

FOR INTERNAL DISCUSSION

A REVIEW OF REDISTRIBUTION WITH GROWTH: AN APPROACH TO POLICY

1. Origin and Objectives of the Study

This report stems from a set of papers commissioned in 1973 from twenty renowned experts in developmental economics which provided the raw material used by a team of five authors to prepare the final document.^{1/} The preparation of this study was motivated by concern over the lack of consistency between the general perception of income distribution and employment as major objectives of development policy on the one hand and the analytical tools available to policy makers on the other. Given the stature of the individuals responsible for the document, expectations would, quite reasonably, run high and the announced objectives certainly stimulate the reader's anticipation. In essence, the report purports "to confront the problem of poverty, to suggest a reformulation of objectives and methods of measuring success in attaining them (by the developing countries themselves), and to indicate the types of programs and planning needed".

2. Constituent Parts of the Report

The volume is organized into four parts. The first contains an evaluation of the dimensions of the poverty problem in developing countries based upon available data. This is followed by a summary statement of the basic strategy proposed which, in brief, pretends to achieve structural

^{1/} The five scholars are Montek Ahluwalia, Hollis Chenery and John Duloy of the World Bank and Clive Bell and Richard Jolly of the Institute of Development Studies of the University of Sussex.

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changes benefiting the poor by a diversion of a substantial proportion of development resources in their favor. In Part II this strategy is discussed in greater detail in terms of particular policies and programs and of their political and administrative implications. It should be noted that the survey is restricted to the mixed economy.

Although the authors claim that they believe that many pertinent lessons and alternatives may be learned from the socialist developing countries particularly China and Cuba, it was felt that the documentation and analysis of these cases are too inadequate to incorporate them in a meaningful fashion. Thus, the document is essentially a study of alternatives which its authors deemed viable within the capitalist system. This is explored from a more technical perspective in Part III in which a range of planning techniques utilizing formal models is surveyed. Finally a short concluding statement is presented.

The structure of the publication as described here and the presence of a section entitled "Conclusion", however, should not lead one to believe that the volume is a unified work whose sections are well meshed with each chapter progressively contributing to novel interpretations of the under-development syndrome and to a theory of income distribution. On the contrary, the final section is merely a brief summary - not an integrated set of conclusions. Considerable contradictions and overlapping exist in the volume as well. These result in great part because of the design of the report which is a collection of separate papers whose common bonds appear only as the now commonplace recognition that the pursuit of economic growth as a major objective of society is a mistaken goal yielding disillusionment and the desire to incorporate non-economic variables in some fashion into development planning and analysis within the framework of the capitalist system to alleviate mass poverty.

3. Theoretical Base

The report parts from the base that a variety of positions exist which lend themselves to considerable scepticism with regard to the efficacy of development strategies as presently conceived. On the one hand it points to the view that the problem of income distribution is essentially a political problem and that attempts to formulate it in

/economic terms

economic terms are fundamentally mistaken. From another perspective existing economic theory (largely based on concepts of marginal productivity) is believed incapable of providing the economic answers to even those questions of a purely economic nature which are posed in attempts to deal with problems of poverty and income distribution.

The base of this study is that both positions are wrong. In the proposed conceptual framework it is assumed that the question of political feasibility can somehow be resolved. It should be noted that although the problems of achieving a political consensus are discussed in a separate paper later in the volume, the basically optimistic idea advanced here that some degree of "muddling through" by means of mass mobilization or pressure from above will eventually overcome the political obstacles involved remains amorphous throughout the document.

Perhaps of even greater significance the question of political viability is never incorporated in operational terms into the model for income distribution which is offered. Essentially this model seeks to demonstrate that the problem is not one of choosing between growth and income distribution but of generating a desired pattern of income growth with special emphasis on poverty groups. In essence, the model purports to achieve "redistribution through growth".

Consequently, it stresses the importance of setting targets for the rates of income in the lower income groups rather than focussing on static presentations of income inequality patterns. For the purpose of setting goals and measuring the efficacy of policy measures, the use of a "poverty weights" index to be applied to the rate of growth of GNP is recommended. Such an instrument would interpret the annual growth of the national product in terms of the increases in welfare of the distinct income groups by assigning different weights to the rate of growth in each income class. This approach however, requires thorough identification of the poor so that the impact of policy measures may be clearly understood in terms of real social groups and not merely artificial abstractions which would in all probability mask the distributional consequences of a given development plan. This need is well recognized in the report, and useful papers on statistical priorities and research directions are included.

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Unfortunately the scope of the new data requirements and analytic techniques called for in these papers far surpasses the parameters of the general model which is presented. Indeed, it is even at odds with the theory of growth and income distribution developed in one of the papers especially, as will be seen, when this is translated into econometric terms.

To construct the model, existing theories of income distribution are reviewed on the one hand and growth theory on the other. The former (primarily neo-classical, classical, Marxist, neo-Keynesian and neo-Marxist) are found deficient since they deal primarily with the functional distribution of income, i.e. distribution of the total product into factors shares, rather than with personal income distribution which is deemed to be at the heart of the problem. All versions are seen to approach the problem of income distribution as essentially a problem of determining prices and employment levels for the individual factors of production usually simplified into two factor situations with capital and labour.

Not only does a lack of consensus on a theory of functional income distribution exist but also knowledge of the functional distribution of income does not suffice to analyse the determinants of income concentration. For this it is necessary to know not only what the various income earning factors and capital assets earn but also how they are distributed among households. The income of any household is defined as the sum of incomes derived from different income earning assets such as land, capital (both physical and financial) and labour of varying degrees of skills (i.e. embodying different amounts of human capital).

Consequently, the role of asset distribution (the means of production plus those elements which combine to form human capital such as education, nutrition, health services, housing etc...) is fundamental in explaining the pattern of personal income distribution. Recognition of this fact has important implications for development strategy in that it enjoins governments to act not only on the functional distribution of income in favour of those factors of production that are owned by the lower income groups, e.g. labour; but also to attempt to alter over time the underlying pattern of concentration of both physical and human capital.

/To extend

To extend the role of asset concentration in distribution policy into a dynamic framework, the study proceeds to draw upon economic growth theory. To clearly identified income groups it calls for an application of the traditional theory of growth in which growth of income over time is determined by the growth of production capacity, i.e. growth of factors inputs and technology. Thus, a "trickle down" approach is recommended which sustains that benefits of growth can be shared if the growth is achieved through encouragement of labour absorbing techniques (by means of modifications in the factor market - the "how" goods are produced) and labour intensive demand patterns (by modifications in the product market which refers to "what" is produced).

The model advocates maximum use of instruments which operate through factors and product markets (e.g. relative prices, taxation and public subsidies) in combination with a range of direct measures such as land reform, and the distribution of education and other public services, and measures to redistribute assets towards the poverty groups. It should be emphasized, however, that this is to be achieved principally by drawing upon the increments of capital formation and the reader is left with the feeling that the authors consider it easier to achieve a more equitable distribution of increases in income rather than a redistribution of existing income. It might well be argued that this is a more realistic approach; but is it? Given that the measures called for are in all instances intensely conflictive in the political arena, how can a strong and sustained government commitment be achieved to make them effective? It is precisely at this point that the conceptual base of the study has little to offer beyond recognition of the problem and even the "trickle down" effects of a pure growth strategy are rejected as not viable in a later chapter.^{2/}

Indeed when the analysis takes its next step, namely the implications for planning models, it retreats from the problem of the redistribution of assets through direct measures and advocates reallocation through budget and credit mechanisms, for example through a policy of transferring a given portion of the GNP from capital accumulation in the upper and middle income groups to capital accumulation supporting the incomes of those in the lowest income groups.

^{2/} Chapter 6 "Political Implications" by Clive Bell.

This policy is expressed in terms of a simplified econometric simulation model which forecasts the effect of a policy of transferring 2 per cent of GNP over a period of ten years under three different assumptions concerning the relative productivity of capital in the organized sector and in self-employment in the lowest income group. The results indicate that by the end of the decade the lowest income group representing the lowest 40 per cent of the population would witness their share of income rising from 11.4 to 14.8 per cent in the most modest hypothesis. In each simulation, however, total GNP suffers a lower rate of growth. Moreover the amounts involved in the reallocation process are quite substantial and amount to between 15 to 20 per cent of total investment. Also, the problem of finding productive opportunities to invest in the target groups of the population is another major constraint to the strategy proposed since the productivity of the transferred capital might prove too low to be acceptable in terms of the opportunity costs it represents for different sectors of the economy.

Finally, the econometric model restricts itself to the use of output capital ratios in the organized sector and self employment to measure the productivity of capital and the functional distribution of profits and wages in the organized sector as the major parameters. The functional theory derived is based on the simplest possible theory of production (constant output capital ratios) and functional distribution (constant factor shares, and it allows of no other than the "trickle down" effect mentioned above making no provision for the direct measures outlined earlier. This mechanism, if it exists at all in the skeletal simulation exercise, is left to the imagination of the reader.

4. Strategy Alternatives

In order to implement the general model the authors identify those types of policy instruments which they consider to be available in most countries, their potential impact on distribution and employment related objectives and some considerations relevant in choosing combinations of such instruments. The scope for policy intervention starts from the premise that the distribution of income is determined by a general equilibrium of the economy as a whole and can be changed by intervening at different points in this interdependent system.

/Six so-called

Six so-called "areas of intervention" are distinguished which correspond to six "major elements in the determination of income distribution in the economy". These are:

1. Relative factor prices and employment. Intervention in the factor market is introduced with the objective of promoting greater absorption of labour. The discussion, however, is almost exclusively centered around a neo-classical framework of the problems of generating employment under conditions in which the possibility of labour substitutability is quite limited. The study uses what fragmentary empirical data exists in this area to conclude that the scope for employment promotion through relative factor price intervention is quite small in most sectors of the economy. Another important limitation of this instrument is that from the perspective of income distribution as long as the elasticity of substitution is less than unity, factor price variations will increase employment but any additional employment obtained is at the expense of changes in the labour share since employment increases by a smaller proportion than the decline in wages to the employer.

A point of interest raised in this section is that the removal of certain distortions such as wage rigidities is probably much less important than providing access to a unified capital market for a large number of small scale and labour intensive enterprises. The lack of access to credit for small scale entrepreneurs can be treated as a price distortion but it is better described as a "non-price" discrimination arising from a host of institutional characteristics of the capital market. Removing these distortions will have some effect on the capacity of the economy to absorb labour but it should be noted that this is not a shift to labour intensive techniques so much as a shift to resources to labour intensive sectors.

2. Concentration patterns of productive assets and labour skills in the population and changes in these patterns overtime. Two approaches are considered in this context. The first of these is the direct redistribution of the existing stock of assets. Although the most radical measure because of its immediacy, it is viewed by the authors as politically feasible in many countries. No reason, however, is given for this feeling and curiously at this point the study regards the major problems not as political but as those /which affect

which affect the total output of the redistributed or nationalized assets. It concludes that the redistribution of assets may fail to redistribute income for some time due mainly to the inefficiency of the new owners and the public sector in managing the new holdings. Under these conditions a trade-off would result in the sense of output losses as the economy adjusts to a new equilibrium during a period of transition. The only solution offered to this problem is a vague appeal for "effective planning".

The authors would rather opt for what is referred to as a "dynamic redistribution through capital accumulation". This involves mobilizing savings generated elsewhere in the economy and transferring them to accelerate the growth of particular types of capital stocks in the economy. In essence it is the "trickle down" effect described in the theoretical model. The limitations to this approach as seen by the authors, and referred to earlier are stressed even more when it implies either a move to some sort of semi-socialist (or mixed economy) situation in which increasing proportions of the total capital stock are owned by the state or when it attempts to increase the earning ability of low income and low productivity occupations by so-called "poverty focussed" public investment programs such as rural development projects. It is concluded that existing constraints of different varieties are formidable, e.g. public sector inefficiency on the production side; the fact that from the viewpoint of distribution, public sector enterprises are usually in wage sectors and often capital intensive which implies minimal direct impact on the most serious forms of the distribution employment problem and practical problems involved in ensuring that "poverty focussed" program benefits do not spill over into higher income groups and yet remain productive. Without even considering the political problems involved the implication is that the scope for meaningful action is not very great.

A variant of the above policy is proposed in the form of a "human capital" approach which stresses the promotion of education so as to develop a more equal pattern of the distribution of human skills. The limitations noted are the inability of the economy to absorb more skilled labour in relatively high productivity - high wage occupations as well as the non-educational screening devices to employment opportunities once education ceases to be an effective screen.

3. Direct taxation of personal income and wealth. This is recognized as an important element subject, however, to substantial institutional constraints which would in most cases impede a significant expansion of the tax net to cover higher incomes more comprehensively. In any event it is an instrument to be implemented in combination with other measures.
4. Public provision of consumption goods. The direct provision of consumption goods financed through the fiscal system is viewed together with public investment and the tax system as the set of fiscal instruments that can be directed to distributional goals. Some examples of specific measures within this public subsidy scheme are: public health expenditures in rural areas, school feeding and other nutrition programs, electrification and extension of rural water supply. The limitations here stem from those problems found already in public investment programs aimed at increasing productivity and income levels in low income groups. Identifying and designing effective consumption support schemes generally present severe implementation problems especially the lack of an effective delivery infrastructure which is usually time consuming and expensive to develop. The implication is that consumption support schemes should be chosen in accord with existing infrastructure such as in the case of school feeding programs. Another problem is that this area of intervention competes directly with other public investment schemes for a limited amount of financial and administrative resources and thus involves a number of trade-offs.
5. Output patterns and relative prices. In this area, the realm of commodity markets, governments may intervene to influence both what is produced and the relative prices of goods. Two approaches are outlined. The first of this is a set of measures designed to discriminate between sectors according to the functional characteristics of the productive process. The second intervenes according to the nature of the goods produced. The former operates by stimulating particular sectors in cases where the production characteristics of the sector benefit employment generation and raise incomes at low income levels. This is appealed to where the scope for promoting technological choice within sectors is limited, the alternative being to shift production in favour of labour intensive sectors

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thus achieving "indirect factor substitution" through demand. The classic example given is the frequency with which the construction sector is presented as the solution to all employment problems. The pitfalls to be found in this approach most especially when it forms the base of a national plan are many and have been treated elsewhere.^{3/}

It should also be emphasized that the ownership patterns of factors and assets employed in the sector must be considered in weighing the distributional impact of this policy. But even where the direct redistribution of concentrated ownership patterns is not a problem, limitations may arise in connection with the degree of substitutability between outputs of various sectors. In those cases where this is very low, foreign trade possibilities provide some escape from the limitations imposed by domestic demand patterns.

The second approach, which discriminates between sectors according to the goods produced, typically calls for policy action aimed at keeping the price of essential consumption products relatively low by inducing a large enough supply either through increased production or imports. This amounts to an income transfer which is proportionately greater at lower levels and, in addition, may have the effect of lowering the real cost of labour to the economy through the lower relative price of wage goods. Thus, where the demand for labour is at all elastic, an increase in total employment would follow. However, this latter effect depends to a great extent on the productive structure of the economy and on the identity of those producers who would meet the increased demand.

The obstacles to the distributional effect are formidable here also. Attempts to hold down prices by operating directly on producers' prices would discourage private domestic production and in all probability lead to rationing. On the other hand, expensive budgetary support for various types of commodity subsidies may be efficient in achieving the correct price - supply combination but may prove undesirable depending on the extent to

^{3/} For a summary criticism see Henry Kirsch, Employment and the Utilization of Human Resources in Latin America (ECLA, Social Development Division, November 1972), pp. 76-79.

which they lead to a permanent and growing drain on scarce resources severely limiting the government's ability to undertake other programs to promote income distribution objectives. Under such circumstances this approach would result in nothing more than a series of superficial stop-gap measures.

6. The state of technology. This area and more particularly the nature of technical progress is a major factor affecting both the level of income and distribution of income in any economy. Technical progress affects the equilibrium of both factor and product markets with direct consequences upon income distribution. For the most part new processes and new products geared to the resource endowments and demand patterns of the developed countries, serve only to support the expansion of the modern sector in underdeveloped economies. The only recommendation made is that governments contribute to research and development in the area of new technology in low productivity sectors.

The conclusion which is drawn from the above is that a wide choice of "areas of intervention" are open to the policy maker and within each area of intervention there exists a range of more specific policy instruments. The formal problem facing the practical planner (operating always under reasonably well defined political constraints) is to devise a framework in which the net effects and relative merits of intervening at particular points can be evaluated. In the absence of formal planning models which simulate the time path of the "target variables" for alternative combinations of policy instruments, the authors speculate on the sort of considerations that would determine in what areas to intervene and what sort of policy combinations to choose.

They distinguish between a doctrinaire approach in which policy options are enveloped in types of intervention elevated to something between dogma and strategy. This approach may be at one end or the other of the political spectrum. It may be "conservative-liberal" solution which focusses entirely on indirect means such as intervention in factor and commodity markets to achieve the price mix or it may be the "radical" solution which places heavy emphasis upon breaking the concentration patterns of wealth. Once again the study opts for an amorphous program termed as an "eclectic" approach which would consist of "a judicious mixture of the indirect and radical approaches to income distribution" varying in nature and intensity according to the characteristics of the particular country in question.

/No indication

No indication is given however as to how the overall model and alternative strategies could be applied in a meaningful fashion and the recommendation of "playing it by ear" is hardly novel nor particularly useful to anyone.

This inability to proceed much beyond a level of generality already reached in a number of earlier symposia is also apparent in the following sections of the study. Thus in a chapter which purports to "put flesh on the strategy outlined" in the conceptual model attention is directed to the relevance and influence on the main paradigms of present day western economics, Neo-classical, Keynesian, dual economy theories and those of international linkages and dependency are briefly reviewed. It is concluded that the base of each of these is too narrow to deal adequately with the problems involved. But although an appeal is made for a broader approach than the exclusively economic, no indications are provided as to how such a conceptual framework might be constructed other than counseling that unless strategies for change consciously take into account the ways in which the existing pattern of interest in terms of power, position and income can be changed, the strategies will have little chance of success.

In the final analysis, in the absence of a well articulated theory to formalize the strategy it is conceded that resort must be had to pragmatism and experience. The document envisions this concretely in the major areas for policy changes recommended in the ILO employment mission reports on Colombia, Sri Lanka and Kenya. But the question may be raised as to just how feasible and pragmatic were the strategies contained in these reports. After all, it is well known that the strategy outlined in the Colombia report was shelved and in its place a very limited program based on public works and the urban construction sector was substituted.

Furthermore, an overall appraisal of four interagency employment missions revealed certain shortcomings common to them all. Among these were mentioned: an inadequate analysis of the relation existing among growth, employment and income distribution as well as an inadequate presentation of the relations between the instruments needed to implement the policy recommendations and the desired goals often resulting in the transmittal of a

/"shopping list"

"shopping list" of recommendations without thorough evaluations or established priorities.^{4/}

5. Political Elements of the Strategy

The issues just touched upon concerning the shortcomings of the proposed strategy in great part derive from the non-economic components which are often alluded to but nonetheless remain elusive. In an attempt to come to grasp with those non-economic variables which determine whether policy recommendations are accepted, to what extent income distribution plans are implemented and how effective they are; an interesting, if incomplete, essay on the "Political Implications" of the strategy is included.

Key issues are raised such as who benefits, who loses and to what degree from a policy of redistribution with growth. Since the model developed in this volume is implicitly one calibrated for non-revolutionary non-totalitarian societies, further questions are posed as to the nature of the forces which delineate the scope for action of policy makers, planners and those who actually implement the decisions adopted within a "style of politics which emphasizes bargaining, mercenary loyalties and endless manoeuvre, and which is epitomized in the institutionalization of factionalism and patronage". For the most part, however, these fundamental questions are only asked; they are not dealt with in sufficient degree to incorporate the nature of the political process and the configuration of social forces into the model and strategy presented earlier. Interesting themes such as the nature of planning and the way in which planners come to play intensely political roles are introduced but only half developed.

As before in the volume it is recognized that both the acceptance and the implementation of a meaningful antipoverty program face formidable difficulties. But the author of this paper sees an obverse to this or at least a potential one. It is that "the mass organized support of the poor constitutes a political resource which can be put to use in carrying through programs to their advantage". The initiative for reform measures presumably could come "from many groups in society". The examples which are given to

^{4/} O.I.T. La política del empleo en el segundo decenio para el desarrollo. (Ginebra, 1973), p. 40.

substantiate the effectiveness of such a mechanism are of interest since they really indicate just how powerful the obstacles to significant reform are. The first case presented is that of Peru where programs are characterized as being pushed through by pressure from the top and the second, representing the importance of pressure from below, is Chile.^{5/}

The impression is conveyed, however, that the author of this paper is not oblivious to the problems involved but that he finds no way to arrive at a compatible interaction between the announced economic goals and the manners by which to achieve the necessary political preconditions. This contradiction, or lack of "follow through", is evident in a brief discussion on mobilization of the poor and decentralization of decision-making and political power:

"If decentralization is not, after all, a self-evident good, then the question becomes not so much how far it ought to go, as what form it should take. The simplistic notion that if power and initiative are devolved to the local level all will be well, is based on the faulty diagnosis that the essential problem lies in center-periphery relations. By contrast, the argument here is that local power structures and their national linkages exercise a dominant influence over the balance and effects, intended and otherwise, of policy measures. Thus the nature and timing of decentralization initiatives must be chosen with care so as to counteract rather than bolster the existing configuration of local social forces, which are typically inimical to the interests of the poor."

To a great extent the problem of the Sussex volume may be one of identification. In the manner of Pirandello, it is a casting about for a likely agent of development. Finally it is the planner as political actor who

^{5/} For the very limited effect of recent reforms on the pattern of income distribution in Peru see: Adolfo Figueroa, "El impacto de las reformas actuales sobre la distribución de ingresos en el Perú" (paper presented to the Seminario Internacional sobre Distribución del Ingreso y Desarrollo, Santiago Chile, marzo 1973).

emerges as the most likely candidate. Since it is sustained that, more often than not, the political process will fail to generate a well-defined or even stable social welfare function, the authors maintain that in those circumstances there will tend to be a good deal of latitude for administrators involved in the planning process to impress their own particular values on the shape and direction of policy. To the extent that they seize on the opportunity thus provided, they come to play an active political role, though not necessarily a coherent interest group.

Like earlier components of the proposed strategy, the issue of planning is one which is discussed but not resolved in the paper. The function of planners is much broader than a merely technical one since in most cases a government represents an "operational alliance between various interest groups which aims to grasp and preserve power, but which also needs to be continuously cemented and possibly extended. "As such, the political leadership is incapable of giving more than limited guidance to the planner, direction which is insufficient for him to act merely as technician".

But if this is the case, then what may be said about the specific role of the planner in integrating a strategy based on social equity into the body of a national plan? And what conclusions may be drawn concerning the relation of the planner to the effective implementation of the proposed reforms, to the dynamics of the political mechanism itself? Undoubtedly the planner himself represents certain interests and this situation together with the identity of the coalition of forces which comprises a government at a given moment will determine whether the planner will serve as a "public relations" man to project an image of a plan in more equitable terms than it really is, as an indoctrinator of the political leadership itself as well as the general public, or as a more effective agent for change. These are problems which remain unresolved in the report and no indication is given as to how to obtain the most desirable evolution of planning when this is inserted into the overall strategy as a political-technical exercise.

