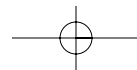
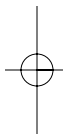
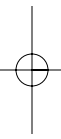


PART ONE:

The Global Economy



Poverty and Inequality

PUNAM CHUHAN

Poverty in developing countries remains deep and widespread. Despite substantial progress in recent decades in reducing poverty—the proportion of people living in extreme poverty has halved since 1980—more than a billion people still subsist on less than one dollar a day. Over three-quarters of a billion people, many of them children, are malnourished. Each year nearly 11 million children die from malnutrition or disease before reaching their fifth birthday; most of these deaths would be easily preventable in any developed country. Over half a million women die every year in childbirth from lack of appropriate health care, malnourishment, or disease. More than 100 million children of primary school age, the majority of them girls, do not attend school.

Staggering as these numbers are, the inequalities in income and other measures both between and within countries are overwhelming as well. Income per capita in the world's high-income countries, on average, is 65 times that in the low-income countries. Rich countries have 3.7 physicians per 1,000 population, compared with just 0.4 per 1,000 in low-income countries. Maternal mortality in childbirth in many low-income African countries is more than 100 times higher than in the high-income countries of Europe. Even though the recent trend in the distribution of world income shows a decline in inequality, it remains quite high: the population-weighted Gini index is over 50 for the world as a whole. (The Gini index is a standard measure of inequality and is discussed further below.) The economic divide within countries is likewise large, particularly in Africa and Latin America.

In an increasingly interdependent world, the high prevalence and stubborn persistence of poverty in developing countries have implications for all countries. Deep deprivation weakens the capacity of states to combat organized crime, armed conflict, terrorism, and the spread of disease, and these in turn can have severe economic, environmental, and security consequences for

neighboring states and the global community. Poverty and its associated outcomes can no longer be contained within national boundaries. This makes poverty a global problem of huge proportions, and it implies that alleviating poverty is critical to maintaining and strengthening regional and global stability.

Recognizing this challenge, the international community has committed itself to a global partnership to promote development and reduce poverty. In 2000 the United Nations adopted the Millennium Development Goals (MDGs)—targets to be achieved by 2015—against which the global community can measure progress toward reducing poverty, and in 2002 the international community adopted the Monterrey Consensus, which created a new framework of mutual accountability between developed and developing countries for meeting these goals. The MDGs call for a dramatic reduction in poverty relative to 1990 levels and the promotion of sustained development. For the billion people in the world who live on less than a dollar a day, a future free of poverty, illiteracy, extreme vulnerability to disease, and lack of opportunities is only possible with sustained development; development holds the key for world peace and security as well. Yet despite a remarkable consensus on the actions and policies needed to achieve these goals, much remains to be done.

This chapter discusses the various dimensions of poverty and inequality and offers a sense of the scope of the problem and the direction of recent trends. It also discusses the international community's response to spur development and alleviate the scourge of poverty. The chapter then highlights the forces shaping the debate over poverty and inequality. Finally, it addresses the recent global actions aimed at accelerating progress on poverty reduction.

Concepts and Measures of Poverty and Inequality

An extensive and growing literature analyzes poverty and inequality. To study the evolution of poverty and inequality, the relationship among growth, poverty, and inequality, and the impact of globalization on the poor, it is useful to have an understanding of the underlying methodological issues. Some of the key aspects of definition and measurement are summarized below.

Definitions

The conventional notion of poverty is narrow, characterizing it in terms of deprivation or lack of essential goods and services. In this view poverty is defined as income or consumption of commodities that is below some minimum threshold. This narrow characterization of poverty is not new. More

than a century ago, Seebohm Rowntree used a survey on earnings and expenditures to estimate that 10 percent of residents of the city of York, England, lived in poverty—that is, below the minimum amount needed to subsist.

But what makes poor people poor is not just deprivation of income or of things to consume; often they are illiterate, have high health risks, and live in squalid conditions as well. A broader view of poverty encompasses these non-income dimensions of poverty such as education, health, prevalence of disease, gender equality, and access to water and sanitation. These dimensions are included in the MDGs and are recognized in the World Bank's *World Development Report 2000*, which defines poverty as a "pronounced deprivation in well being."

An even broader view of poverty is the "capability approach" to well-being promulgated by Amartya Sen. This approach extends the notion of poverty to include vulnerability to risk, lack of voice in society, and powerlessness. Sen argues that what is important to well-being is the "capability to function in society."¹ Key capabilities include not only adequate resources for essential needs—food, shelter, clothing—but also access to education, good health, security from violence and other risks, and political participation and voice. Poverty arises when people lack these basic capabilities to function in the society in which they live.

Closely related to poverty is inequality, or the gap between the poor and the rich. Inequality has to do with the distribution of *outcomes* such as income, wealth, consumption, or other dimensions of well-being.² It is different from equity, which is essentially about the distribution of *opportunities*—economic, political, and social; *World Development Report 2006* argues that inequity in opportunities affects economic development and that greater equity can over time promote stronger growth. The focus of this chapter is on equality in income and other outcomes.

Measurement

Because poverty has these various dimensions, monetary and nonmonetary, and because it is such a complex phenomenon, there is no single perfect measure of poverty. The various measures are complementary, and the choice of which measure to use will depend upon the purpose it is to be used for. So, to measure poverty, one must first define an indicator of well-being. A standard approach is to derive income or consumption per capita from household surveys, which must be well designed in order to provide relevant and representative information. The World Bank has developed the Living Standards Measurement Survey (LSMS) to obtain reliable household income and consumption information; data collected from the LSMS are widely used in

poverty analysis. The next step is to establish a threshold of income or consumption that represents the minimum acceptable level for subsistence. This threshold, called the poverty line, will vary from country to country and can be defined either in absolute monetary terms or relative to some baseline. For example, the poverty line in the United States is set in absolute terms (currently about \$19,000 for a family of four), whereas the European Union proposes a relative poverty line, defined as household income less than 50 percent of the national mean.

The final step is to generate an aggregate measure, based on the poverty line, of the incidence of poverty in the economy. The most common indicator is the headcount index, which is simply the proportion of the population living under the poverty line. This indicator, however, does not measure the depth of poverty among the poor—it counts a person (or household) just below the poverty line the same as a desperately poor person living far below the line. One measure that does address this dimension of poverty is the poverty gap, which weights the headcount index, on a scale of zero to one, by the average shortfall of the poor household from the poverty line. The further the person (or household) is from the poverty line, the larger the weight; for example, someone who is exactly at the poverty line gets a weight of zero, while someone halfway between the poverty line and zero gets a weight of 0.5.

Because they differ from country to country, national poverty lines are not useful in comparing poverty across countries. For that a single uniform poverty threshold is required. The approach most often used today is that first applied by *World Development Report 1990*, namely, the proportion of people living on less than a dollar a day. To derive this “international poverty line,” the 1990 report converted national poverty lines into a single “international dollar” measure using 1985 purchasing power parities,³ and the poverty line that was most typical of those among low-income countries was selected. The current international poverty line that is comparable to the one-dollar-a-day line in 1985 is actually equal to \$1.08 a day in 1993 consumption purchasing power parity terms (but is still referred to as one dollar a day).⁴ Another poverty threshold that is commonly used in international poverty comparisons is two dollars a day.

The Human Development Index (HDI), developed by the United Nations Development Programme (UNDP) in 1993, is a composite measure of well-being based on life expectancy at birth, knowledge (in terms of adult literacy and gross enrollment in primary, secondary, and tertiary education), and income per capita (measured as GNP per capita at purchasing power parity). The UNDP uses the HDI to provide an annual ranking of countries on these three dimensions. A value below 0.5 represents low development. Most

African countries rank among the lowest on the HDI, and the trend for these countries is far from favorable.

Several measures have been developed to analyze the scope and extent of income inequality. These measures typically compare the income of an individual or a group with that of another individual or group. Like poverty, inequality can be expressed in absolute or relative terms—that is, in terms of the absolute gap between individuals or groups or the relative gap. The relative measures most commonly used today are the Lorenz curve and the Gini coefficient. The Lorenz curve plots the cumulative percentage of total income received against the cumulative percentage of recipients, starting with the recipient with the lowest income. If incomes were perfectly uniformly distributed, so that every recipient has exactly the same income, each point along the curve would be higher than the point to the left of it by a constant amount, and thus the curve would trace a straight diagonal line. The Gini coefficient (or Gini index, which is simply the Gini coefficient multiplied by 100) is a summary statistic derived from the Lorenz curve. It measures the area between the actual distribution of income, as depicted by the Lorenz curve, and the diagonal line that depicts perfect income equality; the Gini coefficient is scaled so that it ranges from 0 to 1, with 0 representing absolute equality in distribution and 1 representing complete inequality.

The distribution of income can also be described in terms of the percentage of total income received by various quantiles of the population, where a “quantile” refers to some fraction of the population ordered by income from lowest to highest. For example, the “bottom quintile” refers to the one-fifth of the population with the lowest incomes, the “bottom decile” to the lowest tenth, and so on.

Inequality can be measured within a country, between or across countries, or globally (across all people of the world).⁵ Inequality is commonly expressed in terms of income,⁶ but it can be applied to other indicators of poverty as well:

- Within-country inequality measures the distribution of income or consumption with respect to individuals or groups living in the same country.
- Between-country inequality measures the income gap between people in different countries, assuming each receives the average income for his or her country. There are two concepts of inequality between countries, and the choice of which concept to use will again depend upon the purpose: *Intercountry inequality* compares mean income per capita across countries, focusing on the distribution of unweighted country

means. Thus a country with a large population such as India has the same weight as a country with a tiny population such as Fiji. This measure provides little information about inequality among the people of the world. *International inequality* considers both the country's mean income per capita and the size of its population. Thus it represents the distribution of country means weighted by population. Although this measure does not take account of income distribution within a country, it is useful in assessing income disparities among the people of the world.

- Global inequality focuses on the incomes of individuals and their distribution. Here the individual, not the country, is the unit of observation. This measure relies on national income distributions based on countries' household survey data to estimate a global income distribution. The data requirements for compiling this measure are much greater than for the other two measures.

Poverty and Inequality as Global Issues

The high prevalence of poverty in the developing world and the pronounced deprivation faced by millions living in developing countries have brought poverty and inequality to the forefront of the global agenda. Since 1980, international attention has been increasingly sharply focused on reducing poverty worldwide. More recently the focus has widened to include equality and equity as well.

The latest data available show that over a billion people in the developing world were living in extreme poverty (on less than a dollar a day) in 2002, 450 million fewer than in 1981 and 200 million fewer than in 1990 (Table 2.1). (Although poverty is a worldwide phenomenon, the focus of this chapter is on developing countries.) The greatest reduction in absolute poverty has occurred in East Asia, where the number of poor declined by three-quarters during 1981–2002; South Asia has also made strong inroads in reducing the number of poor. Not all regions have participated equally in this improvement, however. Sub-Saharan Africa has seen a near doubling in the number of poor—from 164 million to 303 million—and the number of people living on less than a dollar a day has risen in Latin America and in developing Europe and Central Asia as well. Prospects are bright for a continued decline in overall poverty, to the point where, by 2015, only 10 percent of the developing world's population will be living on less than a dollar a day—well below the MDG target of 14 percent.

TABLE 2.1 People Living on Less Than a Dollar a Day, by Developing Region, 1981, 1990, and 2002

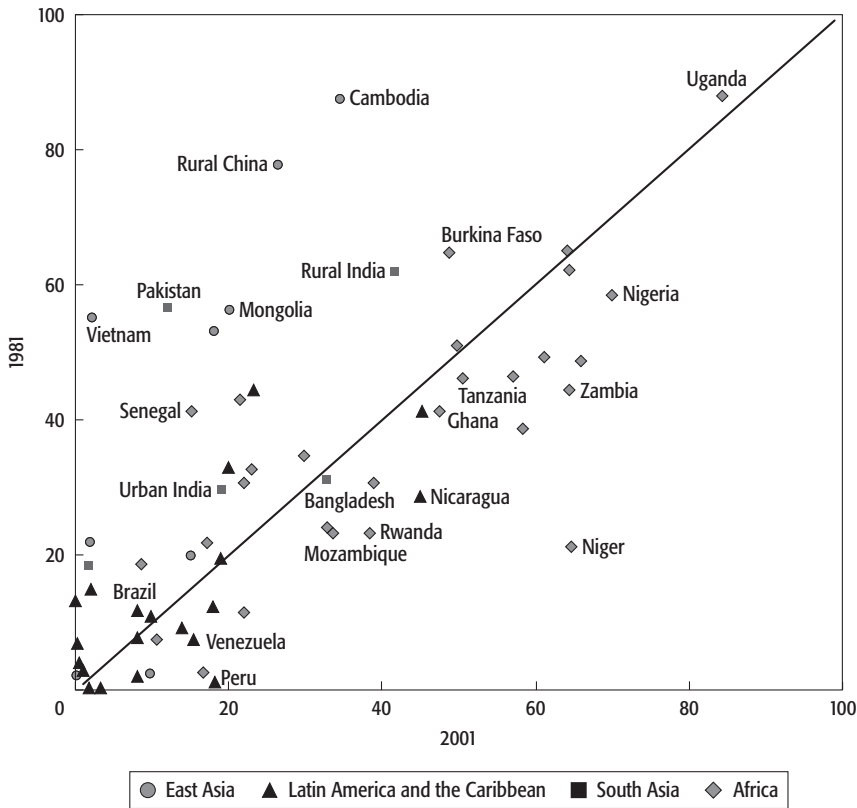
Region	Millions			As percent of total population			
	1981	1990	2002	1981	1990	2002	MDG 2015 ^a
East Asia and Pacific	796	472	214	57.7	29.6	11.6	14.8
Of which: China	634	375	180	63.8	33.0	14.0	
Europe and Central Asia	3	2	10	0.7	0.5	2.1	0.3
Latin America and Caribbean	36	49	47	9.7	11.3	8.9	5.7
Middle East and North Africa	9	6	5	5.1	2.3	1.6	1.2
South Asia	475	462	437	51.5	41.3	31.2	20.7
Sub-Saharan Africa	164	227	303	41.6	44.6	44.0	22.3
All developing countries	1,482	1,218	1,015	40.4	27.9	19.4	14.0

a. The Millennium Development Goal for poverty calls for a halving of the proportion of the population living on less than a dollar a day from 1990 levels by 2015.
Source: World Bank, World Development Indicators.

But not all regions will achieve the goal of halving extreme poverty. Sub-Saharan Africa is the region most at risk: nearly half of the countries there are off track to achieve the income poverty MDG, and an additional 40 percent lack sufficient data to allow an evaluation of their prospects. There has also been overall progress on reducing hunger, yet only 33 out of 77 countries with reliable data on malnutrition are on track to achieve the MDG target for hunger. Here, too, Africa is seriously off track.

Progress in reducing poverty has thus been uneven. Some countries and regions have seen a remarkable decline in poverty, while others have actually experienced an increase. Figure 2.1 shows how poverty reduction has progressed, or not, in selected countries. Each symbol in the figure represents a country, and its position with respect to the vertical scale shows the percentage of that country's population in extreme poverty in 1981, while its position with respect to the horizontal scale shows the corresponding percentage in 2001. Thus, countries that have reduced poverty by this measure will lie above the diagonal line, countries that have seen an increase will lie below it, and countries that have seen no change in poverty will lie directly on the diagonal. As the figure shows, the greatest improvement has occurred in the Asian economies, most notably in China, India, Pakistan, and Vietnam; only one

FIGURE 2.1 Share of Population Living on Less Than a Dollar a Day in Selected Countries, 1981 and 2001
Percent



Source: Author's construction using the World Bank's PovcalNet (Available at iresearch.worldbank.org/PovcalNet/jsp/index.jsp).

East Asian country and one South Asian country fall below the diagonal line. Most of the African countries, in contrast, saw a long-term slippage in poverty reduction, including several that experienced relatively rapid economic growth and some poverty reduction in the 1990s, such as Ghana, Mozambique, and Tanzania. The performance of the Latin American economies was mixed, with nearly half seeing an increase in the proportion of people living on less than a dollar a day.

Progress on the human development MDGs (those addressing education, gender equality, child and maternal mortality, and communicable disease)

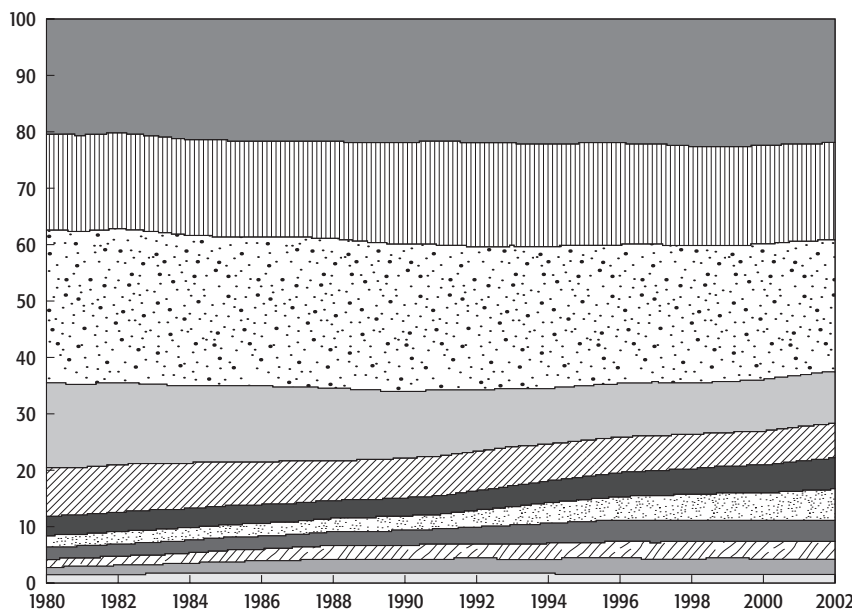
has been mixed. All regions are off track on at least some of the goals, and although some countries in South Asia and Sub-Saharan Africa are meeting some of the goals, these regions are largely off track on all of them. On the goal of universal primary education, progress has been encouraging: the number of countries that have achieved or are on track to achieve this goal has increased, as has the rate of growth in the primary completion rate. Gender disparities in primary and secondary education are also narrowing. By contrast, the pace of reduction in child mortality has been slow: Only 20 percent of developing countries are on track to reduce child mortality rates by two-thirds of their 1990 levels by 2015. Gains toward this goal have been particularly slow in Sub-Saharan Africa. Maternal mortality rates remain unacceptably high in many developing countries as well, although some countries in East Asia and Latin America have substantially improved maternal health through better health facilities and an increase in the number of trained birth attendants. Diseases such as HIV/AIDS, malaria, and tuberculosis continue to exact a heavy toll on populations in Sub-Saharan Africa. Although the prevalence of HIV/AIDS has stabilized, the death rate from this disease is on the rise.

Progress on the environmental MDG is likewise mixed. Despite strong progress in some regions, many countries are off track toward the goal of reducing by half the proportion of people without sustainable access to safe drinking water and basic sanitation by 2015. The situation in Sub-Saharan Africa is particularly critical: 64 percent of the population lack access to an improved water source, and 42 percent lack access to improved sanitation facilities.

Views differ on whether the decline in absolute poverty worldwide has been accompanied by greater equality in the distribution of income. The answer depends upon the concept of equality that is used. In terms of intercountry inequality—that is, when all countries are weighted equally—income inequality has increased since the 1980s. But in terms of international equality—when the more populous countries have larger weights—the gap between countries has narrowed. This favorable result is driven by the strong economic growth in China and India during this period.

A 2004 study used data from 138 countries over 1980–2002 to show how the world distribution of income changed over that period.⁷ If one takes only differences between countries into account, in 2002 the poorest 40 percent of the world's population received slightly more than 10 percent of world income, while the wealthiest 10 percent received nearly 40 percent (Figure 2.2). The population-weighted world Gini index (assuming equal income within countries) was over 50. Although the distribution of world income is thus

FIGURE 2.2 Distribution of Global Gross National Income by Decile, 1980–2002
Percent of total



a. Top two strata represent the top 5 percent and the second 5 percent of the population; the remaining strata represent the ninth through the first (lowest) deciles. Gross national income is measured in 1995 international dollars (dollars adjusted for purchasing power parity).

Source: Bourguignon, Levin, and Rosenblatt (2004).

quite unequal, the recent historical trend shows a decline in inequality: the poorest 40 percent of world population have nearly doubled their share of world income, while the richest 10 percent have seen a small decline in their share. Not all of the lower deciles saw an improvement, however. The second through the sixth deciles gained income share, but the poorest decile and the seventh and eighth deciles all saw a decline in income share on balance.

By contrast, global inequality measures, which combine cross-country differences and income distribution within countries, show mixed results for trends in inequality in the 1990s. Some studies estimate that the world Gini index has declined by between 1 to 4 points,⁸ whereas other studies find either no change or an increase in inequality. The differences in results most likely stem from differences in data and assumptions used to compute the inequality measure. Despite these differences in findings regarding the trend, all studies find global inequality to be very high: the world Gini value for the 1990s is

about 65, indicating that between-country inequality is sharply greater than within-country inequality. The richest 5 percent of the world's population receive about a third of world income (measured in purchasing-power-parity terms), while the poorest 5 percent receive only 0.2 percent.⁹

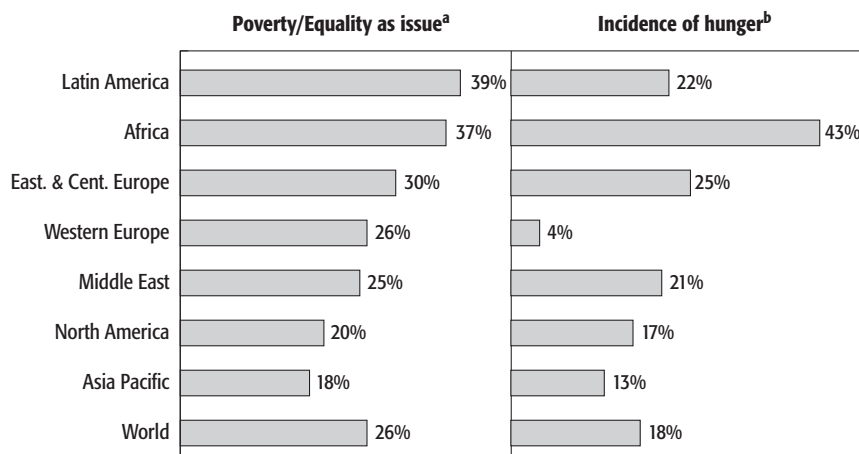
Within-country inequality is high in many developing countries. Nearly 60 developing countries have a Gini index of 40 or more; by comparison, the high-income countries of Europe typically have Gini values of 25 to 35. Gini indexes reveal that countries in Sub-Saharan Africa and in Latin American and the Caribbean appear to be the most unequal in the world. Evidence also suggests that public spending on education and health is often regressive, with the poorest quintiles receiving much smaller shares than the richer quintiles.

Several factors explain why poverty and inequality are global issues. First, as this part of the chapter has shown, poverty remains widespread, and it is readily apparent that, unless action is taken to reduce poverty, the situation will dramatically worsen. Second, there is an increasing recognition that developed and developing countries need to work together to make poverty history; the poor countries cannot achieve the MDGs on their own. Rich countries can help poor countries accelerate progress on reducing poverty by providing resources—aid—to scale up service delivery and investment in much-needed infrastructure. Moreover, by removing barriers to trade that discriminate against developing countries, rich countries can help spur growth and accelerate poverty reduction in the developing world.

Forces Shaping the Agenda

The poverty and inequality agenda today is being shaped by two broad forces: global concern over fairness, and globalization. The persistence of deep poverty and of inequality not only has fueled a sense of deprivation and injustice among the poor themselves, but has also violated a basic sense of fairness in those who are not poor. People everywhere have a general sense of fairness as it applies to themselves and others, which is rooted in the concept of social justice. This shared notion of fairness reflects widely held moral and ethical values of the world community and forms the basis of the international system of human rights. Persistent poverty, large inequalities between and within countries, and lack of opportunity are not consistent with this sense of fairness.

The forces of globalization mean that the problem of poverty is no longer contained within national boundaries. With increasing interdependence through trade, migration, and financial integration, the actions of people in one country have consequences for people in other countries. Both concern

FIGURE 2.3 World Opinion on Poverty and Equality as Major Issue and on Incidence of Hunger

a. Respondents were asked, "What do you think is the most important problem facing the world today?"

b. Share of respondents who said that they or their families had often or sometimes not had enough to eat in the preceding 12 months.

Source: Gallup International (2005).

for fairness and globalization are contributing to an increasing awareness among the citizens of the world's rich countries that they need to help improve the well-being and opportunities of the citizens of poor countries, especially if they are to reduce global inequalities.

A worldwide survey conducted by Gallup International in 2005, covering more than 65 countries and over 50,000 people, reports that more than one in four people view either poverty or inequality as the most pressing global problem (Figure 2.3). This perception is evident across all world regions as well: in Latin America poverty or inequality was ranked as the most important problem by 39 percent of those surveyed, in Africa by 37 percent, in Eastern and Central Europe by 30 percent, and in Asia and the Pacific by 18 percent. All regions also report evidence of hunger. At 43 percent, Africa has the highest incidence of people or families who lack adequate food to eat. The numbers for other regions are lower but still substantial.

Advocacy groups have played an important role in building consensus on key public actions by the international community. Their campaigns on critical issues such as debt relief and a fair global trading system have raised awareness among citizens of rich and poor countries alike. Advocacy groups have been particularly effective in campaigning to reduce the debt burden of

the poorest countries: the international coalition Jubilee 2000, which called for the cancellation of poor countries' debt by the year 2000, played a key role in the Heavily Indebted Poor Countries (HIPC) Initiative; the international coalition Make Poverty History successfully campaigned in 2005 for canceling poor countries' debt through what subsequently became known as the Multilateral Debt Relief Initiative (MDRI).

World leaders have acknowledged the global threat posed by deep poverty. A 2004 U.N. report lists poverty, communicable diseases, and degradation of the environment among the top six threats to international peace and security facing the world in the 21st century.¹⁰ The report takes a comprehensive view of collective security. It addresses the security concerns of all states, not just rich states but poor and weak ones as well. It also recognizes an interconnectedness of poverty, civil war, and possibly terrorism:¹¹ extreme poverty, hunger, and a high incidence of infectious diseases can create conditions for domestic unrest, armed conflict, and failed states.¹² The report argues that the foremost way to promote security is through development. Development reduces poverty and strengthens the state's capacity to govern, and so reduces the threats of organized crime, civil war, and terrorism. Attaining the MDGs is therefore essential to improving global security.

By 2015 world population is expected to increase by over three-quarters of a billion. Virtually all of this growth (95 percent) will occur in developing countries, and many of these people will be born into poverty; simulations show that a third more people could be rescued from poverty if growth is pro-poor rather than distributionally neutral.¹³ Poor countries and the global community must act now so as to provide a better future for all.

Globalization and the Poor

Two controversial issues in the debate over poverty and inequality are whether globalization benefits or harms the poor and whether the extent of inequality adversely affects poverty reduction and thus is bad for the poor.

Does Globalization Harm the Poor?

The impact of globalization on poverty has generated considerable debate. Globalization has many facets, including foreign trade, cross-border financial flows, international migration, temporary movement of service providers, and information flows. The focus here is on openness to trade. Although absolute poverty has declined as the world has globalized, some view globalization as unfair to the poor. Anti-globalizers argue that openness to trade has led to greater poverty and to rising disparities between and within countries.

The standard, macroeconomic perspective is that openness to trade reduces poverty by stimulating economic growth. Another indirect way through which trade liberalization impacts poverty is by boosting productivity, which is necessary for fostering long-term growth. There are a variety of other channels through which trade liberalization can directly alleviate poverty: by lowering the prices of households' consumption baskets (including through lower tariffs), raising wages and employment, and increasing government revenue and spending.¹⁴

Several studies, however, suggest that the linkages between globalization and poverty are not so straightforward.¹⁵ The outcome is influenced by other factors, including the degree of labor mobility across sectors; access to credit markets for the poor, so they can avail themselves of profitable investment opportunities; and access to technical know-how and training programs. Thus globalization can in some situations have a negative impact on the poor, especially in the near term. This points to the need to have appropriate policies in place to ensure that the poor gain from globalization.

A recent survey of the empirical literature found that no simple generalizations can be made about the impact of openness to trade on poverty.¹⁶ The evidence broadly supports the view that, in the long run, trade liberalization reduces poverty on average, and there is no evidence of a generally negative impact on poverty. This is not to say, however, that the employment and wages of the poor have never suffered, or that declining fiscal revenues have never caused spending on the poor to be curtailed, where trade has been liberalized. The empirical evidence also shows that poor households are less able than better-off households to take advantage of new economic opportunities or to protect themselves against negative shocks.

As noted earlier, whether economic inequality has declined or not depends upon what is being measured—that is, the underlying concepts. Not surprisingly, those who claim that economic disparities have widened as a result of trade liberalization generally base their argument on absolute as opposed to relative differences in equality.¹⁷ In fact, studies have shown that, on average, the impact of openness to trade on the distribution of the growth of income is neutral.¹⁸ Thus trade liberalization on average does not affect relative inequality, but it does widen absolute inequality. This is not to say that some countries have not seen a widening of within-country relative inequality during growth spurts. Indeed, in India and China some productive sectors have grown disproportionately faster than others, and this unequal growth has benefited certain groups over others: urban residents and the well educated, for example, saw their incomes rise more than did rural residents and the unskilled.

Inequality Matters for Future Poverty Reduction

While recognizing global inequality as a problem, the international community has been mostly focused on reducing absolute poverty. For example, the MDGs measure the numbers of people living in deprivation and do not address distribution issues directly. However, a growing literature argues that inequality can affect the pace of poverty reduction.¹⁹ One way it can do so is through reducing the effectiveness of growth in achieving poverty reduction. The response of poverty reduction to economic growth depends on inequality, among other things, so that two otherwise identical economies with very different income distributions will have very different poverty responses to growth. The country with high initial income inequality is likely to see a smaller positive impact of growth on poverty reduction than the country with low initial income inequality.²⁰

Recent Actions by the International Community

There is today a broad consensus within the international community on how to reduce poverty and reach the MDGs. The consensus rests on a framework of mutual accountability between developed and developing countries. This consensus recognizes the need to harness global forces to tackle poverty through

- Better access of developing country producers to developed country markets
- Better access to international financial resources to boost investment in health, education, and infrastructure, and to reduce vulnerability to external shocks and natural disasters
- Debt relief to free up resources for investing in health, education, water and sanitation, and to reduce debt overhang; and
- Adapting technological and scientific advances and medical research to directly benefit the poor.

For their part, developing countries need to pursue sound policies and make a commitment to good governance, which is central to development. Governments in developing countries need to be accountable to their citizens for the delivery of services such as health, education, and infrastructure and for their use of resources. Strengthening the quality of developing countries' public financial management is central to this framework. Building on this consensus, there is an urgent need for all parties—developed and developing countries alike—to scale up their action.

Development and the world's poor took center stage in the world arena in 2005. This "Year of Development" kicked off with the U.N. Millennium Project and reached a high point with the U.N. World Summit in September. During 2005 the international community sharpened its focus on aid, debt relief, trade liberalization, and security. At their summit in Gleneagles, Scotland, the leaders of the Group of Eight countries pledged to double their aid to Africa—an increase of \$25 billion a year—by 2010, and donors worldwide agreed to expand their aid to all developing countries by about \$50 billion. Major progress was also made in 2005 in extending and deepening debt relief to the poorest countries through the MDRI. This initiative will cancel 100 percent of the debt that heavily indebted poor countries owe to the African Development Fund, the International Development Association (IDA), and the International Monetary Fund (IMF), delivering over \$50 billion in debt relief (in nominal terms).²¹ Donors need to ensure that they deliver on their aid commitments and that more of the increment in aid is available for reducing poverty.

The U.N. World Summit in September 2005, which saw the largest gathering of world leaders in history, drew sharp attention to the interconnectedness of economic development and security. One of the summit outcomes was the creation of the U.N. Peacebuilding Commission, which will bring together key international actors to marshal resources, advise on postconflict peacebuilding and recovery strategies, and focus attention on reconstruction and institution-building efforts to help lay a solid foundation for sustained development. The work of this commission will be critical to meeting the special challenge facing fragile states, in which government and the rule of law are weak.

Despite world attention, recent progress on multilateral trade liberalization has been modest. The Doha Development Round of multilateral trade negotiations, which began in 2001, has great potential for spurring growth and fighting global poverty. Welfare gains to developing countries from complete liberalization of merchandise trade are conservatively estimated at \$86 billion a year by 2015, according to *Global Monitoring Report 2006*. Of course, not all poor countries are expected to benefit equally, and some might lose in the near term. Nevertheless, the answer is not to postpone trade reform, but rather to assist poor countries in meeting the adjustment costs of competing in freer markets, and to implement measures to improve their investment climates.

Despite the opportunities offered by trade liberalization, members of the World Trade Organization have so far been unable to make progress on modalities for market access for agricultural and nonagricultural products; as a consequence, the Doha round's deadlines have repeatedly been missed.

Members face a challenge to conclude the negotiations in 2006. All parties must redouble their efforts to reach an ambitious conclusion of the Doha round: key items are for the European Union to expand access to its agricultural markets, for the United States to reduce its domestic support to agriculture, and for developing countries to further liberalize their manufacturing and services sectors.

To further influence the global response to poverty, poor countries also need to exert greater influence in international forums. An active debate is ongoing on the appropriate share and representation of developing countries in international financial institutions.

The Role of the World Bank in Poverty Reduction

The World Bank's mission is to work for a world free of poverty. The Bank is helping developing countries and their people achieve the MDGs and sustained development through a two-pillar strategy: building a climate for investment, jobs, and sustainable economic growth; and investing in and empowering poor people to participate in development. The development strategy recognizes that strong growth requires an economic environment that is conducive to investment, job creation, and productivity growth. It also recognizes that economic growth cannot be sustained without human development. Thus investing in education, health, and gender equality and achieving the MDGs are vital in helping to empower people so that they can better participate in the development process.

The World Bank helps countries reduce poverty and sustain development by providing financial assistance—concessionary financing through IDA loans and grants, and nonconcessionary financing through the International Bank for Reconstruction and Development (IBRD)—as well as a wide range of policy advisory and analytical services and technical assistance. In conducting these activities the Bank tailors its support to the needs of the recipient country. The Bank's programs help to foster economic and financial stability, enhance the investment climate and the development of the private sector, promote more open international trade, improve infrastructure services, strengthen governance and fight corruption, and promote environmental sustainability. Through its programs the Bank also supports education, promotes gender equality, improves health outcomes, and combats communicable disease.

IDA is the largest source of concessional financial assistance for the world's poorest countries. Traditionally, IDA provided assistance in the form of highly concessional credits, but since fiscal 2003 it has expanded the use of

grants for the poorest and most deeply indebted countries. IDA commitments totaled \$8.7 billion in fiscal 2005. Africa received \$3.9 billion, followed by South Asia and East Asia and the Pacific at \$2.9 billion. The sectors receiving the largest support were public administration, including law and justice, \$2.2 billion; health and social services, \$1.3 billion; and transportation, \$1.1 billion. IDA allocates resources to individual countries on the basis of their need and performance. The performance factors include the quality of policies and institutions, with a particular emphasis on governance.²² IBRD commitments were \$13.6 billion in 2005.

The Bank works closely and continuously with national governments, bilateral donors, other international institutions, the private sector, civil society organizations, and other stakeholders to improve the effectiveness of its development activities. Through these sustained, cooperative efforts it hopes to come ever closer to achieving its goal of a world free of poverty.

Notes

1. See Sen (2000).
2. See Atkinson and Bourguignon (2000) for a detailed discussion of economic inequality.
3. The purchasing power parity (PPP) exchange rate states the number of units of local currency required to purchase the same basket of goods and services that can be purchased for one dollar in the United States.
4. Current practice is to use a single consumption level or GDP PPP for a country. The International Comparisons Program will produce poverty comparisons where, for the first time, there will be separate conversion factors for each income group—that is, there will be income-specific baskets.
5. See Milanovic (2006) and Ravallion (2003).
6. An added complication is that income per capita measures based on the national accounts can be quite different from those based on disposable income from household surveys. This means that inequality measures will be sensitive to the data source.
7. Bourguignon, Levin, and Rosenblatt (2004).
8. See Milanovic (2006). Dhikanov and Ward (2001) and Bourguignon and Morrison (2002) find a decline of about 1 point in the Gini index. Sala-i-Martin (2002) and Bhalla (2002) suggest that the decline is about 3 to 4 points.
9. Milanovic (2006).
10. United Nations (2004).
11. Krueger and Maleckova (2003) find little evidence of a direct link between poverty and terrorism.
12. There is a considerable literature on the links between poverty and conflict; see, for example, Collier and Hoeffler (2002) and Humphreys and Varshney (2004). The empirical evidence suggests that poverty and slow growth increase the risk of conflict and that conflict worsens poverty by imposing a steep financial cost on an economy and adversely affecting growth.
13. Dikhanov (2005).
14. See Easterly (forthcoming), Winters, McCulloch, and McKay (2004) and Winters (forthcoming) for detailed discussions of the channels through which globalization affects the poor.
15. Harrison (forthcoming).
16. Winters, McCulloch, and McKay (2004).
17. See Ravallion (2003) and Deaton (2004) for a discussion of these issues. Ravallion (2003) argues that quality-of-data issues also contribute to the controversy over the impact of globalization.

18. See Dollar and Kraay (2002).
19. See World Bank (2005), Aghion, Caroli, and Garcia-Penalosa (1999), Dikhanov (2005), and Ravallion (2005b).
20. Ravallion (2005b).
21. The cutoff date for debt relief is the end of 2004 for the African Development Fund and the IMF, and the end of 2003 for IDA.
22. See World Bank and IMF (2006).

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Selected Web Links on Poverty and Inequality

MacArthur Network	www.wws.princeton.edu/rpds/macarthur
Make Poverty History	www.makepovertyhistory.org
Poverty Action Lab	www.povertyactionlab.com
U.N. Millennium Development Goals	www.un.org/millenniumgoals
U.N. Millennium Project	www.unmillenniumproject.org
World Bank PovertyNet	www.worldbank.org/poverty