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2006-2007 WIDER Research Programme

The 2006-2007 WIDER research programme presents 12 research projects grouped into three thematic areas, each of which falls within the overall UNU thematic area of Globalization, Social and Human Development.

Poverty, Inequality, and Human Development

The achievement of poverty reduction in part depends on the extent of inequality, and inequality is an important issue in its own right given its impact on social stability, macro-economic stability, and economic growth. Since non-monetary measures of well-being are critical, the wider issue of human development is also important. Deep methodological problems remain in measuring poverty, inequality, and human development and in assessing their impact on development and economic growth more broadly. Projects within this theme will take account of the Millennium Development Goals.

Globalization, Finance, and Growth

The increasing turbulence of the global economy, as well as the increasing role of trade and external finance in development, raises major difficulties for the developing world, particularly the poorer countries. The global dimensions of development require cross-country research so that lessons learned can be transferred across regions, particularly best-practices in the areas of trade, finance, investment, and other international policy areas.

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This programme traditionally acts as an instrument for the Institute to conduct small-scale projects on topics of immediate policy importance, to experiment with the application of new analytical techniques to development issues, and to build new research ideas that may then constitute the basis of larger projects in the main programme.

Details on current and past research projects:

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Where is the Wealth of Nations?

by Kirk Hamilton

Can poverty reduction be sustained? The end of the twentieth century saw a renewed commitment to ending poverty embodied in the Millennium Development Goals. However, deep concerns remained that current rates of depletion and degradation of natural resources may undermine any progress to date. Achieving sustainable outcomes will require sustaining the total wealth—produced, human, institutional, and natural—on which development depends.

A 2006 World Bank publication, *Where is the Wealth of Nations? Measuring Capital for the 21st Century* approaches the problem of sustainable poverty reduction from two angles: What is the composition of national wealth? And how rapidly is it being accumulated? The latter question is the key to sustainability.

There are no sustainable diamond mines, but there are sustainable diamond-mining countries. Implicit in this statement is the assumption that it is possible to transform one form of wealth—diamonds in the ground—into other forms of wealth, such as buildings, machines, and human capital. Achieving this transformation requires a set of institutions capable of managing the natural resource, collecting resource rents, and directing these rents into profitable investments. Resource policy, fiscal policy, political factors, institutions, and governance structure all have a role to play in this transformation.

Natural resources play three basic roles in development:

- The first role, mostly applicable to the poorest countries and poorest communities, is that of local natural resources as the basis of subsistence.
- The second role is as a source of development finance. Commercial natural resources can be important sources

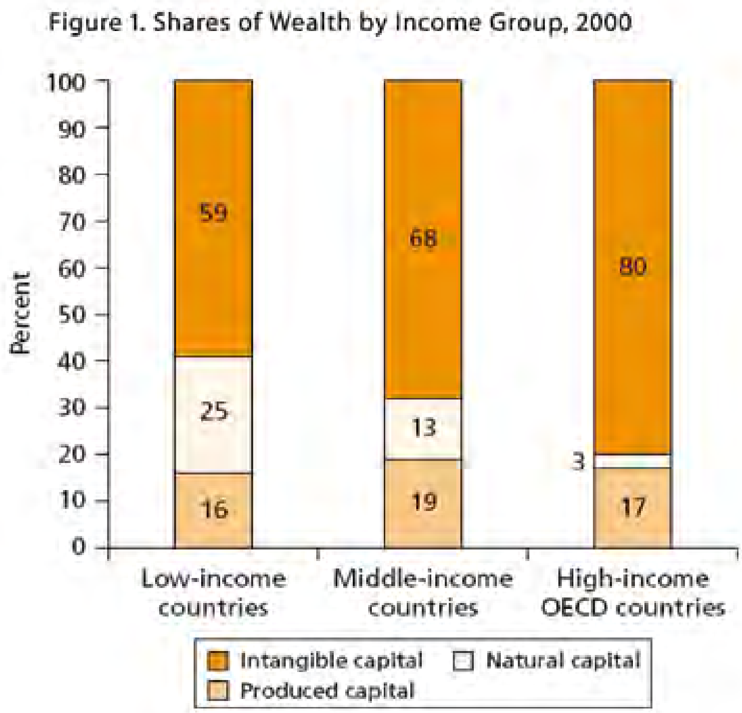
of profit and foreign exchange. Rents on exhaustible, renewable, and potentially sustainable resources can be used to finance investments in other forms of wealth. In the case of exhaustible resources these rents must be invested if total wealth is not to decline.

• The third role is as the source of environmental services—watershed protection and pollination, for example—that underpin many other economic assets. The value of agricultural land, for example, is closely tied to the value of the environmental services supporting its productivity.

Evidence on the importance of natural resources

Figure 1 provides summary information on the shares of natural resources in the total wealth of high income and developing countries. This figure decomposes the total wealth of nations into three broad components across low-, middle-, and high-income countries. Produced capital is the familiar blend of buildings, machines, and infrastructure that is measured in standard national accounts. Natural capital is the value of agricultural land, forests, and subsoil resources such as minerals and energy. 'Intangible' capital is the value of everything else—human capital, social capital, and the quality of institutions and governance. The underlying estimates of total wealth per capita are nearly $440,000 in high-income countries, nearly $28,000 in middle-income countries, and less than $8,000 in low-income countries.

Intangible capital is by far the largest share of total wealth in all countries.



Source: Where is the Wealth of Nations? World Bank 2006. Oil states excluded.

A high share of natural wealth does not automatically imply that natural resources are important for growth, but it does at a minimum imply that these resources are important for current well-being.

For the poorest countries, however, natural capital is a larger share of total wealth than produced capital—demonstrating how important natural resources are for social welfare in these countries. This suggests that properly managing natural resources must be a key part of development strategies, particularly since the poorest households in these countries are usually the most dependent on these resources.

This analysis also shows how the share of natural resources in total wealth declines as incomes rise. This does not mean they are unimportant or that they can be exploited indiscriminately—food, fiber, minerals, and energy are essential for economic activity and well-being. Rather, this demonstrates how intangible assets become proportionately much more important as countries develop, with the productivity of people increasing along with the quality of their institutions. In fact, *Where is the Wealth of Nations?* reports that the value of natural capital per person actually rises with income, from roughly $2,000 per capita in low-income countries to nearly $9,000 in high-income countries.

From a development perspective, a key message of Figure 1 is that natural resources make up a significant share of the total wealth in low-income countries—26 per cent—and that this is substantially larger than the share of produced capital. Sound management of these natural resources can support and sustain the welfare of poor countries and of poor people in those countries as they move up the development ladder.

Natural resources and wealth accumulation

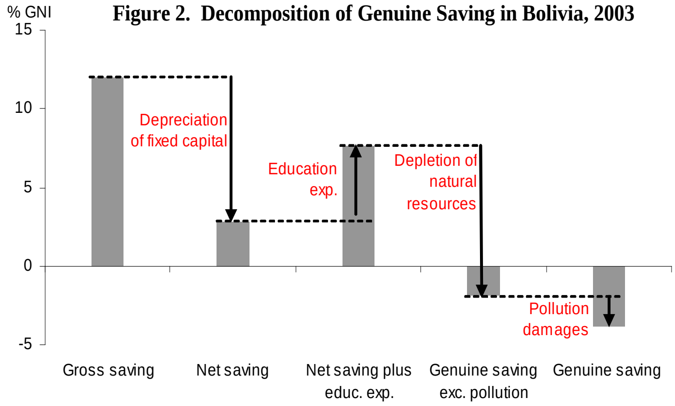
Saving is a core aspect of development. Without the creation of a surplus for investment, there is no way for countries to escape a state of low-level subsistence. Saving is measured in national accounts as the difference between income and consumption—what is saved is by definition that which is not consumed. But standard national accounts do not measure the *dissaving* associated with the depletion of natural resources.

Adjusted net or 'genuine' saving

measures the true level of saving in a country after accounting for depreciation of produced capital, for investments in human capital (as measured by education expenditures), for depletion of minerals, energy, and forests, and for damages from local and global air pollutants. An important body of economic theory suggests that if current net saving is negative in a given country, then its future welfare must decline—in other words, if we care about sustainability, we need to be concerned with the net rate of wealth creation.

Resource dependence complicates the measurement of saving effort because depletion of natural resources is not visible in standard national accounts. Countries can believe they are on a sustainable path, when in fact they are running down their total wealth. Figure 2 looks at genuine saving in Bolivia to illustrate this point.

Figure 2. Decomposition of Genuine Saving in Bolivia, 2003



Source: *Where is the Wealth of Nations?* World Bank 2006.

Figure 2 makes clear the importance of resource depletion and pollution damages in assessing wealth creation in a resource-dependent economy. While investments in human capital partly offset the value of depreciation of produced capital, the depletion of natural resources (mostly natural gas in this instance) plus damages from local and global air pollutants results in a negative net saving rate—total wealth in Bolivia actually declined in 2003.

Decision makers in Bolivia presumably believed that the rate of wealth creation in the country was nearly 12 per cent of Gross National Income (GNI) in 2003—this is what was reported in the national accounts. A fuller analysis highlights the extent to which depletion and damage to the environment affect the bottom line on wealth creation.

Some conclusions on natural resources and sustainability

If development is approached as a process of portfolio management, then the figures make clear that both the size and composition of the portfolio vary hugely across levels of income. Managing each component of the portfolio well and transforming one form of asset into another efficiently are key facets of development policy.

The linkage between measured changes in real wealth and future well-being only holds if our measures of wealth are suitably comprehensive. This is the prime motivation for expanding the measure of wealth to include a range of natural and intangible capital. This richer picture of the asset base also opens the door to a range of policy interventions that can increase and sustain growth.

The notion of development as portfolio management is powerful. Certain assets in the portfolio are exhaustible and can only be transformed into other productive assets, such as infrastructure or human capital, through investment of the resource rents. Other assets are renewable and can yield sustainable income streams. Economic analysis can guide decisions concerning the optimal size of these assets in the portfolio. Some assets, such as produced capital, depreciate over time. National savings can be used to invest in natural assets, produced capital, or human capital, whichever yields the highest marginal return.

Each year some 10–20 developing countries have negative genuine saving rates. What should the policy response be? Monetary and fiscal policies affect saving behaviour, and public sector dissaving can be a key target of policy. If investment in human capital is treated as saving, then efforts to increase education expenditures and make them more effective can boost overall saving. For natural resources, the general prescription is not to simply reduce exploitation but rather to reduce incentives for overexploitation—this will typically entail reforms in the resource sectors. For pollution the question is clearly one of bringing marginal damages to human health and other assets in line with the marginal costs of reducing pollution emissions.

The figures in *Where is the Wealth of Nations?* make visible what is often obscured in our standard economic indicators. The value of natural wealth is nearly twice as large as produced capital in low income countries. And the depletion of this wealth, combined with pollution damages, is placing many countries on an unsustainable path.

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Beyond Formality and Informality

by Basudeb Guha-Khasnobis, Ravi Kanbur, and Elinor Ostrom

The constructed opposites of formality and informality have dominated the development discourse for more than half a century. They have anchored theoretical, empirical, and policy discussion in many disciplines as they have studied the development process. Despite this pedigree, the usefulness of the formal–informal dichotomy has constantly been debated in the literature which still does not provide any consistent definitions. Instead, it turns out that formal and informal are better thought of as metaphors that conjure up a mental picture of whatever the user has in mind at that time. Reviews have concluded that there are competing perspectives rather than a single dichotomy. Discussions of the formal and the informal have been enriched considerably by the literature of the past two decades on (self) organization of common property regimes, and by the push in some policy circles to extend property rights to groups of individuals who do not currently 'enjoy' such rights.

Not surprisingly, the views on the entities that comprise the informal sector also differ greatly. In official statistics, different countries use the terms differently in detail even when they might mean the same thing in a general sense. The international official definitions, for example as codified by the ILO, have been expanding. The current official definition of 'informal sector' was adopted by the 1993 International Conference of Labour Statisticians based on characterizing an enterprise as informal. In 2003, guidelines were introduced to expand the definition to include informal employment outside informal enterprises, with an appropriate definition of the former.

From the mass of alternative uses of the terms and alternative characterizations, we would like to highlight two strands that are particularly relevant for the current policy dialogue. The first strand is the notion of informal as being outside the reach of different levels and mechanisms of official governance and formal as being reachable by these mechanisms. This notion underlies many official definitions of 'informal enterprises' as those that are not registered and are legally outside the tax net. It also underlies many analytical investigations of enterprises and activities that operate illegally, in violation of formal state rules and regulations, even though informality and illegality are not considered to be equivalent in this notion. This notion also animates the lively policy debate on the extent to which the informal sector owes its existence to 'overly constraining' official regulations that lead to economic activity taking place outside this net. And, of course, this is also the dimension that best captures different views on the benefits or otherwise of extending the reach of official structures to where they currently do not reach (e.g. legal property rights), or of reducing this reach (e.g. labour regulations).

The second strand that can be discerned in the discourse has to do with the nature of organization. The informal is often identified with 'lacking structure' and the formal with 'structured'—the term 'unorganized sector' is often used. In the policy discourse, the association of the informal with unstructured has been a powerful impetus for interventions that have often led to disaster. A striking illustration of this is the attempt to nationalize forests in Nepal, based on the analysis that deforestation was being caused by the inability of small local communities to prevent environmental degradation. In fact, as we now know, the local communities had better structures in place to deal with the deforestation that was the result of population and other pressures. These structures were not recognized, and were replaced by the formal state structures which proved to be ineffective and corrupt leading to even faster deforestation. The government in Nepal later reversed its earlier policy and started turning forests over to Forest User Groups. The opposite is true of the software industry of India, now recognized as a world leader. It flourished under the entrepreneurship of some highly skilled and far-sighted individuals, quickly becoming the fastest growing export sector of India. Until recently, India had a highly regulated economy, but the government was surprisingly non-interfering as far as the software sector was concerned. Even until very recently, the industry's output and exports were categorized as 'miscellaneous' in India's national accounts (as opposed to being called 'manufacturing' or 'services'), such was the degree of informality. The initial abstinence of the government was indeed a blessing in disguise.

These two dimensions—the reach of official governance and the degree of structuring provide an initial entry to a framework for capturing the many definitions that abound in the literature. The distinction between the two dimensions is not redundant. This is illustrated for example by the detailed empirical work showing the highly structured interactions within groups that manage common-pool resources, far removed from any interaction with official governance. Moreover, for similar levels of connection with the state tax system, we see enterprises with very different types and complexities of internal structure. The two dimensions do, however, interact. On the one hand, attempts by official governance to extend its reach, for example, by widening a regulation to an area where it was not previously applied, will in general lead to a response that may move some activities outside the reach of the regulation (legally or illegally). In so doing, it may well change the structuring of the activities that escape the official net. It has been observed, for example, that relationships within illegal activities are often very highly structured, sometimes more so than in legal activities, as a response to the risks of the activity in question. By the same token, some types of (re)structuring of activities make official intervention easier, or may even be predicated by the nature of the official governance frameworks.

On the policy front, the issue is not one of 'greater' or 'lesser' reach of government being better in general, as it is so often characterized, but one of the 'right' reach of government. This 'right' reach has to take into account (1) the objectives of intervention, (2) the implementation of the intervention, and (3) the response of the structuring of activities to this intervention (it being recognized that 'more' or 'less' structured does not necessarily correlate with 'good' or 'bad').

The objectives of intervention can then be seen under two broad headings: (1) Improving the well-being of the poor and of society at large by improving the capacity of individuals to self-organize and address their collective action problems by themselves and (2) Improving the well-being of the poor and of society at large by addressing the problems that arise when individuals interact through markets.

These two objectives may be seen as addressing group failure and market failure, through better operation of self-organized groups and through better operation of markets. Of course, it goes without saying that the two objectives interact, with outcomes in one influencing outcomes in the other. The myriad of interventions that we actually see in practice can be assessed in the above framework. But why do some interventions achieve their objectives while others do not? A key step is to focus in on the goals of such efforts and the specificities of time and place. We have repeatedly learned from many studies of policy processes, that no single institutional arrangement works across diverse policy areas or even diverse subtypes within a broad policy area. Copying interventions that worked well in one country may lead to a major failure in another country.

We would propose, therefore, especially in light of official statistical conventions already adopted, that the formal–informal continuum apply strictly to the continuum between relatively high and relatively low levels of the reach of official governance mechanisms, suitably specified and measured in each context. This relates the terminology directly to the policy discourse on the nature and extent of government intervention in economic activity. However, even in this case we would prescribe a health warning—informal does not mean unstructured and chaotic, and does not invite policy intervention on those grounds! More generally, we would keep the 'reach of government' as a purely descriptive term, leaving the issue of whether it is a good thing or a bad thing to be decided on a case by case basis, taking into account the self organizing structures that communities are capable of producing, within or without the reach of official structures. We should move beyond formality and informality, and tackle directly the policy interventions that will help the poor to unlock their potential through groups and through markets.

This article draws on Chapter 1 of 'Linking the Formal and Informal Economy: Concepts and Policies' edited by Basudeb Guha-Khasnobis, Ravi Kanbur and Elinor Ostrom. Oxford University Press, September 2006.

See also 'Informal Labour Markets and Development', edited by Basudeb Guha-Khasnobis and Ravi Kanbur. Palgrave Macmillan, July 2006.

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The New Economy in Development: ICT Challenges and Opportunities

by Anthony P. D'Costa

The last three decades have witnessed a sea change in the character and functioning of the world economy. With the speeding up of the relative decline of the industrial sector, the rise of the services economy, and the growing ubiquitousness of information and communications technologies (ICT) a 'new economy' has been created. There is increasing recognition that knowledge-based economic activities are key to international competitiveness and productivity growth, and that industrialization, particularly manufacturing, is no longer viewed as the principal driver of economic growth. This poses a fundamental question: what are the implications of the new economy for developing countries?

WIDER undertook a major initiative to better understand the relationship between development and the new economy. This initiative, under the direction of Matti Pohjola (University of Helsinki) involved three interrelated research projects undertaken between 1998 and 2003: 'Information Technology and Growth', 'Production, Employment, and Income Distribution in the Global Digital Economy', and 'Information Technology and Global Economic Development'. A book is now published based on selected papers from a related WIDER conference in 2002. It takes a broad look at the new economy, both theoretically and empirically, to understand the development possibilities and attendant challenges associated with ICT in selected non-OECD countries and regions. Theoretically it addresses some conceptual issues pertaining to the new economy and development implications of the new carrier technologies such as ICT. Empirically the book covers Argentina, India, the Philippines, South Africa, the Arab region, and the transition economies of Eastern Europe. The adoption and impact of ICT in both rural and industrial sectors are also analyzed.

Though the emergence and the impact of ICT, which includes computers, software, satellite communications, e-mail, and the internet have been investigated by scholars and policymakers in recent years, the strength of this collection lies in its systematic academic and policy-oriented investigation of the nature of the new economy and its role in the development process. The contributors represent a good mix of academics and policymakers from universities and policy institutions from both OECD and developing country regions. They present a wealth of data that will be useful for both scholars and practitioners.

As services comprise a significant sector in the new economy, this volume addresses some of the vexing conceptual issues pertaining to the measurement and performance of services. Services are intertwined with new technologies such as telecommunications and the internet, making them difficult to measure. Their network characteristics require new global rules of engagement. Consequently, whether developing countries can work effectively with the changing global regime, how they might utilize the open access to knowledge and information, and how they can adopt best practices (such as telemedicine, distance learning, and e-government), are significant questions for development.

The empirical studies show that the impact and potential of ICT for development are at best mixed and there is considerable variation within and among countries. Small domestic markets, as in Argentina, limit the adoption of ICT and thus productivity growth. This can be seen also in the case of several transition economies of central and Eastern Europe. In the Arab region income differences and low levels of human capital development seem to hinder the widespread diffusion of ICT.

Developing countries are structurally disadvantaged in seeking the best from the global regime of ICT infrastructure, which, *inter alia*, is related to their lack of key ingredients such as human capital, physical infrastructure, and venture capital to exploit ICT. But that does not mean the doors are closed. Poor countries (such as the Philippines and India) that have unwittingly created human capital are better placed to interact with the global economy, adapt imported ideas and know-how, and localize them. The wide variation in ICT diffusion is mainly due to weak economic and institutional environments. This suggests that 'old' economy needs such as infrastructure development and domestic market stimulation are still relevant.

Several lessons emerge from these individual studies. First, ICT, in the form of automation, suggests not only increasing competitiveness of small and medium enterprises due to productivity growth it also results in labour displacement, especially of the unskilled. At the same time, productivity-led opportunities thrown open by economic integration suggest that the vast rural poor and illiterate populations may miss out on the benefits of ICT if appropriate social policies are not aimed at improving the quality of their lives. Second, developing countries must still contend with traditional development concerns such as poverty and inequality as well as structural transformation from agriculture to industry. Yet, they must be alert to the possibility that increasing export competition in labour-intensive manufactures means declining terms of trade when not offset by continuous learning and technological upgrading. The new economy also imposes a reduction in social protections due to endemic fiscal crisis and business demands for flexibility and deregulation, open unemployment due to privatization of the state sector, and, paradoxically, by productivity-enhancing ICT. The continued emphasis on investment in traditional development spheres such as education, literacy, basic health, and physical infrastructure is considered necessary to make participation in the new economy more effective.

Third, while the evidence of productivity growth based on ICT diffusion is not robust for developing countries, partly due to productivity lags, it would be foolhardy to ignore the benefits of ICT in poor societies. If anything, ICT is an enabling carrier technology, applicable in both new and old economies. While ICT is not a panacea for poverty, developing countries, if they fail to actively engage in the use and production of ICT goods and services, are likely to be impoverished further and experience deepening problems associated with the global digital divide.

Fourth, to avoid global polarization the consumption of both ICT goods and services must be increased. ICT services can be employed in a wide variety of social and economic sectors such as education, health, rural development, business, banking, and manufacturing activities. Thus, fostering knowledge workers and establishing communications infrastructure is consistent, though in conflict resource allocation-wise, with basic education and human capital development and with infrastructure spending on rural roads and irrigation. The fundamental development challenges of literacy, basic education, alleviation of poverty and inequality, health, and the rural–urban gap could be addressed by wider ICT adoption, complemented by a variety of critical services to under-served rural and low-income constituencies. Poor countries must foster e-development to complement a wider development strategy to meet basic needs. Based on the extensive and intensive use of ICT, public sector services can be efficiently provided to citizens, business, and to various government departments. The expected benefits are lower transactions costs, greater efficiency in service delivery, more transparent governance, and productivity growth.

Fifth, the challenges to the implementation of such projects should not be underestimated as they require financial and human resources, long-term commitment, intra-government coordination, and public acceptance. ICT cannot be seen as a technological fix to what are essentially social and political problems. At the same time, the economics of ICT suggest that developing countries cannot increase their long-term economy-wide productivity if they remain outside the new economy. The role of the government and other institutions cannot be overemphasized, especially in areas of regulatory reform.

Finally, the continued emphasis on knowledge workers, information literacy, and communications infrastructure vital to participating effectively in the new economy also suggests that developing countries must find a political voice at the global level so that they are not excluded from the multilateral negotiations on the emerging global information society. In the end global participation must be complemented by the ensuing 'good' governance that is expected to emerge from the widespread adoption of ICT.

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Increasing Aid Effectiveness by Harmonization Requires Reduced Proliferation

by Mark McGillivray

The international development community, including senior representatives from partner countries, bilateral and multilateral donors, met in Paris in late February and early March 2006 at the High Level Forum on aid effectiveness. What emerged from this forum was the Paris Declaration, an international agreement to which over 100 Ministers, Heads of Agencies and other Senior Officials committed their countries or organizations to various efforts aimed at increased harmonization and alignment of aid activities. This articles looks at aspects of the Paris Declaration in a broader aid effectiveness context. It argues that the international donor community must urgently address aid proliferation if greater harmonization is to occur.

For many decades there were mixed messages as to whether aid was effective in reducing poverty by promoting economic growth in the developing world. Many of these messages came from the research literature. Some studies found that aid decreased growth; others found that it had no impact or that it increased growth. This lack of a consensus regarding the country-level impact of aid combined with strong evidence that aid projects were in general effective in attaining their intended outcomes, was described as the 'macro-micro paradox' of aid. This paradox was widely accepted in the aid policy and research circles.

Times have changed. Donors are now freer to pursue development-first aid strategies, with less emphasis on commercial and strategic objectives. Many more progressive donors provide a larger share of world aid flows. The research literature on the country-level impacts of aid has also come a long way in recent years due to better data and empirical techniques. Research conducted over the last 10 or so years provides overwhelming evidence that aid is effective: economic growth in developing countries would have been lower in its absence. Virtually all of the approximately 50 studies that have been conducted, albeit with a few well-publicised exceptions, draw this conclusion.

While estimates vary, it is reasonable to suggest that average annual per capita GDP growth in developing countries would be as much as 2 per cent lower in the absence of aid flows. Taking into account empirical evidence on the relationship between growth and income poverty reduction, such a contribution to growth means that aid has lifted up to 40 million people out of income poverty over the last 10 years. While these figures are crude approximations, they do give some idea of the effectiveness of aid. Combined with the knowledge that aid contributes to income poverty reduction via other routes and has other developmental benefits, they certainly tell us that the macro-micro paradox would appear to be dead and buried.

Yet this should not imply that aid effectiveness cannot be improved, that it works in all countries, that no resources have been misused or wasted, or that there are no other interventions that might be more effective in reducing poverty. Aid still has many failings, and donors have a responsibility to address them in ways that go well beyond only increasing the level of aid. Indeed, if the above numbers are any guide, increases in the level of aid will need to be accompanied by substantial improvements in its effectiveness if aid is to make any meaningful contribution to achieving the Millennium Development Goal of halving the number of people living in income poverty between 1990 and 2015.

One failing of aid, identified in the Paris Declaration on Aid Effectiveness, is insufficient harmonization. The Declaration calls on donors to be more harmonized and collectively effective. Recognizing that all developing countries have limited or in many cases very weak administrative capacity, the Paris Declaration also calls on donors to be less burdensome on partner countries.

It should be emphasized that there is much more to the aid effectiveness agenda outlined in the Paris Declaration. Progress in any one agendum is very much dependent on progress in the others. Those most closely linked to harmonization are alignment and ownership. Alignment requires donors to base their aid-funded activities on partner country national development strategies, institutions, and procedures, avoiding the imposition of multiple conditions based on other agendas. Ownership requires that partner countries exercise effective leadership over their development policies and strategies and co-ordinate development efforts.

The Paris Declaration contains many strong statements, and rightly so. It states that 'increased aid flows are unlikely to make a serious dent into global poverty if donors do not change the way they go about providing aid and developing countries do not enhance the way they currently manage it'. 'Business as usual' will undermine further attempts to reduce poverty, it asserts. Yet one aspect of 'business as usual' has

Table 1. Aid Proliferation, 1980 to 2004

	Donor-funded Activities			ODA US$ Millions[a]	
	Total	Average per Donor	Average per Partner	Total	Average per Activity
1980					
All Donors	3283	143	23	41462	12.6
Finland	3	-	1	16	5.3
1990					
All Donors	7783	338	50	50286	6.5
Finland	358	-	4	473	1.3
2004					
All Donors	59312	1913	357	90411	1.5
Finland	643	-	67	96	0.5

[a] Constant 2003 prices. Source: OECD *International Development Statistics On-line*.

been given insufficient attention in the Paris Declaration and elsewhere. It concerns the proliferation of aid-funded activities.

Table 1 highlights the growing concerns over proliferation. In 1980, donors funded 3283 activities in partner countries. This corresponds to an average of 23 activities per partner country. By 1990 the total number of activities had more than doubled, to 7783, and the average per partner increased to 50. A radically different picture emerges in 2004. Donors now fund 59312 activities, or 357 per partner country. As a partial result of this proliferation the average dollar value per activity has fallen from US$12.6 million in 1980 to US$1.5 million in 2004. Finnish development aid, for example, follows a broadly similar pattern, with the number of average activities per partner increasing from 4 in 1990 to 67 in 2004. Finland does, however, fund far fewer total activities than other donors do on average. In 2004 it funded a total of 643 activities, compared to the all donor average of 1913.

Proliferation evident from Table 1 clearly sends worrying messages about aid effectiveness in general and the Paris Declaration in particular. The average number of activities per partner country has increased by 1450 per cent between 1980 and 2004. Has there been a commensurate increase in capacity of partners to efficiently handle aid activities? Or has the nature of these activities changed, so that they require much less attention from partners? One would expect not, on both accounts, and can only speculate as to the extent this proliferation has reduced the otherwise reasonably positive impact that aid has had on poverty reduction.

What would appear clear is that the Paris Declaration's attempts to achieve greater harmonization, alignment, and partner country ownership will be frustrated unless the proliferation of aid activities is addressed. The prime purpose of this note is to draw attention to the proliferation issue, and not to propose ways of addressing it. But one way of achieving reduced proliferation, possibly, is for a greater share of aid to be provided as budget support. Other measures also need to be considered.

Mark McGillivray is a Senior Research Fellow at WIDER. His main areas of research focus on issues such as social development indicators, the Millennium Development Goals, and development aid. He is the co-organizer of the WIDER Conference on Advancing Health Equity, 29-30 September 2006.

Focusing Fiscal Policy on Poverty Reduction, Reconstruction, and Growth

by Tony Addison

An effective state is characterized by an ability to mobilize revenue and to spend it on infrastructure, services, and public goods that both enhance the human capital and well-being of communities (especially the poor) as well as stimulate investment and employment creation by the private sector. An effective state also manages the public finances to ensure that macroeconomic balance is maintained, with policy neither too restrictive to discourage private investment and growth, nor too accommodative to create high inflation and crowd out private investment. Fiscal issues are therefore at the heart of the state's role in the development process and failure in this policy area—whether it is in taxation, public expenditures or in managing the fiscal deficit and public debt—can quickly undermine growth and poverty reduction. Moreover, for countries vulnerable to violent conflict fiscal weakness can be fatal to social peace when one or more ethnic, religious, or regional group is taxed unfairly—or receives too little from the allocation of public spending.

These and other crucial issues are addressed in *Fiscal Policy for Development: Poverty, Reconstruction and Growth*, edited by Tony Addison and Alan Roe, and now published in paperback by Palgrave Macmillan for WIDER. The book reviews all of the major areas of fiscal policy, setting out and assessing how thinking around public spending, taxation, and the macroeconomics of fiscal reform has evolved, particularly towards poverty reduction as well as conflict prevention and post-conflict reconstruction.

Fiscal policy is central to aid effectiveness

Fiscal policy also bears on the long-standing debate over aid effectiveness. The pioneers of development economics in the 1950s and 1960s assumed that the basic structures of public expenditure management and taxation that we take for granted in rich countries would not take too long to establish themselves in post-independent Africa and Asia. However they were sorely disappointed in many of the new African states, and in some of the Asian ones as well. In the 1970s poverty reduction was, for the first time, placed at the forefront of development; aid was intended to help governments meet basic needs but the assumption was again made that the associated pro-poor public spending would not be too difficult a job to organize. Pessimism set in with the 1980s and aid flows became organized around highly controversial programmes of structural adjustment, including fiscal reforms that often included crude mechanisms to curb public spending and bring fiscal deficits down (often resulting in unnecessary cuts in already low levels of pro-poor spending). The 1990s witnessed a growing recognition of the fiscal burden of servicing the debt left by the accumulation of aid loans and, towards the end of the decade, the start of a shift in aid towards budgetary support and away from project aid as country 'ownership' came into vogue. This trend is continuing today, although it periodically stumbles over the governance dimensions of fiscal policy, not least in countries reconstructing from conflict and those in unstable regions (notably the Horn of Africa).

The debate on aid and debt relief has taken on a particular resonance over the last year, generating much heat but also some light, with a succession of key events including the UN Millennium Summit in September 2005 (and also the work of the Millennium project which recommends a major scaling up of aid), the report of the Commission for Africa initiated by UK Prime Minister Tony Blair, the G-8 summit in Scotland in July 2005 at which aid and debt relief featured heavily, as well as the Helsinki Process on Globalization and Democracy. For those of us working on development it is difficult to recall any other recent period in which development—and the needs of the world's poorest people—have occupied so much public attention.

Inevitably much of the debate, while certainly well-meaning, has been broad-brush, sometimes simplifying the issues in order to mobilize public support for increased aid. Amidst the earnest pleas for more aid and debt relief, there are dissenting voices, arguing that the poorest countries will find it difficult to absorb and effectively use the additional resources, which the international community is devoting so much time to mobilizing. Certainly for those working on fiscal issues at the country-level how best to use aid (and domestic revenues) has always been a priority issue, and one that raises tough choices for the public finances, which cannot be glossed over. At the heart of the issue of aid effectiveness (as well as the related impact of debt relief), is state capacity in poor countries. This includes the quality and honesty of the public administration, and its ability to channel resources to the best uses, particularly to infrastructure and services which are of most benefit to the poor.

The MDGs cannot be achieved without good fiscal policy

Whether you believe that aid and debt relief can achieve their laudable goals depends therefore, in large part, on your view of the economics and politics of fiscal policy. The successful countries will be those that build effective systems of public expenditure management to transmit these extra resources into development spending and systems of taxation that mobilize domestic revenues to complement external official flows. And they will demonstrate an ability to manage the fiscal deficit and government debt burden, in particular to respond to the external (and internal) shocks which challenge policymaking in poor countries that are mostly dependent upon a narrow range of primary commodities. This is no easy set of tasks, and our ability to get anywhere near meeting the ambitious Millennium Development Goals depends to a large extent on improving the quality of fiscal policy in poor countries. This is especially the case in resource-rich countries where resource extraction is often an enclave activity (oil and natural gas in West Africa, for example) so that growth does not directly generate much in the way of increased employment; in these countries the main way that growth can reduce poverty is through the transmission of the resource revenues into higher pro-poor public spending. For the most part this is not happening, and the poor are missing out on the revenue boom provided by higher commodity prices (especially oil) with revenues instead flowing into spending for elites (or directly into their pockets). Similarly, in societies characterized by high levels of inequality in access to land and other productive assets, the best means for redistribution may not lie in redistributing these assets themselves but by incorporating redistribution into the fiscal system—through progressive taxation (of capital gains from land sales, for example) to finance public spending that creates better livelihoods and human capital for the poor. In summary, growth can contribute to poverty reduction even in societies with very high levels of asset inequality, but only if fiscal institutions are built and focused on the poor.

Fiscal Policy for Development has enjoyed considerable success and, together with the Palgrave Macmillan volume on *Debt Relief for Poor Countries* (co-edited by Tony Addison, Henrik Hansen and Finn Tarp), it offers what we hope is a reasonably balanced view of the issues for policymakers and researchers alike. Certainly, it is vital to improve our technical understanding of how fiscal policy works for development, but fiscal policy is more than just a question of good economics; it is also fundamental to the politics of development. Who gets what from the state, how that public spending is financed, and who pays for it, say much about how a society is governed and whether policy choices do—or do not—give priority to the poor.

Fiscal policy for development
Key Points

- An effective state is characterized by an ability to mobilize revenue and to spend it well on infrastructure and public services with high returns for growth and poverty reduction.

- Economic growth raises the amount of revenue that can be mobilized through taxation: building an effective tax system is therefore a foundation for higher public spending to convert growth into poverty reduction.

- Without good public expenditure management, the poorest countries will find it difficult to absorb and make good use of the additional resources provided by increased aid, debt relief, and 'innovative' sources of development finance.

- Improving the governance dimension of fiscal policy, including increased transparency in the collection and use of public money, will determine progress in shifting aid towards budgetary support and away from project aid—thereby increasing country ownership.

- Failure in fiscal policy can quickly undermine development and, in the worst cases, contribute to conflict as grievances concerning an unfair distribution of spending and taxation spill over into violence.

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WIDER Special Events and Book Launch

Susanna Kekkonen

William Easterly speaking at the first plenary session of the WIDER Conference on Aid: Principles, Policies and Performance, held in Helsinki on 16-17 June 2006.

Plenary speakers included Paul Collier (University of Oxford), William Easterly (New York University), Patrick Guillaumont (Universite d'Auvergne), Peter S. Heller (IMF), Helen Milner (Princeton University), Gustav Ranis (Yale University), Finn Tarp (University of Copenhagen), and Adrian Wood (University of Oxford). The webcast of all plenary sessions is available online at www.wider.unu.edu.

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Launch and presentation of the WIDER study on Macroeconomic Policy in the Franc Zone: What can the European Central Bank learn from Africa? by David Fielding and Jean-Paul Azam. Organized by OECD Development Centre and WIDER in Paris, at OECD Headquarters, 21 February 2006.

From left: Nicolas Pinaud, David Fielding, Kenneth Ruffing, and Jean-Paul Azam. (Bruno Cabrillac absent from photo.)

2006 WIDER Annual Lecture

The 2006 WIDER Annual Lecture will be delivered on 29 September 2006 in Helsinki by **Angus Deaton**, Dwight D. Eisenhower Professor of International Affairs, Woodrow Wilson School, Princeton University. Professor Deaton will address the Annual Lecture to the participants of the WIDER Conference on Advancing Health Equity, and a general audience in Finland at the Marina Congress Center, Helsinki.

WIDER organized two public lectures in spring 2006

The first public lecture was by Kirk Hamilton, on 'Where is the Wealth of Nations? Not Where you Might Think?', 7 March 2006. Kirk Hamilton is Lead Environmental Economist and Team Leader, Policy and Economics, Environment Department, the World Bank, where his current projects include analytical work on the links between poverty and environment, 'greening' the national accounts, and the analysis of public expenditures on the environment.

The second public lecture was by Dennis McNamara on 'Displacement and Conflict: Breaking the Cycle', 8 May 2006. Dennis McNamara is Special Adviser to the UN Emergency Relief Coordinator and Director of the Inter-Agency Internal Displacement Division in the UN's Office for the Coordination of Humanitarian Affairs (OCHA). Details and summaries of the presentations are available on the WIDER website: www.wider.unu.edu.

Advancing Health Equity

WIDER Conference

Comparisons of life styles and living standards increasingly pay attention to non-income dimensions of well-being. Health in particular is recognized for both its intrinsic and instrumental value, contributing directly to an individual's level of well-being, and indirectly through its impact on other components. Substantial and widespread improvement in health outcomes has taken place during the past century. Despite this progress many individuals suffer health deprivation, with outcomes falling far short of those commonly accepted elsewhere. This conference will bring together researchers and practitioners, from both developed and developing countries, to analyze the causes and consequences of health deprivation and inequality, to examine patterns and trends in these outcomes, to evaluate alternative policy options, and to identify future research directions.

Conference topics will include:

- concepts and measures of health status
- trends in health deprivation and inequality
- causes of health deprivation and inequality
- link between health and income deprivations
- labour market outcomes and health status
- nutrition and health
- intra-household issues in health
- evaluating alternative health policies

Helsinki, Finland, 29 - 30 September 2006
Marina Congress Center
Katajanokanlaituri 6

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World Institute for Development Economics Research

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The conference is intended for researchers and policymakers from the academic, government and development communities

For applications and further communication: www.wider.unu.edu

WIDER Publications

Policy Brief

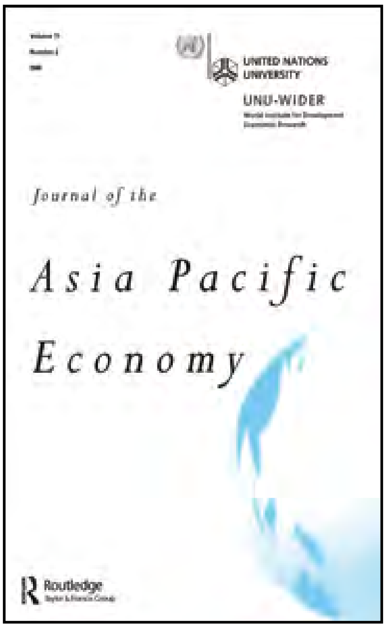
Fiscal Policy for Poverty Reduction, Reconstruction, and Growth
Tony Addison, Alan Roe, and Matthew Smith
UNU Policy Brief No. 5, 2006

Annual Lecture

2005 WIDER Annual Lecture
The World is not Flat: Inequality and Injustice in our Global Economy
Nancy Birdsall

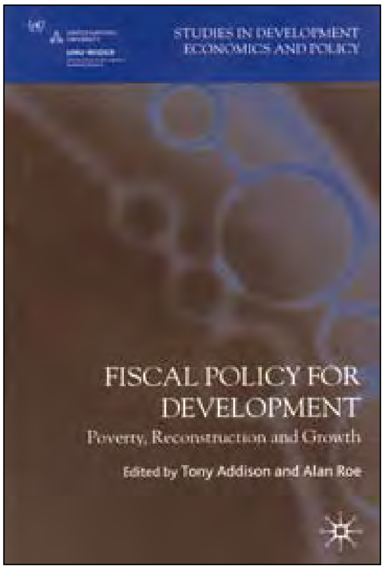
Journal

Journal of the Asia Pacific Economy
Volume 11, Number 2 (May 2006)
WIDER Special Issue
Well-being Achievement in Pacific Asia
Guest Editor: Mark McGillivray



Books

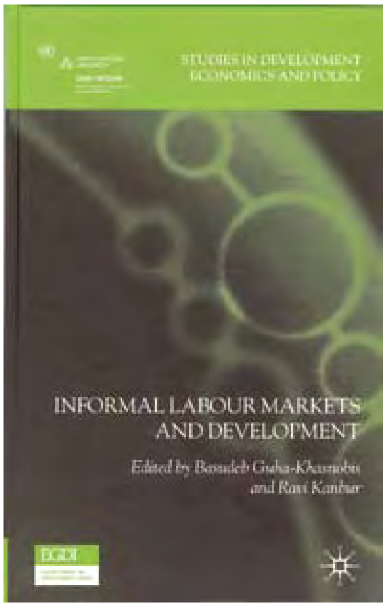
New in paperback
Fiscal Policy for Development: Poverty, Reconstruction and Growth
Edited by Tony Addison and Alan Roe
(paperback 0230004997)
May 2006
Studies in Development Economics and Policy
Palgrave Macmillan



With a new and up to date preface to this paperback edition, *Fiscal Policy for Development* provides the original comprehensive and balanced guide to the current policy debate and new results on the development impact of fiscal policies. It is essential reading for students of development economics as well as all those seeking to improve policy-effectiveness.

In translation
The Quality of Life: Part I, Lives and Capabilities (in Japanese)
Edited by Martha C. Nussbaum and Amartya Sen
(hardback 4898062466)
May 2006
Ribun Publishing Co. Ltd, Tokyo

Informal Labour Markets and Development
Edited by Basudeb Guha-Khasnobis and Ravi Kanbur
(hardback 1403987556)
July 2006
Studies in Development Economics and Policy
Palgrave Macmillan



…this volume from UNU-WIDER is a great contribution to an appreciation of the opportunities and challenges in the informal sector. The countries selected show the rich experience in the informal sector of big and small economies from different regions of the world. A better understanding of the informality will enable policy makers and development practitioners to bring out the best from this sector, contributing to a world with more economic growth and less poverty. This book accomplishes this task very well.
—Sudharshan Canagarajah, Senior Economist, The World Bank

WIDER Discussion Papers

DP2006/06 Markus Jäntti, Juho Saari, and Juhana Vartiainen: *Growth and Equity in Finland*

DP2006/05 Ha-Joon Chang: *Understanding the Relationship between Institutions and Economic Development: Some Key Theoretical Issues*

DP2006/04 George Rapsomanikis and Alexander Sarris: *The Impact of Domestic and International Commodity Price Volatility on Agricultural Income Instability*

DP2006/03 Basudeb Guha-Khasnobis and Gautam Hazarika: *Women's Status and Children's Food Security in Pakistan*

DP2006/02 George Mavrotas and Espen Villanger: *Multilateral Aid Agencies and Strategic Donor Behaviour*

DP2006/01 Mark McGillivray: *Aid Allocation and Fragile States*

Research Papers

For the complete list and free access to the 70 Research Papers published to date in 2006, visit the WIDER website or contact us (see Ordering WIDER publications).

Forthcoming books

Inequality, Poverty and Well-being
Edited by Mark McGillivray
(hardback 1403987521)
August 2006
Studies in Development Economics and Policy
Palgrave Macmillan

Linking the Formal and Informal Economy: Concepts and Policies
Edited by Basudeb Guha-Khasnobis, Ravi Kanbur, and Elinor Ostrom
(hardback 0-19-920476-4)
September 2006
UNU-WIDER Studies in Development Economics
Oxford University Press

No matter how you divide up the developing world—'formal-informal', 'legal-extralegal' (my preference)—one thing is not debatable: most people are poor, on the outside of the system looking in, and getting angrier every day. The message of this book is its time to stop talking and start designing reforms—based on the informal practices and organizations that poor entrepreneurs already use. I second that motion. If you rebuild the system from the bottom-up, they will come with their enterprise, creativity, and piles of potential capital.
—Hernando de Soto, President, Institute for Liberty and Democracy, Peru

The New Economy in Development: ICT Opportunities and Challenges
Edited by Anthony P. D'Costa
(hardback 0230001467)
September 2006
Technology, Globalization and Development Series
Palgrave Macmillan

Human Well-being Concept and Measurement
Edited by Mark McGillivray
(hardback 0230004989)
November 2006
Studies in Development Economics and Policy
Palgrave Macmillan

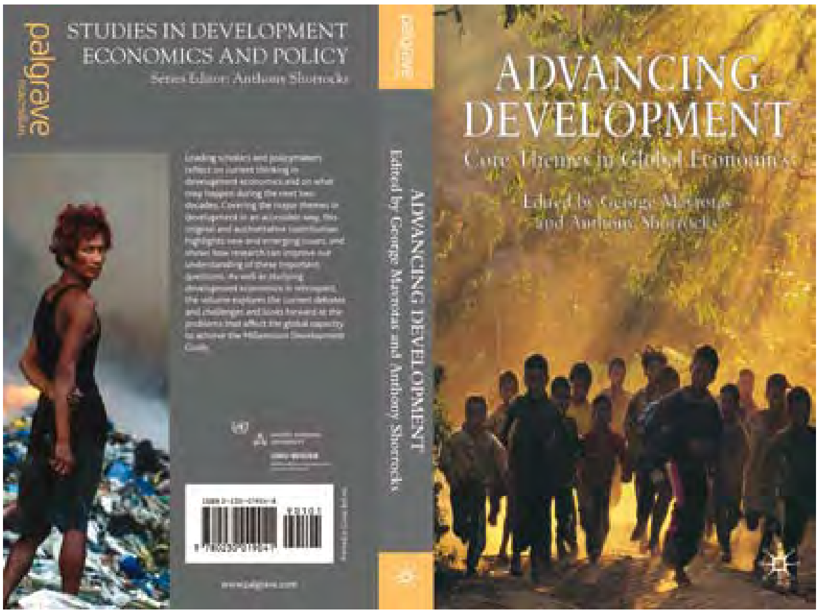
The Impact of Globalization on the World's Poor: Transmission Mechanisms
Edited by Machiko Nissanke and Erik Thorbecke
(hardback 0230004792)
December 2006
Studies in Development Economics and Policy
Palgrave Macmillan

Advancing Development: Core Themes in Global Development
Edited by George Mavrotas and Anthony Shorrocks
(hardback 023001902-1)
(paperback 0230019048)
January 2007
Studies in Development Economics and Policy
Palgrave Macmillan

WIDER *Angle* Newsletter

Mailing, back issues, and inserts

The last few months have seen the WIDER *Angle* mailing list grow to over 10,000 recipients, which means that quite a few new readers may have missed out on previous issues. Please contact us (see Ordering WIDER publications) if you would like to receive, for free, a selection of back issues (subject to availability). The WIDER *Angle* is also available in PDF from our website. We do not sell or share our mailing list with third parties, though we do occasionally include insets about products arising from WIDER research. We welcome feedback on all aspects of the newsletter, and of course on receiving updates about mailing addresses.



DARTS: A model for the Distributional Analysis of the Russian Tax and Transfer System

DARTS enables you to act as the Russian Finance Minister. Using this website model you can change various tax rates and state benefits including pension levels and housing subsidies, and then track the effects on the people of Russia: who pays the taxes, who gets the benefits, and who gains and loses. DARTS does this by calculating the impact of the changes on a representative sample of the Russian population taken from the Russia Longitudinal Monitoring Survey. This is the first time anywhere in the world that a simulation model of this kind has been made available online for use by the general public. A Russian language version is also available via this link. http://models.wider.unu.edu/darts_web/

WIDER Microsimulation Models for Five African Countries

As part of WIDER's project on Designing Africa's Poverty Strategies: Creating the Capacity for Policy Simulation, this website provides a user-friendly access to five African country (Botswana, Cameroon, Nigeria, South Africa and Uganda) microsimulation models. You can develop your own tax and transfer policy scenarios or conduct 'what if' simulation analysis. Each model provides you with the poverty, distribution, and budgetary impacts of your policy choices and compares the simulation results with the current state or the base scenario. As acting Finance Minister, design your reforms, and run the model to test your policy choices. http://models.wider.unu.edu/africa_web/

CALL FOR PAPERS

Southern Engines of Global Growth: China, India, Brazil, and South Africa (CIBS)

Submissions are invited for a WIDER workshop to be held in Beijing, 12-13 January 2007. Papers should focus on the growth experiences of China and India, e.g., performance, process, mechanisms, strategies/ paths, sources, prospects, and implications for other countries.

Send draft papers and a brief CV by 31 October 2006 to: CIBS@wider.unu.edu
Further details, including timetable and funding arrangements at: www.wider.unu.edu

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WIDER was established by UNU as its first research and training centre and started work in Helsinki, Finland, in 1985. Through its research and related activities, WIDER seeks to raise unconventional and frontier issues and to provide insights and policy advice aimed at improving the economic and social development of the poorest nations.

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Editorial contents, design and layout by Ara Kazandjian (e-mail: ara@wider.unu.edu), and Basudeb Guha-Khasnobis (e-mail: basudeb@wider.unu.edu).

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- UNU International Network on Water, Environment and Health (UNU–INWEH)
- UNU Programme for Comparative Regional Integration Studies (UNU–CRIS)
- UNU Institute for Environment and Human Security (UNU–EHS)
- UNU Programme for Biotechnology for Latin America and the Caribbean (UNU–BIOLAC)
- UNU Food and Nutrition Programme for Human and Social Development (UNU–FNP)
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