying perception of social justice.

### Putting the poor first

Pareto efficiency or optimality—one of the core ideas of modern economics—declares that only a change that leaves nobody worse off can be declared “welfare enhancing”. Redistribution from rich to poor is not a “Pareto improvement”, because by definition it makes someone worse off. But, as Amartya Sen has said: “A society can be Pareto optimal and still be perfectly disgusting.”<sup>7</sup> That sentiment powerfully captures the idea that there are limits to the acceptable level of inequality.

In fact, economics itself provides strong arguments for redistribution. Most people, and most democratically elected governments, accept in principle that more weight should be given to improvements in the well-being of the poor and disadvantaged than to the rich and highly privileged.<sup>8</sup> An economy’s income is not a sufficient statistic for evaluating welfare, precisely because it ignores the distribution of income generated by growth. The idea of diminishing returns to increased wealth provides a framework for understanding a simple idea: an extra dollar in the hands of a landless agricultural labourer in South Asia or an urban slum dweller in Latin America generates greater welfare than an equivalent amount in the hands of a millionaire. In fact, a policy that increases the income of the poor by \$1 can be worthwhile, even if it costs the rest of society more than \$1. From this perspective it might make sense for governments choosing between alternative growth paths to choose the option that generates the biggest return to the poor, even where overall growth effects are less certain.

Beyond income, many of the same arguments apply. For example, most people would accept in principle that an additional unit of

public spending directed towards reducing child deaths or extending access to primary school would be preferable on social grounds to a similar amount spent on transfers to services for high-income groups.

### Growth and efficiency

If there were a trade-off between growth and distribution, governments would face tough choices: the welfare-enhancing gains of greater equity could be eliminated by the losses associated with lower growth. In fact, the evidence suggests that the trade-offs work in the other direction. Extreme inequality is not just bad for poverty reduction—it is also bad for growth. Long-run efficiency and greater equity can be complementary. Poor people remain poor partly because they cannot borrow against future earnings to invest in production, the education of their children and assets to reduce their vulnerability. Insecure land rights and limited access to justice can create further barriers to investment.

Deprived of public goods—such as information and legal rights—poor people are denied opportunities to contribute to growth. They enter markets on unequal terms and leave them with unequal rewards. Where extreme inequalities based on wealth, gender or region leave a large section of society with insufficient assets and endowments, society as a whole suffers from the resulting inefficiency. Denying half the population access to education opportunities is not just a violation of human rights. It is also bad for growth. Gender-based education inequalities have held back Pakistan’s economic development, for example. Allowing unequal asset distribution to perpetuate mass poverty is clearly bad for poor people, but it also restricts the development of investment opportunities and markets for the rest of society.

### Political legitimacy

Extreme inequalities also weaken political legitimacy and corrode institutions. Inequalities in income and human capabilities often reflect inequalities in political power. Disadvantaged

Extreme inequality is not just bad for poverty reduction—it is also bad for growth

Absolute poverty and inequality may be different, but they are intimately related

groups—poor people, women, rural populations, indigenous communities—are disadvantaged partly because they have a weak political voice, and they have a weak political voice because they are disadvantaged.

Where political institutions are seen as vehicles for perpetuating unjust inequalities or advancing the interests of elites, that undermines the development of democracy and creates conditions for state breakdown. In countries such as Bolivia and Ecuador conflicts over natural resources management have, at a more fundamental level, become a focal point for disadvantaged indigenous groups denied a political voice by institutions that are seen as unresponsive.

### Public policy goals

Most societies see reducing poverty and removing unjust inequalities as important goals for public policy. Extreme disparities undermine the pursuit of these goals. As we show in this chapter, extreme inequalities in income limit the rate at which growth can be converted into lower levels of poverty. Similarly, extreme disparities in health and education reduce the scope of disadvantaged groups to take advantage of opportunities for improving welfare.

### Counter-arguments—countered

There are counter-arguments to the claim that inequality matters. Some libertarians deny the existence of “social justice”. The free market theorist F.A. Hayek famously argued that it was nonsense to talk about resources being fairly or unfairly distributed. On his account it was up to free markets, not human agency, to determine the appropriate allocation of wealth and assets. This perspective overlooks the role of human agency and unequal power relationships in structuring markets.

Another widely held view is that some inequalities matter more than others and that equality before the law matters first and foremost.<sup>9</sup> However, rights and freedoms cannot stand alone. People are likely to be restricted in what they can do with their freedom and their

rights if they are poor, ill, denied an education or lack the capacity to influence what happens to them. To be meaningful, formal equalities have to be backed by what Amartya Sen has called the “substantive freedoms”—the capabilities—to choose a way of life and do the things that one values. Deep inequalities in life chances limit these substantive freedoms, rendering hollow the idea of equality before the law.

Others have argued that the proper focus for social justice is absolute deprivation, not distribution. Where poor people stand in relation to others, so the argument runs, is less important than their command over income or access to health and education services. “We are against poverty,” runs the common refrain, “but inequality is a different matter, and nothing to do with social justice or the MDGs.” This argument too is flawed. Absolute poverty and inequality may be different concepts, but they are intimately related. Disparities in life chances define prospects for escaping poverty. For example, inequality in access to healthcare, education or political rights can diminish an individual’s prospects for escaping poverty. In this chapter we examine some of the basic disparities that interact with poverty. What links these diverse disparities is that they are rooted in inequalities in power that perpetuate deprivation and destitution. The “pathologies of power”, as one author has described them, are at the very core of the processes that are driving countries off track for the MDGs.<sup>10</sup>

As we show later, progress towards the reduction of absolute poverty is heavily conditioned by inequality. This is true not just for income, but also for wider inequalities in areas such as health, education and politics. Moreover, the idea that poverty and human welfare can be defined solely in absolute terms to the exclusion of relative considerations flies in the face not just of attitude survey evidence, but of basic ideas elaborated in 1776 by Adam Smith. Smith forcefully argued that relative distribution is integral to any assessment of human welfare: “By necessities I understand not only the commodities necessary for the support of life, but whatever the custom of the country renders it necessary for creditable people, even of

the lowest order, to be without. A linen shirt, for example, is strictly speaking not a necessity of life....But in present times, throughout the

greater part of Europe, a creditable day labourer would be ashamed to appear in public without a linen shirt.”<sup>11</sup>

## Chains of disadvantage—inequality within countries

Chapter 1 looked at inequalities between rich and poor countries. These inequalities are mirrored within countries. Deep human development disparities persist between rich people and poor people, men and women, rural and urban areas and different regions and groups. These inequalities seldom exist in isolation. They create mutually reinforcing structures of disadvantage that follow people through life cycles and are transmitted across generations.

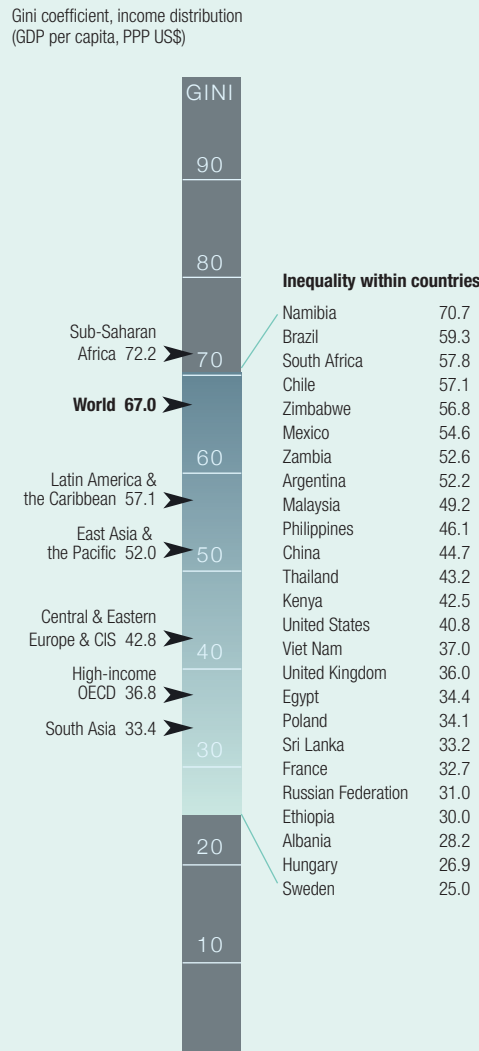
Income inequality varies markedly across regions. In broad terms Latin America and Sub-Saharan Africa register very high levels of inequality, while South Asia and Organisation for Economic Co-operation and Development (OECD) countries register much lower levels. Although there are no clear threshold points, countries with Gini coefficients above 50 can be said to be in the high inequality category (figure 2.1).

Cross-country evidence is often cited in support of the proposition that, on average, inequality changes very little over time. That proposition is misleading in important respects. While it is difficult to compare different surveys across countries and time, there has been a clear trend over the past two decades towards rising inequality within countries. Of the 73 countries for which data are available, 53 (with more than 80% of the world’s population) have seen inequality rise, while only 9 (with 4% of the population) have seen it narrow.<sup>12</sup> This holds true in both high- and low-growth situations (such as China in the first case and Bolivia in the second) and across all regions.

Differences in the Gini coefficient relate to differences in the share of national wealth captured by the poorest people. In broad terms the higher the Gini coefficient, the lower is the share of national income captured by the poorest

sections of society. The poorest 20% of the population in low-inequality countries such as Indonesia and Viet Nam capture three to four times

**Figure 2.1** Inequality in income—selected countries and regions



Source: Regional data, Dikhanov 2005; country data, indicator table 15.



more national income than their counterparts in high-inequality countries such as Guatemala and Peru (figure 2.2). While income gaps between countries account for the lion's share of global inequality, income disparities within many countries rival in scale the inequalities in global income distribution. In Brazil the poorest 10% of the population account for 0.7% of national income, and the richest 10% for 47%. Inequalities within Sub-Saharan Africa are also very large. In Zambia, for example, the ratio of the income of the richest to the poorest 10% is 42:1.

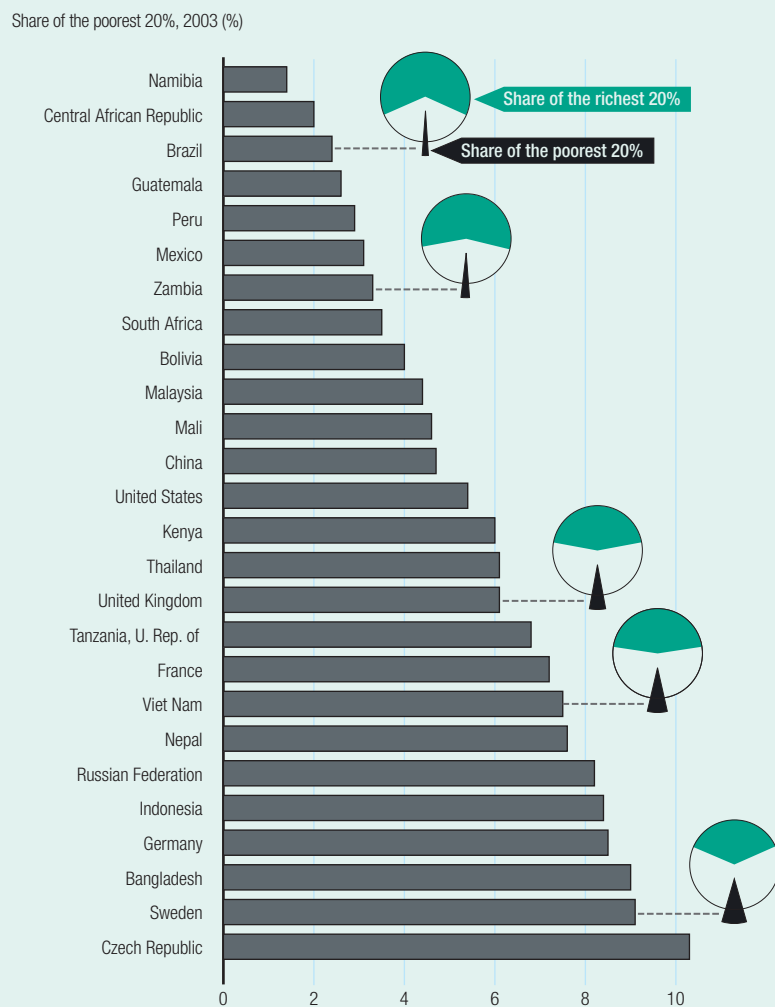
Distribution patterns have an important bearing on the relationship between average incomes and poverty levels. A more nearly equal distribution can mean that poor people in countries

with low levels of inequality have higher incomes than poor people in countries at higher average income levels. This provides a clear example of how distribution affects absolute poverty. For example, average income in Brazil is three times higher than average income in Viet Nam. But the poorest 20% of Brazilians have an income well below the average income in Viet Nam and comparable to the income of the poorest 20% of that country (figure 2.3). The poorest 20% of the population in the United Kingdom have an income comparable to that of the poorest 20% in the Czech Republic, a far less wealthy country.

As these comparisons suggest, average incomes obscure the effects of distribution patterns on real welfare. The human development index (HDI) is also an average indicator. In this sense it too provides a picture of what is happening to the hypothetical average person in a country, not to the average poor person. This can be demonstrated through a simple exercise. Adjusting the income component of the HDI from average income to average income of the poorest 20%, holding everything else constant—including the health and education scores—drops Brazil 52 places in the HDI ranking (to 115) and Mexico 55 places (to 108).

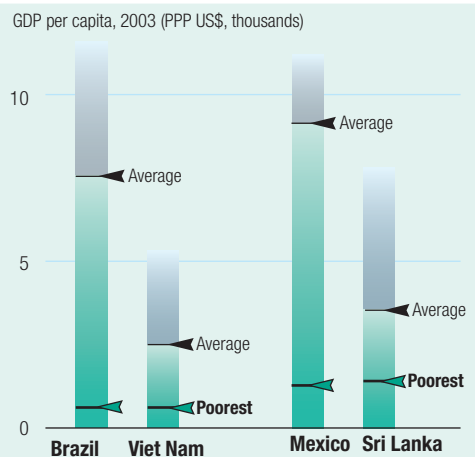
Comparisons between low-income countries and high-inequality countries are revealing in another way. They highlight how, at any given

**Figure 2.2** Slicing the income pie



Source: Indicator table 15.

**Figure 2.3** How the poor fare—average income matters, but so does inequality



Source: Calculated on the basis of data on GDP per capita (PPP US\$) from indicator table 14 and data on the income share of the poorest 20% from indicator table 15.



level of average income, more equitable distribution can be associated with lower poverty levels. One way to illustrate this is to consider how the incomes of different parts of the overall distribution in a country might change if the distribution patterns of a more equal country were imposed. Currently, the poorest 20% of the population in Guatemala have an average income of \$550 a year, or 46% below the \$2 a day international poverty line. Were this group to capture the same share of national income as the poorest 20% in Viet Nam, their average incomes would rise to \$1,560, or 66% above the \$2 a day line.<sup>13</sup> Of course, it could be argued that this example ignores the potentially negative effects on growth and hence on the overall size of the economy of a transition to greater equity in Guatemala. But the example of Viet Nam, a dynamic, high-growth economy with lower inequality, suggests that there may be positive benefits for Guatemala, which has experienced two decades of low growth.

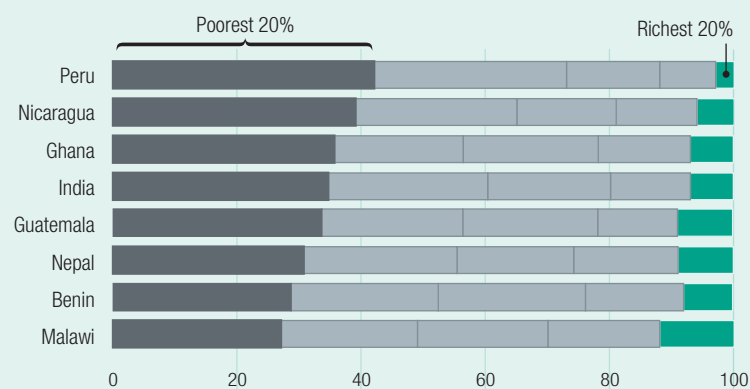
Income inequalities both reflect and affect wider life chance inequalities, starting with the chance of staying alive.<sup>14</sup> In Bolivia and Peru infant death rates are four to five times higher for the children of the poorest 20% of the population than the children of the richest 20%. With more births, the poor are heavily over-represented in the distribution of child deaths (figure 2.4). This is a stark demonstration of how inequality deprives people of substantive freedoms and choices, regardless of their formal legal rights and freedoms.

Wealth-based differences are the first link in a cycle of inequality that tracks people through their lives. Women in poor households are less likely to receive antenatal care and less likely to have their births attended by a trained medical assistant (figure 2.5). Their children are less likely to survive or to complete school. Children who do not complete school are more likely to have lower incomes. Thus the cycle of deprivation is transmitted across generations.

In rich countries, too, basic life chances are unequally distributed. Chapter 1 highlighted the chasm in life chances separating the average person in a rich country from the average person in a poor country. Beyond this chasm, some deprived groups in the “First World” have life chances comparable to the average in

**Figure 2.4** Children of the poorest are most likely to die

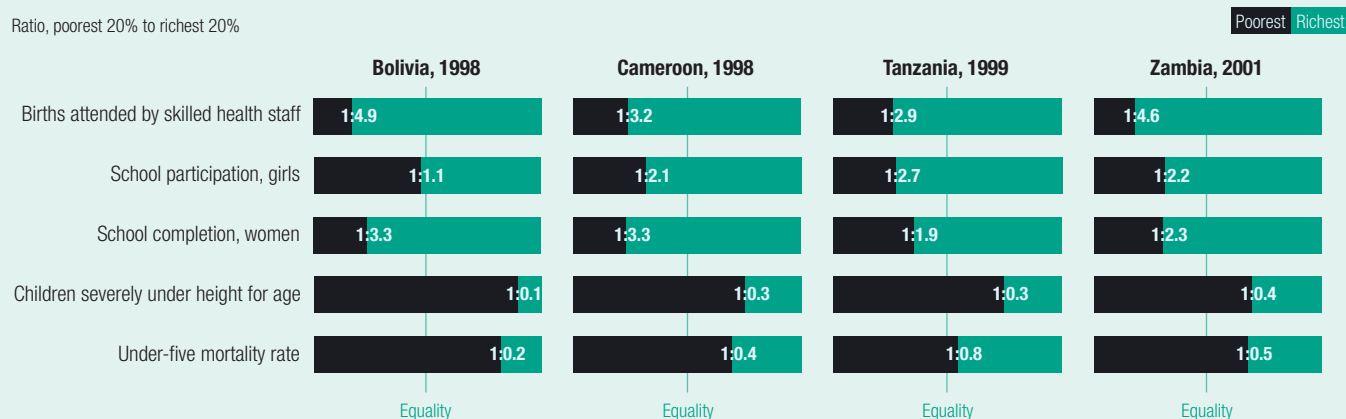
Share of deaths of children under age 5, by wealth quintile (%)



Source: Calculated on the basis of data on under-five mortality rates and births from Gwatkin and others forthcoming.

**Figure 2.5** The cycle of inequality—from birth to young adulthood, the poor fare worse

Ratio, poorest 20% to richest 20%

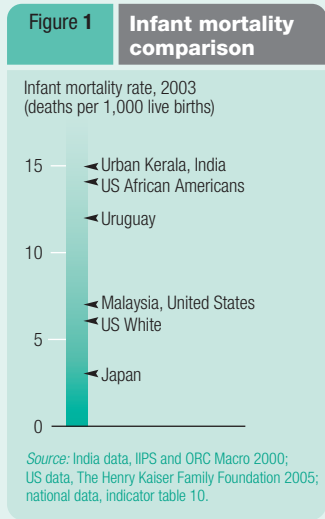


Source: Gwatkin and others forthcoming.

**Box 2.1 Inequality and health in the United States**

The United States leads the world in healthcare spending. On a per capita basis the United States spends twice the Organisation for Economic Co-operation and Development average on healthcare, or 13% of national income. Yet some countries that spend substantially less than the United States have healthier populations. US public health indicators are marred by deep inequalities linked to income, health insurance coverage, race, ethnicity, geography and—critically—access to care.

Key US health indicators are far below those that might be anticipated on the basis of national wealth. Infant mortality trends are especially troublesome. Since 2000 a half century of sustained decline in infant death rates first slowed and then reversed. The infant mortality rate is now higher for the United States than for many



other industrial countries. Malaysia—a country with an average income one-quarter that of the United States—has achieved the same infant mortality rate as the United States (figure 1). And the Indian state of Kerala has an urban infant death rate lower than that for African Americans in Washington, DC.

Wide differences in health across socio-economic groups partly explain the poorer health outcomes in the United States than in other industrial countries.

From the cradle to the grave the health of US citizens shows extreme divergence. For example, racial and ethnic health disparities are persistent—a result of differences in insurance coverage, income, language and education, among other factors (figure 2). African American mothers are twice as likely as white mothers to give birth to a low birthweight baby. Their children are twice as likely to die before their first birthday. Income differences are closely correlated with health differences. A baby boy from a family in the top 5% of the US income distribution will enjoy a life span 25% longer than a boy born in the bottom 5%.

Many factors contribute to health inequalities. One important driver is the coverage of healthcare provision. The United States is the only wealthy country with no universal health insurance system. Its mix of employer-based private insurance and public coverage has never reached all Americans. While more than half the population have health insurance coverage through their employers and almost all the elderly are covered through Medicare, more than one

in six non-elderly Americans (45 million) lacked health insurance in 2003. Over a third (36%) of families living below the poverty line are uninsured. Hispanic Americans (34%) are more than twice as likely to be uninsured as white Americans (13%), and 21% of African Americans have no health insurance. Health insurance coverage also varies widely across the 50 states, depending on the share of families with low incomes, the nature of employment and the breadth of each state's Medicaid programme for low-income people.

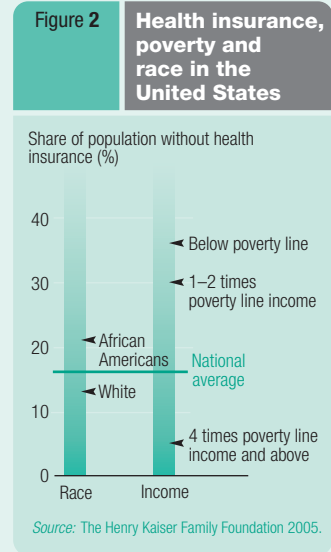
More than in any other major industrial country the cost of treatment is a major barrier to access in the United States. Over 40% of the uninsured do not have a regular place to receive medical treatment when they are sick, and more than a third say that they or someone in their family went without needed medical care, including recommended treatments or prescription drugs, in the last year because of cost.

Unequal access to healthcare has clear links to health outcomes. The uninsured are less likely to have regular outpatient care, so they are more likely to be hospitalized for avoidable health problems. Once in a hospital, they receive fewer services and are more likely to die than are insured patients. They also receive less preventive care. The Institute of Medicine estimates

that at least 18,000 Americans die prematurely each year solely because they lack health insurance. Being born into an uninsured household increases the probability of death before age 1 by about 50%.

Unequal access to healthcare has a powerful effect on health inequalities linked to race, which are only partly explained by insurance and income inequalities. One study finds that eliminating the gap in healthcare between African Americans and white Americans would save nearly 85,000 lives a year. To put this figure in context, technological improvements in medicine save about 20,000 lives a year.

The comparison highlights a paradox at the heart of the US health system. High levels of personal healthcare spending reflect the country's cutting-edge medical technology and treatment. Yet social inequalities, interacting with inequalities in health financing, limit the reach of medical advance.



Source: Rowland and Hoffman 2005; Proctor and Dalaker 2003; Munnell, Hatch and Lee 2004; The Henry Kaiser Family Foundation 2005; Deaton 2002.

countries at far lower levels of income. Poorer people die younger and are sick more often. Men in the top 5% of the income distribution in the United States live about 25% longer than men in the bottom 5%.<sup>15</sup> Meanwhile, high levels of health spending have failed to eradicate large disparities in infant death rates based on race, wealth and state of residence. These disparities have limited progress in reducing infant mortality. The infant mortality rate in the United States compares with that in Malaysia—a country with a quarter the income. Infant death rates are higher for African American children in Washington, DC, than for children in Kerala, India. While other socio-economic factors are involved, financial barriers to adequate health-care are an important contributor (box 2.1).

### Layers of inequality constrain life choices

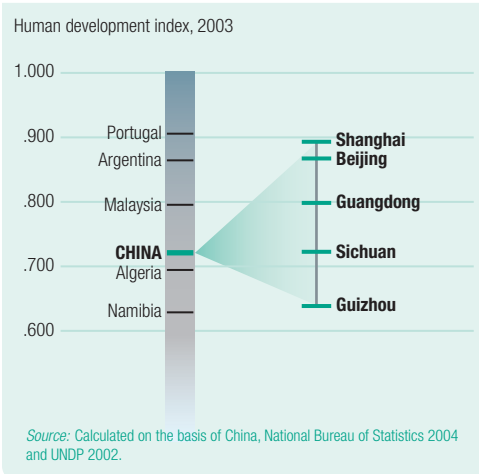
Life chances in any country are constrained by complex layers of inequality. Disparities in opportunities for health, education, income and political influence are to be found in every country, in varying magnitudes. Inequalities linked to wealth, gender, location, race and ethnicity, along with other markers for disadvantage, do not operate in isolation. They interact to create dynamic and mutually reinforcing cycles of disadvantage that are transmitted across generations. Breaking these cycles is one of the keys to accelerated progress towards the MDGs.

### Regional inequalities

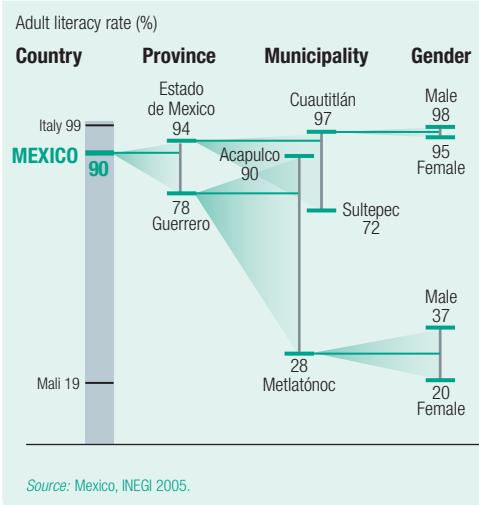
In many countries regional disparities are a major source of inequality. In Brazil the infant mortality rate is 52 deaths per 1,000 live births in the north-east but drops to 20 deaths in the south-east. The 10 municipalities with the lowest infant mortality rates have an average of 8 deaths per 1,000 live births—a level comparable to that in some high-income countries. The 10 worst municipalities have a death rate of 117 deaths per 1,000 live births, which is higher than in Bihar, India. Per capita spending on health is inversely related to the infant mortality rate: it is twice as high in the south-east as in the north-east.<sup>16</sup>

Breaking down national HDIs graphically reveals the scale of regional inequality within countries. The HDI in China ranges from 0.64 in Guizhou to 0.80 in Guangdong and 0.89 in Shanghai (figure 2.6). If they were countries, Guizhou would rank just above Namibia and Shanghai alongside Portugal. The HDI in Mexico ranges from 0.71 in Chiapas and 0.72 in Oaxaca to 0.89 in Mexico City, a range that extends from El Salvador to the Republic of Korea. Education differences are one explanation. Illiteracy rates range from 3% in Mexico City to more than 20% in Chiapas and Guerrero. Figure 2.7 uses an inequality tree to investigate inequalities below the state

**Figure 2.6** Human development differences among China's provinces



**Figure 2.7** The two worlds of Mexican education



level in Mexico. The richest municipalities in Guerrero, such as the resort of Acapulco, have literacy levels comparable to those in high-income countries, and with limited gender gaps. Meanwhile, in the predominantly rural, indigenous and mountainous municipalities literacy levels fall to 28%—half the level in Sudan—and to 20% for women. Inequality trees provide a way of tracking the complex patterns of inequality that operate beneath the national average.

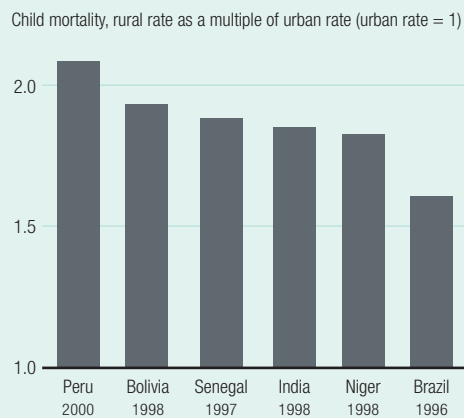
### Urban-rural disparities

Living in a rural area is, in many countries, a marker for disadvantage. Poverty rates are

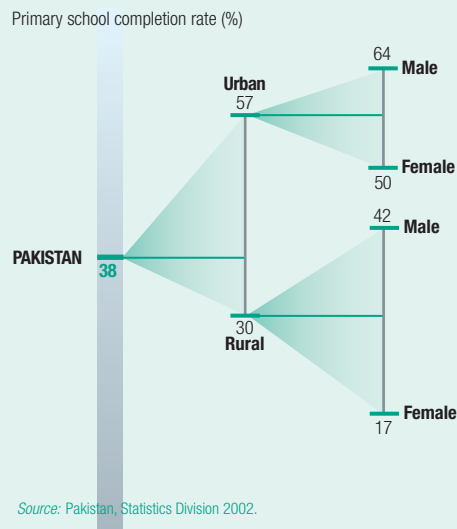
higher, and access to services is lower. In Ghana the incidence of poverty is 2% in the capital city of Accra but 70% in the rural savannah. The rural savannah accounts for one-fifth of Ghana's population, but two-fifths of the population living in poverty. While poverty has been declining in Accra, it has remained unchanged in the savannah.<sup>17</sup>

Ghana's rural-urban divide is equally marked in access to basic services. One in five rural residents has access to piped water compared with four in five urban residents. Death rates for children under age 5 are far higher in rural areas, reflecting a higher incidence of poverty and more limited coverage of basic services. In Bolivia death rates are nearly 1.9 times higher among rural children than among urban children (figure 2.8). The rural-urban divide magnifies gender inequalities, dramatically so in many countries. In Pakistan the rural-urban gap in school attendance is 27 percentage points, but the gap between rural girls and urban boys is 47 percentage points (figure 2.9). In many countries the rural-urban divide also exacerbates inequalities within and between groups. Indigenous people in Guatemala are far more likely to live in poverty, but rural indigenous people have an incidence of poverty almost five times the average for urban non-indigenous people (figure 2.10).

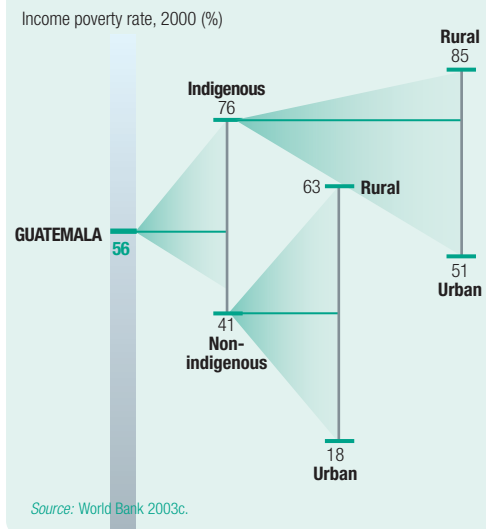
**Figure 2.8** Rural children face greater risk of mortality



**Figure 2.9** School completion in Pakistan



**Figure 2.10** Poverty in Guatemala—ethnicity and location



## Gender inequality

Gender disparities are among the deepest and most pervasive of inequalities. They are revealed most brutally in parts of South Asia. In India the mortality rate among children ages 1–5 is 50% higher for girls than for boys. These girls, deprived of life because they were born with two X chromosomes, are among the 100 million “missing women” in South Asia. The higher mortality rates among girls and women from birth to about age 30 inverts the normal demographic gender balance, pointing to structural inequalities in nutrition, healthcare and status.

Income inequality reinforces unequal health outcomes for women. In Indonesia maternal mortality ratios are four times higher among women in the poorest 20% of the population than among women in the richest 20%. Women who die during pregnancy are twice as likely to be unschooled and 50% less likely to have access to clean water.<sup>18</sup> Across the developing world poor women are less likely than women in higher income groups to have their births attended by a trained assistant—a key indicator for maternal mortality. In Peru and Yemen women in the richest 20% of the population are six to seven times more likely to have births attended by trained assistants than are women in the poorest 20%. Gender-based inequalities, including infant mortality, link back to wider life chance inequalities. In Burkina Faso infant mortality rates are three times higher for children of uneducated mothers than for children of educated mothers.

The very visible disparities in human development described here are the product of deeper structural inequalities, including less visible inequalities in power. Empowerment of the poor is both an instrument to reduce poverty and, because participation in society is a dimension of human development, an aspect of poverty reduction. Poor people and disadvantaged groups often lack the capacity to influence institutions controlled by elite groups. More broadly, the disadvantage is perpetuated by inequalities in what can be thought of as the factors shaping the political capabilities of the poor: self-confidence, capacity to influence political processes and recognition by the rest of society.

Nowhere are power inequalities and their consequences more clearly displayed than for women. Women experience inequality in power relative to men from the household level to the national level, where they are universally under-represented in legislative bodies, organs of government and local political structures. Women, especially those with low incomes, tend to have less control over household resources, less access to information and health services and less control over their time. These factors are closely linked to their nutritional status, the quality of care they receive and the nutritional status of their children (see box 1.3).

## Unequal chances—health inequalities and the MDGs

Life chance inequalities on the scale described above are not just inherently unjust. They are also bad for the MDGs. Deep inequalities are holding back progress in many areas. To demonstrate how strategies to reduce inequality could accelerate progress, this section considers child mortality.

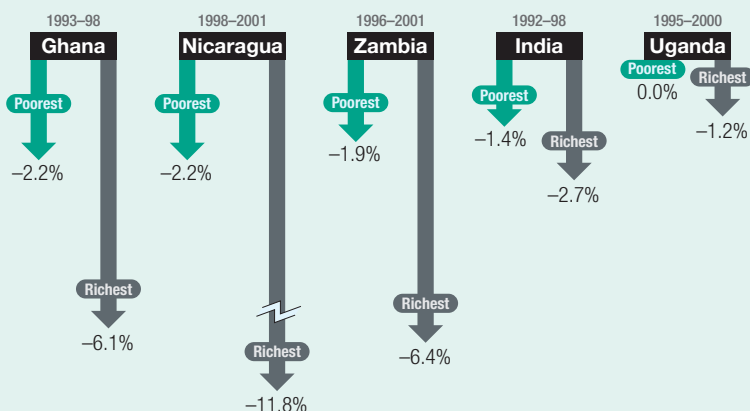
### Income

As chapter 1 shows, the MDG target of reducing child deaths by two-thirds will be missed by a wide margin on current trends. Two inter-related factors explain much of the deficit. First, in most countries the poor account for a far larger share of child deaths than is commensurate with their share of the population. Put differently, the children of the poor are overrepresented among the victims of child death—heavily so in many countries. In Ghana 36% of child deaths occur among the poorest 20% of the population, while 7% occur among the richest 20% (see figure 2.4). Second, the rate of child mortality is falling much more slowly among the poor than the average rate of decline in most countries. Cross-country data suggest that the child mortality rate among the poorest 20% is falling at half the average rate of decline, so that the mortality gap between rich and poor children is widening. In Zambia child mortality among the richest 20% fell by 6% a year in the second half of the 1990s—three times as fast as for the poorest 20% (figure 2.11).

In India the mortality rate among children ages 1–5 is 50% higher for girls than for boys

**Figure 2.11** Child mortality—a growing gap between rich and poor

Change in under-five mortality rate, annual average, by wealth quintile (%)



Source: Calculated on the basis of data on under-five mortality from Gwatkin and others forthcoming.

No avoidable child death should be tolerated. But this current pattern of progress is also suboptimal from the perspective of achieving the MDG target of a two-thirds reduction. The slowest decline is happening in precisely the population group in which accelerated progress could lead to the biggest reductions in child mortality. On one estimate, closing the gap in child mortality rates between the poorest 20% and the national average would cut child deaths by 60%, saving about 6.3 million lives a year. This would also put the world on track for achieving the MDG target.<sup>19</sup> This suggests that the failure of national governments and the international community to overcome inequalities based on wealth costs the lives of more than 6 million children a year.

It could even be argued that this comparison yields an unduly conservative assessment. Using Demographic and Health Survey data, we estimate what would happen if the average child mortality rate fell to the rate of the richest 20%. For many countries this would translate into very large declines in child deaths, reducing the overall total by more than one-half in India and in Nicaragua. For India the reduction in child mortality would reduce overall deaths by about 1.4 million. In just three countries—Bangladesh, India and Nepal—half a million of the lives saved would be of children in the first month of life.

## Gender

Reducing gender inequality would have a catalytic effect on cutting child deaths. That effect would be especially pronounced in South Asia, where gender inequality is most deeply entrenched. If India closed the gender gap in mortality between girls and boys ages 1–5, that would save an estimated 130,000 lives, reducing its overall child mortality rate by 5%.<sup>20</sup>

Overcoming wider gender inequalities would have even more pronounced effects because of the negative links between maternal nutritional deprivation and child mortality. The percentage of underweight women is four times higher in South Asia than in Sub-Saharan Africa, and deficiencies in nutrients and vitamins linked to child death are far greater. South Asia has lower levels of poverty and higher average incomes than Sub-Saharan Africa but South Asia's child malnutrition rate is 20% higher than Sub-Saharan Africa's. Half of the world's underweight children live in South Asia. These human development deficits are strongly associated with gender inequalities.

Greater gender equity would act as a powerful force for reducing child mortality. Using cross-country data, the International Food Policy Research Institute has estimated that equalizing the access of men and women to education, nutrition, income and property rights could reduce the underweight rate among children less than three years old by 13 percentage points in South Asia, meaning 13.4 million fewer malnourished children vulnerable to early mortality. For Sub-Saharan Africa child malnutrition would fall by 3 percentage points, with 1.7 million fewer malnourished children.<sup>21</sup> The pathways through which the empowerment of women influences child well-being include wider spacing of births through enhanced control over fertility, greater use of health facilities and better knowledge of health interventions.

## Public policy

Reducing the deeply rooted inequalities based on gender, income and region that generate unequal child mortality rates requires wide-ranging reforms. Public policy has a critical role



to play in addressing the three “As” for reducing inequality:

- *Access.* The poor often live in areas that are sparsely covered by basic health services or covered by facilities that lack drugs and trained staff. Chronic underfinancing is part of the problem. Providing basic health-care coverage in a low-income country costs an estimated \$30–\$40 per capita. Across much of Africa spending is less than \$6 per capita. Under these conditions, even where facilities exist, they are likely to lack essential medicines.
- *Affordability.* Charging for basic health-care increases inequality. Payments for

healthcare can represent a large share of the income of poor people, leading to reduced demand, uncompleted treatments or increased debt. In Viet Nam a single hospital visit costs 40% of the monthly income of people in the poorest 20% of the population. High levels of household health spending not only deter use of services, but by one estimate have pushed 3 million people in Viet Nam into poverty.<sup>22</sup> In China the erosion of the public health system after the economic reforms of the late 1970s has exacerbated inequalities in health (box 2.2). Removing fees can improve equity. When Uganda did that in 2001, visits to public

## Box 2.2

**China—rising inequalities in health**

Over the past four decades China has registered some of the most rapid advances in human development in history. During the 1990s the country climbed 14 places in the HDI ranking (to 85). China has been the world’s fastest growing economy over the past two decades, with per capita incomes rising threefold in constant purchasing power terms. However, there are worrying indications that social progress is starting to lag behind economic growth performance, with the slowdown in the rate of reduction in child deaths a special concern.

Health inequalities appear to be contributing to the problem. Children living in the poorest provinces and in rural China face the highest death risks. Child mortality levels in urban areas average about one-third of those in rural areas. Under-five mortality rates range from 8 per 1,000 live births in Shanghai and Beijing (comparable to the United States) to 60 in the poorest province of Guizhou (comparable to Namibia). The gap between rich and poor provinces appears to be widening. So does the survival gap between girls and boys. Recent research indicates that child mortality rates are rising at 0.5% a year for girls while falling at 2.3% a year for boys.

Public policies have contributed to these inequalities. Until 1980 most of China’s poor people living in rural areas were covered by the Cooperative Medical System. That system was dismantled with market reforms. One effect was to shift the burden of financing healthcare costs from public providers to household transfers. Most people now have to buy health insurance, meet costs as they arise or go without healthcare. Today, China spends 5% of GDP on health, which is relatively high for countries at comparable levels of income, but public spending on health amounts to less than 2% of GDP. In effect, health financing has been privatized.

Fiscal decentralization has reinforced the transition to a market-based system. Poorer counties and districts have been unable to

raise sufficient revenue through taxation, intensifying the pressure on health service providers to demand payment for services. This includes basic immunization and other preventive health services. Charging for services that are public goods is economically inefficient and inequitable.

The erosion of public provision has resulted in a mismatch between need and provision: average per capita spending on health in urban areas is now 3.5 times the level in rural areas. Between 70% and 80% of the rural population have no health insurance coverage. This means that treatment for sickness episodes has to be paid for out of pocket. High healthcare costs are a cause of household poverty and a deterrent to using health services. One study commissioned by the Chinese Ministry of Health covering three provinces (Guangdong, Shanxi and Sichuan) found that half of respondents reported not seeking healthcare despite needing it in the past year. The main reason cited was cost.

Price barriers may be partly responsible for a downturn in immunization coverage. During the 1980s immunization for diphtheria, pertussis and tetanus (DPT3) increased from 58% to 97%—one of the highest rates of coverage in the developing world. Since then coverage has slipped back to 90%, according to data from the World Health Organization and the United Nations Children’s Fund.

There is now a danger that China will miss the Millennium Development Goal target for child mortality and that deepening inequalities will slow progress towards other health goals. These inequalities are rooted in a privatized health financing system that seems inappropriate in a country with high levels of poverty. While economic reform has clearly generated important gains, market principles have been extended too far into the health system. The Chinese government itself is now reviewing healthcare financing with a view to strengthening service provision for poor households.

**Source:** Lim and others 2004; Liu, Liu and Meng 1994; Sen 2004.



Even small shifts in distribution can significantly reduce poverty

health facilities rose by 80%, with half of the increase among the poorest 20% of the population. The share of households that reported not having used a health service because of high costs decreased from about 50% in 1999 to 35% in 2002—a reduction that was particularly pronounced in the country's poorest region.<sup>23</sup>

- *Accountability.* Even where public health services are available, they are often not used by poor people. For example, in India a large share of demand is directed towards poorly qualified private providers. A survey in one of the poorest districts of Rajasthan found that poor households used private health providers even when nominally free public services were available. One reason: over half of health centres were closed during periods

when they were supposed to be open. When facilities are open they often lack a trained staff member on site. For India as a whole survey evidence based on unannounced visits to health clinics found that 40% of clinics lack a trained person on site at the time of the visit.<sup>24</sup> Developing more accountable health systems can dramatically improve access and health indicators. For example, in 1987 the Brazilian state of Cereá, one of the poorest in the country, set up a decentralized, community-based healthcare system that now employs more than 170,000 health workers. The programme has been accompanied by strategies to support community monitoring of health providers. In less than 15 years the infant death rate fell to one-third of its 1987 level.

## The human development potential of pro-poor growth

Trends in income inequality have an important bearing on wider dimensions of human development as well as on income poverty. Moves towards greater distributional equity could sharply reduce the rate of income poverty, with attendant benefits for the MDGs and wider human development goals.

Improved distribution can enhance development through two pathways: one static and the other dynamic. At any given growth rate the larger the share of any increment in economic wealth that is captured by the poor, the higher the ratio of poverty reduction to growth—referred to as the poverty elasticity of growth. This is a static effect. Dynamic effects emerge when changes in distribution affect the growth rate. Extreme inequality can act as a brake on growth. This effect is especially strong for asset inequality. Limited access to productive assets, or limited capacity to enforce legal claims, can restrict poor people's ability to borrow and invest, holding back growth.<sup>25</sup> Cross-country evidence suggests that greater distributional equity

can accelerate growth and that there are no inherent trade-offs between growth and equity. Thus improved distributional equity can generate a double benefit: it increases growth and the size of the economic pie and it enables the poor to capture a bigger slice of that pie.<sup>26</sup>

### Improving the distribution of growth

In countries where inequality and poverty levels are high even small shifts in distribution can significantly reduce poverty.

### Accelerating poverty reduction in individual countries

Using national household income and expenditure data for several countries, we estimated the potential impact on income poverty of doubling the national income share of the poorest 20% of the population through a transfer from the top 20% (see *Technical note 2*). For high-inequality countries with large populations in poverty, shifting even a small share of the income of

the top 20% could lift large numbers of people above the poverty line. For Brazil and Mexico the transfer of 5% of the income of the richest 20% would have the following effects:

- In Brazil about 26 million people would be lifted above the \$2 a day poverty line, cutting the poverty rate from 22% to 7%.
- In Mexico about 12 million people would be taken out of poverty, as nationally defined, reducing the poverty rate from 16% to 4%.

Of course, this is a static exercise. It illustrates the poverty impact of a hypothetical transfer from rich to poor. In a society that attaches greater weight to welfare gains for the poor than the rich the transfer might be considered welfare enhancing for the whole of society even if some lose.

Another route to improved distribution is progressive growth—a growth pattern in which average incomes are growing, but the incomes of poor people are growing even faster. This is a positive-sum process in which nobody loses and

the poor gain proportionately more. Progressive growth can be thought of as a dynamic process in which poor people produce their way out of poverty, while increasing their contribution to national wealth (box 2.3).

Even modestly progressive growth can have a powerful impact on poverty. Once again, we use growth simulation models based on national household income survey data to demonstrate the effects for Brazil and Mexico. We build two scenarios. The first, a distribution-neutral scenario, assumes a continuation of current growth trends with no change in distribution. Increases to income are distributed in line with existing income shares: if the poorest 20% account for 1% of current income, they would receive 1 cent of every \$1 generated by growth. The second, a progressive growth scenario, assumes that people living below the poverty line double their share of future growth. In the case mentioned above, if the poorest 20% represented the population living in poverty, their

#### Box 2.3

#### Pro-poor growth and progressive growth

Like motherhood and apple pie, everybody is in favour of “pro-poor growth”. The concept, like its increasingly popular and more recent variant “shared growth”, captures the idea that the quality of growth, as well as the quantity, matters for poverty reduction. But the concept means very different things to different people. The World Bank and international development agencies favour an absolute definition of pro-poor growth. What matters in this definition is not whether the incomes of poor people are rising in relation to average income, but how fast their incomes are rising. Pro-poor growth on this definition can be consistent with rising inequality, even in countries already marked by extreme inequalities.

The progressive definition of pro-poor growth adopted in this Report focuses on the relative position of poor people. It highlights the potential for small distributional shifts to produce major gains for poverty reduction.

Are these just semantic differences? Or do they have a direct relevance for human development? The differences can be overlaid: all parties in the debate favour rapid poverty reduction. By extension, nobody argues that low levels of inequality are inherently good for poverty reduction. If they were, low-growth, low-inequality (a Gini coefficient of about 36 throughout the 1990s) Benin would be outperforming China. However, two important issues are at stake, both connected to the balance between economic growth and distribution.

The first issue is one of social justice. In the absolute definition distribution-neutral growth is pro-poor: any growth that increases the income of the poor can be deemed pro-poor. It is difficult to square this with basic ideas of social justice. If everybody in Brazil shared in increments to growth on the current distribution pattern, the richest 20% would receive 85 cents of every \$1. The poorest 20% would receive 3 cents. Everybody—including the poor—is better off, so growth might be deemed pro-poor. But if more weight is attached to the well-being of poor people, that distribution pattern is not consistent with basic principles of fairness and social justice.

The second, related concern is about the conversion of growth into poverty reduction. If maximizing the impact of growth on poverty reduction is a central policy goal, then distribution matters. Other things being equal, the bigger the share of any increment to growth captured by poor people, the faster the rate of poverty reduction. Increasing their share of additional growth can accelerate the rate at which rising prosperity reduces poverty, while at the same time raising the overall growth rate.

The progressive growth approach focuses attention on the structural inequalities that deny poor people and marginalized groups an opportunity to contribute to and participate in growth on more equitable terms. It puts redistribution, alongside growth, at the centre of the policy agenda for reducing extreme poverty.

Source: Kakwani, Khandker and Son 2004; Ravallion 2005; DFID 2004b.

The smaller the poor's share of any increment to income the less efficient growth is as a mechanism for poverty reduction

share of future growth would rise from 1 cent to 2 cents of every \$1. Considering the high degree of inequality in both Brazil and Mexico, this is a modest scenario for pro-poor growth. Even so, the results are striking. For Brazil it shortens the time it takes the median household to cross the poverty line by 19 years. For Mexico it shortens the time by 15 years (see *Technical note 2*).

It is sometimes argued that distribution has more relevance for high-inequality middle-income countries than for the low-growth low-income countries that are farthest off track for meeting the MDGs. This is correct in the sense that, as the Brazil and Mexico simulations demonstrate, even modest redistribution can produce big results for poverty reduction in high-inequality middle-income countries. But the distribution of growth also matters a great deal for low-income countries.

Sub-Saharan Africa demonstrates the point. One consequence of economic stagnation for the region has been a rise in the growth rate required to achieve the MDG target of halving poverty. Some countries—Ethiopia, Senegal, South Africa and Tanzania among them—need to grow at about 3% per capita a year to reach the target. However, analysis based on household surveys (in countries accounting for 78% of the region's population) suggests that the weighted average annual growth rate required to achieve the MDG for the region is 5% per capita for 10 years.<sup>27</sup> This is in a region where the average annual growth per capita for 2000–06 is 1.6%. Even if the current recovery in some countries is sustained, for a large group of countries the MDG growth requirements are implausible.

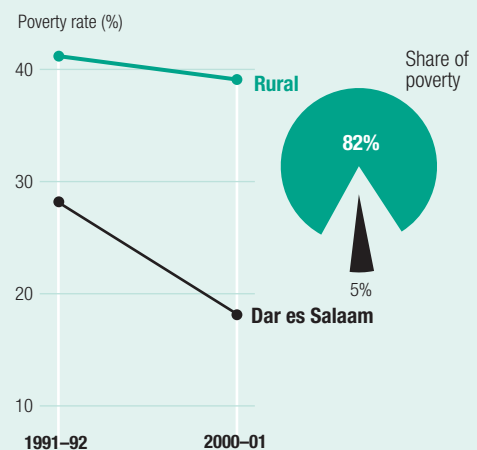
Does this mean that Sub-Saharan Africa is destined to fail on the MDGs? Not if the region combines a more modest increase in growth with an improved pattern of income distribution.

The point can be demonstrated by reference to Kenya—a country that is unequivocally off track for halving extreme poverty by 2015. If Kenya were to achieve a 1% per capita growth rate on current distribution patterns, it would not halve poverty until 2030. Doubling the share of the poor in future growth even at the 1% per capita growth rate would enable Kenya to halve poverty by 2013, meeting the MDG target. In

other words pro-poor growth would reduce the time horizon for halving poverty by 17 years. The broader point here is that extreme inequality can constrain poverty reduction in low- and middle-income countries for the same reason: the smaller the poor's share of any increment to income the less efficient growth is as a mechanism for poverty reduction. In Viet Nam the ratio of average income growth to poverty reduction is approximately 1:1. For high inequality countries such as Bolivia and Zambia the ratio is about 1:0.5.<sup>28</sup> In other words, it takes twice as much growth to achieve the same level of poverty reduction.

These cases demonstrate that the quality and composition of growth matter as much as the quantity. As Sub-Saharan African governments seek to consolidate economic recovery, prioritizing the quality of growth has become increasingly urgent. There is a danger that on current growth patterns economic recovery will leave the poor behind. For example, Tanzania's success in raising overall growth has had a negligible impact on poverty rates. Average per capita incomes have risen 1.8% a year since 1995, but poverty has been falling far too slowly to achieve the MDG. Between 1991 and 2001 the poverty rate fell from 39% to 36%, with large underlying variations. Poverty levels have fallen sharply in Dar es Salaam, but only marginally in rural areas (figure 2.12). The problem: rural areas account for 82% of poverty.

Figure 2.12 Tanzania—poverty reduction restricted to the capital



Source: Demombynes and Hoogeveen 2004.

Across much of Africa the challenge then is not just to accelerate growth, but to ensure that poor people contribute to the growth process, through increased output and rising productivity, and capture a bigger share of increments to growth than they do now. For public policy this means far more attention to small-holder farmers; to marginal, rain-fed agricultural areas; and to public investments to build the assets of the poor and the infrastructure serving them.

The role of the private sector is also critical for pro-poor growth. Small and medium-size enterprises in particular play a pivotal role—as employers, as suppliers of inputs and as a link to markets. Private firms can contribute to poverty reduction by empowering people, extending choice and providing a broad range of goods and services. In Bangladesh, Grameen-Phone, the country's largest cellular phone service provider, operates a rural programme that serves more than 50 million people, enabling microenterprises to operate more efficiently by improving access to market information. Elsewhere, the absence of microenterprises can reduce competition, driving up costs of inputs and driving down prices for goods sold by communities in poor or remote areas. The high costs of government regulation and limited access to credit are among the major constraints on small-scale private enterprises' ability to operate as a more dynamic force for poverty reduction. On average, the cost of starting a company in Sub-Saharan Africa is 224% of average national income, compared with 45% in South Asia and 7% in high-income countries.

### Accelerating poverty reduction globally

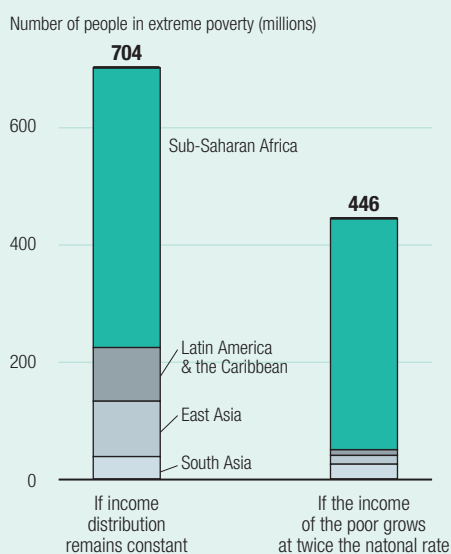
So far, we have looked only at the potential benefits of pro-poor growth in accelerating poverty reduction in individual countries. Using the global income distribution model outlined in chapter 1, we scale up this exercise. The model provides an approximation of the global distribution of income adjusted for purchasing power parity to take into account price differences across countries. We use the model to simulate what would happen to the global poverty trends set out in our projection to 2015 if people

living below the poverty line captured a share of future growth that is double their current share—in effect, extending the national pro-poor growth model to the global stage. As in the national exercises, for countries with positive growth trends, we assume that the trend will continue. For countries with negative growth trends we use a positive growth projection based on regional averages for 2000–06.

The results of the simulation are striking (figure 2.13). Redistribution in favour of the poor has a marginal effect on overall world income distribution, but it has a marked effect on poverty. Under the pro-poor growth scenario in 2015:

- The number of people living in extreme poverty drops from 704 million to 446 million—a decline of one-third.
- The worldwide incidence of poverty falls from 10% to 6%.
- The pro-poor growth track reduces poverty sharply in all regions, though it also increases the share of poverty accounted for by Sub-Saharan Africa—an outcome that demonstrates the importance of boosting economic growth as well as improving distribution.

**Figure 2.13** Extreme poverty: two scenarios for 2015



*Note:* Extreme poverty refers to a poverty line of \$700 a year (personal consumption expenditure); for details see *Technical note 2*.  
*Source:* Dikhanov 2005.

In most developed countries poverty is measured in relative terms rather than absolute terms. This means that the benchmark for measuring poverty—and poverty reduction—is usually defined in relation to average or median income. It follows that when governments set targets for reducing poverty, they are targeting changes in distribution that involve narrowing the gap between the poorest end of the income distribution and the benchmark.

Experience in the United Kingdom highlights some of the problems associated with reducing relative poverty. At the end of the 1990s the UK government set ambitious targets for reducing the incidence of child poverty, thus putting the issue of distribution at the centre of government policy. Child poverty in this context is defined as living in a household with income below 60% of the median after housing costs. Fiscal policy and targeting transfers to the poor have been central planks in measures aimed at achieving the target. However, labour market developments, including rising incomes at the top of the distribution, have pulled in the opposite direction.

At the end of the 1990s the United Kingdom had one of the highest rates of child poverty in Europe. In 1998 some 4.6 million children—around one in three—were living below the poverty line. These high poverty levels, double those at the end of the 1970s, were a legacy of the 1980s—a decade characterized by a distinctly pro-rich growth pattern that left poor people behind. At the end of the 1970s the richest 10% of the population received 21% of total disposable income. Twenty years later it received 28%, nearly as much as for the entire bottom half of the population. Average annual incomes for the richest 20% increased at about 10 times the rate for the poorest 20% (3.8% compared with 0.4%). The United Kingdom's Gini coefficient climbed from 25 to 35 by the mid-1990s—one of the biggest increases in inequality in the world.

Two main forces drove the rise in inequality: changes in the underlying distribution of earnings, and the impact of government policies that cut taxes for higher earners and lowered benefits for the poor.

While the rise in inequality stabilized at high levels by the early 1990s, child poverty remained exceptionally high by historic standards. More than one in four children still lived below the poverty line during the economic boom of the late 1990s, reflecting a further rise in the Gini coefficient.

In 1999 ambitious targets were announced for eradicating child poverty within a generation. The first stage was to reduce child poverty by a quarter from the 1998 level by 2004–05 and then to halve it by 2010.

Fiscal redistribution has played a central role in strategies for meeting the target. Large increases in financial support for families with children have been introduced. Most of the extra spending was directed to in-work benefits and tax credits that boosted the incomes of low-income working families with children. Out of work income benefits were also increased for families with children.

The gains for the poorest families have been considerable. The Institute for Fiscal Studies estimates that the incomes of the poorest fifth have risen by over 20% as a result of the reforms between 1997 and 2004. While government has played down the redistributive effect, that effect has been pronounced. Labour market effects have also had a bearing on progress towards the targets. As the United Kingdom's jobless rate fell to historic lows from the end of the 1990s, wage gains at the lower end of the spectrum contributed to substantial falls in relative child poverty. By 2003–04, 600,000 fewer children were living in poverty than in 1998.

Impressive as the decline has been, prospects for meeting the target remain uncertain. Another 400,000 children will have to be lifted out of poverty over the next year to achieve the 2004–05 target. The next target—halving child poverty by 2010—will prove even more challenging. Why has it been so difficult to achieve the target even with strong fiscal redistribution?

The answer is because fiscal policy has its limits. While fiscal transfers have reduced inequality since 1997, labour markets and other changes appear to be pulling in the other direction. Income levels are rising at below the median rate among roughly the poorest 15%. Meanwhile, the overall level of inequality now remains effectively unchanged from its 1997 level.

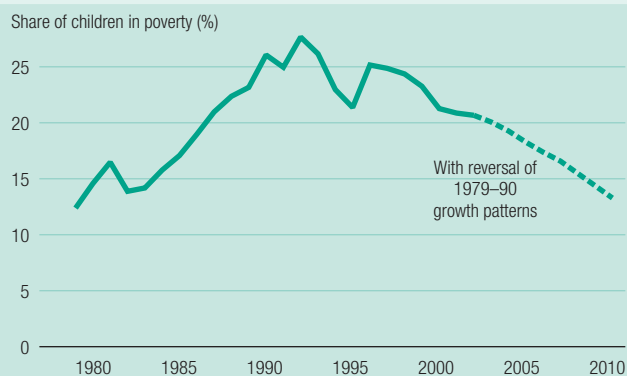
Beyond the labour market, analysis by the Institute for Fiscal Studies shows that much of the rise in the United Kingdom's child poverty rate is accounted for by the changing relative position of families in the income distribution. For example, the number of single-parent families and families where both parents are jobless has risen sharply. Both factors are strongly associated with poverty. This suggests that meeting the 2010 target will require more redistribution, a change in working and employment patterns among parents and more fundamental changes to the underlying distribution of earnings and incomes.

The importance of changing the distribution of earnings can be demonstrated by reference to a variant of the pro-poor growth model used elsewhere in this chapter. As noted earlier, the 1980s was a pro-rich decade, with incomes at the top end of the spectrum rising far more rapidly than those at the bottom end. In an exercise carried out for the *Human Development Report* the Institute for Fiscal Studies simulated what would happen to child poverty over the next 10 years if the distribution pattern of the 1980s were reversed. So, for example, the income of the poorest 10% was estimated to grow at 3.7% a year, the average rate of growth experienced by the richest 10% between 1979 and 1990, while the richest 10% was estimated to grow at 0.4%, the average growth of the poorest 10% between 1979 and 1990.

The distributional shift would have cut the incidence of child poverty from 23% to 17% by 2010 (see figure). While this is still above the 2010 target, the simulation does not take into account the potential for fiscal policy to close the gap. In other words, if the next 10 years did for the poor what the 1980s did for the rich, that



### Child poverty in the United Kingdom



Source: Goodman 2005.

Source: Goodman 2005; Hills 2004.

would bring the United Kingdom within touching distance of the child poverty goals.

Developments in the United Kingdom raise poverty issues that are different in character than those associated with the MDGs, though with some striking similarities. Perhaps most obviously, the setting of targets has brought a crucial human development problem to the centre of public policy debate. The target itself signals an important message about government priorities. Fiscal policies have been geared towards that priority. At the same time, the wider social and economic forces shaping income distribution patterns during a period of high growth and low unemployment are slowing progress towards the target. Ironically, economic success, combined with the limits to fiscal redistribution, can raise the absolute income of the poor without accelerating progress towards child poverty reduction.

### Relative poverty in rich countries

These simulation exercises look at absolute poverty. The effects of growth on distribution depend on the definition of poverty used. Distribution effects are stronger for a relative definition of poverty for the obvious reason that the poverty indicator becomes a function of distribution. Ultimately, the decision about the appropriate measure is a value judgement.

Most rich countries define poverty in relative terms. Child poverty is a particularly sensitive indicator for income poverty in rich countries. It provides an insight into the scale of deprivation, and it is also an indicator for inherited disadvantage and the transmission of poverty across generations. For 17 of 24 OECD countries in the 1990s research by the United Nations Children's Fund shows a rise in child poverty, defined as living in a family with an income below 50% of the national median.<sup>29</sup> This means that 40–50 million children are growing up in poverty in the world's richest countries. Two OECD members—Mexico and the United States—have the dubious distinction of having child poverty rates of more than 20%. The United Kingdom has had some recent success in reversing a rapid rise in child poverty. Redistribution through fiscal transfer has played a central role, suggesting that pro-poor spending can be a potent force for reducing child poverty.

But it also demonstrates that wider forces shaping income distribution, notably labour market inequalities, are difficult obstacles to overcome (box 2.4).

### Achieving pro-poor growth

What emerges from the simulation exercises presented in the previous section is that policies and growth patterns that improve distribution can be powerful weapons in the fight against poverty. Of course, not all policies to improve distribution are inherently good for growth—and low levels of inequality are not a substitute for accelerated growth. But policy-makers are not always forced to make trade-offs—many strategies for narrowing inequality will have positive effects on growth. This suggests that increasing poor people's share of growth should be a central part of strategies for achieving the MDGs and wider human development goals (see box 2.3).

There is no single path for achieving this objective. Closing gaps in educational opportunity is a critical starting point. In almost all countries inequalities in education are among the most powerful drivers of inequalities in income, health and opportunity, including opportunities to participate in society and influence political processes. Education has the potential to act as

an equalizer of opportunity, as well as a force for economic growth and efficiency. But that potential can only be unlocked through public policies that systematically remove the social, economic and cultural barriers facing disadvantaged groups. Similarly, deep inequalities in health and the increased vulnerabilities associated with unequal access to healthcare are associated with deep differences in opportunities. Repeat episodes of ill-health undermine productivity, diminish the ability of children to benefit from education and lock households into cycles of poverty. As in the education sector, overcoming these inequalities in health requires public investment to increase the supply of good quality education, and measures to reduce obstacles to demand.

Inequalities in income reflect the distribution of assets and opportunity and the operation of markets. But they are influenced by government taxation and spending. In many countries fiscal transfers are already narrowing extreme inequalities. In Chile, for example, they narrow the gap between the income ratios of the richest and the poorest 20% of the population from 20:1 to 10:1. From a human development perspective the fiscal transfers with the highest returns are investments that build capabilities and provide protection during periods of acute vulnerability (box 2.5).

An obvious requirement for meaningful fiscal transfers to alleviate poverty is the willingness—and capacity—of the state to

#### Box 2.5 Public investment in social transformation

At the end of the eighteenth century the great thinkers of the European Enlightenment advocated ambitious social programmes to reduce inequality and poor people's vulnerability and dependence on welfare—with a central role for public policy in financing the needed socially transformative investments. The ideas remain profoundly relevant.

In France Antoine-Nicola de Condorcet set out a bold plan for eradicating all inequality “entailing either poverty, humiliation or dependence”. The plan saw publicly financed education, protection against sickness and old-age pensions as the key to social progress. The practical application of this approach in England was set out in Thomas Paine's *Rights of Man*, which advocated a system of universal insurance financed through taxation. Underpinning these approaches was the idea that public policy needed to create a sustainable exit from poverty by equipping people with the assets, security and opportunities needed to break out of the cycle of poverty.

Well designed fiscal transfers provide more than temporary relief. They provide a redistributive mechanism through which investments in poverty reduction can yield human development and economic returns far greater than the initial investment. Among the strategies:

- *Income transfers to vulnerable groups.* Income transfers enable policy-makers to raise the income of vulnerable groups. Take South Africa's old-age pension system, for example. Originally intended to provide benefits for white people, it has been extended to elderly black people and to vulnerable families with children. In 2001 the payment was over 80% of the welfare budget. Transfers have been instrumental in lowering income inequality (South Africa's Gini coefficient fell from 67 in 1991 to 59 in 2000). The payments have enabled households to secure credit and invest in productive activities (hire equipment,

buy improved agricultural inputs), refuting the idea that social transfers crowd out private initiative. The transfers have also resulted in tangible health gains. Among black children under age 5 these transfers have led to an estimated 8 centimetre increase in height—equivalent to six months' growth.

- *Employment-based transfers.* Transfers linked to employment can provide vulnerable households with security during periods of extreme stress—in the aftermath of drought, for example. The Maharashtra Employment Guarantee Scheme is one of the best known examples. Since the mid-1970s it has provided agricultural labourers and small farmers with up to 100 days in paid employment on rural works programmes. Women account for just under half the beneficiaries. Extending the programme to the whole of India would cost an estimated 0.5%–1% of national income in transfers to 40 million rural labourers and smallholders. If effectively targeted, this would lift most of the recipients above the poverty line.
- *Incentive-based transfers.* Governments can use fiscal transfers to promote wider human development goals. In Mexico the Oportunidades programme targets income transfers to households in vulnerable municipalities, with eligibility being conditional on children attending school and visiting health clinics. More than 5 million families are covered, and there is strong evidence of improvements in school attendance, nutrition and income status: recent evaluations suggest that more than 60% of the transfers reach households in the poorest 20% of the population. The programme currently costs 0.2% of GDP. Low income is not a barrier to incentive-based transfer. Several very poor countries have used such systems, for example to increase girls' participation in school (see box 1.7 on Bangladesh).

**Source:** Jones 2004; Lund 2002, 2004; ODI 2004; Case and Deaton 1998; Indiatgether.org 2004; Coady, Grosh and Hoddinott 2004; Coady and Parker 2005; Mexico, Secretaría de Desarrollo Social 2005.



mobilize revenue. In much of Latin America aversion to taxation restricts this condition. Mexico raises only 13% of GDP in revenue—less than Senegal does. India's capacity to redistribute the benefits of higher growth through the fiscal system is similarly constrained by a tax to revenue ratio of only 10%. After two decades of growth that ratio has not increased.

Fiscal transfer is one mechanism for raising the income of the poor above the level dictated by current growth and distribution patterns. More broadly, pro-poor growth requires a public investment focus on the markets in which poor people operate. In many countries the challenge is to shift the policy focus to the smallholder producers and to the more marginal areas that account for the bulk of poverty. The problem is that the production of food staples and cash crops in poor areas is constrained by limited access to markets, high transport costs and restricted access to credit. Compounding this problem, poor people—especially poor women—lack the assets, legal entitlements and political power needed to raise productivity and income.

Control over assets is critical. It is sometimes argued that there is a potential trade-off in agriculture between greater equity through land reform and greater growth. Here too the trade-offs are more apparent than real. Redistributive reforms in agriculture have proven results in reducing poverty, leading to major advances in countries such as China, the Republic of Korea and Viet Nam. In West Bengal, India, agricultural output and incomes rose following tenancy reform and recognition of the land rights of the poor. The contrast with Pakistan is striking. The *Pakistan National Human Development Report* found that the poorest tenant farmers pay 28% of the value

of their production to landlords, while other tenant farmers pay 8%.<sup>30</sup> Cash and crop transfers from poor tenant farmers to landlords are a major source of income poverty. Many of the payments are disputed. Yet the poor do not use the legal system to pursue claims. The main reason: the median cost of a dispute is 20% higher than the annual average household income of the poorest tenant farmers.

\* \* \*

The central message of this chapter is that distribution should be put at the centre of strategies for human development. At a national level this implies that plans for achieving the MDGs, including the Poverty Reduction Strategy Papers that set out a framework for cooperation between developing countries and aid donors, should include measures for redressing extreme inequalities. The MDG agenda needs to go beyond national averages to address the structural inequalities linked to wealth, gender, location and assets that are hampering progress in human development. Governments should expressly commit themselves to targets for reducing inequality and gaps in opportunity, in addition to aggregate MDG targets.

At a global level the international community needs to act on the commitments made in the Millennium Declaration to overcome extreme international inequalities. International action cannot compensate for poor governance and bad national policies. But it can create an enabling environment in which governments committed to human development can succeed. The rest of this Report focuses on three pillars of international cooperation that need reconstruction for human development: international aid, trade and the prevention of violent conflict.

The MDG agenda needs to go beyond national averages to address structural inequalities

