



WILEY-  
BLACKWELL

---

Efficiency, Equity and Poverty Alleviation: Policy Issues in Less Developed Countries

Author(s): Pranab Bardhan

Source: *The Economic Journal*, Vol. 106, No. 438 (Sep., 1996), pp. 1344-1356

Published by: Blackwell Publishing for the Royal Economic Society

Stable URL: <http://www.jstor.org/stable/2235526>

Accessed: 24/09/2008 16:39

---

Your use of the JSTOR archive indicates your acceptance of JSTOR's Terms and Conditions of Use, available at <http://www.jstor.org/page/info/about/policies/terms.jsp>. JSTOR's Terms and Conditions of Use provides, in part, that unless you have obtained prior permission, you may not download an entire issue of a journal or multiple copies of articles, and you may use content in the JSTOR archive only for your personal, non-commercial use.

Please contact the publisher regarding any further use of this work. Publisher contact information may be obtained at <http://www.jstor.org/action/showPublisher?publisherCode=black>.

Each copy of any part of a JSTOR transmission must contain the same copyright notice that appears on the screen or printed page of such transmission.

JSTOR is a not-for-profit organization founded in 1995 to build trusted digital archives for scholarship. We work with the scholarly community to preserve their work and the materials they rely upon, and to build a common research platform that promotes the discovery and use of these resources. For more information about JSTOR, please contact [support@jstor.org](mailto:support@jstor.org).



Royal Economic Society and Blackwell Publishing are collaborating with JSTOR to digitize, preserve and extend access to *The Economic Journal*.

<http://www.jstor.org>

## EFFICIENCY, EQUITY AND POVERTY ALLEVIATION: POLICY ISSUES IN LESS DEVELOPED COUNTRIES\*

*Pranab Bardhan*

### I. INTRODUCTION

In the poor countries of sub-Saharan Africa and South Asia (the areas where mass poverty in the world is geographically concentrated) poverty by any reasonable measurement is so pervasive that policies of poverty alleviation encompass practically the whole range of development policies. Most policies that significantly affect the national economy have also substantial implications for the poor. The efficiency–equity trade-off which is at the heart of much of mainstream policy economics is thus central to the policy debates on poverty. A society may very well consider the objective of redistribution in favour of the poor as a sufficiently worthwhile goal to warrant some sacrifice in terms of efficiency. But if such a redistribution comes at a substantial cost in terms of misallocated resources and aggregate income losses, it may not be politically or economically sustainable; in fact it can be a much more serious issue in economic policy in poor countries (both because the poor form a much larger proportion of the population and because one can afford such losses less at low levels of income) than even the controversies that rage around the efficiency impact of the ‘welfare’ budget in rich countries.

This issue is reflected in a running policy debate in poverty alleviation over the last twenty-five years, on the relative importance of market-driven growth as it trickles down to the poor as opposed to a programme of massive and direct intervention to help the poor. In this paper we shall start with a discussion of some of the issues in this debate, and proceed to situations where the efficiency–equity trade-off may be false or exaggerated (particularly when agency costs and coordination problems are taken into account), which in turn may have interesting policy implications in terms of possible efficiency-enhancing redistributive projects. In this context we shall also discuss the relative efficiency effects of asset distribution policies (like land reform) as opposed to tax-transfer policies that take the form of subsidies. Within transfer policies in general we shall discuss the merits and costs of efficient targeting, including issues of self-selection by the poor and of targeting underprivileged groups and backward areas. Finally, we discuss governance structures and focus on the role of local self-governing institutions in improving efficiency and equity in poverty alleviation.

\* I am grateful to Martin Ravallion for comments on an earlier draft.

## II. POVERTY ALLEVIATION, INTERVENTION AND GROWTH

In the recent past and, even currently, the governments in many poor countries have heavily interfered in the market in the name of helping the poor. They have used high tariffs, quantitative trade restrictions and overvalued exchange rates, subsidised credit and underpriced energy, water, and other publicly provided inputs to help domestic producers. They have used price control and trade restrictions on agricultural commodities to keep food prices low for the urban poor. They have used industrial and investment licences to keep larger producers at bay and help small-scale, sometimes inefficient, producers. They have imposed high marginal tax rates and public sector dominance in production with the objective of reducing concentration of income and wealth. The experience of the last four decades has shown that many of these policies have been counterproductive from the point of view of both efficiency and equity. Economic growth has often been stunted, while the conditions of inequality have not significantly improved, and in some cases even worsened.

In the more recent literature on poverty there is a better appreciation of the fact that market-driven economic growth need not be inconsistent with poverty alleviation. In many countries, in East and Southeast Asia in particular, fast outward-oriented growth has been associated with substantial reductions in mass poverty. In general, the most important way for economic growth to help the poor is by expanding their opportunities for productive and remunerative employment (including self-employment on farms and in artisan shops). There is now some measure of agreement that policies that contribute to growth by improving the allocative efficiency of resource use (say, by reducing distortions in relative prices, exchange rates, and trade policies) may help the poor. This is particularly so if the traded goods sector is more labour-intensive than the non-traded goods sector and if exports are more labour-intensive than import-substitutes (assuming, of course, that the workers have some basic education and skills). Underpricing of scarce inputs – such as capital, energy, and environmental resources – often leads to the adoption of capital-intensive and environment-damaging projects that have adverse distributional consequences. Movements of terms of trade in favour of agricultural commodities and removal of restrictions on their trade may help the poor if the sector consists of a larger number of small farmers who market a significant part of their output and if the wages of landless labourers do not lag far behind the price rises.

## III. EFFICIENCY ENHANCING EQUITY

Of course, some types of growth do not help the poor. In situations of severe capital market imperfections the escape routes from poverty for the unskilled and the assetless may remain blocked, while growth improves the prospects for capital-intensive or skill-intensive projects. The centripetal forces of growth with increasing returns may drain resources away from backward regions reinforcing regional polarisation, as economic geographers have repeatedly shown. Large projects of industrialisation and commercialisation may uproot