The World Development Report 2006: Brief Review

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A tempting first reaction to the World Development Report 2006 (henceforth WDR 2006)[2], entitled *Equity and Development*, is that it represents a significant advance. Whereas previous WDRs (in particular WDR 1990 and 2000/01) had concerned themselves with the need to reduce the absolute disadvantages experienced by countries and by persons, WDR 2006 is the first WDR centrally to be concerned with relative inequalities between nations and between persons. Relative inequalities are viewed in WDR 2006 as concerns in themselves. The report defines equity as the requirement that "individuals should have equal opportunities to pursue a life of their choosing and be spared from extreme deprivations in outcomes" (p.2). It thus combines the emphasis of recent normative reasoning on 'starting gate equality" with an insistence that outcomes that fall beneath a threshold of minimal adequacy must be deeply disvalued. This construction is rather clunky and appears to be the product of a political compromise rather than a foundational philosophical view, but is workable.

In many respects, WDR 2006 reflects the most progressive face of the World Bank (henceforth Bank). The report is concerned with absolute and relative disadvantages in their many dimensions (including health, education, political power, and real income). The report recognizes that disadvantages in these dimensions are often related. The report notes that self-perpetuating low level equilibrium traps are often associated with severe absolute deprivations or large relative inequalities and that there are often deep historical origins for these traps. The report also recognizes that inter-generational social mobility is often low and that specific policies are necessary to increase it. These features of the report are significant, and are worthy of praise. It can be argued that the report constitutes a landmark in terms of the breadth of its analysis and the choice of its theme.

However, from the standpoint of the developing countries, the report also possesses central inadequacies. Three of the classes into which inadequacies can be placed are the following:

1. *Data and Inferential Inadequacies*

The authors of the report cannot be blamed for making use of flawed data, as it may have been the best available to them. However, they can be blamed for failing to recognize the implications of the inadequacies in existing data for their ability to draw meaningful conclusions. For example, the choice of the specific PPPs for many countries (including large ones, such as such as India and China), used to compare real incomes across countries and to form global assessments, is highly questionable. Many countries have

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not recently, or in some instances ever, participated in benchmark surveys of the International Comparison Program, on the basis of which PPPs are identified. The implications of alternative choices of PPPs for assessments of global deprivations and inequalities are enormous, and must be centrally confronted [See e.g. Reddy and Minoiu (2005a, 2005b)]. Similarly, the report places great store in assessments that there have been reductions in global income poverty, deriving from the World Bank's money-metric ($1 and $2 per day) approach to poverty assessment. These assessments are open to questioning on the basis both of their foundational assumptions and estimation techniques [See e.g. Reddy and Pogge (2003)].

2. *Selective History and Analysis*

The report recognizes the role of historical phenomena (for example, the imprint of slavery and colonialism) in shaping existing patterns of inequality and deprivation within and across countries. The report also recognizes that within-country inequalities have risen in many countries in the recent period. However, it fails to recognize that the policies recommended by the Bretton Woods Institutions may have been among the major reasons for the increases in relative inequality observed in these countries in recent years. Structural adjustment policies and their successors may have among the central causes of widening relative income inequalities in many countries, contrary to what had been anticipated on the basis of simple trade models (and in particular the Stolper Samuelson theorem, which in its most simple variant predicts that trade liberalization in particular will lead to decreases in relative income inequality in developing countries). A considerable body of respectable technical literature (much of it focusing on Mexico's experience in the aftermath of NAFTA) has in recent years concerned itself with explaining possible theoretical explanations for the apparent unexpected impact of trade liberalization in developing countries [See for example the work of Robert Feenstra, Gordon Hanson, Ann Harrison, James Galbraith, Zadia Feliciano, Pinelopi Goldberg, Nina Pavcnik and Ana Revenga, cited in the references]. This literature is not even mentioned in the WDR's treatment of the effects of trade liberalization in Mexico (p.195). Similarly, there is reason to think that financial liberalization and labor market liberalization may each have contributed to widening relative inequalities within countries. Arguments of this kind, which assert that at least some of the reason for widening inequalities within countries may be the implementation of policies recommended by the Bretton Woods institutions, do not appear adequately to be recognized and confronted. The role of policies eagerly promoted by the Bretton Woods institutions in the past (for example, the implementation of user fees in the health sector) respectively in increasing absolute disadvantages within nations and widening relative inequalities between nations (at least relative to the counterfactual in which these policies were not pursued), has not been forthrightly examined.

The report often relies on questionable indicators and analytical tools. For example, more secure property rights, as judged by foreign investors, are used as a proxy for the quality of institutions. A blithe footnote (p.108) avers without offering further evidence that "These data…are imperfect as a measure of the relevant institutions because they pertain to investments by foreigners only. Even so, they seem in practice to capture how stable property rights are in general".

The report seeks too often to place the diverse phenomena that it confronts into an accustomed lens. For example, it describes domestic violence as an "inefficiency" (p.54). Although domestic violence is abominable, the reason that it is so is surely not that it constitutes an "inefficiency". Language of this kind is indicative of the lack of commitment of the authors of the report to a conceptual framework in which human beings are foregrounded over abstract ends such as "efficiency" which are employed in an obscurantist manner.

3. *Weak, Questionable or Unhelpful Prescriptions*

It is perhaps not surprising, in view of the partial nature of the history provided and the analysis undertaken in the report that the recommendations for policies that may decrease absolute disadvantages and relative inequalities are also perhaps overly restrictive. There are some excellent innovative proposal in the report, some of which may be in the interests of developing countries (for example, the proposal to create a "generic drug region" in which "inventors in developed countries make legally binding commitments to their own governments not to enforce patent rights in certain pharmaceutical markets" (pp. 224-5)). Similarly, the report correctly emphasizes the role of certain agricultural policies in developed countries (for instance, cotton subsidies) in depressing opportunities in poor countries. The report rightly takes note that aid should be targeted where it is most needed as well as it is most effective. It recognizes that there has been an influential move to target aid toward countries that are perceived to possess "good policies" but is perhaps not adequately critical of the recent attempts within the Bretton Woods institutions to articulate this view, which have often taken a very narrow view of what constitute "good policies" and appeared to recommend that countries which do not possess such policies (which centrally emphasize liberalization and privatization) should not be beneficiaries of development aid at all.[3]

The policies recommended in the report are more often than not accustomed policies which have been recommended in the past. It is a miracle that the same set of policies appears to be the prescription for all ills. For example, labor market deregulation (in particular reduction in the cost to employers of firing and hiring) is once again held up as being in general a highly desirable policy, and "overly generous unemployment benefit and social assistance systems, which discourage[s] job search" (p.192) are decried in blanket terms. Although there may occasionally be some merit in such recommendations, the reader is given the sense that alternative views have not been seriously considered. Increased competition in domestic financial markets is similarly advocated as a general policy. The need to identify policies that specifically benefit the poor or relatively disadvantaged is too often glossed over in favor of broad prescriptions the primary effect of which may be to serve other interests entirely. For example, the epilogue to the report concludes that the "twin pillars" of a national development strategy

[3] See e.g. Burnside and Dollar (2000).

aimed at increasing "equity" are a "better investment climate" and "empowerment". It is stated that "for most people in the developing world, and certainly for the poor, it is not possible to have one without the other". Many actual and potential conflicts of objectives are glossed over here; a better investment climate for the poor may not always be what makes for a better investment climate for relatively wealthy domestic or foreign investors, at least in the short run. The report notes, for example, that it is possible (p.228) that "the government…will not enforce tax collection, rather than build rural roads", presumably because underlying conflicts of interests are resolved in favor of the relatively wealthy, whether at home or abroad. How potential conflict of this kind should be handled is not addressed. In this and other respects, the report presents an account of political economy that is naïve. The general invocation of the need for a "better investment climate for all" without any effort to address such conflicts can have at most limited value in the formulation of policies that reduce absolute deprivations and relative inequalities. The treatment of property rights protections in the report is in this respect especially incoherent. Sound institutions are equated with those that protect property rights. However, land reforms including "expropriating with compensation" (p.167) are treated favourably, and the reader is told that (p.122) "The key to China's equitable development was the combination of initial conditions and the economic reforms" without apparent recognition that China's favourable "initial conditions" were the consequence of an earlier and comprehensive economic and social revolution, in which established property rights were overturned. One need not take a view on the merits of that revolution to recognize its historical importance.

Conclusion:

The WDR 2006 is a commendable effort in comparison to many of its predecessors. However, it is still dissatisfying. Its intellectual basis is often weak, its contents are not adequately complete and its prescriptions are often either questionable or of limited practical value.

A question that must be asked is: "Who does the WDR serve?" The substantial resources expended each year in the production of the WDR could perhaps better be used by supporting independent competitive research institutes (located in developing countries to the extent feasible) charged with the task of generating development research that is autonomous, intellectual rigorous and globally relevant. Competition can be beneficial in policy analysis, just as it is alleged to be beneficial in labor, capital and product markets. Perhaps this is the lesson that should be learned in this third decade of the WDR.

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