

2. CONCEPTUAL FRAMEWORK FOR POVERTY REDUCTION STRATEGY

A. Introduction

The most important findings to emerge from the data presented in the previous chapter are (i) that there are relatively wide variations in poverty incidence across the rural-urban divide, ecological zones, development regions, and gender, ethnic, and caste groups in Nepal; and (ii) that poverty incidence overall has in all likelihood worsened, and may have worsened substantially. Further, these findings are expressed in relative terms. Economic and social indicators have improved in Nepal from 1961 to 2000. However, due to relatively rapid population growth, the absolute number of people living in poverty in Nepal has doubled over the period 1981–2000. This substantially increases the magnitude of the overall task of poverty reduction, and thus the amount of resources that will be required to reduce poverty incidence.

In light of the fact that the Government has prepared an Interim Poverty Reduction Strategy (IPRS), and that its refinement is intended to be an ongoing exercise, it is appropriate to revisit the poverty situation in Nepal and evaluate why there has been a lack of progress in reducing poverty incidence, despite the considerable resources devoted to achieving this goal. A convincing explanation as to why poverty incidence has not fallen would be very useful in supporting the Government in refining its strategy to reduce poverty, and to the funding agencies as well, since they may wish to adjust their poverty reduction programs to complement the Government's approach.

B. Conceptual Framework for a Poverty Reduction Strategy

Figure 2.1 presents a conceptual framework for considering the constraints on peoples' productive activities, and within that context, the potential effectiveness of investment and foreign development assistance in reducing poverty.⁵ It is thus a useful framework for prioritizing poverty reduction interventions, and for formulating or assessing a strategy for reducing poverty. Going from the top of the figure to the bottom is, in a sense, like peeling away the layers of covering to find out what is at the core. So the figure is designed to be read from the bottom up. The central goal of the strategy is poverty reduction, and the objective of the exercise is to identify where, along the path from civil and social order to poverty reduction, the constraints to effective participation of people in the growth process lie. The assumption is that constraints have to be removed from the bottom up.

To the immediate left of the central boxes or goals are listed the institutions that have to be in place and work effectively for the particular goal to be achieved. To the immediate right are the policies that can be carried out effectively when that central goal has been achieved or the policies that influence how well the goal is achieved. To the far right of the figure is noted the length of time needed to achieve those goals (short term, medium term, or long term). To the far left of the figure is shown whether generally rising incomes can be expected or not. Economies not generating "quality" growth, i.e., growth in which most in society participate, are likely to have constraints at the bottom of the figure.

⁵ The contents of this section, as well as Figure 2.1, is drawn from Duncan and Pollard (2000).

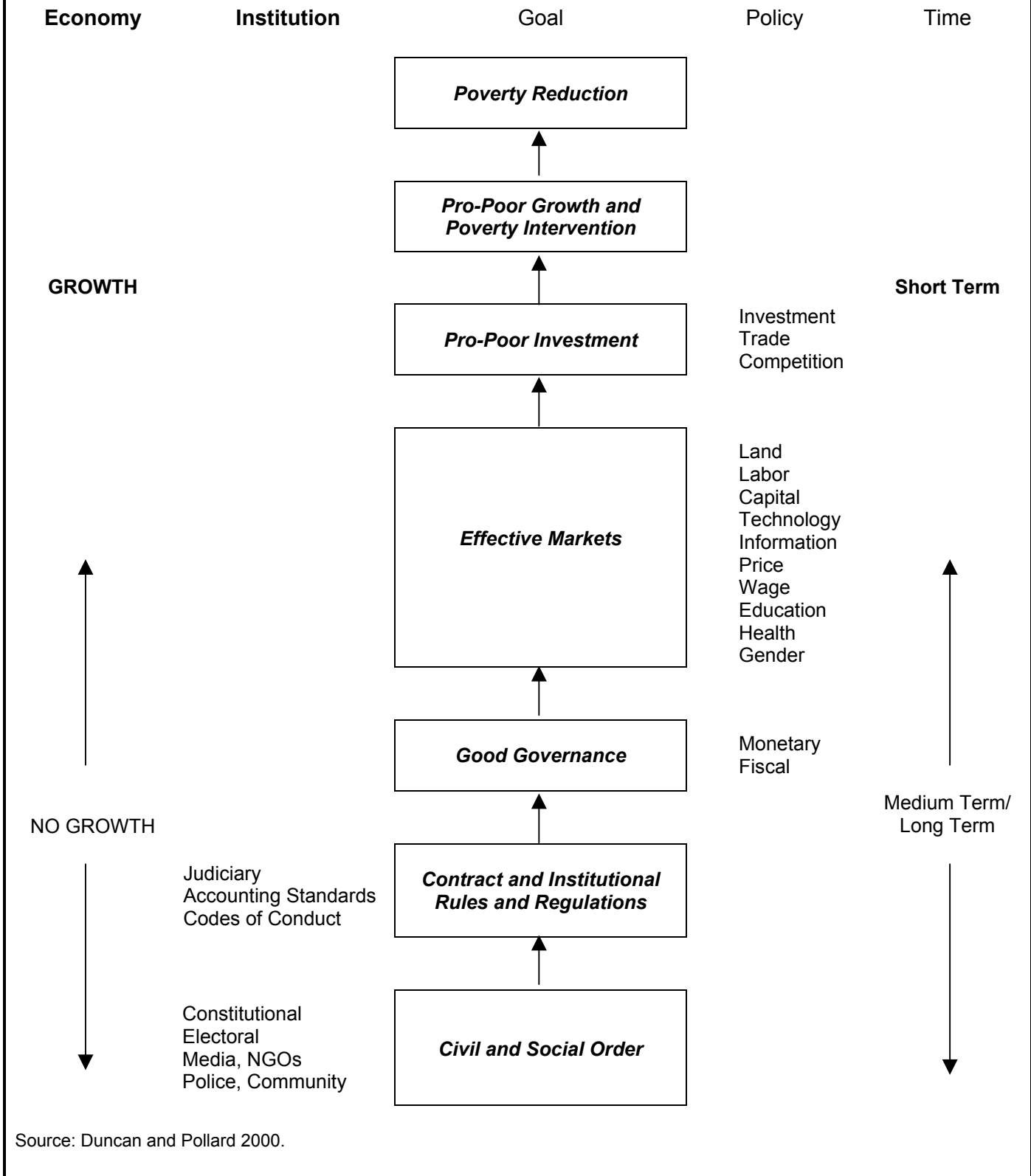
Working from the bottom of the figure to the top we see that without civil order there can be no economic development. Where civil and social order has not been established, it is likely that only intervention in the form of humanitarian aid can be helpful. Efforts to implement infrastructure or other investment projects in countries where a stable environment of civil order has not been established—as in several sub-Saharan Africa countries over recent years—has yielded a frustrating history of stop-start development assistance, with the total failure of the assistance the usual outcome. The institutions that have to be in place for maintaining civil and social order are the police and the judiciary. As well, self-policing by the community—in the sense that there needs to be a degree of trust and concern for others—is also important in maintaining civil order. A constitution and a body of common law or custom will also be necessary to codify the rights of the members of the society.

The next building block that has to be put into place comprises the institutions that form the basis for a market economy, i.e., property rights and impartial enforcement of contracts, as well as informal institutions such as codes of conduct and accounting practices. For these to be effective, the judicial system will have to be working effectively, in particular without intervention by politicians or the bureaucracy. Trust within the society is an important ingredient in the effective workings of property law and contracts. If there is no substantial degree of trust between parties involved in contracts, the load on the judiciary in resolving contract disputes will make the system unworkable, i.e., the transaction costs will be too high for the institution to function.

The next building block is good governance. If the broader definition of governance is adopted, i.e., to include institutions and organizations as well as “good government” matters, there would be a single governance block. As we said earlier, we believe that it is a good idea to separate institutions and governance as it forces a focus on the basic institutions necessary for a market economy to function well. To have good governance, there needs to be political stability. This will depend on the effectiveness of the electoral system and the constitution, as well as the checks and balances that operate through the media and community groups, and perhaps supra-government or supra-parliamentary bodies that have the power to monitor government behavior (such as administrative tribunals and an ombudsman). The main policies that will be affected by the state of governance are fiscal and monetary policy. These in turn will determine exchange rate policy and the inflation rate.

If they are not already in place, establishing civil and social order, effective market institutions, and good governance will usually take a considerable length of time, and without these building blocks in place there will be no, or very limited, widespread growth in incomes. Therefore, a poverty reduction strategy will have to give prior attention to what may be done in the short to medium run that may assist in bringing about desirable changes. To gain an understanding of any shortcomings in these areas, it will likely be necessary to undertake detailed cultural, social, and political economy studies to gain the required information about the society before recommending any action. One issue that will be important in bringing about change will be to find ways to promote widespread “ownership” of desirable reforms.

Figure 2.1: Conceptual Framework for Assessing a Poverty Reduction Strategy



Source: Duncan and Pollard 2000.

The next building block for effective development assistance is effective factor and output markets. Secure property rights and contract enforcement are the basis for effective factor and output markets; however, for effective markets there has to be effective regulation to ensure freedom of entry and thereby avoid anticompetitive pricing, and ensure provision of quality goods and services and health and safety standards. The development of factor markets that are open to participation by all, and do not discriminate in terms of gender, ethnicity, religion, etc., is fundamental to the exploitation of a country's comparative advantages and having inclusive economic growth.

Secure individual title to land (whether through long-term lease or freehold) appears to be a prerequisite for the rapid growth of poor countries and their development into modern economic systems. Secure title to land is necessary for people to have confidence in making the fixed investments that lead to increased productivity. Without such security, private investments are likely to be confined to those having a government guarantee of some kind (such as a joint venture with government), or to "footloose" industries that will exit when there is a contract dispute, or to be exploitative (such as "high grading" in mining or logging). As has been dramatically demonstrated in the People's Republic of China and Viet Nam in recent years, providing farmers with secure, long-term tenure to land leads to remarkable agricultural growth. The absence of such rights in many other countries provides clear counter examples.

Secure, individual title to land is also a basic requirement for developing a financial sector, as without land as security for loans, creditworthiness is difficult to establish. The result will be the locking-up of assets and savings that de Soto (2000) highlights in poor countries.

As populations grow, secure access to land for agricultural purposes becomes a less likely avenue for people to participate in income growth. Good health and education (human capital) have become the main income-generating assets for most people in today's knowledge-driven world. Moreover, while land redistribution and secure rights to land may be able to play some role in increasing the poor's access to income-earning assets, land redistribution is extremely difficult to achieve, while education can be a much more easily achieved and even more productive route to higher incomes. However, there will need to be secure title to land as the base for any productive agricultural, industrial, and services activities.

Provision of the opportunity for all to be educated and to be free of debilitating infections and disease will allow all in society to participate to the full in the labor market. For the labor market to be fully effective in mobilizing labor, there should be no discrimination on the basis of gender, ethnicity, religion, etc. Moreover, care should be taken to see that the public sector does not become a wage leader to the detriment of the private sector, which often happens when the economy is heavily dependent on aid and/or natural resource rents. Minimum wage legislation may be seen as an essential social safety net; however, if the minimum wage exceeds the productivity level of unskilled labor, it will become an impediment to the employment of the poor.

With these building blocks in place, investment should be effective in promoting economic growth, particularly growth in which all can share, providing that policies directly affecting investment are not restrictive. Experience has shown that policies that place few restrictions on domestic and foreign investors and on trade within and between countries are favorable to growth. Moreover, openness to trade and investment

will serve as an effective means of preventing monopolistic behavior by firms. However, there may still need to be legislation outlawing anticompetitive behavior. Competition policy should also provide for competitive access to natural monopolies in essential services such as power, water, and transport.

The above framework can now be used to assess the poverty reduction strategies of both the Government and ADB, and ultimately to make suggestions on how these strategies might be improved. This is the topic to which the discussion now turns in the following two chapters.