

Chapter 2: Evaluation Highlights

- Achieving poverty reduction remains a substantial challenge because growth has remained uneven and sporadic and has translated into poverty reduction with varying efficiency.
- Strategies for poverty reduction need to consider where the poor live and how they earn income.
- Strengthening urban-rural linkages and strategies to improve rural productivity requires more attention.
- The distributional effects of growth-enhancing reforms need to receive more attention.
- Assistance strategies have been effective when they have taken political and institutional capacity into account. When they have not done so, they have been overly ambitious and lacked focus.



Achieving Poverty-Reducing Growth

When focusing on results at the country level, the World Bank's overarching objective is poverty reduction. Economic growth is essential for poverty reduction, yet all growth is not equal in improving the welfare of the poor. Effective poverty reduction also requires that low-income groups be able to participate in economic growth.

This chapter reviews how well countries assisted by the Bank have fared in achieving poverty-reducing growth and examines the factors contributing to Bank effectiveness in getting this result. The chapter draws on IEG Country Assistance Evaluations completed in fiscal 2003–06, as well as IEG analyses of Country Assistance Strategy Completion Reports from fiscal 2004–06, for a total of 48 countries. It also uses poverty data available from the Bank's Povcalnet database over the periods covered by the IEG evaluations. Such information is available for 25 of the 48 countries. The chapter will refer to the group of 48 countries as the *full sample* and the group of 25 countries as the *subsample*.

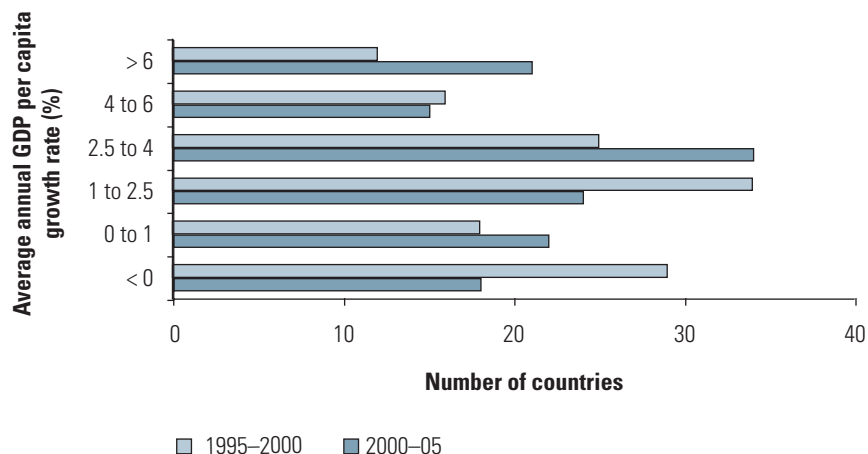
Economic Growth—the Recent Record

Growth in the majority of Bank borrowers has been stronger in the most recent five years than in the first half of the decade from 1995 to 2005 (figure 2.1). Nevertheless, achievement of sustained increases in per capita income, essential for poverty reduction, continues to

elude a considerable number of countries. The aggregate picture of growth and income in client countries over the past decade has three main characteristics:

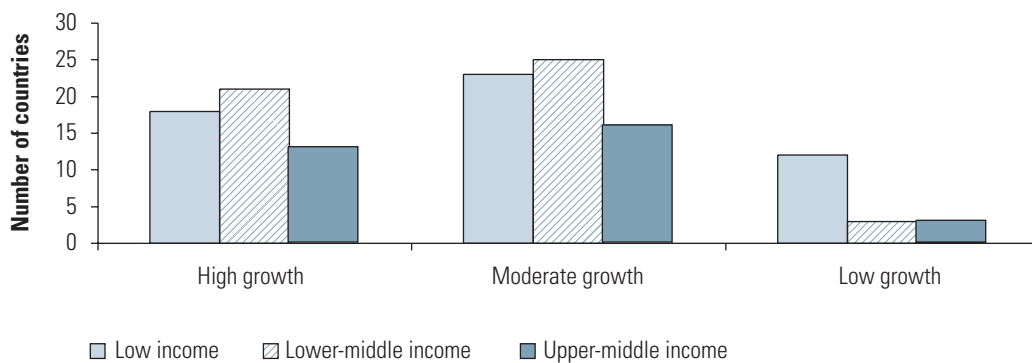
- ***Middle-income countries were more likely to grow than low-income countries.*** Almost 90 percent of middle-income countries achieved a positive annual per capita income growth rate during 1995–2005, and about three-quarters of low-income countries did so (figure 2.2).
- ***There are still many slow growers.*** Only two of five countries were able to increase per capita income at an average annual rate of 2.5 percent or better during 1995–2005, and one in seven countries had a negative average annual per capita income growth rate during this time (figure 2.2).
- ***Among countries that did grow, sustaining growth was a challenge.*** Only 2 of 5 countries recorded continuous per capita income growth during 2000–05, and just 1 in 5 did so for a full 10 years from 1995 to 2005.

Figure 2.1: Growth Performance Has Improved, but Sustained Income Growth Remains a Challenge for Many Bank Borrowers



Source: World Bank 2006n.

Figure 2.2: Middle-Income Countries Were More Likely to Experience Strong Growth than Low-Income Countries (1995-2005)



Source: World Bank 2006n.

Note: High growth = average annual per capita GDP growth rate of > 2.5 percent; moderate growth = average annual per capita GDP growth of 0 – 2.5 percent; low growth = average annual per capita GDP growth < 0 percent.

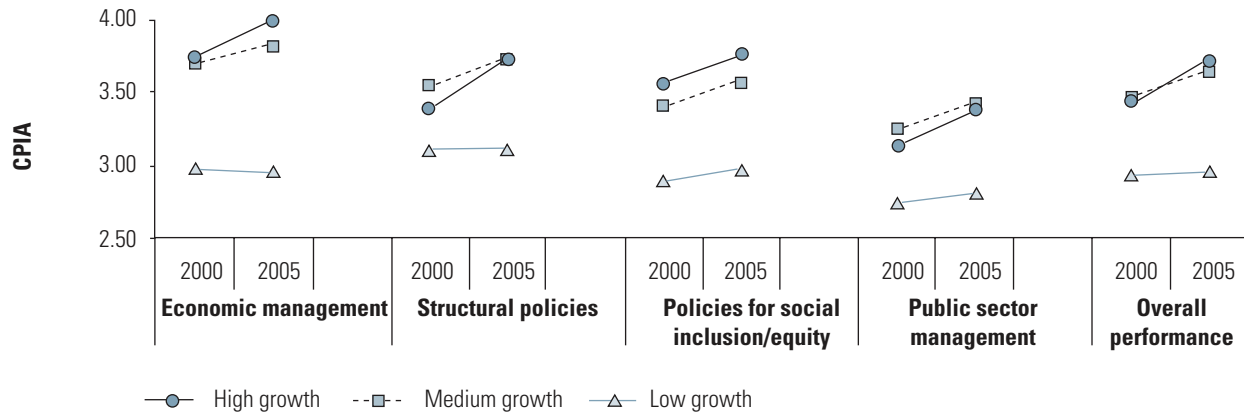
High-growth countries have stronger policies and institutions than countries with slower growth.

Sustained and sustainable growth is the result of multiple interlinked factors, including a country’s stock of physical, human, and environmental capital and the efficiency with which it is formed and used. Efficient capital formation, in turn, depends on the quality of macroeconomic,

structural, social, and environmental policies and institutions.

The overall quality of policies and institutions (as measured by the Country Policy and Institutional Assessment, or CPIA, score) has been stronger in moderate- and high-growth countries than in low-growth countries. The performance gap of the slower-growth countries is most acute in their quality of economic management. High-

Figure 2.3: Countries with Higher Growth Have Stronger Economic Management and Better Policies for Social Inclusion and Equity than Slow Growers



Source: World Bank CPIA database.
 Note: CPIA = Country Policy and Institutional Assessment.

growth countries also have stronger policies for social inclusion than moderate- and low-growth countries (figure 2.3), which demonstrates that high growth can be achieved alongside policies for social inclusion.

How Quality Growth Delivers Poverty Reduction

How effectively economic growth leads to the reduction of income poverty depends on how much the poor participate in growth. Increases in income and decreases in inequality can both lead to poverty reduction. The efficiency with which economic growth translates into poverty reduction depends on three factors: the initial level of income, initial inequality, and whether growth is accompanied by changes in inequality or not (Bourguignon 2004a, 2004b; Lopez and Serven 2006; Ravallion 1997, 2004; World Bank 2005f).¹ Specifically:

- A lower-income country will need to grow faster to achieve the same poverty reduction as a higher-income country with the same inequality level.
- A country with high inequality will need to grow faster than a country with a more equal income distribution to achieve the same poverty reduction.

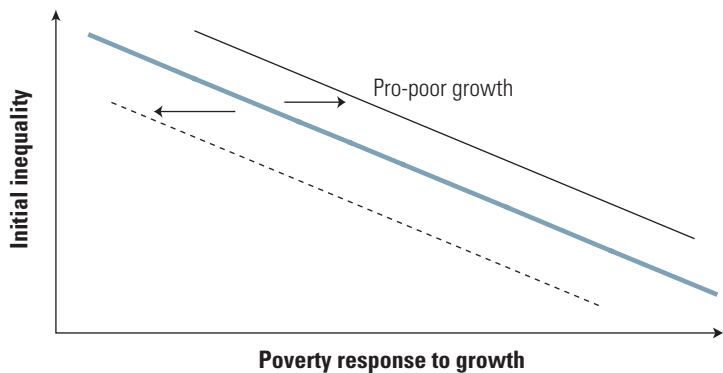
- An increase in inequality will lower the poverty-reducing effect of growth.
- Poverty in richer and more unequal countries responds more strongly to changes in inequality than to changes in income.
- Poverty in poorer and more equal countries responds more strongly to changes in income than to changes in inequality.

Cross-country regression suggests that for a given level of income and inequality, growth translates more efficiently into poverty reduction in countries with high literacy rates, low regulatory burdens, and broad access to credit for the private sector (Chhibber and Nayyar 2006).

The extent to which growth reduces poverty is influenced by the initial levels of income and inequality and the pattern of growth.

Higher literacy facilitates poverty reduction because it increases the share of the population that can take advantage of better employment opportunities created by growth, while at the same time providing entrepreneurs with a larger pool of skilled labor. Broad access to credit and a lower regulatory burden can facilitate entrepreneurial investment, which in turn

Figure 2.4: Policies and Investments that Enhance Equity Strengthen the Growth Effect on Poverty



Source: Based on Chhibber and Nayyar 2006.

helps create employment. Access to credit can also help low-income groups hedge against risk.

Other factors found to increase the efficiency of growth in reducing poverty are investments that increase the poor’s access to infrastructure, measures that ensure market access for rural producers, investments in productivity-increasing agricultural technologies, and labor market regulations that create attractive employment opportunities for poor workers (World Bank 2005f).

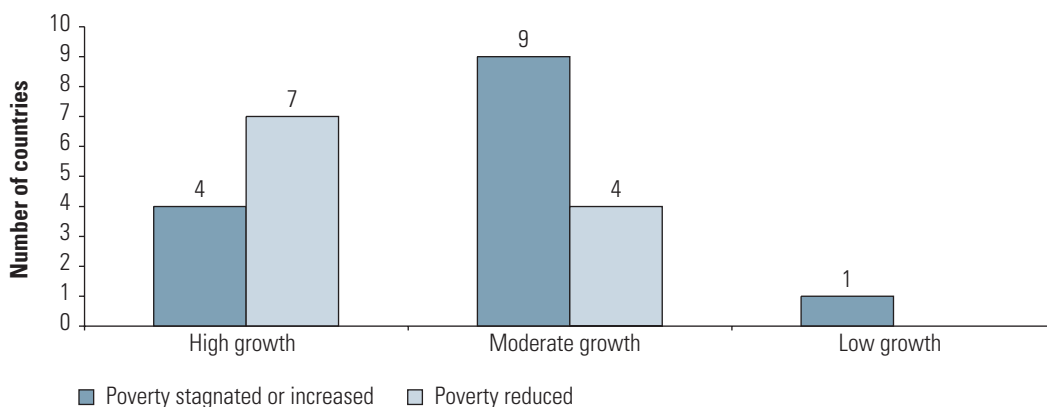
Policies and investments that take these factors into consideration can help enhance the efficiency with which growth reduces poverty (figure 2.4). The extent to which each of these factors constrains the ability of low-income groups to participate in growth depends on country-specific conditions, and thus calls for country-level analysis to help guide the formulation of growth strategies that translate efficiently into poverty reduction.

Reduction of Income Poverty in Bank-Assisted Countries

The share of people living on less than one dollar a day declined from 28 percent to 19 percent between 1990 and 2002 (World Bank 2006n). The global reduction in the number of poor people has been driven by impressive advances in East and South Asia, particularly China and India (box 2.1).²

To see how well Bank-assisted countries have fared in achieving poverty-reducing growth since the mid-1990s and how effectively Bank assistance has contributed to this result, we use the *subsample* of 25 Bank-assisted countries for which IEG has recently assessed the outcome of the Bank’s country assistance and for which comparable poverty data are available from Povcalnet for at least two periods between the mid-1990s and the early 2000s.³

Figure 2.5: Poverty Reduction Remains a Significant Challenge, Even in Countries with Positive Growth Rates



Source: Povcalnet, DECRG poverty database, World Bank 2006n.

Note: High growth = average annual per capita GDP growth rate of > 2.5 percent; moderate growth = average annual per capita GDP growth of 0–2.5 percent; low growth = average annual per capita GDP growth < 0 percent between survey years.

Box 2.1: China and India Account for a Large Share of the World's Poverty Reduction

The reduction in the absolute number of the world's poor has largely been driven by poverty reduction in the world's most populous countries, China and India.

China

No country has been more successful at reducing poverty in the past quarter-century than China. Between 1990 and 2005 alone, the number of people living on less than \$2 a day fell by over 400 million. While migration to urban areas has helped reduce poverty nationally, the bulk of the poverty reduction through the mid-1990s came from within the rural areas, fuelled by policy reforms and technologies that increased productivity.

Since the late 1980s, however, an increase in vulnerability and inequality has dampened the poverty-reducing effect of growth. The Bank made several contributions to poverty reduction through its analytical and advisory services, poverty monitoring, and investments in agriculture, health, and transport. Most important, the Bank has helped establish successful models of targeted interventions through integrated rural development projects.

The Bank has been less successful in persuading the government of the implications of broader development policies for poverty and inequality. The mismatch between intergovernmental fiscal resources and responsibilities has exacerbated regional inequality, while migration restrictions have limited economic integration.

India

In India, there is broad agreement that poverty declined in the 1980s, although there is much dissent on the extent of poverty reduction in the 1990s. The official statistics indicate a 10-percentage-point drop in poverty—from 36 percent in 1993/94 to 26 percent in 1999/2000.

India's economy has performed impressively since the liberalization of trade and industrial policies in the early 1990s. This growth has enabled India to reduce poverty but has led to increasing income inequality that acts as a constraint to higher growth and stronger poverty reduction. The aggregate growth rate during the 1990s could have reduced poverty in India even more had growth been more balanced, sectorally and geographically. Poverty is increasingly concentrated in lagging regions where growth rates are substantially lower than in the rest of the country.

The Bank provided strong support for the reforms of the early 1990s. It expanded assistance to the social sectors and devoted more attention to improving participation. After the mid-1990s the Bank focused assistance on reforming states, with a notable measure of success. In the late 1990s, it sharpened its focus on poverty reduction and governance. Overall, however, the Bank had limited impact on fiscal and other structural reforms and failed to develop an effective assistance strategy for rural poverty reduction through much of the 1990s.

Sources: Datt and Ravallion 2002; Deaton and Kozel 2005; Devarajan and Nabi 2006; IEG 2001, 2005f; Ravallion and Chen 2004; World Bank 2006e.

Despite impressive advances in many East and South Asian countries over the past decade, poverty reduction remains a formidable challenge in many of the countries assisted by the Bank. Of the 25 countries in the subsample, only 11 reduced the incidence of poverty between the mid-1990s and the early 2000s, while poverty either stagnated or increased in the remaining 14 countries. Lackluster and volatile growth was a major reason for the limited poverty-reduction progress in the latter group (figures 2.5, 2.6).

Distributional changes are important for poverty reduction

Growth has been an important driver of poverty reduction in all of the sampled countries where poverty dropped. These countries experienced an

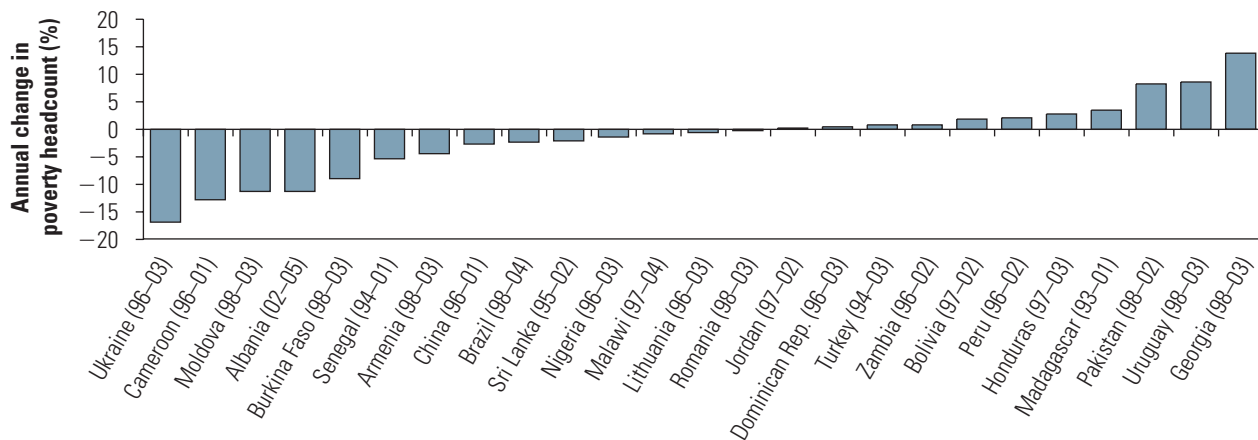
average annual growth rate in per capita gross domestic product (GDP) of 2.5 percent or higher, except for Brazil. But in some countries growth did not efficiently trans-

late into poverty reduction, because growth and changes in distribution did not work in the same direction (figure 2.7).

In the recovering transition economies of Armenia, Moldova, and Ukraine and in African countries that saw substantial poverty reduction, the poverty-reducing effect of growth was reinforced by a reduction in inequality. By contrast, in China, Lithuania, Sri Lanka, and Romania and in several Latin American

Poverty reduction remains a formidable challenge in many of the countries assisted by the Bank.

Figure 2.6: Of 25 Sampled Countries, 11 Witnessed Poverty Reduction Between the Mid-1990s and Early 2000s



Sources: Povcalnet, DECRG poverty database.

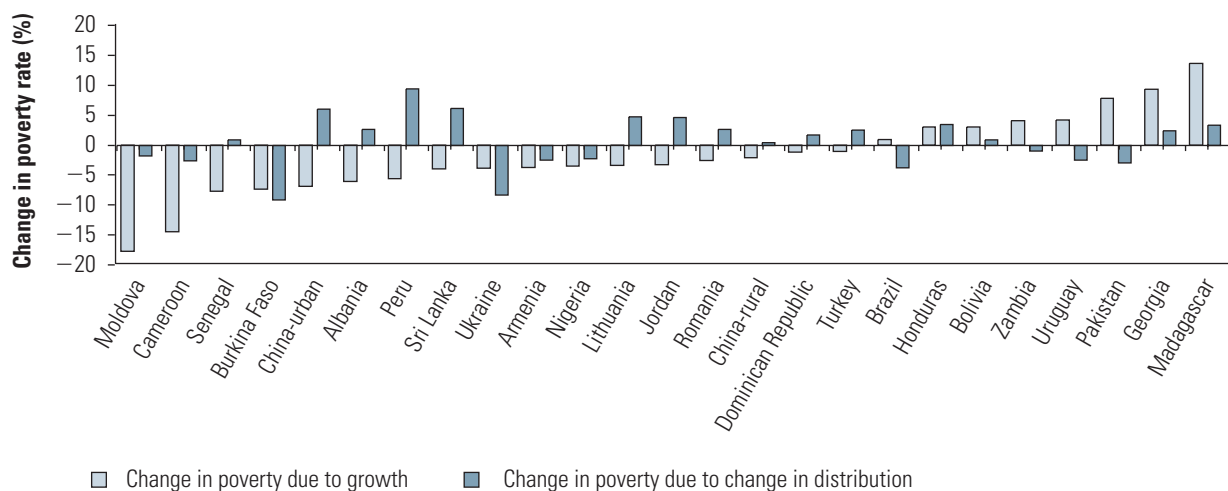
Note: Poverty changes based on per capita consumption/income and a poverty line of US\$1.08/capita/ for low-income countries and US\$2.15/capita/day (in 1993 purchasing power parity \$) for middle-income countries and transition economies. Poverty figures may differ from country poverty estimates because of the use of different poverty lines and purchasing power parity exchange rates, as well as use of per capita rather than adult equivalent consumption.

countries, the positive effect of growth was dampened by worsening income distribution.

In some of the countries where poverty increased, such as Bolivia and Georgia, negative household consumption growth was accompanied by an increase in inequality. Brazil was an exception, because improvement in the income

distribution translated into poverty reduction, despite the lack of income growth. While growth accounted for most of the poverty reduction across the sampled countries, even seemingly small changes in income distribution contributed substantially to either reinforcing or dampening the poverty effects of growth (appendix D).

Figure 2.7: Changes in Distribution Reinforced the Poverty-Reducing Effect of Growth in Some Countries, but Dampened It in Others



Sources: Povcalnet, DECRG poverty database.

**Table 2.1: Country Assistance Outcomes and Poverty Changes
(number of countries)**

Poverty change	Country assistance outcome	
	Satisfactory/ moderately satisfactory	Moderately unsatisfactory/unsatisfactory
Poverty reduced	9	2
Poverty stagnated or increased	6	6

Source: Based on Country Assistance Evaluations and IEG analysis of Country Assistance Completion Reports.

How Effectively Has World Bank Assistance Contributed to Poverty-Reducing Growth?⁴

To explore the correlation between the effectiveness of Bank assistance and poverty reduction, the subsample of 25 countries was divided into groups (table 2.1), depending on how well Bank assistance programs achieved their stated objectives. Not surprisingly, the successful outcome of a Country Assistance Strategy was correlated with the extent of poverty reduction achieved in a country, though this does not mean that poverty-reduction results can be attributed to Bank assistance alone. This assistance often represents only a small portion of the factors that influence overall country performance. Furthermore, while poverty reduction is the World Bank’s overarching goal, individual Country Assistance Strategies set varying intermediate objectives toward contributing to this goal, and IEG evaluates the outcome against these strategy-specific objectives. This explains why the outcome of the Bank’s assistance strategy was assessed as satisfactory by IEG in 40 percent of the subsampled countries that did not succeed in reducing poverty, while it was unsatisfactory in two countries where poverty was reduced (table 2.1).

Countries that reduced poverty and where the outcome of the Bank’s assistance was satisfactory (countries in the upper-left quadrant of table 2.1) are distinguished from those with poor outcomes (lower-right quadrant) by substantially stronger economic management policies. Strong economic management helped spur growth, which translated into poverty reduction with varying efficiency. In these countries, the Bank supported government

efforts to maintain—and at times reestablish—macroeconomic stability and fiscal discipline, including better targeting of public expenditures.

What makes for successful country assistance programs?

Three characteristics mark most of the assistance programs in the subsample countries where Bank assistance led to satisfactory results:

- The country assistance programs were *selective* and in support of a government-owned program that the Bank had often supported through prior analytical work and policy dialogue.
- The pace of program implementation was *aligned with government capacity*.
- Assistance strategies were based on analytical work, often done in collaboration with local specialists, which helped *tailor them to country conditions*.

The experiences of Brazil, Burkina Faso, and China illustrate how important it is for the Bank’s assistance program to be focused and tailored to country conditions. In Burkina Faso, the recently completed Country Assistance Strategy was closely aligned

Growth was an important driver of poverty reduction, but even seemingly small changes in income distribution either dampened or reinforced the effects of growth on poverty.

Successful assistance programs were selective, aligned with government capacity, and tailored to country conditions.

Box 2.2: Burkina Faso—Focused Country Assistance Strategy with Measurable Milestones Yields Results

The Bank's Country Assistance Strategy (CAS) in Burkina Faso was closely aligned with the government's own strategy as outlined in the Poverty Reduction Strategy Paper (PRSP).

The Bank's interventions in support of the PRSP were deliberately selective and focused on well-specified objectives within each pillar of the government's program. Assistance combined support for policy reforms to strengthen the competitiveness of the economy, targeted public sector reforms, and specific poverty-targeted

interventions designed to improve the access of the poor to public services and to increase rural productivity.

To assess its effectiveness, the CAS identified 14 monitorable indicators and specific monitoring instruments for each indicator. Progress was monitored against benchmarks, but IEG found that further progress could be made by closely tracking intermediate indicators and ensuring measurement of the effects of IDA-supported interventions on higher-order country objectives.

Source: IEG analysis of World Bank 2005a.

with the government's own strategy and focused on well-specified objectives (box 2.2). Progress was monitored against benchmarks and yielded good results in the reduction of both income and non-income poverty. In China, the Bank recognized that its lending accounts for only a small share of resource flow and relied mostly on policy dialogue through analytical work and the demonstration effect of successful projects to leverage policy outcomes (IEG 2005f). In Brazil, the Bank's strategy in the 1990s and early 2000s became more selective. The program's main component focused on the poor Northeast and on activities expected to address directly the roots of poverty, particularly lending in support of human development and to improve access of the poor to basic infrastructure (IEG 2004d).

Unsuccessful assistance strategies are frequently overly ambitious⁵

Over-ambition is a widespread characteristic of Bank assistance programs. About half of all the Country Assistance Strategies reviewed and evaluated by IEG over the past four fiscal years were assessed as having been too ambitious. Ninety percent of assistance programs in the

subsampled countries where poverty was not reduced and where the Bank's assistance failed to deliver the expected results were overly ambitious and not sufficiently tailored to country conditions.

There are two main ways in which Country Assistance Strategies have been overly ambitious. They have either lacked selectivity or they have centered on Bank support for reform programs that were not commensurate with institutional capacity and the political situation in the country. Forty-eight percent of the strategies IEG assessed as overly ambitious fell in the former group and 36 percent fell in the latter, with the remainder suffering from a combination of the two.

Country Assistance Evaluations suggest that several factors can help determine ex-ante whether an assistance strategy is realistic or not. These include past record with reform implementation and realization of Bank assistance programs (including dropped operations in previous assistance programs and implementation delays), judicious analysis of the political economy and implementation capacity in a country, and clear identification of country risks.

Country Assistance Strategies that lacked selectivity led the Bank to spread its resources too thinly across too many sectors, which diluted its effectiveness. This was the case, for example, in Honduras and Malawi, where the Bank's program covered more areas and institutions than could be handled effectively by either the Bank or the country (IEG 2006f, 2006i).

The need to strategically focus Bank assistance on a selected number of important areas is particularly strong in smaller countries and in fragile states. In Cambodia and São Tomé and

Overly ambitious strategies led to programs that either were not sufficiently selective or established unrealistic expectations for reform programs.

Principe, for example, IEG analysis found that the Bank's lending program stretched its resources too thinly across too many sectors, which prevented it from effectively engaging in policy dialogue and supervision.⁶

Overly ambitious strategies have also led to unrealistic expectations for reform programs supported by policy-based lending. In Malawi, for example, the Bank proceeded with policy-based lending for reform programs that were not adequately scaled to country conditions and achieved few sustainable results (IEG 2006i).

The Bank sometimes also proceeded with such lending under external pressure to help prevent default. Its financing then perpetuated unsustainable fiscal situations, without addressing the underlying causes. In Pakistan, two policy-based loans had little sustainable impact on structural reforms, despite the large amounts of funding advanced to avoid default. But a policy-based operation achieved satisfactory results in subsequent years, when it was adequately tailored to local conditions and supported a government-owned reform program (IEG 2006j). In Zambia, external pressure for balance of payment support weakened the design and supervision of successive policy-based operations and delayed privatization of mines and necessary structural reforms (IEG 2002c). In Bolivia, the prolonged high level of aid prevented adherence to hard budgetary constraints and, when a crisis arose, the Bank and other donors were compelled to provide further assistance at a time when its likely effectiveness was most questionable (IEG 2005c). The Bank should be cautious about providing emergency liquidity to avoid default in the absence of a strong reform program.

Analytical work with country participation helps tailor assistance strategies to local conditions

A realistic Country Assistance Strategy requires an accurate assessment of the country's political economy and of the main constraints to poverty-reducing growth. Assistance strategies built on analytical work done in collaboration with local specialists have tended to be more realistic and

resulted in better outcomes. Collaborative work also helps enhance local capacity and build ownership of Bank-supported programs.

In Brazil, for example, the Bank's strategy was underpinned by high-quality analytical work on poverty and growth, done with substantial participation by top Brazilian researchers (IEG 2004d). In Armenia, the most successful periods of the Bank's assistance were those underpinned by strong analytical work on growth and poverty (box 2.3). A hiatus in analytical work prevented recognition of important constraints to growth and the strategy failed to recognize the need to push the agenda in new directions (IEG 2004a). In Turkey, a broad program of analytical work, often done with substantial participation of Turkish experts, helped build consensus for overdue reforms that proved essential to revitalizing Turkey's economy (IEG 2005n).

Achieving poverty-reducing growth—challenges for Bank assistance

Designing assistance strategies that are well grounded in country analysis, set out realistic expectations, and can contribute to achieving poverty-reducing growth poses a host of challenges. Recent IEG evaluations provide evidence on some of them, including the need to:

- Deepen country analysis to understand what factors in a given country can lead to a pattern of growth that efficiently translates into poverty reduction.
- Find more effective ways to reduce rural poverty.
- Increase attention to the distributional effects of growth-enhancing reforms.
- Find more effective ways to reduce poverty in low-income countries under stress and fragile states (LICUS).

Assistance strategies that are not selective spread the Bank's resources too thinly and dilute its effectiveness.

Assistance strategies built on analytical work done with local participation have tended to be more realistic and resulted in better outcomes.

Box 2.3: Analytical Work on the Constraints to Poverty-Reducing Growth Helped Reshape Bank Assistance to Armenia

The study "Growth Challenges and Government Policies in Armenia" demonstrated how poverty-focused analytical work can help shape Bank assistance in support of poverty-reducing growth. It analyzed why the steady rise in Armenia's real GDP during the second half of the 1990s had not led to significant improvements in poverty and employment creation. It found that improvements in wage levels had disproportionately benefited labor in a few sectors that employed a small proportion of total

labor. It showed that a poor business climate and weak private sector capabilities hindered the establishment or expansion of private firms. It recommended policies and actions designed to accelerate enterprise restructuring, attract investment, and encourage the creation of new businesses in the medium term. Largely as a result of this analysis, the Bank's assistance was redirected to support government efforts to improve the overall business climate, rather than pursuing privatization in isolation.

Source: IEG 2004a.

They also illustrate the circumstances in which the Bank can effectively help cushion the impact of a crisis.

Paying attention to the pattern of growth

The ability of the poor to participate in growth depends on how much growth is driven by

Strategies for poverty reduction need to consider where the poor live and how they earn their income.

productivity increases in sectors where a large number of the poor work, how much growth translates into job creation, and how well the poor are equipped to take advantage of such job growth. Growth in more labor-intensive sectors and in sectors where large numbers of the poor work, such as agriculture and manufacturing, has been found to lead to more poverty reduction than growth in less labor-intensive sectors, such as mining or utilities (Christiaensen, Demery, and Kühl 2006; Loayza and Raddatz 2005; Ravallion and Chen 2004).

This does not mean that countries should not invest in sectors with low labor intensity, but it does suggest that they should pursue a strategy that balances growth in those sectors with growth in sectors that have the potential to absorb a higher share of labor. Strategies for poverty reduction thus need to consider where the poor live, how they earn their income, and what constrains growth in those areas. They also need to consider the constraints to intersectoral

mobility of the poor, such as low skills or lack of access to capital, infrastructure, or market outlets. Identifying such constraints and devising the proper response is an involved task and will require country-level research and analysis, which the Bank and other donors can support.

In the subsample of countries that experienced positive growth without poverty reduction, growth was concentrated in subsectors with low labor intensity and where few of the poor could earn their incomes. The Bank's assistance often contributed to bringing these countries back to a growth path through improved economic management, but it was less successful in bringing about job-creating growth. In Georgia, for example, the oil transport sector was a major driver of growth, but it created little employment.⁷ The Bank Group's assistance was successful in helping to reestablish macroeconomic stability and contributed to growth in the oil transport sector through related infrastructure investments, but it was less successful in helping to remove obstacles to more broad-based growth. In Madagascar, the Bank's assistance strategy sought to put the country back on a sustained growth path by putting the overextended public sector on firmer ground and by establishing the conditions necessary for private sector growth. It focused on sectors with high growth potential that would allow for relatively quick payoffs, but their impact on poverty was limited. The strategy succeeded in bringing the country back to a growth path, but

the growth was concentrated in a few export-oriented sectors that created only limited and cyclical urban employment. It thus made few inroads into poverty, although preliminary data suggest that recent reforms in the rural sector may have led to poverty reduction over the past two years (IEG 2006h).

Many resource-rich countries, among them Madagascar, Nigeria, and Zambia, have performed well below their potential over the past decade. Underperformance in resource-rich countries has been linked to unsound revenue management and poor governance. While Country Assistance Strategies suggest that the Bank is aware of the main reasons for underperformance in such countries, formulating a viable approach to address them remains a challenge (IEG-World Bank, -IFC, and -MIGA 2005). The Bank is preparing guidelines for staff on the challenges to consider when developing Country Assistance Strategies for resource-rich countries.

Finding effective ways to reduce rural poverty remains a challenge

Poverty reduction was faster in urban than in rural areas in the majority of the relevant subsample countries. The rural poor continue to outnumber the urban poor in all subsample countries except Brazil and Uruguay, which have a high urbanization rate⁸ (appendix D). The incidence of poverty remains higher in rural areas than in urban areas in most of the subsample countries (figure 2.8).

Country Assistance Evaluations show that the Bank has found it challenging to help countries formulate and implement strategies that effectively reduce rural poverty. Of the full sample of 48 Country Assistance Strategy reviews completed by IEG over the past four fiscal years, about half concluded that the Bank's assistance in rural areas did not lead to satisfactory results and/or that rural poverty reduction required increased attention.

Performance was particularly weak in Africa. In some countries the strategy supported by the

Bank has been based on the premise that the engine of growth needs to be jump-started in urban areas. But insufficient attention has often been paid to strengthening urban-rural linkages and to implementing strategies that also help improve farm and off-farm productivity in rural areas. In Senegal, the poverty focus of Bank lending came late, and with a strong bias in favor of urban areas (IEG 2006q). In Malawi, where poverty has remained unchanged over the past decade, the Bank attempted to address rural development issues through adjustment lending and largely failed to help the government develop policies to address low agricultural productivity and food security (IEG 2006i). In Pakistan, the Bank's rural assistance program lacked vision and insufficiently addressed rural poverty (IEG 2006j).

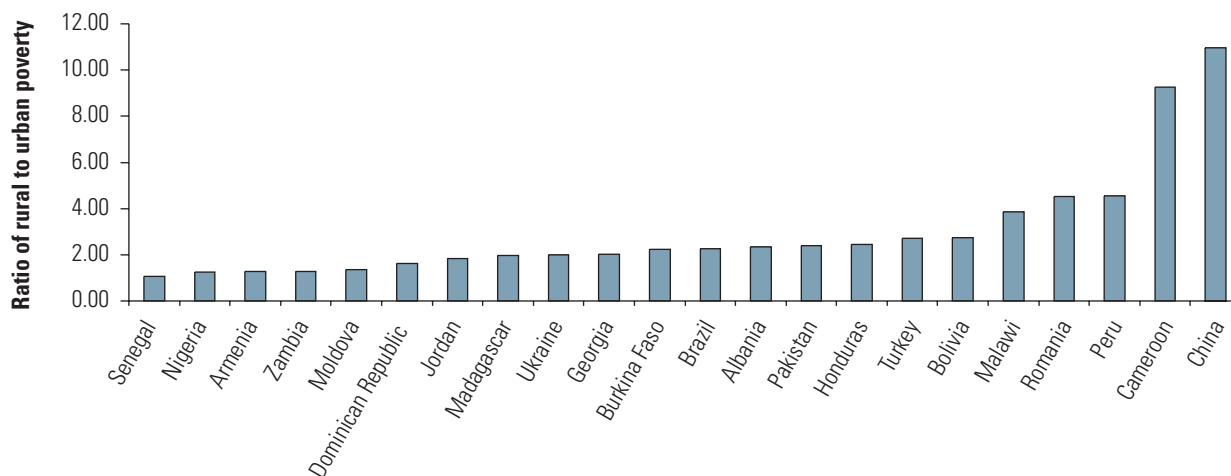
Even in transition economies and some middle-income countries in Latin America, IEG Country Assistance Evaluations conclude that the Bank should focus more on rural poverty. In Armenia, as in a number of other countries of the former Soviet Union, increased focus on rural poverty reduction was highlighted as a priority for future Bank involvement because few inroads have been made into rural poverty, despite strong growth (IEG 2004a). In Honduras, the Bank's economic and sector work needs to intensify research on new economic opportunities for the poor, particularly in the agricultural sector, and future Bank support needs to include a focus on improving agricultural growth (IEG 2006f). Even in Brazil, where the majority of the poor live in urban areas, the Bank and governments need to

Many resource-rich countries have performed below their potential.

Half of IEG's country assistance reviews concluded that assistance in rural areas either did not yield satisfactory results or that rural poverty reduction required more attention.

Strengthening urban-rural linkages and increasing rural productivity require more attention.

Figure 2.8: Poverty Remains More Widespread in Rural than in Urban Areas in Most of the Sampled Countries



Source: World Bank, DECRG poverty database.

find ways to increase agricultural productivity outside the large commercial agricultural sector to help curb rural poverty (IEG 2004d).

In countries where rural poverty remains pervasive, future Bank assistance will need to focus more on working with governments to identify ways to establish stronger urban-rural linkages and increase intersectoral mobility, as well as strategies that improve productivity in the rural sector.

Some reforms entail undesirable distributional effects⁹

Not all pro-growth policies have a positive or neutral impact on income distribution.¹⁰ The empirical literature suggests that sound macroeconomic policies, access to infrastructure, and educational attainment tend to improve income distribution. But the literature also finds that the impact of financial sector liberalization, trade reform, and the size of government on income distribution varies, depending on such factors as

Not all pro-growth policies have a positive or neutral impact on income distribution.

existing distortions and the extent of complementary reforms undertaken (see World Bank 2006h for a summary of the literature).

For example, some have found that financial sector liberalization has a positive effect on income distribution by creating enhanced conditions for entrepreneurial investments that generate employment (see, for example, Chhibber and Nayyar 2006). Financial sector liberalization can also positively affect income distribution if the lower-income groups gain access to credit. Others have found that such liberalization can result in increasing inequality during the early stages of financial sector development if financial sector institutions are geographically concentrated or if gaining access to credit involves large setup costs for low-income groups, so that they initially remain outside the formal credit markets. But they have also found that as the financial sector develops further and a larger share of the population gains access to credit over time, income distribution eventually improves (see World Bank 2006h).

IEG's evaluation of Bank assistance for trade policy reform found that the reforms had mixed effects on employment and poverty, depending on the extent of both complementary reforms and diversification in the economy. At times, short-term adjustments led to worsening income distribution, while the longer-term

effects on poverty were positive because they enhanced growth (IEG 2006c).

The Bank has not always paid sufficient attention to the distributional effects of growth-enhancing reforms. As a result, the effects of the pro-growth reforms it supported were not always cushioned by safety net interventions. In trade reform, for example, the Bank often failed to conduct sufficient analysis to inform its policy advice and lending about the employment and poverty effects of reforms. Consequently, trade-related projects did not adequately attend to these effects (IEG 2006c). Similarly, in many transition economies, price and exchange rate liberalizations were not accompanied by the necessary offsetting measures to protect food security and provide social safety nets (IEG 2004e). In its support for reforms of pension systems, the Bank's assistance focused primarily on improving the fiscal sustainability of pension systems, but it often failed to sufficiently address the pension system's primary goal of reducing poverty and providing adequate old-age income within fiscal constraints (IEG 2006k). Efforts to promote private sector participation in the power sector were found to require more focus on how the poor can be assured of access to energy (IEG-World Bank, -IFC, and -MIGA 2003).

Given the demonstrated importance of distributional changes to poverty reduction, an increased focus on the distributional impact of Bank-supported reforms at the country level is needed. The Bank has recently prepared guidelines for staff on analyzing the distributional impact of reforms.

Many Organisation for Economic Co-operation and Development (OECD) countries use taxes and transfers to smooth income inequality. Transfers from the rich to the poor and from the working to the nonworking have been found to lower the Gini inequality measure by up to 18 percentage points in some OECD countries.¹¹ Income transfers can help the poor obtain education and health services and protect against risks of losing income—for example, by

allowing children to stay in school or credit-constrained poor people to take up productive opportunities. On this premise, several middle-income countries have initiated poverty-targeted income transfers that are conditional on beneficiaries investing in education, and often on participating in maternal and child health programs.

The distributional effects of growth-enhancing reforms have not always received sufficient attention.

The Bank has widely supported conditional cash transfer programs in Latin America, and more recently in such countries as Bangladesh, Pakistan, and Turkey.¹² Evaluations indicate that the transfers can be an effective way to invest in human capital among poor households, while also reducing poverty, and can even lead recipients to invest part of the transfer in income generation (box 2.4).

Conditional cash transfers can help reduce poverty and invest in human capital formation of the poor.

To attain the intended objectives, these operations must be supported by improvements in the supply and quality of health and education services when the existing capacity is not sufficient to respond to the increased demand by program beneficiaries. Because these programs are costly, they need to be carefully targeted. It may also be necessary to make trade-offs between coverage and size of transfers.

The long-term impact of these programs remains to be assessed. The sustainability of behavioral changes and the effectiveness of conditional cash transfers as a mechanism to address chronic—as distinct from transient—poverty still need further evaluation. Also unclear is the extent to which such programs could be effective in countries with weaker institutional capacity, including lower-income countries.

Many OECD countries use taxes and transfers to smooth income inequality.

Box 2.4: Conditional Cash Transfers Help Latin American Families Increase Human Capital Formation

Conditional cash transfer programs in many Latin American countries provide cash assistance to poor families in exchange for beneficiary compliance with human development actions, such as school attendance or participation in health programs. These programs have demonstrated positive impacts on education, health, and poverty reduction.

School Attendance—*Mexico* increased secondary enrollment for girls by 14 percent and boys by 8 percent. *Brazil* achieved a net 3-percentage-point increase in school attendance within the target group. In *Nicaragua*, school enrollment for targeted children increased by 18 percent and attendance by 30 percent. In *Columbia*, school attendance for children between 12 and 17 increased by 10 percentage points in rural areas. In *Ecuador*, primary school enrollment increased by 10 percentage points.

Reduction in Child Labor—In *Nicaragua*, with increased enrollment, the percentage of working children between ages 7 and 13 declined by 5 percentage points. In *Mexico*, the probability of children of ages 8–17 working decreased by 10–14 percent.

Health—*Mexico's* program increased child growth by 16 percent among participating children ages 1–3 years. It also reduced child illness by 12 percent, while participating adults were 17 percent less incapacitated by illness. *Colombia's* program increased the height of participating children from 0–2 years by .76 centimeters, weight by .3–.5 kilograms for children 2–4 years old, and reduced the occurrence of diarrhea from 32.6 percent to 22 percent for rural children under 24 months of age. *Nicaragua* decreased the number of stunted children by 5.5 percentage points and of child illness by 7 to 12 percentage points, and increased immunization rates among beneficiaries by 30 percentage points.

Poverty Reduction—In *Mexico*, there was a 10 percent reduction in poverty and a 45 percent reduction in severe poverty among the target population. In *Argentina*, an extra 10 percent of the participants would have fallen below the food poverty line without the program in 2003. *Colombia's* program helped reduce extreme poverty by 6 percent in one year.

Sources: Cardoso and Souza 2004; Ferreira, Leite, and Litchfield 2006; Gertler 2004; Maluccio and Flores 2004; Attanasio and others 2005; Skoufias 2005; Skoufias, Benjamin, and De La Vega 2001.

More effective ways need to be found to reduce poverty in fragile states

Low-income countries under stress (LICUS), also known as fragile states, are home to almost 500 million people, roughly half of whom live on less than a dollar a day. These countries face poor governance, conflict or post-conflict transitions, and a multiplicity of problems that make the achievement of development results particularly challenging.

Awareness of the need to provide development assistance differently in these countries has risen in recent years. The Bank has improved its operational readiness to engage with fragile states, and substantial progress has been made

The Bank has effectively contributed to macroeconomic stability and the delivery of physical infrastructure in post-conflict countries.

on donor coordination at the international policy level. Significant challenges remain, however. The Bank has generally been effective in contributing to macroeconomic stability and

delivering physical infrastructure in the immediate post-conflict phase, but the Bank's effectiveness needs to be improved following this phase, when structural change is needed.

The Bank still has to sufficiently internalize political understanding in its LICUS country strategies. For example, the Interim Strategy for Papua New Guinea contained a good discussion of the political system and recognized problems such as clan loyalties, political patronage, corruption, and lack of capacity, yet it treated these problems as technical in nature and did not directly use this knowledge to underpin the overall approach.

Strong donor coordination at the international policy level still needs to be carried over to the country level. In adopting state building as one of its two main objectives, the Bank has made an area of traditional weakness (capacity development and governance) a part of its central focus in LICUS, but it still needs to demonstrate how past weaknesses will be

avoided and better capacity development and governance outcomes ensured (IEG 2006r).¹³

Bank support can help cushion the impact of a crisis

The Bank's assistance has yielded satisfactory outcomes, even in some countries where poverty stagnated or increased. This was, for example, accomplished when Bank assistance helped the government weather a crisis and then supported the implementation of structural reforms to bring the economy back onto a growth path.

In Uruguay the Bank quickly changed its assistance strategy to support the government's adjustment program following the 2002 financial crisis, which helped to cushion the impact of the crisis. The Bank's program successfully supported fiscal consolidation, financial sector reforms, and measures to enhance the efficiency of poverty reduction programs. At the same time, it supported social and infrastructure investments that helped improve access of low-income groups to these services.¹⁴ In Turkey, a portfolio cleanup and a concerted effort by the Bank to sharpen the strategic focus of its assistance program produced significant improvements in the Bank's dialogue with the authorities and allowed the Bank to provide timely policy and financial support in response to the 2001 financial crisis (IEG 2005n).

To swiftly respond to a crisis, the Bank needs strong knowledge of the economy based on prior

analytical work. In Turkey, development of the knowledge base in the years before the crisis allowed the Bank to respond quickly when

the Turkish authorities recognized the need for decisive action on structural reforms following the financial crises of 1999 and 2001 (IEG 2005n). Similarly, in India and Morocco, in-depth knowledge of the economy acquired through economic and sector analysis positioned the Bank to advise and support governments on the sequencing of macroeconomic, trade, and structural reforms following crises (IEG 2006c).

Where the Bank's support to crisis-ridden countries had successful results, it supported a

reform program developed and owned by the government, often with elements based on prior analytical work carried out with the Bank. In contrast, where the Bank's assistance to crisis countries did not yield satisfactory results, the Bank, often under external pressure to provide liquidity, proceeded with policy-based lending without government commitment to fiscal adjustment and structural reforms.

But it needs to find better ways to help build capacity and strengthen governance in LICUS.

When the Bank has successfully assisted a crisis-ridden country, it has supported a reform program developed and owned by the government, often underpinned by prior analytical work.