

# Getting growth right



We believe in life before death

Economic growth can make a hugely valuable contribution to development yet, in all too many cases, it has failed to do so.

This failure is now widely recognised but responses to it vary. Some see it as a judgement on the policies, others as a judgement on the policymakers – in developing countries or in international financial institutions or bilateral donors, according to taste. Others see it as evidence of a failure of economists or economics. Still others see the failure as inherent to development. They therefore feel that no progress is possible – which in turn is interpreted variously to mean that poorer countries are fundamentally incapable of development, or that the international economic and political structure is immutably stacked against it.

These caricature positions cannot be supported, although failings have certainly been widespread. To mention just one, non-governmental organisations (NGOs) often lack the capacity, as well as the opportunity, to engage fully in economic debates, so may not always contribute positively. The UK Secretary of State for International Development, Douglas Alexander, is critical of some in the development community for being ‘uncomfortable discussing economic growth without caveats’.<sup>1</sup>

Yet the UK government, as well as other donors, also bears responsibility for the less than constructive debate in this area. Successive Department for International Development (DFID) ministers, for example, have repeatedly claimed that growth, rather than redistribution, has accounted for 80 per cent of the poverty reduction around the world since 1980. On inspection, this turns out to depend on a result drawn from an early version of a research paper, which was subsequently dropped from the published version and which came with an explicit caveat that it should not be interpreted in this way. See box ‘One way to get growth wrong’, below.

Economic growth is an instrument, not a goal, of development. It must form a part of every development strategy (including where an explicit choice is made not to prioritise it at a particular stage in a particular country’s development). Ultimately, growth can play a major role in improving the lives of the poorest people, but only if we get it right.

This means leaving overblown and inaccurate rhetoric behind, on every side of the debate. It means recognising – as the important Commission on Growth and Development (CGD) report makes clear – that ‘no generic formula exists’ for a strategy to generate sustained growth in individual countries.<sup>2</sup>

The CGD is made up of political and development leaders, supported by two Nobel prize-winning economists. For more than two years they considered the views of around 300 distinguished academics. No serious economist or other development specialist would now argue for a fixed list of policies like those labelled the ‘Washington Consensus’.<sup>3</sup>

Growth is one of many instruments, not a goal in its own right, and this must be reflected in the approach to policy analysis. Exhaustive country-specific analysis of the constraints on development – not of the constraints on growth – must underlie the generation of effective strategies. All parts of the development community – from academics and non-governmental organisation (NGOs), to policymakers and civil servants, and in the global South and the North – must contribute to that analysis.

Getting growth right is of fundamental importance for development. Understanding that we have, in great part, failed in this task does not mean that we should throw our hands up in despair and walk away. The recognition that there is no one-size-fits-all

approach is a highly positive step, for it opens the door to better economic analysis – and to better growth.

Such analysis exists. Key policymakers may have been less open to hearing advice that conflicted with their expectations, or which did not offer simple and easily replicable policy options, but it is available.

The CGD brought together much important academic research and experience from different countries, and its report offers many examples of better analysis (while still leaving room for improvement). Above all, openness to country-specific approaches – if understood by policymakers – can greatly increase the chances of their getting growth right.

This briefing sets out Christian Aid's thinking on the state of the debate and specifically on the implications of the consensus: that growth is one instrument, while the goal is development; and that there is no one-size-fits-all approach to getting growth right.

### **Shifting the goalposts**

'Human development is the end – economic growth a means'  
– Human Development Report, 1996

'We should [not] value economic growth as an end in itself'  
– Douglas Alexander, 2008

'Growth is not an end in itself'  
– CGD, 2008

There is no dispute among serious development specialists that economic growth is not the goal but rather one instrument of many. But what, then, is the goal? Clarity on this is essential if policy is to produce the desired results.

Some define the goal as sustainable development, others as the eradication of poverty; but these are in effect the same goal, since poverty is now generally defined not as deprivation of income but rather as deprivation across a full range of development indicators. This must be sustainable and not only apply to current generations.

'Development' is taken to refer to human development, which the first United Nations Development Programme (UNDP) Human Development Report in 1990 defined as 'a process of enlarging people's choices. The most critical ones are to lead a long and healthy life, to be educated and to enjoy a decent standard of living. Additional choices include 'political freedom, guaranteed human rights and self-respect' (p 10).

'Sustainable development' is such a process, but with the additional qualification that benefits for current generations do not diminish those available to future generations. This qualification entails a range of constraints on policy, from fiscal prudence (to avoid passing on unreasonable burdens of debt to future generations) to protection of the natural environment.

Development economists Gustav Ranis, Frances Stewart and Emma Samman<sup>4</sup> have compiled a list of human development categories, which gives a clearer – though necessarily subjective – view of the component factors of human development:

- the UNDP's human development index (HDI), which includes health, education and a measure of income (broadly covering bodily health, literacy and basic aspects of material well-being)
- mental wellbeing (an individual's psychological state)
- empowerment (particularly of the deprived)
- political freedom
- social relations
- community wellbeing
- inequalities
- work conditions
- leisure conditions
- dimensions of security – political (for instance freedom from political violence or instability)
- dimensions of security – economic (for instance freedom from economic fluctuations)
- environmental conditions.

What is the contribution here of growth? Economic growth refers to the rate of increase in the economic activity of a country, most commonly measured as its gross domestic product (GDP) – although preferably, for development purposes, by GDP per person. Even in this latter form, however, it captures directly only one development indicator, average income per person.

This measure in itself is, of course, imperfect since it takes no account of inequality and hence says little about income poverty. Economic freedom is clearly important, alongside social and political freedoms, but average income measures with no inequality information reveal little about the economic freedom of individuals and households.

Growth can contribute to some but far from all of the components of the complex development goal. This should not be taken to imply that growth is bad or somehow in opposition to development. It should, however, have more serious implications for policy than it has arguably had thus far – among donors in particular.

### **Getting growth wrong**

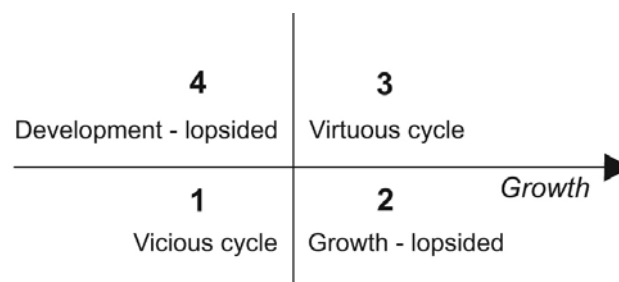
There are three main reasons why policies pursuing growth have failed in different countries and at different periods:

- in many cases the policies pursued have simply not generated growth
- of those cases where growth has been achieved, it has in many cases contributed little to development
- even where growth has been achieved and has contributed to development, the outcome may still have been lower development than if development itself had been prioritised over growth.

Where policy capacity and resources are scarce, development will suffer if growth is prioritised above all else.

Figure 1, showing growth on one axis and development on the other, clarifies this analysis. In quadrant 1 both growth and development are negative (or zero) – a vicious cycle where countries are unable to make progress. In quadrant 2, countries achieve growth but this does not translate into development benefits – a growth-lopsided outcome. Quadrant 3 sees both growth and development achieved (a virtuous cycle), while in quadrant 4 a development-lopsided outcome occurs without growth.

**Figure 1: Growth and development outcomes<sup>5</sup>**



If we put into practice the consensus view that growth is not a goal but an instrument, and development the goal, then by definition only quadrants 3 and 4 represent successful policy. All too common, of course, has been a focus on quadrants 2 and 3, reflecting the prioritisation of growth over broader development goals.

The three failures listed above relate to quadrants 1, 2 and 3. The first is the worst outcome, where policies to achieve growth fail to do so, and have no development benefit either. An obvious example is the pressure put on developing countries to liberalise their international trade regimes, a policy primarily motivated by a growth agenda rather than a development one – and which has been broadly unsuccessful in delivering either.

As Dani Rodrik has shown, 'The cross-national evidence on this issue is easily summarised. The available studies reveal no systematic relationship between a country's average level of tariff and nontariff restrictions and its subsequent economic growth rate.'<sup>6</sup>

The Haitian economy is an extreme example, with powerful liberalisation in the mid-1980s and mid-1990s shifting the country from self-sufficiency in food to using more than 80 per cent of its export earnings to pay for food imports – even in 2006, well before the current food price spikes.<sup>7</sup> By 2005, imports were around 45 per cent of GDP, compared to around 15 per cent for exports. Average growth in GDP and in GDP per person was negative in the 1980s and the 1990s. In 1980, imports accounted for around 30 per cent of GDP, compared to around 20 per cent for exports.

A different example concerns focus rather than specific policy prescriptions. Donors have often focused on large and multinational businesses at the expense of any concern for the small and medium-sized enterprises (SMEs), which are responsible for the majority of employment and of economic activity in most developing countries, and offer the best growth prospects in many.

This year, for example, the UK government has enlisted a number of multinationals in its Call to Action for the millennium development goals (MDGs). Questions around policy on SMEs were referred to its civil society group rather than the key research group on growth.

### **One way to get growth wrong**

Recent high-profile speeches by DFID ministers have featured a powerful claim for the importance of growth: namely, that 'growth has accounted for as much as 80 per cent of the poverty reduction around the world since 1980'.<sup>8</sup> This is used to justify a focus on growth 'without caveats such as "sustainable" and "pro-poor"'.

Sadly, however, the claim does not withstand scrutiny. It is referenced to a 2002 paper by David Dollar and Aart Kraay of the World Bank, entitled 'Growth is good for the poor'. This is not the well-known publication of that name, but rather the working paper which preceded it.<sup>9</sup>

The result in question relates not to the effect of growth, but rather to the level of income: 'Over 80 per cent of the variation in incomes of the poor is due to variation in overall per capita incomes' (p 5). So richer countries typically have less income poverty, and poorer countries more – but, crucially, this result does not say anything about the effect of changes in the level of income, that is of economic growth, in particular countries.

Dollar and Kraay do in fact consider the effect of growth specifically. In the same paragraph they summarise the relevant finding: 'Just under half of the growth of incomes of the poor is explained by growth in mean income' (p 6). This is an interpretation of the fact that their regression has an explanatory power ( $R^2$ ) of 0.44. So rather than growth explaining 80 per cent of changes in poverty, it explains less than half – according to the very authors who are being cited.

Interestingly, we can take the same data and the same approach, but instead test for the effect of redistribution – that is, we look at the distribution of income rather than mean income. We regress the change in income of the poor on the change in their income share. From this regression we obtain an  $R^2$  of 0.59 – so changes in income distribution over the past 40 years can explain substantially more of the changes in the income of the poor, than can growth.<sup>10</sup>

There are legitimate statistical disputes over the interactions of growth, inequality and poverty – but the claims of growth being responsible for 80 per cent of poverty reduction are a clear misinterpretation of the evidence. The same analysis shows redistribution has been more important than growth.<sup>11</sup>

The second failure of policy, with growth-lopsided outcomes as in quadrant 2, sees policies achieving growth without development – of which Equatorial Guinea's oil-driven growth is a clear example. Equally, Bolivia was characterised in a 2004 study for DFID as 'a country in which there has for more than 15 years been economic growth (respectable until recently) but in which poverty has not fallen from its early 1990s level and since 1999 has shown a very perceptible rise'.<sup>12</sup> The study highlights the 'severe discrimination' faced by ethnic Aymaras and Quechuas in particular, and inequality in general, among the causes of the country's growth-lopsided performance.

Interest in specifically pro-poor growth among policymakers appears to have diminished, with Douglas Alexander making the argument that such 'caveats' on growth are unhelpful. There may be a case for moving on from a focus on pro-poor growth, and seeing growth as delivering only that – an increase in the economy activity (per person) of a country. Distributional elements, for example, would then be

considered elsewhere – but the frequency with which growth is accompanied by rising inequality, weakening or reversing any poverty benefits, means that such a decision would raise concern, and at the least require great care in monitoring the effects.

### **Growth, inequality and income poverty**

Growth that is accompanied by rising inequality will not deliver the same benefits in terms of reducing income poverty as growth that is accompanied by falling inequality. A serious concern with the pursuit of growth is that the quality of growth has not been considered, and hence through rising inequality the effects on poverty have been substantially less than was possible.

Two types of analysis emphasise this point: those that assess the potential effect of growth (*ex ante*), and those that assess the actual effects of growth (*ex post*).

By looking at the mathematical implications of different initial levels of income poverty and inequality, Stephan Klasen and Mark Misselhorn (2007)<sup>13</sup> consider the effects of growth in reducing poverty. Unsurprisingly, they find that growth in mean incomes will have hugely different results in different situations. In particular, where the mean income in a country is not far above the poverty line (in poorer countries), then higher levels of initial inequality dramatically reduce the contribution of growth to poverty reduction.

Hyun Son and Nanak Kakwani (2008)<sup>14</sup> examined periods of positive and negative growth in 80 low- and middle-income countries between 1984 and 2001. They found that substantially more of the periods of positive growth can be characterised as ‘anti-poor’ than as ‘pro-poor’, in terms of their impact on per capita household consumption or income.

On this basis, analysis of the appropriate development policies in a country must take into account the impact of initial inequality and poverty on the likely poverty reduction benefits of any growth achieved, before committing to the pursuit of growth as a priority. Second, the likelihood that any growth is achieved, and the likelihood that such growth is ‘anti-poor’ and hence of reduced benefit, must be considered in deciding what resources to devote to pursuing growth. Finally, recognising that poverty is not simply a question of income, the analysis must also consider – as do Melanie Grosse, Kenneth Harttgen and Stephan Klasen (2008)<sup>15</sup> – whether growth is pro- or anti-poor in terms of broader development indicators such as education, mortality, and so on.

The third failure of policy actually appears in quadrant 3 – the virtuous cycle in which both growth and development are achieved. The specific concern here is that since growth has been prioritised over development, the actual level of development progress that results is less than it would have been had it been the priority.

Policy prescriptions that prioritise growth more or less regardless of the impacts on key human development components – for example inequality, social justice or environmental protection – will inevitably give rise to inefficiently low gains in poverty reduction and/or broader human development.

Imagine a business that becomes confused in a similar way, perhaps recognising the potential contribution to profit of research and development (R&D) but then becoming

confused and unable to distinguish between instruments and goals. Rather than maximising profit then, it maximises R&D – and in doing so inevitably arrives at an equilibrium outcome with sub-optimally high R&D and sub-optimally low profit. In the case of a growth-development confusion, the outcome would be growth that is higher than optimal and development that is lower.

The added complexity here is that policymakers are unable simply to choose the level of growth they desire. As a result, while the firm in the example will at least end up with high levels of R&D (albeit with low profits), policymakers mistaking growth for a goal in its own right cannot even be sure of delivering this – but will certainly deliver lower returns and hence unnecessarily poor development.

There are, however, more positive messages to draw from the quadrant analysis. First, periods in which development progress has been achieved without growth (development-lopsided outcomes in quadrant 4) should be treated as successful, for so long as the development is sustained. Indonesia and China, for example, shifted from development lopsidedness in the 1960s into the virtuous cycle in the 1970s and 1980s. In contrast, the Philippines slipped from development lopsidedness in the 1960s, to growth lopsidedness in the 1970s, and from there into the vicious cycle in the 1980s.

This raises the question of the time period over which outcomes should be evaluated, which also relates to periods of growth without development (growth-lopsided outcomes in quadrant 2). Is there a systematic relationship between growth and development over time, and if so, how does it work? How can policymakers exploit it?

### **Growth, distribution and climate change**

In general, on current patterns of distribution, a greater share of every additional US dollar of growth goes to the non-poor than to the poor. Indeed, 'between 1990 and 2001, for every \$100 worth of growth in the world's per-person income, just \$0.60 contributed to reducing poverty below the \$1-a-day line.'<sup>16</sup> The extent of inequality has been identified, even by the World Bank, as a central obstacle to development in countries across Latin America.<sup>17</sup>

Meanwhile, the need to contain carbon emissions generates a pressure to ensure that each dollar of growth is as clean as possible, and does as much good for development as possible.

This twin pressure intensifies the need to get growth right: if we pursue growth that does not deliver development, and allow unnecessarily 'dirty' growth in rich and poor countries alike, the world's chance to deliver sustainable development to the poor and marginalised (the bottom billion and beyond) will simply go up in smoke.

### **The relationship between growth and development**

It is often claimed that growth and improvements in the HDI are highly correlated, and hence that targeting the former will (necessarily) deliver gains in the latter. Aside from the latter's limitations as a measure of broad human development, this approach is flawed in any case. The relatively strong correlation that exists is between levels of income per person and of the HDI.

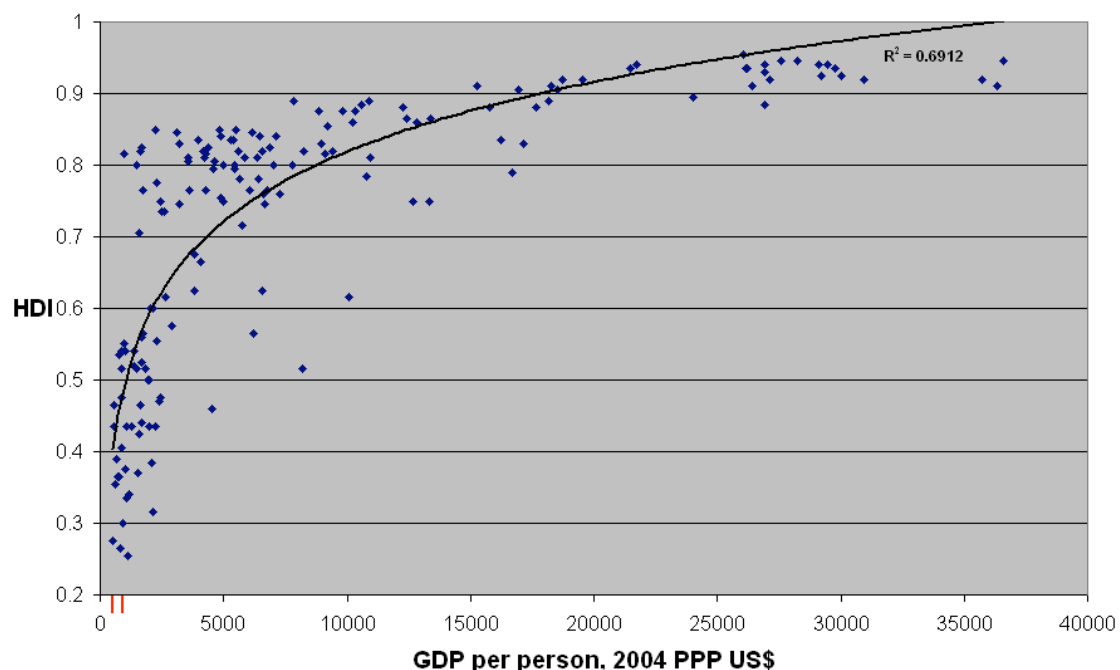
Figure 2 appeared (without the red lines) in a recent DFID presentation. It shows a scatter plot of per-person GDP levels (income and not in fact growth) against the HDI

after removal of income per person (an index based on health and education outcomes only).

Taking Tanzania as an example, consider the possibilities for growth. Were Tanzania's GDP to grow by 5 per cent annually, on a completely stable basis, then using (and extending forward) DFID's forecast of 3 per cent population growth, it would take 37 years for per person income to double (from \$580). This would mean a shift from roughly one-tenth of the first separator on the horizontal axis to roughly one-twentieth, or from the first red line to the second.

Even assuming such an unrealistically long and stable period of growth, for a period approximating the average life expectancy in a number of sub-Saharan African countries, the predictable impact of this growth on HDI in Tanzania would be limited. Note, too, that this is where the curve is steepest, so it is in countries at these lower incomes where growth can play the most valuable role. Yet even under such extremely favourable assumptions, growth alone may not provide the hoped-for improvements in development.

**Figure 2: 'Growth is associated with better human development'**



Source: DFID presentation, BOND AGM, 24 October 2007.

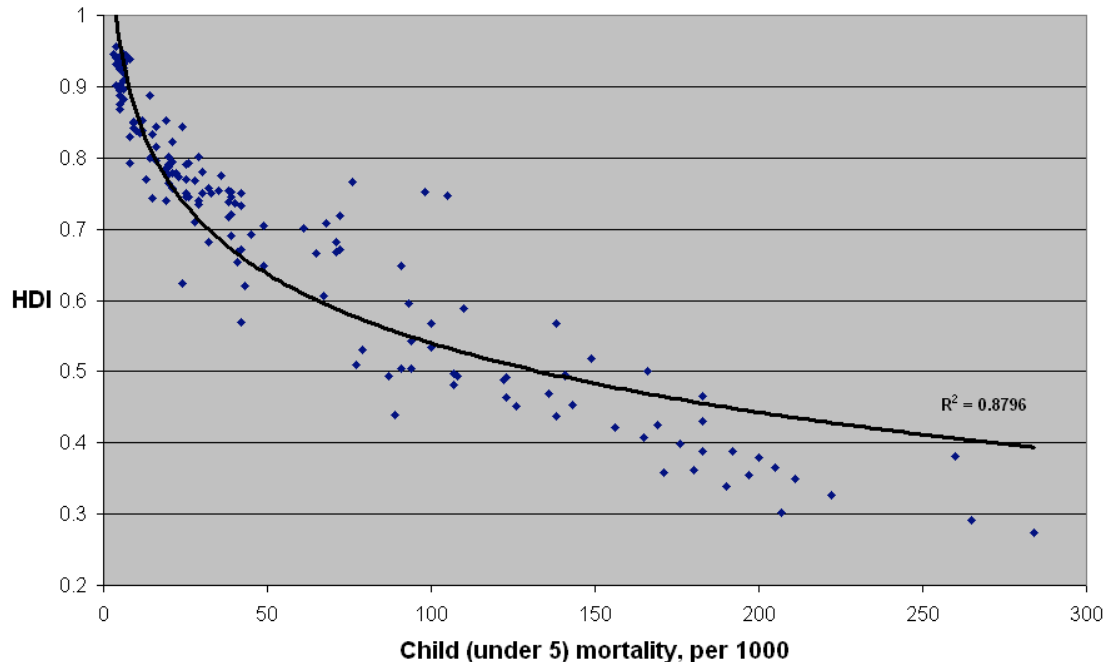
Mathematically, there appears to be a logarithmic relationship between GDP per person and the HDI, which the black line shows. This relationship 'explains' around 69 per cent of the variation in HDI.

A much higher share of the variation, 88 per cent, is similarly 'explained' by the rate of infant (under age five) mortality, as shown in Figure 3. It seems obvious that if a strategy were pursued of targeting a single factor in order to raise development, it would fare rather better if the single factor in question were not growth but rather infant mortality.

Such a single-factor approach would of course be foolish, even with this more appropriate choice of factor. It clearly makes no sense for policymakers to use all but

one of the many instruments available with the aim of maximising the remaining one, instead of focusing their resources on the ultimate goal.

**Figure 3: Lower infant mortality is associated with better human development**

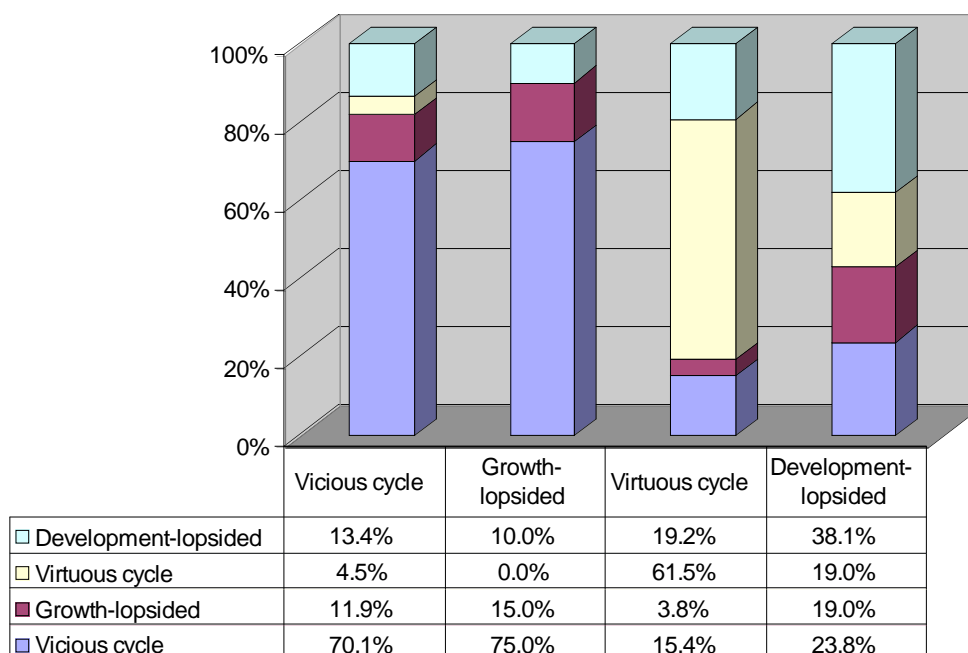


Returning to the question of time, maximising the benefits of growth (rather than maximising growth itself) requires that it be maintained over a significant period, since the generally greater vulnerability of the poor and marginalised to macroeconomic volatility and reversals is well established. Fortunately, research on the linkages over time between growth and development seems unequivocal in its conclusions: **human development, rather than growth, must be prioritised if sustained improvements are to be obtained.**

Ranis, Stewart and Ramirez (2000)<sup>18</sup> show how economic growth and human development each reinforce the other through a variety of linkages. For example, higher growth can fund government expenditures on health and education, and stronger human development can – through a more educated workforce or more equal income distribution – contribute to stronger, more broad-based growth.

Examining data for the period 1960 to 1992, the authors find that some countries were able to enter a virtuous cycle where both human development and economic growth were improving (equivalent to quadrant 3 in Figure 1), but many more fell into a vicious cycle where performance on both was poor (quadrant 1). Figure 4 shows the authors' results, from tracking countries' performance in the periods 1960-70, 1970-80 and 1980-92. For countries experiencing each outcome in a given period, the graph shows which outcomes were obtained in the subsequent period.

**Figure 4: Country performance over time**



Source: adapted from Ranis et al, 2000.

For a country that in any given period is in the vicious cycle (little or no growth and little or no development), there is a 70 per cent chance that it remains there during the subsequent period. Fewer than 5 per cent move directly to the virtuous cycle. For a country starting in the virtuous cycle, there is a greater than 60 per cent chance that it remains there, while 15 per cent fall back into the vicious cycle.

The question of relevance here is what happened in those countries that initially saw progress on only one or other indicator. Three-quarters of those countries that initially obtained growth without human development were unable to sustain it, and fell back into the vicious cycle. None of these countries were able to move into the virtuous cycle by maintaining growth but subsequently introducing development progress.

By contrast, consider the last column in Figure 4. Of those countries that experienced human development-lopsided outcomes in a given period, without significant growth initially, almost a fifth were able to move into the virtuous cycle. Almost 40 per cent continued with development-lopsided outcomes. Only a quarter fell back into the vicious cycle.

In other words, **countries that pursued growth without improvements in human development were unable to sustain either**. Countries that prioritised human development first were both more likely to sustain it, and more likely to see growth follow.

The CGD studied 13 countries that had experienced sustained growth – growth at an average of 7 per cent a year for 25 years or more: Botswana, Brazil, China, Hong Kong, Indonesia, Japan, Malaysia, Malta, Oman, Singapore, South Korea, Taiwan and Thailand. Not all continued to grow strongly; the authors note that Brazil is ‘the most striking example’ of a country that lost momentum, with ‘fast economic growth petering out around ...1979’ (p 20).

The Ranis et al (2000) study includes nine of these in its sample (omitting Japan, Malta, Oman and Taiwan). During the 1960s, each one was in the virtuous cycle except Brazil (growth lopsided), China (development lopsided) and Botswana (vicious cycle).

By the 1970s, each of the countries was in the virtuous cycle except Brazil. China has made the relatively common step of moving from development-lopsided outcomes to the virtuous cycle, while Botswana became one of the rare cases of a country breaking from the vicious cycle straight to the virtuous, managing to combine resource-led growth with a persistent emphasis on human development expenditures and relatively strong governance.

Brazil was characterised by Ranis et al as growth lopsided in the 1960s and 1970s, and by the 1980s – as in most other such cases in their sample – it had fallen back into the vicious cycle.

The growth and development analysis is able then to provide valuable additional information on the pattern of growth successes that the CGD sets out – in particular to predict accurately which countries would see sustained growth, according to whether or not they were able to combine it with development progress.

This gives a clear steer to policymakers considering whether a short-term ‘push for growth’ might provide the best response to weak development – the answer is almost certainly negative. Improvements in human development must be prioritised, if they – and growth – are to be sustained.

Rather than carrying out ‘growth diagnostics’, which aim to identify the key constraints to growth and respond accordingly, policymakers should be seeking ‘development diagnostics’ – to do the same for this more complex goal.

### **Learning the lessons**

The need for complex ‘development diagnostics’ in each specific country case means that the policy prescription will vary. Nonetheless, some broad points can be made – on particular policy areas and on the approach to making policy.

Perhaps the most welcome feature of the growth debate in recent years has been the recognition, by all sides, of the need to allow individual countries greater space in which to set their own policies.

One area in which this was emphatically not agreed, however, is economic openness. Over the past three decades, the prescription of greater market opening has been dominant in both trade in goods and services and in flows of financial capital. With both trade and finance, advice from bilateral and multilateral donors rested on the weakest of bases: an absence of proven growth benefits for poorer countries, and growing questions over distributional and broader development impacts.<sup>19</sup>

The recognition that there are no clear growth benefits, and indeed that reliance on foreign finance can damage growth,<sup>20</sup> should ensure rather more emphasis is given in practice to the need for developing country governments to be less restricted over policy in this area.

This should absolutely not be construed as an argument that openness is bad for development. Equally, on the other extreme, enforced closure is highly damaging –

as the impact of Israeli policies on the economic and human development of the occupied Palestinian territories makes painfully clear.<sup>21</sup>

The implication, again – even if it does not lend itself to simple advice for policymakers – is that policy space is fundamental.

A second important point emerges from thinking about growth policies that prioritise development rather than growth itself: this is that having ‘broad-based’ growth is key to achieving development. This can imply some quite specific outcomes, dependent on the situation: consider examples in energy policy, agriculture and investment.

In energy policy, we need to change the carbon emissions trajectory of the world if we are to avoid a rise in temperatures above 2°C and the irreversible climate change damage that could ensue. Given this, it is of even greater importance that each unit of growth contributes the maximum possible to development and the minimum necessary to emissions.

Large-scale, heavily emitting power stations, which impose the need to distribute energy widely, result in global average efficiencies of electricity production of just 34 per cent for coal, 37 per cent for oil and 40 per cent for natural gas.<sup>22</sup> Small-scale local power solutions can offer much greater efficiency due to the absence of losses in transmission, and hence the economic arguments in favour of the former would have to be overwhelming for the case to be made. Note that the same analysis should apply to rich countries also, whose responsibility for climate change – and need to reduce future emissions – is far greater.

In agriculture, the analysis relates both to productivity and to development impact. It is an established fact of the economic research, confirmed for many individual countries and regions in different continents, that there is an inverse relationship between farm size and yield per acre – that is, that small farms obtain much higher yields.<sup>23</sup> In part, this is due to greater labour input – which supports a view of these farms as ‘efficient but poor’.<sup>24</sup>

As researchers at the International Food Policy Research Institute have highlighted, much more needs to be done to provide a supporting economic environment for these farms.<sup>25</sup> The development impact of support to small-scale farming, directly on the most impoverished and marginalised, is also likely to be greater than that of large-scale commercial farming – since, for example, around 65 per cent of the population of sub-Saharan Africa relies on this source of sustenance.<sup>26</sup>

This is not to romanticise the life of small-scale farmers, nor to ignore the higher labour contribution that is likely to underlie the difference in yields. It is, rather, to demand that policy-making and prioritisation reflect the reality of developing countries and respond to the growth and development opportunities as they exist – rather than, for example, systematically under-funding rural development.

Agricultural policy should therefore look to establish broader opportunities, and to provide again some of the mechanisms that offer some stability of prices and credit availability, such as agricultural marketing boards and rural banking provision.<sup>27</sup> These institutions have been shut down and privatised, respectively, across many developing countries, and there were certainly issues with their operation. But the failure of the private sector to fill the gap is also clear, and the possibility of creating superior institutions this time round should not simply be dismissed.

In policy geared to the investment climate, there is a rather strange emphasis in much donor work. Measures such as the World Bank's Doing Business Indicators emphasise features such as the tax rate, with lower corporate taxes guaranteeing a higher score and in some cases greater access to aid. For countries where weak government revenues restrain desperately needed public expenditures (and where greater public investment is likely to lead to additional private investment), this is a bizarre policy incentive for donors to impose.

More broadly, the focus of too much investment policy is on large enterprises and multinationals. In most countries, however, and especially in developing countries, it is not large firms but small and medium-sized ones which are responsible for the majority of employment and of economic activity. Why, then, should these not be the focus of investment policy, for growth or for development, if targeting broad-based enjoyment of the fruits of economic activity is a significant aim?

From energy to agriculture to investment, small is not necessarily beautiful – but nor should it be invisible to policymakers. Local energy production can be more efficient, small-scale agriculture more productive, and small business – in farming or elsewhere – can be the most effective way of ensuring the benefits of growth are spread widely.

On the making of policy, there are two particular areas of concern, both of which relate to the practical application of the ministerial recognition that growth is one instrument, and development the goal.

The first relates to the Poverty and Social Impact Analysis (PSIA) to which various donors, including the World Bank, International Monetary Fund (IMF) and DFID, have committed. This is intended to be a process driven by those in developing countries, supported by donors, using qualitative and quantitative techniques to analyse a range of policy options in terms of their likely impacts on a range of development indicators.

Arguably, if this was well done, it could produce exactly the 'development diagnostics' required to ensure that scarce resources, and scarce policy and administrative capacity, are used more effectively to promote development.

Instead, for a range of reasons from limited impact on actual policy design, to limited country ownership of the process, to limits on the options actually considered, PSIA is not living up to its potential.<sup>28</sup>

The second policy concern is relatively specific: DFID has announced the creation of an international growth centre (IGC) to which it intends to allocate £40-50 million of funding. This will be a resource for policymakers in developing countries to call on in order to avail themselves of high-quality and country-specific analysis. Christian Aid welcomes this as an important element of the new approach needed.

Currently, however, the objectives are defined as follows:

'The objective of the IGC is to increase economic growth rates and progress towards the MDGs in developing countries by:

- providing practical analytic and policy support to governments around constraints and opportunities to faster growth
- enhancing analytic methodologies for understanding growth at the country level
- broadening the understanding of economic growth successes and challenges in developing countries
- bringing together world experts and practitioners on growth to share experience.'<sup>29</sup>

This must be aligned with the ministerial recognition that growth is not the goal. Specifically, this funding (and DFID's own policy research capacity, which is heavily weighted towards growth) should be focused on lifting the constraints to development that will often, but not always, include growth, and almost always include a range of other factors.

We suggest a limited but specific redrafting of the IGC objectives:

'The objective of the IGC is to increase the contribution of economic growth towards progress towards the MDGs in developing countries by:

- providing practical analytic and policy support to governments around constraints and opportunities to improving the contribution of growth to development
- enhancing analytic methodologies for understanding growth and development linkages at the country level
- broadening the understanding of economic growth in development successes and failures
- bringing together world experts and practitioners on growth to share experience.'

Finally, as highlighted in the box 'Growth, inequality and income poverty' above, analysis of the potential benefits of pursuing growth in a given country situation must be informed by assessment of the existing distribution and poverty levels, and of the likely inequality impact of growth if achieved by particular policies. In some circumstance (notably poor countries with low levels of inequality) growth may well prove the most powerful instrument for development – but this must emerge from the analysis, not by assumption.

## **Conclusions and recommendations**

Christian Aid recognises the potential of economic growth to contribute to development, possibly fundamentally for the poorest countries in particular.

In order for growth to fulfil its potential, however, the development community (and policymakers in particular) must ensure their analysis reflects the consensus that growth is not a goal but rather one instrument among many – with the complex goal of sustainable human development.

This requires country-specific analysis that takes into account the limitations on growth, not least from existing inequality and from pressures related to climate change. It also means a need for focus – to avoid pushing for just any growth, for example from the consumption and asset price booms that typically follow financial liberalisation, but for growth that can be sustained and will deliver development across as broad a base of poor people as possible.

The 'social development' agenda – targeting the poor and broader human development objectives – remains absolutely valid. More than that, it should be recognised as the dominant element of policy strategy – rather than this dog being wagged by the tail of growth.

To address the pressure of climate change, each US dollar of growth needs to be as effective as possible in contributing to sustainable human development. That means returning more seriously to a redistributive agenda, and ensuring a deal on cutting global carbon emissions that provides each country with the right incentives for clean development – and enough resources to do so.

Growth is important to development – important enough to get it right.

## Endnotes

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- 2 Commission on Growth and Development, *The Growth Report: Strategies for Sustained Growth and Inclusive Development*, Washington, DC: World Bank, 2008.
- 3 A term coined, and a policy list first provided, by John Williamson, 'What Washington means by policy reform', paper presented at Institute for International Economics, November 1989.
- 4 Gustav Ranis, Frances Stewart and Emma Samman, 'Human development: beyond the human development index', *Journal of Human Development* 2006, 7(3), pp 323-358.
- 5 This quadrant analysis is based on the approach taken in Gustav Ranis, Frances Stewart and Alejandro Ramirez, 'Economic growth and human development', *World Development* 2000, 28(2), pp 197-219.
- 6 Dani Rodrik, *One Economics, Many Recipes: Globalization, Institutions, and Economic Growth*, Princeton: Princeton University Press, 2007, p.217.
- 7 Agricultural Liberalisation in Haiti, Christian Aid, 2006.
- 8 Douglas Alexander, 'Growth at the heart of development', speech by the Secretary of State for International Development, at the Institute of Directors, London, 31 March 2008, see [www.dfid.gov.uk/news/files/Speeches/alexander-growth-fulltext.asp](http://www.dfid.gov.uk/news/files/Speeches/alexander-growth-fulltext.asp). See also 'Growth and poverty reduction', speech given by then International Development Minister Shriti Vadera at the launch of the *Doing Business Report* 2008, 12 October 2007, see [www.dfid.gov.uk/news/files/africa-shriti-position.asp](http://www.dfid.gov.uk/news/files/africa-shriti-position.asp) (site accessed 24 June 2008).
- 9 See: [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=632656](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=632656).
- 10 Christian Aid is grateful to Liam Wren-Lewis, University of Oxford, for this analysis.
- 11 This is to say nothing of the fundamental criticisms that have been levelled at the whole approach taken by Dollar and Kraay. See, for example, Richard Ashley, 'Growth may be good for the poor but decline is disastrous: on the non-robustness of the Dollar-Kraay result', *International Review of Economics and Finance* 2008, 17, pp 333-338. Ashley finds that 'DK's principal conclusion [...] is evidently not supported by their data. In fact, a re-analysis of their data [suggests] that the poorest quintile probably does not share proportionately in growth, but bears the brunt of any decline in real income. One might then conclude that income inequality increases either way, but more quickly for economies in decline. However, in view of the above-noted defects in the DK framework and data, it seems inappropriate to generalize based solely on results obtained using these data' (p 337).
- 12 Paul Mosley, 'Severe poverty and growth: a macro-micro analysis', *Chronic Poverty Research Centre (University of Sheffield) Working Paper* 2004, 51, p 23.
- 13 Stephan Klasen and Mark Misselhorn, 'Determinants of the growth semi-elasticity of poverty reduction', paper presented at the World Bank, 2007.
- 14 Hyun Son and Nanak Kakwani, 'Global estimates of pro-poor growth', *World Development* 2008, 36(6), pp 1048-1066. The authors use a standard definition of pro-poor: 'Following Kakwani and Pernia (2000), economic growth may be called pro-poor if the poor enjoy the benefits of growth proportionally more than the non-poor. In this scenario, inequality declines concurrently during the course of growth' (p 1049).
- 15 Melanie Grosse, Kenneth Harttgen and Stephan Klasen, 'Measuring pro-poor growth in non-income dimensions', *World Development* 2008, 36(6), pp 1021-1047.
- 16 NEF, *Growth isn't Working*, London: New Economics Foundation, 2006.
- 17 World Bank, *World Development Report 2006: Equity and Development*, Washington, DC, World Bank, 2006.
- 18 This quadrant analysis is based on the approach taken in Gustav Ranis, Frances Stewart and Alejandro Ramirez, 'Economic growth and human development', *World Development* 2000, 28(2), pp 197-219.
- 19 On trade, see Rodrik, 2007; on finance, see Cobham, A, 'Capital account liberalisation and poverty', *Global Social Policy* 2000, 2(2), pp 163-188. On the distributional impact of the combination of trade and financial liberalisation, see Lance Taylor, 'External liberalization, economic performance, and distribution in Latin America and elsewhere', UNU-WIDER Working Paper 215, 2000.
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- 22 IEA, *Worldwide Trends in Energy Use and Efficiency*, Paris: International Energy Agency, 2008.
- 23 See for example Giovanni Cornia, 'Farm size, land yields and the agricultural production function: an analysis for fifteen developing countries', *World Development* 1985, 13, pp 513-534; and Shenggen Fan and Connie Chan-Kang, 'Is small beautiful? Farm size, productivity, and poverty in Asian agriculture', *Agricultural Economics* 2005, 32 (s1), pp 135-146.
- 25 Ibid; and Peter Hazell, 'Is there a future for small farms?', *Agricultural Economics* 2005, 32 (s1), pp 93-101.
- 26 *Fighting Food Shortages*, Christian Aid, 2008,
- 27 *Farmers Left Behind*, Christian Aid, 2007.

**28** Joint NGO Briefing Note, 'Blind spot: The continued failure of the World Bank and IMF to fully assess the impact of their advice on poor people', 2007.

**29** Draft terms of reference, see [www.dfid.gov.uk/procurement/files/ojec8363tors.pdf](http://www.dfid.gov.uk/procurement/files/ojec8363tors.pdf) (accessed 24 June 2008).