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The political economy of pro-poor growth

The challenge of making growth pro-poor

Key points

- A state must be developmental in nature if it is to enable a pace and pattern of growth which is pro-poor
- Institutions matter — attempts to reform or build robust pro-growth institutions must first identify a narrow and specific set of 'growth-enhancing' institutions, and then support them
- Overt opposition to pro-poor change is less common than indifference, and the wealthy can often be persuaded to support pro-poor policies, particularly if they see changes as being in their interest

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Pro-poor growth — growth that benefits the poor — relies on the state providing an enabling policy environment. Evidence from East Asia, where pro-poor growth has occurred, suggests that the government's role in enabling such growth has resulted from the provision of public goods and social protection mechanisms, and the creation of institutional conditions for more inclusive and equitable development. Achieving this requires that policies be adopted and implemented effectively, which in turn means that there must be institutional and governance structures that are capable and willing to devise, operationalise and implement such policies.

However, reaching this point of effective policy-making might require changes to the political settlement between the state, the private sector and civil society. For donors to support such changes, they need to have a good understanding of a country's political economy, power relations and drivers of change. Their support needs to strengthen the demand for pro-poor change and the capacity of the state to respond to such demands.

This paper focuses on the political economy challenges to making growth policies pro-poor. It explores: the importance of governance, institutions, the developmental state and corruption in setting the conditions within which pro-poor growth becomes possible (or not); the role of power sharing and downwards accountability in pro-poor policy formulation and implementation; key challenges in policy formation and implementation; and implications for donor and government action.

Governance requirements

The state clearly has a role in terms of pro-poor growth. This role is normally seen as including (but not being limited to) investing in public goods, delivering services and providing an enabling environment for private sector investment. However, institutional change is necessary in many countries before the state is capable of engaging effectively in dialogue with its citizens, the private sector and civil society — which is necessary if it is to know what goods and services are needed, where and by whom. Weak accountability to the electorate and poor capacity to deliver means that the state is currently often unwilling or unable to fulfil these roles.

Working at a furniture factory in Ghana

The relationship between democracy and growth is more complex than it was thought to be a decade ago, and there are differences of opinion regarding the changes in governance, institutions and political economy that are needed if growth is to be pro-poor. Governments in Africa have been found to be more likely to be developmental if they have to compete politically to stay in power and where their discretionary authority is restrained by effective institutional mechanisms (Alence, 2004). Evidence from 170 countries shows that good governance supports wealth creation, but economic growth does not result in improved governance (Kaufmann and Kraay, 2003). Re-analysis of a number of quantitative cross-country studies shows that political stability and the rule of law are associated with growth but not necessarily with poverty reduction. Also, enhancing civil liberties and political freedom are linked with poverty reduction but not

Box 1: Characteristics of developmental states

State control and legitimacy: State authority and systems are strong and viewed as legitimate, maintaining political stability. Progressive taxes are collected, labour is regulated and the chronically poor protected. There is a sense of nationhood. Investment is attracted and promotes national development goals.
Public service: A powerful, competent, autonomous and stable bureaucracy exists. Its political loyalty is not tested and it has the authority to create, direct and manage economic and social development. Other effective institutions and networks exist to promote and implement economic policy.
Government legitimacy: Government has legitimacy and support and is not required to redistribute public goods or to change or block development policies or processes in order to retain support and power.
State and non-state actors: The state is relatively independent of special interests although it is well linked with non-state actors who contribute to policy formation.
Policy priority: Economic development is consistently prioritised by government policy, which promotes productive entrepreneurship.
National behaviour and attitudes: Social and technical innovations are generated domestically, or adopted from overseas, then adapted and used to solve problems and create functional institutions and systems. Tolerance, meritocracy, social mobility and high levels of education are valued and promoted.
Elite: Leaders promote development (which may also benefit them) and corruption is limited or at least not predatory.
Source: Cammack (2007).

necessarily with growth (Resnick and Birner, 2006).

Democratic systems are not always pro-poor. Governments may lack the capacity or incentives to promote economic growth or to institute pro-poor policies. Poor people may have limited influence over policy and the way in which the state allocates rights and resources. This suggests that regime type does not necessarily matter as long as the state is 'developmental' in nature (see Box 1).

Institutional requirements

The organisational structure of the state clearly matters but so does the quality of a country's institutions. Globally, it tends to be institutions rather than governance that underpins patterns of prosperity. Dominant economic institutions affect the distribution of resources and determine the incentives and constraints faced by economic actors. As a result, they shape economic outcomes. It is no coincidence that in rich countries, economic actors have secure property rights and can feel confident about law and order, that governance and monetary and fiscal policies are generally good, or that various forms of insurance are available to mitigate risk. Nor is it a coincidence that in many poor countries, these arrangements are less strongly present.

Specific 'growth-enhancing' institutions are required to overcome structural constraints that developing countries face in attempting to achieve pro-poor growth. These might include institutions to stabilise property rights, acquire technology and generate political stability. However, such institutions only emerge when: 1) political institutions allocate power to groups with interests in broad-based property rights enforcement; 2) political institutions create effective constraints on power holders; and 3) there are relatively few rents to be captured by power holders.

When thinking through how to support pro-poor growth, it is important to remember that policy innovations and attempts to improve institutional functioning must be appropriate to a particular context and fit the prevailing characteristics of the local economy and society. As a result, transplanting institutional forms from one country to another is often ineffective.

In some countries, institutional weaknesses may be so widespread that it may be difficult to know where to start. Reformers should therefore seek to identify and address the binding constraint to pro-poor growth.

Although institutions are clearly important for pro-poor growth, this focus must not allow undue pessimism or the implication that there is no scope for political agents to overturn established ways of doing things. By definition, rules are usually followed. However, individuals and organisations can and do periodically break the prevailing rules in deliberate ways, which can eventually lead to the establishment of new rules. This is how institutional change occurs. Changing traditional institutions, such as informal rules and social customs, may take a long time, or even prove impossible, whereas newer institutions can be transformed more quickly. Such moments are rare but they are crucial in opening new opportunities for policy improvement and setting countries on better development trajectories.

The effect of corruption

Corruption, in this instance the use of public resources for private gain, not only affects the level and efficiency of private investment and public spending, with negative effects on economic growth and development, but also increases income-inequality and poverty. It affects poor people's daily lives. If corrupt officials demand bribes, it can mean even basic services are put beyond poor people's reach, and can make them feel voiceless and powerless. It can also impose costs on businesses which have the same effect as taxation, and tend to be most difficult for small and poor entrepreneurs to avoid. However, corruption can differ in its effect. A kleptocracy can devastate growth, investment and poverty reduction, while systemic but more limited corruption can occur alongside development and growth (as in many Asian countries).

Tackling corruption requires a good understanding of its structural drivers. These include low civil-service salaries, weak downwards accountability and an absence of the rule of law. Also, fiscal constraints in poor countries limit the redistribution possible through the budget and can lead to off-budget transfers within patron–client networks.

Downward accountability, transparency in the management of public finances and participatory budgetary planning and monitoring have been advocated as anti-corruption strategies. But where there are severe financial constraints, increased transparency and accountability are unlikely to solve corruption on their own.

Explanations for 'anti-poor growth'

By increasing employment, returns to livelihoods and incomes through pro-poor growth, poor people could see an improvement in their social status and political voice. This change can be empowering and allow them to undertake more independent action.

However, for the dominant players in patron–client relationships, such a change can appear highly threatening. They might actively block poverty-reduction measures and prefer that economic growth does not include or benefit the poor. Poverty reduction might also be resisted where elites view change as a zero-sum game, particularly where there is competition over resources. Reversing such resistance is difficult and historically has mostly been achieved when a strong state has been able to push through reforms, despite opposition.

Overt opposition to poverty reduction is less common, however, than indifference. The wealthy can be persuaded to support pro-poor policies and programmes, particularly if they see such changes as being in their interests, for example, if a link is identified between poverty and crime, social unrest or poor economic performance; by describing poverty as having implications for the country's reputation; or by demonstrating the political gain to be made from pro-poor measures.

Barriers to pro-poor policy

Achieving pro-poor public policy is not always straightforward. There are three key stages — agenda setting, policy formation and implementation — in which benefits to the poor might be forgotten or omitted.

Agenda setting

An issue that is important to the poor may never get on the policy agenda. This is particularly true of the chronically poor, marginalised and vulnerable, who tend to have low visibility, low priority or represent seemingly peripheral (or contested) issues.

Many barriers prevent the interests of poor people being represented in national policy debates. Their problems may not be seen to be sufficiently severe or large scale, and policy-makers may not feel they can justify allocating time or budget to their issues. This can be because the issues are poorly understood or because other constituencies and interest groups are more effective or more powerful and therefore more able to dominate the attention of policy-makers. It may also be that international or national policy narratives are such that there is low demand for information on these issues, and so little research has been undertaken or it has been poorly disseminated.

Policy formulation

Once an issue is on the policy agenda that does not automatically mean that an appropriate policy is formed. Problems might be fully understood and the scale and severity of the problem recognised, but policy-makers may still be reluctant to respond, perhaps because they think that existing policies will be effective in tackling the problem.

Alternatively, policy-makers and other elites may perceive some poor people to be undeserving of attention and resources. National political realities can also contribute to the failure to act. There may not be enough people facing the problem in key constituencies or democratic processes may be weak. Reducing poverty is complex and can be expensive, making it unattractive to politicians, who tend to want to appear decisive and effective over the short term.

Resistance may be greater towards policies and programmes targeted at the poor. Universal policies, which nevertheless benefit the poor, tend to be supported by both taxpayers and elites.

Implementation

Once a policy has been designed, even if it is pro-poor in orientation, numerous factors can prevent its implementation from being pro-poor. The political economy of a country not only influences policy formulation, it can also have a very substantial effect on whether policy implementation is pro-poor or not.

The policy may not be implemented at all because it is politically contested or opposed by powerful vested interests. Or, policy-makers may have failed to build a constituency around the policy — the intended beneficiaries may not recognise that the policy is aimed at them or that it is an adequate response to their needs. Or, even if policies are implemented, their implementation may be partial or distorted, limiting the gains experienced by poor people. The non-poor may capture benefits, and this is especially the case where benefits are, in effect, private goods and relatively large.

The policy may not be implemented because of institutional weaknesses – administrative structures may be weak, human resources may be inadequate and policies may be distorted by 'street-level bureaucrats' (i.e. frontline staff).

The policy may fail to be implemented because it has not been budgeted for through the national budgeting processes. A policy may have been formed and accepted by key stakeholders, but unless the money is made available to implement it, no action will be taken. This makes national budgetary processes crucial. In many developing countries, there is a substantial discrepancy between the publicly announced annual national budget and the figures disbursed to line ministries and implementing agents. Owing to limited voice, the interests of the poor are likely to be ignored or downplayed. Pro-poor budgeting attempts to incorporate the interests of the poor in the budget process. But for expenditure to be pro-poor, public expenditure management must be seen as a political, rather than purely technical process. Without accountability, there is little incentive to make a budget realistic and the leakage of funds means that allocated resources often do not reach the intended beneficiaries.

Implications for donors

The governance problems that block the development of pro-poor policies go deeper than weak technical capacity and lack of political will. Increasing the effectiveness and accountability of government cannot be achieved just by creating new formal institutions. Instead, improvements depend on an uncertain, incremental process that recognises the country's historical circumstances and changes society, economic structures and political culture.

Thus, donors wishing to support pro-poor growth should start from an analysis of the country's context rather than a list of narrow policies. This will be a complex approach, linking economic, social, political and institutional agendas with a long-term view that identifies medium-term, incremental steps to address the root causes of bad government and create positive incentives for change. The 'drivers of change' approach, supported by DFID, has attempted to deliver this analysis, but the challenge of how best to operationalise results remains.

This paper has outlined a challenging set of issues for donors to grapple with when seeking to support pro-poor growth. First, donors need to recognise that they are political actors themselves. Second, it is important to recognise that, although a better understanding of the political economy surrounding pro-poor growth is not a panacea, it is something that responsible donor organisations cannot do without. Third, donors have limited power to influence the fundamental politics of a country, but whether they behave in a politically intelligent way or not can make an important difference at the margins. So, for instance, where the 'developmental state' is absent, they might support measures to improve governance and accountability over the long term and encourage government to deliver certain universal policies, welcomed by elites but which will nevertheless benefit the poorest. It is important to recognise that both the process of supporting the emergence of a developmental state and encouraging the delivery of universal policies must relate strongly to the local context and cannot simply be a process of policy transfer. Fourth, donors can support positive changes to the political equilibrium by encouraging transparency about performance and by working with civil society to mobilise voters around service delivery issues. Fifth, donors should seek to shift their attempts to improve governance from a narrow emphasis on laws, rules and administrative procedures to a broader agenda including political accountability, transparency and an independent media. Finally, donors should focus initially on encouraging governments to eliminate anti-poor practices and policies before promoting pro-poor policies.

Implications for government action

Governments have an important role in enabling pro-poor growth. In order to deliver on their role, governments should firstly familiarise themselves with the requirements of entrepreneurs, workers, agricultural producers and traders active in their country. Secondly, they need a robust understanding of the structure of the national economy and how it relates to key regional and global markets; they should have detailed knowledge of the extent to which the current pattern of economic growth supports employment growth (across the whole country), competition in key markets and the delivery of important goods and services to all sectors of the population. Thirdly, they need to understand how transmission mechanisms — by which economic growth influences prices, employment, taxes and transfers, institutions, assets and access to goods and services — work on the ground. Fourthly, governments can build the capacity and accountability mechanisms that will enable them to improve their performance in the delivery of public goods, public service provision and the generation of an enabling environment for private sector investment. Fifthly, many may have to accept that (pro-poor) institutional change is necessary. In some countries, the number of institutional weaknesses will mean that only the binding institutional constraints should be identified, with reforms being sequenced carefully in order that they are manageable and fit the context and prevailing characteristics of the local economy and society. Lastly governments can ensure that growth is pro-poor by identifying opportunities for domestic taxation and redistribution, to ensure that the winners from growth help to underwrite broadly-based economic development.

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