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Report on the Meeting of the Latin American and Caribbean Forum on Poverty, Inequality, and Vulnerability

Buenos Aires, October 19-20, 1998

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Summary

The World Bank's Latin America and the Caribbean Region (LAC), the World Bank Institute (formerly the Economic Development Institute [EDI]), and the team working on the Bank's *World Development Report on Poverty and Development (WDR2000/1)* organized a "Forum on Poverty, Inequality and Vulnerability" in Buenos Aires, Argentine, on October 19–20, 1998. Its objective was to discuss the issues mentioned in the forum title, as well as the policies, programs, and projects required to reduce their magnitude in Latin America and the Caribbean. This event sought to contribute to the *WDR2000/1*, but also to generate a multisectoral discussion on poverty in the region.

The following summary of forum discussions also delineates the elements identified as priorities in a research agenda that should continue to refine the debate on the dimensions of poverty, inequality, and vulnerability, as well as the policies to fight them.

Note: At the time of writing, the current World Bank Institute (WBI) was the Economic Development Institute (EDI) of the World Bank. Most references to the EDI in this document have been left unchanged.

Introduction

Those participating in the introduction session were Vinod Thomas (director of the World Bank's Economic Development Institute), Robert Ayres (principal social scientist, Poverty Unit, Latin America and the Caribbean Regional Office of the World Bank) and Katherine Bain, (specialist in Civil Society for the Latin America and the Caribbean Regional Office of the World Bank).

Thomas highlighted the changes taking place in the World Bank as it directs its attention not just to financing infrastructure construction projects or structural adjustment programs, but also to generating and disseminating knowledge. In this context, governments and other entities at the local, national, and international levels should capitalize on developing countries' experiences and knowledge for the benefit of all concerned. This information should freely circulate among these levels, breaking down the existing communication barriers.

Quoting James Wolfensohn, president of the World Bank, Thomas said that one objective of these knowledge-dissemination efforts is to contribute to the collective construction of a new development framework in which governments and private sector for-profit and not-for-profit entities jointly discuss a long-term vision for development priorities. This would form the basis on which donor actions would subsequently be enunciated. To promote development, partnerships involving

actors from all the sectors—public and private, national and international—must be created. These processes are already underway in different countries in the region.

The process of preparing the report itself is proof of the changes taking place. Multiple consultation processes are being developed, and some of these have already been initiated. The *WDR2000/1* project also includes a research program in which academics from developing countries will actively participate. This report seeks to act as the catalyst to generate new research. In this regard, the World Bank, together with the IDB and the Latin American and Caribbean Economic Association (LACEA), will promote a network of Latin American researchers on poverty and inequality. Thomas concluded, emphasizing the importance of this particular event for the Bank and for the region.

Ayres presented a report on the recent evolution of discussions about regional poverty as they responded to the diagnosis and recommendations contained in the 1990 *World Development Report on Poverty (WDR1990)*. That report had suggested three core strategies to reduce poverty: (a) labor-intensive economic growth, (b) access to basic services, especially education and health, and (c) social safety nets for the vulnerable sectors.

He pointed to the need to review the validity of these priorities, given the present situation. The *WDR1990* could be criticized for emphasizing an economic approach, for giving little attention to inequality and social capital, and for not including the political dimension of change necessary to reduce poverty.

In addition, important changes have occurred during the last 10 years in the determinants and context of discussions on poverty reduction. On the one hand, trends such as globalization, liberalization of domestic markets, democratization, privatization, reform of the state, and political and fiscal decentralization have transformed the framework in which poverty issues must be faced, demanding an evaluation of the impact of these trends on the poor.

On the other, during the same period scholars' and social actors' perceptions of the following changed radically: (1) the rediscovery of inequality as a central issue for the region, (2) the role of social development in poverty reduction and the importance of understanding how social capital is generated among the poor, and (3) the political economy of poverty reduction. Despite our progress in advancing knowledge in these critical areas, the gaps are still very striking.

Bain discussed the creation of the forum as part of the WDR2000/1 initiative and of the Bank's changing relationship with non-governmental sectors. The Bank has initiated participatory processes through projects, analytical programs, and consultations such as this forum, recognizing that other actors have valuable inputs and contributions to make to the issue of poverty reduction. Similarly, she presented the mechanics of the forum and its main objective a broad, candid discussion by all present participants on what happened in the last decade with respect to poverty in the region; on the policies designed to reduce poverty, including their successes and failures; and on the challenges ahead.

Finally, Bain highlighted the forum's importance as the beginning of a process of continuous dialogue about poverty and about actions to be taken to reduce it in

the next millenium. She asked participants to reflect on the future of this forum and to identify, during the meeting's final session, the networks, issues, actors, and initiatives that should be included in future forums.

Session I: Development for All: Toward a More Equitable and Inclusive Pattern of Development

In his presentation, Jorge Castañeda, professor at the National Autonomous University of Mexico and New York University, emphasized that inequality is the central factor of the poverty problem in Latin America. Within that framework, he highlighted its historical and persistent nature. In the face of this "foundation clash" he upheld the need to persevere with policies to fight inequality and discrimination.

According to Castañeda, the paradox of inequality is that interventions to reduce it, when confronted with a deeply rooted status quo, may lead to a worsening of the inequalities. Such is the case in Chiapas, where the resources invested to fight inequality in the region were captured by an historically unequal structure of elites. The same may happen with the decentralization processes, dominated by rent-seeking elites. The difficulty in fighting inequality is reflected in the fact that the two countries that have made real and perceptible advances in reducing inequality are Puerto Rico and Cuba. In both cases, he stated, this has been the result of massive financial investments and transfers (from the United States of America and from the former Union of Soviet Socialist Republics, respectively).

In concluding, he highlighted the importance of the "social citizenship" concept as a tool to build modern democracies and proposed separating social rights from employment.

The debate that followed, facilitated by Adolfo Figueroa, professor of the Pontificia Universidad Católica of Peru, highlighted a variety of important factors related to the understanding and study of, and the fight against, inequality. The following issues were frequently mentioned:

- The majority of the participants identified the amplitude of inequality as a central factor in the discussion of the social development model, and affirmed that its reduction should be a priority. For some, reducing inequality is an imperative per se, while for others, its reduction is an effective way of diminishing poverty. However, despite the close relation between poverty and inequality, they must be seen as separate issues. Inequality would be more closely related to the social structure, though not irreversible. Poverty would be more flexible to policies and growth and, therefore, more easily reduced. Similarly, their impacts and implications also differ.
- The measuring tools of inequality and poverty must continue to be refined, particularly household surveys, because of the potential problems of underdeclaration of income (especially in the higher strata), which leads to an underestimation of inequality. The need to strengthen research on income distribution was emphasized, paying increased attention to both low- and high-income strata.

- Lack of quality education was clearly the essential factor explaining inequality, while access to quality education was viewed as an effective way to reduce inequality. Improving poor people's access to quality education that provides the knowledge and the necessary skills to find productive employment is essential. However, some participants voiced concern about the risk of turning to simplistic answers, such as thinking that education alone is enough to reduce inequality.
- Inequality may be reduced, but it requires time, perseverance, and resoluteness in social policies. In this sense, social policy should receive as much importance as economic policy. This is particularly valid in the region since—in contrast to other regions—Latin America has sufficient means to reduce poverty and inequality through a system of income transfers and asset redistributions. In this respect, issues such as agrarian reform or the minimum guaranteed income system were discussed from opposing perspectives.
- Policy design acquires increasing importance. It must be more participatory, encompassing, and respectful of the visions and priorities of the groups targeted for assistance, as well as of their cultural values—especially in the case of indigenous populations.
- However, inequality reduction requires more than a simple increase in service provision to the poorest sectors. It demands greater social cohesion, resulting from a change in social relations. Social capital, trust, and solidarity must be strengthened, as they are the foundation of social cohesion.

Finally, the following subjects were identified for research:

- Relations between inequality, poverty, and culture and institutions. Societies are the product of complex social processes that determine the relations among the groups and the ethical values of the whole. Thus, the understanding of these processes must be strengthened. In this field, the comparative economic history is fundamental, particularly with developed countries.

  Given education's impact on inequality, it should occupy a significant place. In particular, its impact on income should be studied in more depth. Is this a simple and lineal relation or does it follow thresholds? Similarly, research efforts should focus on identifying concrete ways to ensure equal access to high-quality education at all levels.
- Theoretical and empirical content of social citizenship.
- Study of the liberal reforms and their impact on poverty.
- Impact of external shocks and of globalization on the social welfare and redistributive policies.

Session II: Delivery of Basic Services: Institutional Changes and New Challenges

Ariel Fiszbein, EDI's Economic Growth and Poverty Reduction coordinator, focused his presentation on the different policy options available to improve poor people's

access to basic services. He highlighted experience gained in the region while applying four options: (a) decentralization, (b) privatization, (c) participation and (d) public-private partnerships. Fiszbein proposed an analytic framework of three factors: (a) Who controls decision-making in each of the stages, (b) what tools and authorities they have available, and (c) what incentive system they face to promote access to quality services for the socially excluded sectors.

In most cases, implementing decentralization has avoided worsening the interregional differences thanks to transparent mechanisms in the transfer of resources that include measures of regional fiscal capacity. To avoid the risk that benefits are captured by local elites, decentralization's political design must be considered, emphasizing the importance of democratic and independent elections, as well as mechanisms for local citizen participation.

For privatization to have positive impacts on the poor's access to quality services requires a regulatory policy that includes, as one of its priorities, the obligation to expand coverage or provide universal services, as well as transparent information mechanisms. Various schemes, such as the "education vouchers" system in Chile, have produced interesting results, once they have included compensation and information mechanisms to make effective the parents' notional capacity to choose.

Establishing more participatory policies is one of the clear trends in which the region has made progress. These range from simple consultations on priorities up to management schemes giving users full responsibility. However, in order to be successful, this "demand-driven" approach must be consistent throughout the project's stages, so that what has been achieved in one phase is not lost in the next. Similarly, participation demands high levels of information. Ultimately, project success requires contributions from the beneficiaries.

Partnerships are a mechanism for transcending the traditional state-non-governmental division regarding management schemes, in which the sum is superior to the parts in terms of productivity and the generation of positive externalities such as social capital. In order to exist, partnerships require decentralization, privatization and participation schemes, as well as efforts and investments to generate trust.

In concluding, Fiszbein highlighted the importance in all cases of the adopted institutional design, since it creates the conditions to effectively improve the poor's access to quality services.

The plenary session, facilitated by Manuel Chiriboga, executive secretary of the Latin American Association of Development Organizations (ALOP), acknowledged the difficulties in finding replicable institutional models, since they depend to a great extent on the general political and economic conditions of each society, as well as its degree of institutionalization. In all cases, projects must be thought out in such a way that they maximize their impact on the social capital, and must be designed with poverty reduction as an integral and critical objective. The need to differentiate between the types of services—particularly between the social and the productive services—and to create programs for each of them was emphasized.

Participation was identified as the core element of any initiative geared toward improving poor people's access to basic, quality services. Such participation requires training and strengthening grassroots organizations. However, participation should not be made into a fad, or presented as an objective in itself that replaces objectives such as the redistribution of wealth and the generation of assets and services for the poor.

Due to the profusion and diversity of the experiences gained in Latin America, the importance of having evaluations that allow learning from specific experiences and making available such information to researchers, nongovernmental organizations (NGOs), and public officials was emphasized.

The need for research in the following areas was identified:

- Costs and sources of funds to finance these institutional reforms.
- Decentralization and privatization. It is necessary to have a better understanding of the role of the intermediate organizations, in terms of both their design and their implementation.
- Impact of institutional reforms on the relations between political and social actors, beyond their impact on the services.

Session III: Employment and Poverty in the Global Economy: A Latin American Perspective

Barbara Stallings, director of the Economic Development Division of CEPAL, focused on two points: (1) the importance of understanding how labor markets function and (2) the labor market crisis in the 1990s. She recalled how structural adjustments that give priority to the important macroeconomic balances and to the reduction of inflation have tended to rely, to a great extent, on reduction of public expenditure and appreciation of the real exchange rate. Similarly, she highlighted the importance and breadth of the reforms initiated (deregulation, privatization, and regional and world commercial and financial integration), particularly those related to labor market flexibility. Concerning the latter, Stallings pointed to the ongoing debate on its magnitude: for some, deregulation has been too superficial, while for others, it has gone too far.

She highlighted certain common regional trends, with respect to labor market evolution in this decade. Among them is the growth in open urban unemployment, probably linked both to decreased public-sector and privatized enterprises' employment (layoffs) and to inadequate job creation due, in turn, to a limited and capital-intensive economic growth. As a result, the earning gaps between skilled and non-skilled workers increased. On the other hand, she emphasized the fact that 80 percent of newly created jobs are created in the informal sector (micro-enterprises and/or precarious jobs without benefits). However, real salaries have improved as a result of increased productivity. Finally, an element worth noting was that urban earnings grew more than rural earnings, reversing the trend of the 1980s.

Stallings indicated that, in the face of this situation, a certain consensus exists regarding policies: (1) to try to maintain and/or increase the rate of economic growth, (2) to improve access to and quality of education at the intermediate level, as well as training for current and unemployed workers, (3) to give greater attention to small and medium-sized enterprises (SMEs), and (4) to find ways of integrating the informal sector in order to improve the working conditions of its workers.

The discussion, facilitated by Guillermo Perry, the Bank's chief economist for Latin America and the Caribbean, was in depth and dynamic. Different visions and options were discussed. The majority of the participants identified employment as one of the principal poverty-fighting mechanisms. Education and training were also mentioned as the most efficient paths to stable employment. Other issues gave rise to controversies, and disagreement persisted over the convenience, utility, and modalities of unemployment insurance and other forms of social protection (including minimum guaranteed income) and the role of the unions in the labor market.

Participants believe the following list of issues require greater understanding and research:

- the informal sector role, content, and functioning mechanisms after the reforms
- ways of supporting and strengthening SMEs, particularly by large enterprises
- measurement: differences in concepts on employment, unemployment, and formal-informal sectors
- operation of the labor market in rural areas
  mobility between and within sectors
  social protection mechanisms, including the concept of minimum income
- means to improve competitiveness without affecting workers negatively

Presentation of Shahid Javed Burki, Vice President of the World Bank for Latin America and the Caribbean

Burki's presentation touched on the subjects and priorities discussed by the forum during previous sessions. He stated that inequality is at the core of the debate and therefore must be a priority objective of all antipoverty efforts in the region. For such efforts to be successful, the poor must also participate actively in their design, application and evaluation. Labor markets that provide employment access to the poorer sectors are a crucial instrument to improve the quality of life of the most disadvantaged.

Globalization has produced tensions with which we still do not know how to deal. Capital now flows in and out of emerging markets almost instantaneously. When capital is invested in the productive sector, it creates employment and wealth. However, its withdrawal, often without being directly related to a country's economic fundamentals, generates serious tensions that disproportionally affect the poor.

Evidence exists for two types of poor. On the one hand are those who, due to their circumstances, require sustained social interventions to improve their life conditions. On the other are those who can overcome poverty more rapidly, thanks to a stable and sufficient economic growth of, for example, 2 to 3 times the population growth for a period of 5 to 10 years. But we also recognize that this second group remains vulnerable and may be affected again by poverty if the general economic situation changes significantly. The current crisis in the Asian markets is proof of this. Therefore, even though the region will be able to avoid the current financial crisis, an inevitable decrease in the growth rate will affect the poor and those that have barely overcome poverty. Safety nets are thus essential in times such as the present.

During preparation of the *WDR2000/1*, we must analyze carefully the effects of a globalization that introduces instability, and thus affects the poor. That is why we must continue to emphasize the study of globalization, volatility, vulnerability, and safety nets, in order to be prepared for the challenges ahead. We must create a set of various interventions (subsidies, temporary employment, and training) to protect the poor. Structural adjustments must be made to protect these interventions. Other crises will occur; we must be prepared to confront their adverse effects to avoid affecting the poor to a point in which progress achieved in past years could be totally reversed.

Session IV: Presentation of the *World Bank Report on Poverty and Development 2000/1*

Nora Lustig, chief of the Advisory Unit on Poverty and Inequality of the Inter-American Development Bank and assistant director of the *WDR2000/1*, and Ariel Fiszbein led this session. Ramón Daubón, from the Kettering Foundation in Washington, was the moderator.

Lustig emphasized the report's innovative elements with respect to methodology (an intensive consultation process), preparation (a research agenda to be developed in a decentralized manner), and the drafting team (multidisciplinary, with extensive female participation, and including non-World Bank staff).

She presented the core elements of the *WDR2000/1* proposal, based on the following propositions:

- Poverty is multidimensional. Measurement instruments must be improved.
- Despite the successes achieved in poverty reduction in the past, its levels continue to be unacceptable.
- The world is going through great processes of technological and economic change. These changes represent a risk and an opportunity.

With respect to what directly affects the region, 150 million people live with less than two dollars per day. In addition, a large, high-risk group of people lives close enough to the poverty line to be vulnerable to economic shocks. The region is also

characterized by major differences among regional, rural versus urban, and social groups. However, despite this diversity, common characteristics are found among the poor: they are generally from large households whose head has little education and is unemployed. A clear relation exists between poverty and belonging to indigenous or black groups.

Given this situation, global growth trends are not sufficient to eliminate poverty within a reasonable time period, despite the fact that 1 percent of per capita growth generates between 1.5 percent and 4 percent in poverty reduction. Therefore, other actions are required to fight poverty, including the following:

- Modification of income determinants: employment and labor regulation; microenterprise support; asset redistribution (agrarian and urban reforms, taxes on wealth); investment in human capital; rural development; policies in developed countries (migration, protectionism).
- Income-transfer policies: minimum-income proposal. A redistribution of 2 percent of the gross domestic product (GDP) would be enough to eliminate poverty.
- Protection against adverse shocks, economic and/or environmental.

Ariel Fiszbein then presented the proposed consultation scheme. Clearly, two types of audiences should be reached by the process;

- Civil society in its broadest sense, researchers, and political representatives. This would occur at the regional and national levels as two types of events—participatory forums (such as this one) and dialogue spaces taking advantage of modern communication technology (e-mail consultation with civil society organizations throughout the world, via the Internet).
- The poor themselves. The process proposes accessing 15 to 20 poor communities in 10 to 12 countries to find out their perceptions on poverty, its solutions, and how policies affect them, as well as their relation with other actors—NGOs, government, and international agencies.

One additional instrument will be used to reach both types of audiences: the participatory studies on poverty at the national level undertaken by the World Bank as part of its strategy to support the countries (CAS).

Ramón Daubón led the plenary discussion. The comments may be organized around two types of concerns:

Regarding the methodology, consensus existed on the usefulness and importance of direct consultations with the poor. However, the need to expand these consultations to other segments of society, particularly to privileged groups, was emphasized, since their attitude toward the poor plays a crucial role in the political economy of the reforms, as well as in manifestations of poverty such as exclusion and discrimination. Using surveys and consumer panels promoted by the private sector was also suggested, because they constitute a rich source of information on the type, quality of life and structure of expenditure of the poor. Finally,

the greatest emphasis was placed on the importance of maintaining adequate communication on the proposed research program and on the report itself. For this, the *WDR2000/1* team must turn to existing networks and organizations to disseminate and circulate all the materials and to continue listening to the inputs of these organizations to the debate. Once the *WDR2000/1* is completed, its dissemination is critically important. In order to fulfill its purpose, the report must reach as many audiences as possible and be discussed in the most diverse spaces.

With respect to the thematic aspects, it was suggested that greater emphasis be placed on the gender approach, as well as on racial aspects that may point to discrimination and exclusion patterns. Social capital, especially that of the poor sectors, must be the subject of special attention both as a diagnostic mechanism and as a potential policy objective. The diversity and heterogeneity of the populations in poverty status should lead to the establishment of typologies and thematic, geographic and economic distinctions that reflect the variety found among countries and regions and among groups within a country itself.

The political economy of reforms, the consensus building around social policies, and the ranking of the latter in the national agenda were also considered crucial. It is necessary to understand and study how these processes may be advanced to provide the political support required by the fight against poverty.

The need to evaluate the costs and efficiency of interventions must be addressed by the research agenda. Various participants insisted repeatedly on the need to estimate the costs of new policy proposals and to evaluate the impact of existing ones. With respect to the latter, it was suggested that the *WDR2000/1* should include an annex describing the policies, recommendations and evaluations of the "best practices" identified for poverty reduction, so that such information be shared to benefit a large number of people.

Conclusion: The Future of the Forum

The final session was devoted to evaluating the forum and exchanging ideas and proposals regarding its future. Bain focused the debate on three questions: (1) the forum's usefulness as a regional and multisectoral space for discussion and proposals, and thus its future; (2) the actors and sectors that should be invited to participate but have yet to be included; and (3) the specific activities that should be developed for the forum to fulfill its objectives.

The participants valued highly this forum, particularly because it allowed voices from the different sectors to be mutually heard and listened to. They concurred on the need to continue to this process, thus contributing to consensus and the acceptance of differences. However, many emphasized the need to prepare future activities far in advance, in order to allow greater depth in the discussion of the issues and to obtain, thanks to annotated agendas, specific and feasible proposals. Many of those present highlighted the forum's importance in terms of the change process currently underway in the World Bank, as it seeks ways to open up to other audi-

ences. Other participants indicated the need for the poverty reduction issue to receive continued, not cyclical, attention.

Various specific activities were proposed:

- Articulate the regional forum with similar endeavors at the national level in different countries, such as Peru, Mexico, El Salvador, Colombia and Argentina.
- Organize working groups electronically around common issues to share ideas and make proposals to the whole forum and to the *WDR2000/1* team.
- Create a bimonthly newsletter for forum members and an electronic mechanism to circulate information that would allow the continuation of the dialogues.

With respect to the national dimension, the World Bank and the Inter-American Development Bank presented their initiatives in Mexico and Peru.

Knowledge as a Development Tool: The Knowledge Bank

Vinod Thomas

Director, World Bank Institutute

Opening Remarks

Greetings and welcome to the first Latin American and Caribbean Forum on Poverty, Inequality, and Vulnerability. This event promises to be the beginning of several new partnerships that will foster work on the creation and dissemination of knowledge on the global stage of development.

As many of you know, the World Bank has been undergoing an enormous transformation over the last few years in its efforts to become a Knowledge Bank. No longer just concerned with financial assistance and conditionality, the Bank realizes it must develop a deeper understanding of the development needs of countries around the world. The Bank focussed first on building roads, and then on making Structural Adjustment Loans in the 1980s. We now understand that this is insufficient for achieving real and sustainable development. We understand that the solutions to complex problems lie with people, not just with governments or with multilateral agencies.

The Bank wants to move beyond the vision of constructing only roads and dams to building international connections through knowledge. Its vision of becoming a learning institution contributes to this goal, one of which is to create inroads into the information highway that will give access to people who may have been left stranded at the wayside.

But we must think of knowledge dispersal as more of a two-way street than we have in the past. Not only do we need to develop links among think tanks, but we need to start conceptualizing knowledge as an international public good. We must also be willing to realize that knowledge created in developing nations is often key to constructing a solid base. While we can import and impart knowledge as a public good, we recognize that communities must play a large role in creating that knowledge in the first place. We need to foster incentives to translate knowledge into sound policy and to disseminate local knowledge on an international scale. We need to learn from others, without repeating the mistakes of others. For this, knowledge needs to be transferred across international borders; the information highways must cross through what were once seen as impenetrable barriers.

To fill these knowledge gaps, the Bank is fostering dialogue spaces such as this forum to broaden the development paradigm. For it is not knowledge in the hands of the elites, but knowledge from different sources and shared by all, that will ultimately have a positive impact around the world.

Two weeks ago, I attended the World Bank–Internationl Monetary Fund Annual Meeting where Mr. Wolfensohn, president of the World Bank, noted that "we need a new development framework." He emphasized that we must learn from the past, and that the way in which a development framework is developed and applied is as important as the contents of that framework.

As he stated:

> What if it were possible for governments to join together with civil society, with the private sector, to decide on long-term national priorities? What if it were possible for donors to then come in and coordinate their support, with countries in the driver's seat, with local ownership and local participation? What if it were possible for these strategies to look 5, 10, 20 years ahead, so that development could really take root and grow and could be monitored on an ongoing basis? Too ambitious, some will say. Too utopian. But what if I told you it is already happening?
>
> In El Salvador today, there is a national peace commission, born of civil war, which together with civil society, the private sector, and the government, is drawing up a list of national priorities—so that those priorities can extend beyond the life of one government and become part of a national consensus for the future. And the same thing is happening in Guatemala and is being considered elsewhere in Latin America.

He emphasized the need for a new approach to development partnership, led by governments and parliaments, influenced by the civil society of those countries, and joined by the domestic and international private sectors, and by bilateral and multilateral donors.

Despite Mr. Wolfensohn's encouraging statements, we still have a long way to go to arrive at a place where partners are at the center of strategic discussions. At the Annual Meetings, I had the opportunity to read dozens of country briefs and it is amazing how little these briefs have changed compared with those of 10 years ago. The majority of them still focused on tackling short-term macroeconomic issues, and very few touched on issues of learning or incorporated knowledge as part of their overall strategic objective.

The country meetings in which I participated focused on these briefs. I know the interest in learning and partnership work is there on the side of our clients and donor-partners, and that the direction is there, but we aren't there yet.

The good news is that gender and development issues are becoming mainstream in these meetings. Also, the expansion of Economic Development Institute (EDI), the creation of Learning and Innovation Loans (LILs), and the fact that the Bank now has participatory Country Assistance Strategies (CASs) all signify a change. But the bad news is that we still have several country briefs and discussions composed as if the Bank, rather than the country, were in the driver's seat, and as if the government of a country were the only player in a country's development work.

I was the director of *WDR1991*, titled *The Challenge of Development*. I was very much interested in the views of diverse groups of people and did seek their inputs.

But the report was still written by a small team, and I can't say the process was fully participatory. The new *WDR2000/1* shows how much we've changed.

The most visible product of the *WDR2000/1* will be the report itself, providing a synthesis of the relationship among development strategy, structural and social development, and poverty. But there will be other products, not least of which will be the intensive process of consultation born out of events like this one, especially the interaction with poor communities directly and through participatory research and projects. The research program will produce a combination of conferences and also research papers, with strong participation of researchers from developing countries.

Broadening the Bank's learning agenda cannot be done without knowledge. All *World Development Reports* should become more than mere documents. They should be used as platforms upon which to broaden the knowledge agenda.

Today we will be discussing a report on poverty that delves into social development issues and is very participatory. Let us use the *WDR* as a catalyst to foster informed research groups on a wide range of development issues. We need to work beyond the *WDR*, by furthering research and policy work in the areas of governance and anticorruption, as well as areas of gender and inequality.

The Bank wants to listen, to participate in, and to facilitate these discussions.

After this meeting, we are launching a poverty and inequality Research Network of Latin America and Caribbean (LAC) Region researchers (many of whom are in today's audience) to encourage informed dialogue on issues of poverty and social development. This will be a joint venture with the Inter-American Development Bank (IDB) and the Latin American and Caribbean Economic Association (LACEA).

The consultation for *WDR2000/1* will be done through many instruments and media, including conferences and workshops primarily focused on the research program. The workshops will serve as venues for authors to present papers and get feedback from other researchers and from practitioners. Knowledge that comes out of forums like this one is particularly important. We need to work together to mobilize the intellectual energy in regions like LAC. We need to mobilize resources in LAC to create broader consensus on social development. Your active participation in these workshops is crucial to help build a knowledge base upon which development work can flourish.

Let us work together in the spirit of partnerships to begin the next millennium on a solid foundation.

The New Context of Poverty Reduction in Latin America and the Caribbean

Robert Ayres

Principal Social Scientist, World Bank

In 1990, I had the privilege and responsibility of being a member of the team that produced the *World Development Report on Poverty* (*WDR1990*).

First, let me begin with a sobering fact. The report estimated that approximately 19 percent of the population in Latin America and the Caribbean were living in poverty. The report also attempted to project the incidence of poverty in the region for the year 2000. Making certain favorable assumptions, the report projected that poverty in the region would fall to about 11 percent by the year 2000. In fact, the World Bank's latest estimate is that approximately 38 percent of Latin America and the Caribbean's population continues to live in poverty.

The fact that the incidence of poverty in the region is more than three times what *WDR1990* projected it would be illustrates the enormous challenge that confronts us as we seek to analyze the problems of poverty, inequality, and vulnerability, and to identify priorities for future actions against poverty.

As many of you are undoubtedly aware, the 1990 *World Development Report* elaborated a framework for poverty reduction that has guided much of the World Bank's work during the current decade. It had three important emphases: first, economic growth that would be "broad-based" and "inclusive" and that would make productive use of the poor's most abundant asset—that is, their labor; second, human capital development, with an emphasis on the delivery of quality education and basic health care to the poor; and third, the provision of social safety nets for those left out of the process of economic and social development. One of the important questions that will confront the authors of the *World Development Report* in the year 2000, and that will undoubtedly occupy us during our discussions over the next two days, is whether this poverty-reduction framework still remains viable in the light of changed circumstances.

Despite the 1990 *World Development Report's* achievements, which were considerable from both an analytical and operational point of view, it was obviously not without its shortcomings. What, then, are some elements of a critique of the report—or, to be more precise, of my critique?

1. The report's analysis was excessively rooted in an exclusively economic approach to poverty and its reduction.
2. The report adopted a quantitative definition of poverty, measured solely by the presumed adequacy or inadequacy of personal income.

3. It gave relatively little attention to inequality or to vulnerability.
4. It paid little attention to issues of social development and social capital.
5. It had little (or virtually nothing) to say about the political economy of poverty reduction, or about the political feasibility of the report's recommended strategy.
6. The 1990 *World Development Report* said little about prospective structural changes in the global economy and their likely impact on the poor in the developing world.

Permit me to turn briefly now to what has happened—in my view—since 1990, first, in the so-called "real world," and, second, in academic perceptions of poverty and development.

Regarding changes in the world around us, I would like to point to a half-dozen "megatrends" that I believe have radically altered the context in which issues related to poverty and its reduction need to be addressed. My list is as follows:

1. globalization—at least with regard to trade and financial flows
2. liberalization of domestic markets
3. privatization of previously publicly owned enterprises
4. democratization, with its numerous dimensions—including the holding of regular and relatively free elections, the increasing importance of the legislative power, and the proliferation of the diverse forces in civil society
5. reform of the state—not only administrative reform of public bureaucracies to make the state leaner and more efficient, but also a redefinition of its role in the economy and social sectors
6. decentralization, in both its fiscal and political dimensions

I would like to suggest to you that the implications and consequences of these various megatrends for the poor have been insufficiently explored. A useful way to assess the new context would be to attempt to gauge the net effects on the poor in Latin America and the Caribbean of various developments that have accelerated so markedly since 1990. For example:

- Globalization could help reduce poverty through its presumed effects on growth, or the possibility of increasing the export of products that are labor intensive. But it could also exacerbate disparities in wage levels between skilled and unskilled labor, and it could significantly increase the vulnerability of large segments of national societies, thus markedly increasing the demands on instruments of social protection.
- Liberalization of domestic markets could make the whole economy run more efficiently and productively, even for the poor, but it also might prohibitively increase the prices of items that are disproportionately consumed by the poor.
- Much the same can be said for the effects of privatization on the poor. Will they be able to afford the newly privatized electricity, telephone, water, sanitation, and other basic services? If not, how can we ensure that these services become accessible to those with low incomes?

- Is democratization really increasing the participation and representation of the poor in national political systems, or is it simply providing a façade for "politics as usual"? Who speaks for the poor—especially at the national level—in the newly democratic political systems of Latin America and the Caribbean? Are grassroots organizations of the poor enough to ensure that their interests are systematically represented in executive and legislative decisionmaking in national capitals—or even in municipal councils and provincial or regional assemblies?
- In theory, a reformed state can deliver both traditional and nontraditional services better to poor and nonpoor alike. In practice, many questions exist concerning the provision of such services to the poor by the so-called "reformed" state. For example, will educational vouchers or an increasingly privatized educational system help the poor? Where do they fit into the reform of health care financing?
- Decentralization doubtless can bring greater "voice" and services to the poor. However, it can also bring "neo-*caciquismo*" and the capture of benefits by well-entrenched local elites, thereby increasing disparities between rich and poor areas.

At the most general level, these observations raise the issue of whether the development model prevailing in the region today is really capable of significant and sustained reduction of poverty.

For some of us, the current challenge may be characterized as how to give the neoliberal model a more "human" face, not how to replace it with something else. For others, however, the quest is for a true social democracy in the region. In any event, the fundamental question is whether the poor in Latin America and the Caribbean would fare better under a significantly different development model from the one prevailing in the region today and, if so, what such a significantly different model might be.

To conclude, I will limit myself to just three broad observations concerning new perceptions of poverty issues. They are as follows:

- First, there is what I would call the "rediscovery of inequality"— a heightened awareness of the linkages between inequality, growth, and poverty reduction. Agreement is increasingly widespread that development in Latin America and the Caribbean has been narrowly based and exclusive. In fact, it has been virtually the antithesis of the broad-based development strategy recommended by the 1990 *World Development Report*. The question is, what to do about this situation and, in particular, what are the policy tools for doing anything about it?
- The second changed perception stems from the discovery that "social development" has its own independent importance in contributing to poverty reduction, as well as the fact that it is related, perhaps quite strongly, to economic development. We require much greater attention to the determinants and consequences of "social capital" among the region's poor.

- Third, and finally, is the discovery, also rather recent, that "institutions matter." The reduction of poverty in Latin America and the Caribbean requires enhanced institutions—whether in the education, health, and financial sectors, or in the judicial system. More generally, we must give substantially greater attention to the political economy aspects of poverty reduction in the region. In many areas, a broad consensus exists on the necessary actions to reduce poverty. Political obstacles are often preventing the implementation of what needs to be done, and we need to think more creatively about how they can be overcome.

What does all this mean for this meeting of the Forum on Poverty, Inequality, and Vulnerability? For me, it means that the subjects we are about to address are significantly more complex than they were perhaps made to appear in the 1990 *World Development Report*. It means that poverty and related topics are even more central to the development debate in the region today than they were a decade ago. It means that we know a lot more, and of a more multifaceted nature, than we knew then—but that the gaps in our knowledge are still notable.

In summation, it means that this forum is beginning a truly challenging and exciting venture that demands—and I am sure will receive—your sustained attention, analysis, commitment, and participation.

After Neoliberalism: A New Path

Jorge Castañeda

Professor, Universidad Nacional Autónima de México

and New York University

To an overwhelming extent, Latin American societies, unequal for ages and divided in countless ways, are now more fragmented than ever. In a few countries, poverty decreases, but injustice remains. In most others, the number of citizens condemned to miserable, unacceptable, and outrageous living conditions increases, while the gaps dividing rich and poor, abysmal in themselves, widen, along with those that separate the cities from the countryside, blacks and Hispanics from whites and natives, men from women, and children from the rest of the society. Employment remains stagnant, income continues to be puny, and expenditures on education, health, housing, children, and the "future" cannot make up for the countless lost decades. Our emerging democracies are constantly threatened by the possibility of coups d'etat, by poor economic outcomes, and by the understandable apathy of a population overwhelmed by the burdens of daily survival and the persistent feeling of not belonging.

The still unfinished nature of our national identities is being devastated by a merciless globalization—blown out of proportion by the media—that constantly overpowers the frail sovereign nations constituted only in the last 150 years.

We must undertake to remedy, to improve—in a word, to reform—this situation in a world that is both more and less resistant to change. The narrowing ideological parameters, added to the imperative to abide by the requirements of capital, trade, and people flows, have reduced the maneuverability of each nation, of each government, of each party or movement. To be blind to these facts is not just futile but destructive for both the beneficiaries and the victims of the millennium's-end apportioning of vices and virtues. But the same transformations wrought during the century's final decades have partially opened new possibilities for change, for the battle, and for the advancement of utopias previously unimaginable. The technology available only to some (although in theory utilized by all), the end of the cold war and the phenomena of regional integration, the possibility of stripping social reform efforts of nineteenth-century ideological connotations, the growing awareness that if the world is global it is also unique—all of these are planks in a new, feasible staging, one that will allow the development of societies that are fairer and more united, freer and more aware, at peace with themselves and at home within a financial, ecological, commercial, and judicial universe that is less aggressive and polarizing.

We must leave behind the neoliberal policies that have drawn the market away from its role as an instrument and instead raised it to the status of a religion. We

distinguish between the market economy (and its need to be democratized) and neoliberalism. The latter, an extreme stream of the market economy, has failed to generate growth and development, particularly when faced with the challenge of achieving a more equitable distribution of income and wealth. Today, the notion that capital is the determining and almost exclusive factor of economic processes has been manifestly discredited. The policies of privatizing at any price, of systematically reducing taxes, and of deregulating labor markets so characteristic of the neoliberal approach have. in the majority of cases, served to aggravate social conflicts and tensions and to increase the poverty level of huge sectors of the population. We do not just reject the idea of humanizing neoliberalism, however; we also suggest an alternative approach: to democratize the market economy.

Obviously, the pursuit of this aim involves major dilemmas: If we propose reforms that are too far removed from the status quo, they will be labeled attractive but utopian. If we propose transformations limited to the current situation, they will be considered viable yet insignificant. This is, indeed, a false dilemma, produced by the lack of understanding that changes occur in a timely and cumulative way. Any change management worth considering can be unmade by arguments either close to or distant from reality. What matters is how change is managed, and how it effects the people's understanding of their interests, their identities, and their problems.

Economic and financial globalization accelerated the universal expansion of the so-called "unique thought," the neoliberal doctrine that in Latin America acquired features and embellishments absent in the industrialized countries' version. Several countries in the region adopted the most extreme version of this economic organization, thus considerably restricting the role of public policies and of state regulation. In neither the Japanese experience (and that of other Asian countries that have developed a market economy) nor in the European model has such a small margin been left for the regulatory or proactive mechanisms of the state. Even in the United States, areas are reserved for state action that are unknown in some Latin American models of the market economy. Those models result from the logic of the "financial capital" that does not recognize controls and that flows to areas with the most lax regulations, and also from the actions of these same national states that, because of an ideological exaggeration, have decreased their regulatory mechanisms. Hence the development of the following sequence of events:

- Globalization creates the conditions for the unrestricted circulation of capital and its almost immediate reallocation for the maximization of profits.
- Financial logic, sustained by a US$1.3 billion volume of daily transactions, tends to prevail over productive logic.
- The capacity of speculative capital to flow towards areas with the fewest restrictions leads the whole system, and each country, to adopt a downward approach to deregulation or reduction of controls.
- This tendency towards deregulation increases even more when the consequences of national policies driven by extreme neoliberal models are added. Under these

circumstances, the financial and speculative logic tends to dominate national economies.

- The phenomenon is further expanded when it[?who concludes?]is concluded that the advent of a "single world" will sooner or later render national states anachronistic.

Public power is therefore subjected to the financial and speculative logic, the fate of societies escapes from the decisions of their inhabitants, and, in short, we are led into a world devoid of premeditated purpose or, in any case, of majority decisions, in which the power to shape the future is lost.

But this is neither an irreversible fate nor an unalterable scenario. It is only a probable future, one that can be altered. It will be impossible to do so, however, if the internal sovereignty of the state—in other words, its capacity to implement policies elected by the majority—is not strengthened in some cases, or reconstructed in others. A state is not sovereign when a private power has more authority in the definition of a society's objectives or when an everpresent but devoid of non-territorial financial logic prevails over nations. This state's sovereign capacity has little to do with the classic argument pertaining to its dimensions or its levels of intervention; it refers rather to the state's existence as a public power, as the executor of democratic will. This argument is the starting point of our proposal, and the exact extent of its aims.

Latin America's link to the global economy and to the international community, particularly to so-called financial globalization and large capital movements that traverse and shake the world, can be redefined on three levels, each one supporting the other. At the national level, it is both feasible and desirable to implement various regulatory mechanisms on speculative capital from abroad, along with giving priority to the domestic savings that reduce dependence on these flows. Through various entry and departure taxes—similar to those that already exist or that have been in force in several countries such as Chile, Brazil, and Malaysia—and encouragement of direct foreign investment (as opposed to portfolio investment), it is possible to increase the margin of (relative) autonomy in the nation-states.

Second, regional economic integration processes such as Mercosur, Colombia-Venezuela, and the efforts to revive the Central American Common Market offer additional possibilities for regulating and legislating relations with worldwide capital circulation networks. Obviously, the capacity and effectiveness of regulatory measures will be greater at the regional rather than the individual country level, because the markets in question are bigger and more attractive, and the costs are higher for those deciding not to enter those markets because they reject the limitations set by integrated countries.

Finally, we must promote proposals for regulation or taxation (for example, the Tobin tax proposed by the late President François Mitterand) of speculative capital movements at the international level, in multilateral financial organizations, and in other forums. The use of market mechanisms to redefine the relations between countries and regions and the new globalization phenomenon are the keys to constructing new forms of sovereignty.

Regional economic integration must not only be supported, but also must go much further, covering more areas and being more ambitious than at present. The error of integration as presently envisioned and implemented lies in the fact that it is restricted exclusively to the commercial sphere; we must simultaneously reduce tariffs among our countries, and start building the regulatory institutions, social unions, and common policies that in other parts of the world were created over times. The only way to avoid the sense of alienation that the citizens of other countries experience with bureaucratic entities distant from and free of any accountability is to gradually build social solidarity among the participating countries. This is particularly relevant to the case of Mercosur, which should further explore a privileged association with Chile. We must seek a greater degree of integration among ourselves and among equals. To this end, we must promote the encounter of political, social, civic, and professional actors from our countries. Economic integration is too important to remain solely in the hands of commerce or finance ministry bureaucrats.

A democratizing development is needed, based on (1) the reorganization and the refinancing of a state that is proactive and equipped with abundant resources, capable of investing in individuals, and of becoming a powerful and useful promoter of private initiative, especially of small and medium-sized enterprises (SMEs); (2) the struggle against the rigid and tragic dualism between the economic and social vanguards and rearguards that divide all our countries; and (3) the strengthening of democracy by means of institutional reforms that favor the implementation of required structural changes and that generate, in daily civic and social life, an authentic, liberating shock. Until now, persistent efforts to reduce inequality solely through compensatory social policies have failed. We must not fear a freer democracy. We must insist on the possibility of and the need to create political and economic institutions based on new types of links between representative democracy and citizen participation that make human and economic development a priority. Poverty should be measured not only by lack of income, but also by lack of basic opportunities for individual development. To the extent that access to the basic goods of development is missing, we will be poorer. Consequently, particular attention must be paid to political and economic institutions in order to include those who are excluded from development's fruits.

We do not wish to revert to populist nationalism, nor to the semiautarchic strategy of import substitution that ends up protecting inefficient domestic oligopolies. Nor do we want to revert to the inflationary public financing of other times. We are advocating a strong and democratized state, not the state that we presently have or had in the past. We want to democratize the market economy and return to a democracy that is capable of fighting inequality. The market must be the main distributor of resources, but it falls on the state to create the conditions that enable the needs of the poorest sectors to be converted into sound claims that the state can process. We reject the idea that the market economy adopts the natural and necessary form of economic institutions that are predominant today in industrialized democracies. We insist on the possibility and the need for institutional innovations that contribute to real economic decentralization in hierarchical and excluding societies such as our own. We want to create the bases for a new generation of na-

tional development projects that transcend the erroneous choice between submission to the new rules of the international economy and to faith in the development authoritarianism of a guide-state. We are not proposing a third option, since a second one does not exist. We are proposing a democratizing alternative to the path that is wrongly flaunted as the only one.

In recent years, the region's unionism has changed from earlier conceptions to the so-called "sociopolitical unionism." The latter has adopted less conflicting positions on regional integration, advocating the inclusion of social clauses and charters that limit competition among workers, thus guaranteeing a core of basic rights. Of particular importance are collective bargaining, trade unionism, nondiscrimination, and the abolition of child labor. Value is also given to worker participation, always through collective bargaining, in order to guarantee the competitiveness and productivity of enterprises. This unionism tends to be defined by what we might call the democratization of globalization, extending "social citizenship" to workers and those excluded.

Basically, the notion of social citizenship can become the core of a new social policy in Latin America that originates from a historical fact recognized in other parts of the world: it is impossible to build united, democratic, and stable nations without extending the same rights of social citizenship to a majority, at least, of the inhabitants of a given territory. In the long term, the division of political-legal citizenship and of social citizenship, characteristic of current Latin American democracies, is unsustainable. Moreover, transformations in the market economy and a revolution in mass media have resulted in the expansion, in industrialized countries, of the rights traditionally identified with social citizenship. Such expansion does not take place in isolated compartments: it is immediately communicated to developing countries.

One of the best examples concerns access to credit in the form of mortgages, or as medium or major consumer loans (for automobiles, for example). It is unlikely that access to credit was considered a right of Marshallian social citizenship in the nineteenth century, or even during the first half of the twentieth. However, today it is so considered in industrialized countries, thanks to various public and private mechanisms; this is not the case in our nations. Thus the gradual building of social citizenship in Latin America is the great challenge of the immediate future and a condition for the survival of the evolving hemispheric democracy.

A strong, active, supportive, and refinanced state is needed in order to realize a democratized market economy. The tax system should provide an increased public income that rises progressively to international levels. We should bear in mind that until now, no country has succeeded in generating a stable social balance with public expenditure levels lower than 30 percent of the gross domestic product (GDP). To reconcile an increase in taxes with the requirements of savings and private investment, we have to assign an important role to the set of taxation instruments. If adequately implemented, the indirect taxation of consumption, generally achieved through the value-added tax, could help to achieve this objective; its regressive bias can be more than compensated for by the redistributive effect of the social expenditure it will allow.

Three types of direct and highly distributive taxes deserve special attention: a direct and progressive tax on every citizen's personal consumption (taxing the difference between total earnings and established savings); an estate tax, especially with regard to inheritances and grants; and a natural resource tax that allows the nation to capture part of the income derived from a favorable supply of resources. The exemplary punishment of the big tax evaders and the widening of the taxpayer base will complete the task of tax system reorganization.The state's fundamental obligation is to optimize the fiscal resources that it receives from society. Latin American governments must completely eradicate corruption, dishonesty, and inefficiency, so that the management of every fiscal peso yields maximum productivity in social and human development terms.

In some countries, a burdensome domestic debt demands an enormous part of public income and causes extremely high interest rates. the state's economic sanity needs to be restored. To this end, privatization of public enterprises may be advisable, as long as the resulting profits are used to reduce domestic public debt and to lower the interest rates paid by the government ——and by private agents at international levels. We reject measures to finance current expenditures or external deficits through the sale of state assets. Privatization is an economic policy resource that is circumstantial in nature; it is not an ideological bias or dogma. New public enterprises can be created tomorrow, while others are privatized today. We must also use privatization to divide up property and increase competition, avoiding the substitution of public monopolies with private monopolies or oligopolies. Above all, we must create three mechanisms, the absence of which has contributed to higher costs for our nations during the privatizing euphoria of recent years. First, a long-term national development strategy should be established that delineates the major parameters for the privatization and the conservation or creation of public-sector entities,, and that also defines the administration standards—subject to market criteria—of the latter. Second, transparent fiscal institutions that control the sale of state assets must be created, not only to prevent classic vices such as influence peddling, sharing of privileged information, or prices below market value, but also to ensure that the buyers are acting in the national interest, and that their resources come from lawful businesses and means. Finally, the regulatory framework necessary to ensure the adequate performance of large-scale private enterprises that provide public services in a semimonopolistic manner is conspicuously absent in most of our countries, and must be established. Without such regulatory frameworks, privatization may prove counterproductive and onerous.

The state must guarantee a basic set of social rights for all, recognizing that a social compensation policy can only intensify and never substitute for the struggle against economic and social dualism—, that is, the gulf that in our countries separates the privileged and organized sector of the economy from the backward and disorganized sector. These social rights must give priority to children and to education, guaranteeing children access to schools that, in addition to knowledge, provide them with daily food and medical care. Assistance to children must be complemented by assistance to mothers, especially those who are single heads of family or heads of households. In some Latin American countries, about half of

working-class families are headed by women, while men serve as unstable partners. The state must guarantee equal access to the education project for each and every one of its citizens. More than anything else promoting the gap between rich and poor is the lack of opportunity for the poor and those excluded from development to participate in the education process up to the university level. This deficiency may be corrected with intelligent policies, technological modernization of educational processes, and through distance, electronic, and televised education. Current projects cannot stop at the sixth grade of elementary school or, in the better cases, the secondary level. As a matter of urgency, the state must set up mechanisms to ensure that public education includes each and every one of its citizens, covers each and every level of education, and reaches every part of its territory. When citizens are provided with higher levels of education, with knowledge and technology, sustainable development will be truly guaranteed. Thus, investment in human development will be much more important than other forms of government investment.

The school's mission in a democracy is to analyze the possibilities of imagination and of life that society is incapable of confronting. Schools must be the voice of the future (and its alternatives) in the present; they must recognize the child as the worker of the future, the citizen, the small prophet. It is essential to prevent a specific authority of the government–even of the community itself–from having a preponderant voice in matters relating to educational content. A system of multiple responsibility, of multiple financing, of multiple orientation—federal, state and municipal—will free public schools from exclusive dependence on local control and will provide them with the economic and cultural resources to create free men and women.

We must begin to unlink basic social rights from employment in order to avoid reinforcing existing inequalities. This can be done by increasingly financing those rights through the central tax system, instead of through payroll taxes that reduce the competitiveness of enterprises and intensify the division between holders of stable jobs and the vast strata of unemployed or informally employed. Future development of these rights calls for the extension of the principle of social inheritance: everybody inherits from society, not just a privileged, family-endowed few. A social account, opened in the name of each individual, is the practical means to social inheritance. The amount in the account could be increased according to one of two opposing principles: through special needs or vulnerabilities or through special merits, competitively proven.

The idea of unlinking social rights from employment is directly associated with the notion of social citizenship. In North Atlantic countries and in Japan, a large part of the social rights that constitute social citizenship—medical insurance, pension, vocational training, unemployment insurance, transport, and housing—are linked to employment. In some cases, they are part of a nonmonetary salary, in the form of benefits, and are financed by payroll taxes. This has been so for more than a century in some cases: on the one hand, this mechanism allowed a certain gradualism—those that secured employment, at the beginning at least, gained access to certain social rights (and to certain political ones through the extension of universal

suffrage). At a later date, the mechanism assured ample coverage in periods and countries in which there was full employment.

But in societies where political rights are already in force and where full employment is, in the best of cases, a distant hope, making the enforcement of social rights a condition of employment and financing them through payroll taxes could be catastrophic. In fact, the great defect bequeathed to our countries by the now simplistically vilified populist regimes of the 1930s and 1940s may originate in the association between social rights and employment, transferred to societies unsuited for such association.

For this reason, it is advisable to start, through the central taxation system, an unlinking and financing process affecting social rights already existing but of reduced quality—such as public education—and the remainder: health, housing, unemployment insurance (or negative income tax), support to counteract poverty, pension, vocational training, and so forth. The costs will be undoubtedly higher as coverage is expanded, but the search for fiscal financing mechanisms outside the payrolls may also serve to reduce the social responsibilities of the business sectors, and to improve the competitiveness of enterprises. Without reducing existing rights, it is essential to begin exploring this rich vein of possibilities.

It could well be that the struggle against inequality should be considered from a different historical perspective analogous to the fight against racial discrimination in the United States—in other words, to see it as a deliberate and active attempt to rectify a status quo in the face of ancestral inequality that is linked in some way, albeit enigmatic, to the conquest in Latin America. We have known for some time that any social or economic effort in Latin America that does not take into account the enormous inequality prevailing in practically all the countries of the region only reproduces the existing inequality. At the same time, it is evident that this inequality has historical roots: it is not the product of a current situation, but one originating from the reproduction of a previous situation that dates back to the beginnings of the colonial period. Thus exists the analogy with North American "affirmative action," that in spite of all its real problems and faults has produced unquestionably positive results and enjoyed wide social consensus for several decades.

The possibility of raising real wages above the limits imposed by the productivity gains has proven to be one of the thorniest, most controversial topics of our discussions. On the one hand, all the participants agreed on the need to raise the proportion of national income represented by the salaried masses. It is not enough to raise nominal wages, or to increase employment with miserly salaries. At the same time, although possible, it is not easy to impose income increases without productivity increases. We all recognize that salary appreciation must be backed up by increased rights to work, without falling into the straightjacket of employment stability: the dismantling of labor rights. We must adequately resolve the tension between the need to create stable, quality jobs and the need for negotiated instruments that reduce the weight of nonsalary labor costs on companies. Only a new development cycle, sustained by an enriched state and by increased domestic savings, can reconcile salary appreciation with an extended labor market.

Any national development project, and above all an antidualist project, involves raising the level of domestic savings and opening new links between private savings and productive investment. "Capital is made at home": nowadays, no country can rely on the possibility of developing itself with money from others. Foreign investment is much more useful the less one must depend on it. Wealth-generating fiscal adjustment by the state (enabling public savings and an increase in social expenditures and in public investments in infrastructure) and public organization of private savings are two supplementary ways of mobilizing national resources for development. The target should be a savings rate higher than 30 percent of the GDP. Social security system reform provides a favorable opportunity to organize and increase private savings. The combination of the "preestablished benefits" social security system (which guarantees a fixed pension, independent of price quotations) and the "fixed contributions" system (which returns to pensioners what they saved during their working life), makes the requirement for obligatory, progressive, and redistributive savings feasible. Thus an obligatory private savings system is combined with a mechanism that redistributes part of the richest accounts to the poorest ones.

However, increasing savings alone is insufficient. New channels between savings and productive investments must be opened. If even rich economies squander a large part of the productive potential of savings in a financial "casino," and production is largely self-financed through the reinvestment of profits, the nexus between savings and production in our countries is even more tenuous. We must establish, beyond banking and stock exchanges, an additional mechanism to productively mobilize savings: mutual funds, starting with social security funds, administered through an autonomous management and financial responsibility system. Some funds would offer incentives for direct investment in SMEs of the economic rearguard. Because access to credit is extraordinarily reduced for the majority of the population, the traditional financial system should be extended until it provides total coverage to the entire population, with institutions such as savings banks, trust funds, credit unions, solidarity groups, and, in particular, microcredit institutions guaranteeing access to this vital and elitist resource for all citizens, regardless of their poverty, isolation, or education level.

Increased domestic savings, combined with the search for and creation of new links between private savings and productive investment, is one of the conditions of the new national project to democratize development. The consolidation and realignment of monetary stability is another. Monetary stability is an unavoidable standard. The traditional imbalances in Latin American public finances—with the resulting inflation and foreign overindebtedness— were symptomatic of a weak state that was incapable of imposing the cost of investment in individuals and productive infrastructure on its wealthy classes. Nevertheless, once the stabilization stage is completed, monetary stability must be freed from its dependence on the overvaluation of the exchange rate, on salary compression, and on the high domestic real interest rates. This can only be done through a wealth-generating fiscal adjustment on the part of the state that, by increasing the tax burden, is able to reconcile increased fiscal revenues and a widened tax base with strengthened savings and

investment. We need a fiscal adjustment that enriches the state instead of impoverishing it.

The proposed development project must combat and, in the long term, end the division between productive vanguards and rearguards. A development strategy that adjusts to the current international distribution of comparative advantages and disadvantages, and that encumbers all individuals with the same slow, painful scaling that has proven unable to close the gap between rich and poor, advanced and backward sectors, is unacceptable. A productive vanguard within each country inserts itself within the international network of vanguards, while the remainder of society, supposedly pacified by a social welfare policy, waits its turn. The working majority toils in the purgatory of underemployment or employment in an industry made up of subordinate parts of the internationalized production process.

It is not necessary to choose between reducing the state to merely regulatory and social activities and adopting a centralized industrial and commercial policy, along the lines of northeast Asian economies. The right approach is to decentralize the desirable alliance or association between public power (and its alternative policies of support and development) and private initiative. Instead of a unified Asian-style strategy, Latin American countries require a flexible and decentralized scheme led by a variety of funds, public and private banks, and support centers that, with a wide margin of autonomy in decisionmaking, can position themselves between central governments and SMEs. Networks of these small and medium-sized enterprises, linked through cooperative competition, should receive the support necessary to consolidate and integrate themselves in the worldwide network of productive vanguards.

The objective of this policy of bold, decentralized alliances between governments and enterprises is to combat economic and social dualism. A technological vanguard, located in public and private enterprises, must perform two tasks: (1) to reduce the dependence of international competitiveness on salary compression, and (2) to make progress in the production of the equipment and materials that SMEs can assimilate. The objective is to actively promote vanguard economic practices—continuous innovation, reduction of the contrast between supervision and execution, and a mixture of cooperation and competition—outside the traditional vanguard sector. Extending vanguardism requires a new type of linkage between public power and private initiative. For example, agrarian reform is neither an archaism nor an exception; it is a matter of central importance. The successful experience of many rich countries in developing family-centered farming through partnerships between government and small farms is an example to be followed by our agrarian sectors.

The counterpart of antidualist development is the imposition of market logic on all agents of the large private economy. Private oligopolies and cartels tolerated or protected by the state, direct or indirect subsidies obtained by those who have access to public favor, nepotism in large family enterprises, the offensive treatment of minority shareholders, and the reduction of stock markets to mechanisms for attracting capital without risking company control often transform our capitalism into a travesty of the market economy. We must not allow the discourse on public-

sector privatization to serve as a pretext for the state continuing to service special interests and the private sector from continuing to receive the unjustified support of the state. On the contrary, rearrangement of state support to small and medium enterprises, strong antitrust legislation in favor of competition and against private or public oligopolies, protection of minority shareholders against controlling shareholders, fiscal punishment of obstinant large family enterprises, termination of shares without the right to vote, and publication of benefits enjoyed by senior executives, are all means to impose competition on those who claim to want it. They complement the work to end the division between the vanguard and the rearguard.

This type of economic program is compatible with nondogmatic free-trade. This means that deprivatizing the state and strengthening democracy will empower the strategic selectivity of the opening-up process, thus preventing selective, temporary tariff protection from serving only to transform political influence into economic privilege. It means that the raising of domestic savings levels will free our countries from the vicious circle of dependence on financial capital attracted by high internal interest rates, while favoring the entry of capital dedicated to increased production and productivity. It invalidates rigid distinctions between the management of capital (free to circulate) and the management of work (trapped within the nation-state). It involves the obligation to be active within the organizations of the Bretton Woods system in order to prevent their functioning solely as enforcers of prevailing ideas.

The antidualist development program is based on strengthening of democracy, which involves institutional innovations. A first component of this program to strengthen democracy is electoral authenticity and an organized and enduring civic mobilization. It is not sufficient to respect popular suffrage: it is also necessary to reduce the influence of money in politics. To this end, we must demand public financing of campaigns and transparency of private contributions. It is crucial to combine the austere measures so necessary in electoral campaigns in poor countries with the need to prevent corrupt and illicit financing, whether from interest groups or drug traffickers.

At the same time, we have to open up mass media to society. In the majority of Latin American countries, it has passed from heavy state control, especially in the areas of electronic media and radiotelephony, to the overpowering control by huge private monopolies. In the absence of adequate regulatory frameworks and with the fragmentation proceeding from the cable and DTH systems in industrialized countries, it is essential to promote measures that, without in any way reducing freedom of expression and private ownership of the media, guarantee both plurality and access in harmony with the aspirations of Latin American societies. This can be achieved by limiting the concentration of concessions and frequencies, and by decentralizing and diversifying the ownership of the media, as well as its production of information and communication. Similarly, free access to the mass media of political parties, social movements, and different sectors of society, including cultural, ethnic and ideological minorities, must be increased.

An essential component of a program to strengthen democracy is the need to make leaders liable and accountable. On the one hand, it is necessary to increase

measures such as revoking mandates by popular initiative, referendum by popular initiative, making secretaries of state answerable to parliament, establishing an independent and legitimate public ministry to challenge the government in power, and creating summary judicial solutions against abuse of power. With these resources, filling the gaps between elections and rendering a watered-down version of the equation "Democracy = Sporadic Elections" is possible. Similarly, the appointment of these authorities within the state—in regulatory areas and in those concerning fiscal audit and corruption—guarantees an element of distance between the supervised and the supervisors. On the other hand, core political and administrative activity should promote the community participation in formulating and implementing government proposals and programs—above all, local proposals and governments—taking care to ensure that the opportunity for participation does not only result in a transferal of power to mobilized minorities. Brazilian experiences in this area are especially interesting here.

An additional element of the democratizing political program is presidential system reform. While we do not share the predilection for fragmentary parliamentarianism, we believe that the presidential system copied from North America is not entirely adequate for our societies. Consequently, if we retain the presidential system in the light of its antioligarchical potential, we must cure its major defect: the favoring of legislative impasses over reform programs. We must supply the political presidential regime with mechanisms that enable a rapid resolution of programmatic impasses, and that strengthen the power of states to make decisions and to effect change. Such mechanisms include a series of instruments: legislative privilege or "fast track," used to describe legal initiatives of a programmatic or strategic nature that go beyond punctual law; plebiscites and referendums called by agreement of the two authorities; and other mechanisms of direct democracy that reconcile the latter with representative democracy.

The last proposal of this political program is to give a liberalizing shock to the core of national life or (if preferred) to cause long and continuous explosions of civil society that will allow the vulnerable citizens of Latin America to know their rights and defend them. In our fragmented and heterogeneous societies, almost no one is "just" a citizen: the number of groups, sectors, minorities, regions, and ethnic groups who are victims of some kind of discrimination or oppression beyond those to which all of society is exposed, both obliges and inspires us to adopt a policy of continual activity. Women, youth, workers, indigenous communities, negroes and mulattos, minorities of a certain sexual preference, oppressed ethnic groups, marginalized religious sectors, and many other groups who suffer from the nonfulfillment of their rights and aspirations must be encouraged to take action, and to claim spaces, rights, and interests. We must multiply the practical means by which citizens may confront racial, ethnic, and generic prejudices that divide society and intimidate people. We must separate the correction of class disadvantage from compensations for disadvantages of race and sex. The accumulated disadvantages of certain groups must be the first target of a liberalizing policy.

A doctrine has propagated around the world that suggests there is only one possible path to economic prosperity and political freedom. The task of reformers is

limited solely to humanizing the implementation of that doctrine. Their program winds up being that of their opponents, only with a "50% discount."

We, on the other hand, propose another path, one that associates productivity with redistribution; that connects democratic strengthening to the conquest of social and economic dualism; that combines a strong, active, and refinanced state with decentralized support to small and medium-sized enterprises, introducing advanced and experimental economic practices that reach beyond traditional economic vanguards. This path establishes the foundation for a high-intensity, popular policy and radically democratizes the market economy. It involves a sequence, gradual but accumulative, of changes in economic, political, and social institutions. It does not involve the humanization of the inevitable. It is rather, the alternative—possible and necessary—to a destiny that we do not deserve.

Poverty, Exclusion, and Access to Services: The Role of Institutional Reforms

Ariel Fiszbein

Coordinator, Economic Growth and Poverty Reduction, EDI

In this session we will approach the issue of poverty, inequality, and exclusion from a particular angle: access to basic services. I would like to focus on the role played by institutional reforms in promoting a more equitable and inclusive pattern in access to services. I would say that in this critical area we have more questions than answers. Therefore, it is absolutely necessary to make a systematic effort to assess the impact on poverty and equity of the different reforms and changes of an institutional nature being developed in the region.

Introduction

Improving access to quality services constitutes a critical component of any anti-poverty strategy. Traditionally, we have tended to focus our attention (at least within the Bank) on services such as education, health, or drinking water. However, as time has gone by, new services—such as justice or public safety—have begun to be considered essential. By the same token, even though in a strict sense they are services, access to housing or to credit also constitutes a critical aspect of the development of strategies to fight poverty.

This emphasis on service provision as a strategy in the fight against poverty is consistent both with an approach to basic needs that highlights the consumption nature of those services, and one that highlights the fact that these services constitute assets of a different nature. Thus, improving access to them promotes the accumulation of human (for instance, in the case of education), physical (as in the case of housing), and social capital (as in public safety). At the same time, looking at it from the viewpoint of social exclusion suggests that an equitable access to basic services is a precondition to promoting greater social cohesiveness.

Beyond the reasons why it is important to pay attention to the issue of access to quality, basic services, the reality is that—with few exceptions—most countries in the Latin American and the Caribbean Region (LAC) perform poorly when it comes to ensuring achievement levels in education or access to drinking water consistent with the prevailing income levels. As an example, it is worth mentioning that in Brazil only 46 percent of children from poor families complete the fifth grade, while in Zimbabwe, that percentage is 89 percent. Even though the highly unequal nature of income (and capital) distribution throughout LAC is generally acknowledged

(at least in the academic literature), the inequality among social groups and subregions in the access to quality services is equally alarming, although it is mentioned less frequently.

Traditionally, debates surrounding these issues have focused on the level of public expenditures ("the government should spend more in education"), the efficiency of such expenditures ("the government misuses the resources earmarked for health"), and the effectiveness of such expenditures in targeting the neediest ("the government apportions too many resources to serve high-income groups"). However, it can be argued that these are only symptoms of the deficiency of institutions regulating such service provision, and that, therefore, institutional change is essential to deal with the problem.

Thus, the so-called "Washington Consensus" seems to be giving way to the purported "second-generation reforms" that focus on institutional reform, understood as the change in the rules of the game (formal—such as constitutions, laws and regulations—and informal—such as standards and values) that regulate service provision. These changes affect who is responsible for the different parts of the process of providing a service (financing, production, delivery, quality control, and so forth); what authority and capabilities they have to carry out those responsibilities; and what incentives they have to discharge such responsibilities in a manner that is conducive to offering quality services to the poor and/or excluded sectors. In other words, what accountability mechanisms exist that to some extent would force those responsible for providing services to serve the poor?

Ongoing Reforms

Fortunately, this is not just a theoretical discussion. LAC countries have already been experimenting with different institutional reforms, in some cases for more than a decade. Although it is not easy to classify those reforms—risking oversimplification—I would venture to group them in four categories: decentralization, privatization, participation, and public-private partnerships.

Decentralization implies the transfer of responsibilities for service provision from the national level to a subnational level (that is, provincial or municipal). Privatization implies the transfer of responsibility for service provision from the state to the private sector (particularly to the for-profit sector). Participation is understood as institutional reforms seeking to promote the role of beneficiaries in the management of basic services. Finally, public-private partnerships constitute the development of institutional mechanisms that go beyond the traditional boundaries separating the state from the market and civil society or the dichotomies between state-market or for-profit–not-for- profit, adopting mixed management models.

In all these areas, we can find examples of reforms and innovations that—although not always inspired by the objective of fighting poverty—have the potential of radically changing service provision conditions, improving or worsening access to them by the poor.

It is worth asking ourselves how much we really know about how these reforms are affecting the poor. Can we say—confidently and based on empirical evidence—what type of institutional arrangements are more prone to improve the access and reduce the exclusion of the least fortunate groups? Or, perhaps more important, do we know the conditions under which these reforms could help fighting the exclusion and inequality pattern noted above?

The answer is only partially positive. In the last years, we have taken stock of several interesting studies offering partial evidence (for a country or subregion, or for a specific type of service) on these questions. But I believe that we still do not have the critical mass of evidence or any systematic methodological approach that is necessary to answer the questions that concern us.

In approaching these issues we should ask ourselves three main questions. First, what has been the impact of specific institutional reforms—for instance, the privatization of the drinking water utility—on different social groups' access to basic services, and what aspects of such institutional reforms explain that outcome? Second, are the new institutional arrangements sustainable from the financial and political viewpoints, and are the effects observed only short term in nature (as a result of the introduction of the reforms), or, on the contrary, do they represent a deep and lasting change in the rules of the game? Third, have the reforms in question produced effects (expected or unexpected) that leverage and advance other initiatives in the fight against poverty—for instance, strengthening the organizational capabilities of the poor or improving relations between the State and civil society? My comments are primarily addressed to the first of these questions.

A Bird's-eye View

It is beyond the scope of this meeting (and my capabilities) to try to offer a report detailing the knowledge surrounding these four types of institutional reforms. Just to "whet the appetite," I will try to review some critical points in each area. I am sure that forum members—from different angles and based on a deeper knowledge of the situation in their own countries—may expand and correct my concepts.

Decentralization

The movement towards state decentralization has been a very clear trend in LAC during the last decade. We are aware that this is not only a fiscal decentralization but also a political decentralization (through popular elections of mayors and governors) and an administrative decentralization (through transfer of the responsibility for the management of various public services to the subnational level). Thus, when evaluating the impact of this type of institutional reform on access to services for the poor, it is necessary to look at the combined changes in the fiscal, political, and administrative areas. Bolivia, Brazil, and Colombia are noteworthy, because—when compared with other countries in the region—they show important progress in the three dimensions mentioned above.

Let us begin by distinguishing between interregional impacts (have the poorest regions benefited from this?) and interpersonal impacts (have the poorest persons or families benefited from this?) of decentralization. Interregional impacts on basic service provision depend essentially on two underlying factors in the institutional design adopted in decentralization programs. The first factor to be considered is the extent to which the fiscal design offsets differences in fiscal capacity between regions and localities. From this viewpoint, the prevailing experience in LAC is that fiscal decentralization has implied a redistribution of resources towards rural and lower-income areas. The adoption of intergovernmental transfer systems that are transparent, automatic, and based on formulas that incorporate necessary fiscal capacity measures seems to offer an effective answer to the question of interregional impacts.

The second factor to be taken into account is the extent to which the transfer of administrative responsibilities reduces the efficiency of the service —compared with the centralized service—because of a low management capability in the most backward localities. This is a difficult question to answer empirically, partly because we have very little information on the evolution of local management capability in response to decentralization programs. My own work in Colombia[1] and recent studies in Bolivia[2] suggest that local management capacity, by itself, does not seem to be a bottleneck. Beyond whether or not these results can be generalized, the important message is that institutional design is key not only from a fiscal viewpoint (particularly with respect to the transfer system), but also from an administrative viewpoint. As long as the new rules of the game establish conditions for service delivery that are impossible or difficult for out-of-the-way, small, or poorer territorial entities to meet, they potentially face discrimination that may decrease certain social groups' and regions' access to services. . That is why certain authors have begun to talk about the need for an asymmetrical decentralization that takes these factors into account and assigns differential responsibilities, according to capabilities, so as to control the quality of services.

From my own perspective, the interpersonal aspects are the most difficult to evaluate, because the institutional factors conditioning results in this dimension are rather complex. The basic question is: does the institutional design allow or facilitate situations in which the benefits derived from the decentralization of basic services are captured by local elites, instead of contributing to improved access for the poor? In fact, it is possible to divide the question in two parts with respect to the institutional design underlying the decentralization programs: first, does this lead to the concentration of political power in the hands of local elites? and, second, does it generate enough incentives for those elites—notwithstanding their gaining or losing political space—to address access of the poor and/or excluded groups to basic services by.

My reading of the available evidence is that, generally speaking, decentralization is not leading towards a concentration of political power in the hands of local

[1] Ariel Fiszbein, "The Emergence of Local Capacity: Lessons from Colombia," 25 *World Development* 7: 1029–1043.

[2] See, for example, Jean-Paul Faguet, "Decentralization and Local Government Performance." Paper presented at the Technical Consultation on Decentralization, FAO, Rome, December 16–18, 1997.

elites. Bolivia—from which we are only now beginning to draw results based on systematic research—seems to suggest the opposite. The institutional design in this area is directly linked to the characteristics of political decentralization. The existence of local elected authorities may seem to be a necessary condition, but it is not enough. The existence of legal mechanisms favoring the monitoring of public management and citizen involvement, as in the case of Bolivia, and the characteristics of the electoral system at the local level also seem to be important factors.

However, the evidence (not only from Bolivia but also from countries such as Brazil and Colombia) suggests that, independent of the formal rules of the game regulating citizen involvement, decentralization's main impact is the emergence of a new generation of local political leaders who are more capable and less traditional. In fact, some of the most interesting mechanisms of democratization in decisionmaking at the local level—such as the participatory budget in the Brazilian city of Porto Alegre—have occurred in the absence of legal standards.

The assumption that greater concentration of power in the hands of local elites will necessarily lead to the reduction of access to quality services by groups in poverty status or to an increase in exclusion, assumes that those elites do not have enough incentives to be concerned by those issues. Once again, the institutional arrangements adopted may play an important role in the creation of those incentives.

An example of the type of such institutional design is the use of a targeting system (such as the SISBEN in Colombia) that forces local governments to follow certain consistent criteria in assigning public expenditures (and, in a more general manner, in delivering services) to benefit the poorest sectors. On the one hand, through these regulatory systems decentralization may help the poor by limiting the autonomy of local governments in deciding who will benefit—an attractive option, assuming that decisions at the local level are strongly influenced by elites devoid of sensitivity to the interests of the poor—and imposing certain controls on the clientelistic practices prevailing in the region. However, this type of system is certainly controversial—first, because it assumes the existence of commonly accepted criteria of need, efficiently available at the central level, and second (and perhaps more important), because as these institutional arrangements limit local autonomy, they tend to alter the local political dynamics that may, in the long term, weaken the internalization of social problems within the local political debate. Beyond these debates, a transparent targeting system within a decentralized management context (such as the SISBEN) has clear advantages compared with targeting systems managed from the center, which tend to be highly prone to political and electoral manipulation, as documented by new studies on Peru.

As we will discuss in greater detail in the Participation section, a key question is whether or not it is possible to develop supplementary mechanisms that increase the voice of socially excluded sectors and therefore alter the local political dynamics without the need to overimpose bureaucratic patterns that in many cases are relatively easy to avoid.

An issue of great importance is that the negative consequences of excluding certain social groups from basic services are often felt more by the elites at the local level than at the national level. Two typical examples are the exclusion of certain

groups from drinking water, sanitation, and garbage disposal systems that bring about environmental consequences suffered even by the local rich, and the lack of basic quality education that—in a context of greater competition—is "suffered" by local businessmen in terms of workers' low productivity levels. The institutional design underlying a decentralization program may strengthen these natural incentives, mainly by avoiding generating opportunities for the subnational governments to "export" these consequences or the cost of solving them to other jurisdictions or to the national government. This changes the analytic line from one of choosing targeting mechanisms to one based on making local and regional leaders feel the costs of poverty.

Privatization

A second type of institutional reform consists of transferring responsibility for providing services from the state to the private sector. In many cases, privatization implies the sale of state-owned assets (water and sanitation public utilities, telephone, energy, and so on). In other cases, often not considered privatization, this implies opening opportunities to the private sector to offer services previously monopolized (formally or informally) by the state. Such is the case, for instance, with reforms in the education sector in Chile (the introduction of vouchers) or in the health sector in Colombia (the introduction of health services delivery organizations).

This is an area of increasing interest levels, but relatively little empirical evidence. I will mention a couple of examples only to show the possible importance of the adopted institutional arrangements in terms of their impact on access to—and quality and cost of—services to poor families.

An interesting case to consider is the privatization of infrastructure services such as drinking water, electric energy, gas, and so forth. Microeconomic theory suggests that the impact on the poor depends to a large extent on the regulatory system established. On the one hand, since in most cases we face natural monopolies, the pricing policy is critical in determining the distribution between service providers and users (particularly low-income users)of gains in productivity caused by privatization. On the other hand, adoption of "mandatory services" or "universal service obligations" systems that are efficient and transparent is critical to ensure that low-income groups or groups living in isolated areas benefit from the expanded coverage and improvements in the quality of services resulting from private-sector management.

The empirical evidence that I have in mind comes from Argentina, where some recent studies provide us with interesting results.[3] The potential gains to users of a pricing system that ensures the transfer of cost reductions to users are extremely

[3] See Omar Chisari, Antonio Estache, and Carlos Romero, "Winners and Losers from Utility Privatization in Argentina," Policy Research Working Paper No. 1824, The World Bank; and Omar Chisari and Antonio Estache, "The Needs of the Poor in Infrastructure Privatization: The Role of Universal Service Obligations. The Case of Argentina," prepared for the seminar on the subject organized by the World Bank's Economic Development Institute, Washington, D.C., November 10–11, 1997.

high for all economic strata. However, such gains have not occurred in a generalized manner. The redistributive impact has been less progressive than that resulting from a more effective regulatory system. From the perspective of coverage expansion, the evidence suggests that even though adopting a mandatory service scheme in which private operators are required to guarantee connection to all interested users (who pay the service connection fees and normal rates) has shown positive results, certain low-income groups have remained outside the system. The latter's exclusion can be partially reversed with changes in the regulatory structure (for instance, extending the terms to recover the investment costs or through certain cross-subsidies).

It is not my intention to provide details of an effective regulatory system (which, by the way, is beyond my area of expertise) but simply to emphasize, on the one hand, the importance of thinking about the institutional design of a privatization scheme from the perspective of inclusion and poverty reduction, and, on the other, of evaluating the lessons emerging from these experiments in institutional reform.

In the education sector, the "privatization" example I have in mind involves promoting educational delivery in private schools, within a competitive framework, through demand subsidies—the so-called vouchers. In this case, the state transfers the responsibility for service provision to private operators while keeping to itself the responsibility of offering basic financing. This scheme has been applied in Chile for more than a decade and several evaluations are available.[4] Once again, I will refer to this case somewhat superficially in order to highlight the importance of the institutional design adopted (and adapted to a certain extent since the restoration of democracy).

From our viewpoint, the key question is whether the reforms promote improved access to quality education and, therefore, contribute to improve the social mobility of children from low-income families. The Chilean experience offers a series of lessons. For example, evidence exists that the capacity of family heads to exercise their opportunity to choose varies, depending on the neighborhood where they live, their income level, and their social status. The supply of services is, obviously, more limited in rural areas than in urban areas, but even in urban areas, transportation costs and the differences in access to information (commonly obtained through contacts and informal networks) are an important source of exclusion.

The experience in Chile is also indicative of how these problems can be dealt with by changing the institutional design so as to generate compensatory mechanisms that increase the capabilities and opportunities of the less fortunate. The introduction during the 1990s of new curriculum standards (supplemented with a more aggressive use of the information on school performance as an information strategy for parents) and of targeted assistance programs to schools with higher enrollments of low-income groups are examples of how the democratic authorities sought to compensate for the inequalities in opportunity and capability disregarded

[4] A very recent summary on the issue may be found in Martin Carnoy, "National Voucher Plans in Chile and Sweden: Did Privatization Reforms Make for Better Education?" 42 *Comparative Education Review* 3: 309–337.

in the initial design. It is less clear, however, to what extent an effort was made to generate additional incentives or other conditioning factors geared towards altering the behavior of private operators. More generally, the question remains if, in a scheme where the vouchers are targeted exclusively toward the low-income sectors, results would be better, from the distributive point of view. Again, this is not the place to begin specific discussions on this type of reform. We can only take note of how crucial—from the standpoint of fighting poverty and exclusion—the specific forms of reform implementation are. It is in those fine points that the differences in results are found.

Participation

The term "participation" is very general, encompassing different concepts. The point that I want to emphasize is that one change observed in LAC is the different direction taken to grant a more active role in the delivery process to users of the services.. This ranges from consultations about priorities and user satisfaction surveys, through delegation of only certain aspects of service management, to adoption of management modalities in which the users are responsible for the entire operation. This process is often referred to as "demand-orientation," understood as institutional arrangements where state agencies offer options, objective information, and funds to support community initiatives. Conversely, beneficiaries are required to show their interest by contributing resources and/or labor.

The movement towards participatory programs is very strong in the region, at least at the rhetorical level. Our generic question, however, is still valid: What is the institutional design (that is, the rules of the game, the assignment of responsibilities, the necessary conditions for the development of authorities and capabilities, and the accountability mechanisms) that makes these participatory schemes effective mechanisms to fight poverty and exclusion on a sustainable basis?

While preparing these notes, I had the opportunity to review recent papers on experiences related to participatory management and demand-orientation in the education sector (such as the EDUCO program in El Salvador), in the drinking water and sanitation sector, and in social investment funds, that offer some very valuable responses to our previous question. In fact, the responses do not seem to vary among services and are similar to those emerging from work in other areas such as low-income housing in urban areas.[5]

Clearly, designing demand-driven schemes is not easy and, in fact, many programs that identified themselves as such are not (and many that are, show much variation in different localities and regions). The basic conclusion is that the effectiveness of these programs as mechanisms for service delivery to the poor and/or excluded groups depends to a large extent on their institutional designs favoring the beneficiaries themselves, and not intermediaries or representatives who express their demands.

[5] See, for instance, "Encuentros: Seminario sobre alianzas entre estado y ONGs para la reducción de la pobreza," World Bank Economic Development Institute, Washington, D.C., October 21–25, 1996.

What has been observed in many programs and initiatives supposedly participatory (or directed toward the demand) is that the institutional arrangements that are adopted restrict the capacity of the poor communities to fully benefit from them. Two simple examples may serve to illustrate this. A recent study on water supply programs in rural areas[6] showed that even though the communities took educated decisions based on the participatory program in question, since the construction of the systems continued to be the responsibility of a "nonreformed" state agency, they were unable to ensure that the works were carried out according to plan. Similarly, an evaluation of the social investment fund in a Central American country showed that the private-sector contractors ended up controlling the use of the funds far beyond the participatory planning process engaged in by the poor communities.[7]

Three conclusions emerge: (1) demand-orientation must take place consistently in all the stages of the provision process (financing, production, delivery, and so forth), or the "weaker" link of the chain ends up dominating the rest; (2) participation as the approach for the provision of services to traditionally excluded groups is information-intensive. In this sense, we find ourselves facing demands that are not too different from those we identified in the case of private management schemes; and (3) to be effective, the articulation of the demand must be accompanied by contributions (in cash or in kind) from the beneficiaries, which indicates—given our focus on low-income groups, as in the case of privatization of services—how crucial it is to have a well-designed subsidy policy.[8]

At the same time, it is valid to emphasize that community participation as an alternative management strategy of a service requires a transfer of power typically resisted by many social actors (by the state itself and, in the specific case of education, by the unions). Thus, even in radical experiments, such as the participatory budget in the city of Porto Alegre, it has not been easy to extend to recurrent expenditures (which constitute the heart of the basic services delivery process) the strong role that the citizenry—especially the poor neighborhoods—takes in assigning investment expenditures.

In addition to the assignment of responsibilities and the loss of control by the most traditional actors are key factors, there is another important aspect to the institutional design of participatory programs: the management capability of poor communities. We all have heard, many times, the condescending view—based on the supposedly low capability of the poor—that rejects participation as an alternative. I will not waste time discussing this notion, on which we have enough contrary evidence. The question is, however, to what extent does the institutional design favor the creation of new capabilities among the poor? An implied need exists to

[6] See Harvey A. Garn, Travis Katz, and Jennifer Sara, "Lessons from Large-scale Rural Water and Sanitation Projects: Transition and Innovation," paper presented to the Technical Consultation on Decentralization, FAO, Rome, December 16–18, 1997.

[7] See Anthony G. Bigio (ed.), "Social Funds and Reaching the Poor: Experiences and Future Directions," World Bank Economic Development Institute, 1998, p. 174.

[8] An example is whether or not to subsidize only capital costs, or operational and maintenance costs as well.

design programs that take into account the time and the resources necessary to strengthen the capability of the excluded groups' community organizations. Also by implication, there seems to be an acknowledgment that, given the need to have capable organizations, the level at which these participatory instances may occur is essentially local. This emphasizes the link between participatory approaches and decentralization.

Finally, it is worth considering that the participation of beneficiaries in the management of basic services should not have to follow such radical examples as the ones that I have mentioned so far. Today there is much talk about client-oriented management— understood as the adoption by state entities of management and administration styles that seek to respond to the needs of the beneficiaries without transferring the responsibility (totally or partially) for the delivery to individuals or nonstate entities. The question is, if a public enterprise, a health service, or an educational system wants to move forward in this direction, what are the conditioning factors and steps necessary to ensure that the poor and the excluded will be clients with as much voice and vote as the rest? Are opinion polls valid? When we think "results indicators" and "management by results," how do we ensure that the weight given to the excluded is sufficiently high, without resorting to parternalistic formulas? As in the other issues discussed here, the list of questions is, at least at the moment, substantially longer than the list of answers.

Public-Private Partnerships

Up to now we have discussed institutional reforms pushed by the state that in one way or another have altered the rules of the game for providing services, transferring responsibilities within the state sphere or to the private and community spheres. However, some of the institutional innovations taking place in the region do not fall neatly within these categories. I am thinking of the emergence of schemes in which service provision is made through mixed public-private management modalities that, in a recent report,[9] we have labeled "partnerships." As I mentioned in the introduction, the partnerships—as a new institutional modality—question up to a point the current paradigms of public economics that tend to consider service provision on the basis of dichotomies among the state, the market, and self-management. For this reason I would like to conclude these notes with a quick discussion of the role of public-private partnerships as a mechanism for service provision, and their impact on poverty and exclusion.

Perhaps it is worth beginning with an illustration; the Escuela Nueva program in Colombia is a good example. Basically, this is a rural, multigrade education program in the coffee-growing region of Colombia jointly implemented by the state (the Ministry of Education and the regional and municipal authorities), the pri-

[9] See Ariel Fiszbein and Pamela Lowden, "Working Together for a Change: Government, Business, and Civic Partnerships for Poverty Reduction in LAC," World Bank Economic Development Institute, Washington, D.C., 1999.

vate sector (essentially the organization grouping the coffee growers in the area), organizations from civil society, and, of course, the community itself. All these stakeholders provide financing, contributions in kind, technical assistance, and participatory management. In fact, the partnership nature is so ingrained in all the stakeholders that it is difficult to say whether this is a state, coffee-growers', or community program. The quantitative and qualitative impact is striking and well documented. Although at a lower scale, documented examples of this type of partnerships exist not only in the education sector (even though this seems to be a sector where partnerships are more abundant) but also in the health services, nutrition, water and sanitation, housing, microcredit, employment reinsertion, and other sectors.

The partnerships' common denominator (and their most attractive aspect) is that, in transcending the traditional schemes of separation between what is state-controlled and what is nongovernmental (including the community, philanthropic, academic, and business sectors), they achieve quantitative and qualitative results that exceed the sum of the parts. This is due to a combination of factors. First, in a context in which certain inputs (for example, technical knowledge) are scarce and hard to obtain through the market, a partnership constitutes the only way to obtain them; therefore, it allows a significant increase in output. Likewise, in allowing a specialization in the management of a service among the members of the partnership based on comparative advantages, the partnership encourages improvements in productivity. Second, in promoting the systematic interaction between individuals and various organizations, the partnership tends to generate trust and social links among them. This, together with the strengthening of the individual organizational and management capabilities of the members of a partnership that results from such interactions, constitutes a very powerful accumulation of social capital. The evidence suggests that such social capital not only makes a direct contribution in the improvement of the quality of the service provided, but also contributes indirectly by generating the conditions for the sustainability of such partnerships, as well as the development of new partnerships (in certain cases applied to other services) at a lower cost.

At the macro level, the necessary institutional reforms to promote the development of this type of partnership leads us once again to decentralization, privatization, and participation schemes. Essentially, although the development of partnerships—at least for the time being—basically depends on the initiative of state and nongovernmental stakeholders at the "micro" level, reforms at the "macro" level are the ones generating the favorable conditions for the partnerships. Decentralization (the transfer of power to the local level, where the public-private interaction is most successful), privatization, and participation are ways of making the state more open to new stakeholders and therefore constitute the minimum conditions necessary to develop partnerships. Still debatable is whether or not partnership development requires additional changes to the formal rules of the game. An example is the adoption of legal frameworks that acknowledge the dynamic nature of the partnerships and that allow the efficient integration of the state's administrative procedures with the flexibility needed in a scheme in which the state is just one more player. At the

same time, the importance of informal factors (the generation of a culture of social accountability, for example) should not be minimized; they underscore the significance, of actions that tend to improve the flow of information and contact between the state, civil society, and business—or the existence of intermediaries that play such roles.

Finally, our knowledge is relatively limited on how to design the microlevel partnerships in order to improve their impact on poor and/or excluded groups' access to basic services. . We are aware of the partnerships' potential, and that the beneficiaries themselves must become active members in the partnership, but we still do not have clear and simple answers about how we can organize a partnership in order to achieve those results. It may well be that we can only achieve this by focusing our attention on specific services (for example, education, health, and drinking water).

A Work Plan

In the introduction to these notes, I posed three questions related to the impact of institutional reforms, their sustainability, and their indirect effect on the relations among the social stakeholders. However, since my comments have responded primarily to the first question, I do not want to close without speculating about the other two.

The question of whether these institutional reforms (and their impacts) are sustainable leads us to think about the political economy of institutional change. Such a vast variety of experiences exists in the LAC on decentralization, privatization, and other reforms of a constitutional nature that my comments did not even try to reflect it. The factors that led to the initiation of these change processes (as well as those that stopped many of them) can tell us much about the long-term sustainability of the impacts that we are observing today. My perception—not very scientific, by the way—is that many of the changes in the rules of the game between the state, the market, and the civil society are sufficiently profound to probably last. But at the same time, I believe that the sustainability of these reforms depends on introducing changes and adjustments to the specific institutional arrangements that seek to compensate for the undesired effects on social inclusion.

An interesting aspect of the reforms we have discussed is that changing the rules of the game in a certain dimension tends to change the way different groups in society organize and conjoin with each other. For example, a rural education program that transfers the authority to community groups tends to strengthen the organizational capability of those communities and, therefore, to also change the local political dynamics in other dimensions. This is, in part, the subject of another session in the forum. However, it is worth emphasizing that, in designing institutions that seek to improve the access of the poor to basic services, we must think not only in terms of the direct impacts, but also in terms of the impact on the capability of the different groups (social, political, regional) to participate in the political processes in order to change the rules of the game.

I hope that this quick, somewhat cursory review of some of the reforms taking place in the institutions that provide services in LAC encourage us sufficiently to continue debating the following premises:

- Reversing the pattern of unequal access and exclusion of basic services prevalent in the region requires profound changes in the institutions that regulate service provision. This requires changing the rules of the game of whoever is in charge, their powers and available tools, and their incentives to serve the poor.
- The question is not whether or not to decentralize or to privatize, but rather, how to decentralize and privatize. In other words, what should concern us are the specific institutional designs that create the conditions to improve access for the poor to quality services.
- The previous point requires systematic efforts to learn from the empirical evidence and from specific cases of institutional reform. The variety of innovations and reforms taking place in the region offer a wealth of "natural experiments" from which we can learn.
- This learning process should be of a multidisciplinary and multisectoral nature (that is, incorporating visions and perceptions from different groups and social stakeholders) in order to contribute effectively and in a sustainable manner to the necessary change process.

The return on this "investment", I believe, can be enormous.

Latin American Labor Markets in the 1990s

Barbara Stallings

Director, Economic Development Division, CEPAL

The first line of defense against poverty and inequality in Latin America is the labor market. While government expenditures on social services and transfers can make important marginal adjustments to the primary distribution of income, the payment of wages and salaries has a much more significant impact. A very rough quantitative indicator of this relationship is the fact that some 40 percent of national income in Latin America consists of wages and salaries, while government expenditure on social services and transfers amounts to only around 4 percent.[1] Thus, it is crucial to understand how labor markets function and the distributional outcomes they produce.

Given this assumption, this paper will first provide a brief overview of the new context in which labor markets have been operating in the 1990s. Next it will look at employment trends, with respect to both quantity and quality of jobs. In discussing the latter, the relationship between the formal and informal sectors will be introduced. Next, the paper will review two "gaps" in the distribution of income: skilled versus unskilled workers and urban versus rural workers. It will conclude with some comments about impact of labor market performance on poverty and inequality and some policy recommendations. The main basis for the discussion is a project currently under way at the Economic Commission for Latin America and the Caribbean (ECLAC) to evaluate the impact of the structural reforms of the last 10 to15 years on prospects for growth, employment generation, and equity in 9 countries in the Latin American region.

Structural Reforms

The reforms of concern here are the so-called "first generation" reforms, designed to open economies and increase the role of market forces. Shortcomings in the results of the first-generation reforms are now leading to calls for a "second generation" of institutional reforms (see Ariel Fiszbein's paper for this meeting). We will return to this issue at the end of this discussion.

Because of these first-generation reforms and the accompanying macroeconomic adjustments, labor markets have been functioning in a new context during the 1990s. The macroeconomic component reflects the new value that the region's gov-

[1] A very approximate calculation based on information in various numbers of ECLAC's *Statistical Yearbook for Latin America and the Caribbean*. Generally these figures exclude self-employed workers.

ernments have put on macroeconomic balances as a consequence of the hyperinflation and very large deficits during the years of the debt crisis. Bringing inflation rates down to the single-digit level became a priority in many countries; to accomplish this, budget deficits were slashed. A key point for the labor markets discussion is that budget equilibrium was frequently attained by cutting expenditures rather than raising taxes. Another instrument that has been used in the battle against inflation is fixed or semifixed exchange rates, leading to real appreciation of local currencies, which has had the negative side effect of enlarging balance-of-payments deficits and leading to stop-go growth cycles based on the availability of external financing.

The structural reforms can be grouped in two main categories. First were changes designed to increase the integration of the region into the world economy. These included liberalization of imports (lowering tariffs and eliminating nontariff barriers) and opening the capital account of the balance of payments (liberalizing rules for foreign direct investment, and eliminating barriers to the entry and exit of short-term capital).

The other set of reforms aimed to lower the role of the government in the economy and to give greater emphasis to market forces. A crucial aspect of this process was the reform of the domestic financial sector, whereby interest rates and credit decisions were made dependent on market forces rather than government direction. A second such reform lowered the maximum marginal rate of taxes on corporate and personal income taxes and partially replaced them with a value-added tax. Third, many state firms were sold to private entrepreneurs, either domestic or foreign.[2]

Although labor flexibility has sometimes been discussed as part of the first-generation reform package, less has been done in this area than in some others mentioned above.[3] (An important exception is Chile, which began its reform process much earlier than other countries; several other countries have recently adopted labor reform packages.) Nonetheless, despite the absence of comprehensive legislation, important changes have occurred at the firm level, taking advantage of existing exceptions in the old laws. For example, temporary contracts are now more frequent, as is job flexibility within the firm. The rationale for labor reforms has been that employers are reluctant to hire workers because of labor immobility and high taxes; limiting these would thus increase the number of jobs created. Until now, little indicates that this has happened, although the low unemployment rate in Chile might be seen as evidence in favor of the argument.

Employment Trends

One of the principal problems in the labor markets in the 1990s has been an insufficient job generation. This is reflected in the increase in unemployment in most Latin

[2] Quantitative indicators of these reforms can be found in Samuel Morley, "Measuring Structural Reform in Latin America," ECALC Working Paper on Economic Reforms, 1998.

[3] IDB, *Economic and Social Progress Report*, 1996 and 1997.

American countries in recent years. In 1996, the rate of open urban unemployment reached an average of 7.7 percent, compared to 5.9 percent in 1990. This masks the double-digit levels in a number of countries: Argentina, Colombia, Uruguay, Venezuela, and several Central American and Caribbean nations. (Unemployment rates generally fell slightly in 1997, but are expected to rise again this year.) It is important to note that this increase in unemployment occurred despite the fact that the total work force is increasing at a slower rate in the 1990s than in the 1980s.[4]

Another way of describing the same problem is to look at the relationship between the growth rate of gross domestic product (GDP) and growth of employment. In the 1980s, a 1 percent GDP growth resulted in a 2.6 percent increase in employment. In the 1990s, by contrast, 1 percent GDP growth produced only a 0.6 percent rise in employment. As a result, the economies must grow by about 4 percent per year in the 1990s for unemployment not to increase; in the 1980s the figure was only 1 percent.

Why have these differences occurred? One reason is that, as governments have restructured to increase their efficiency and lower their costs, they have reduced the size of their work force. Thus, public-sector employment has fallen as a share of the total during the 1990s. In a similar way, newly privatized firms have fired workers who were considered to be "redundant." Contrary to (perhaps overly optimistic) assumptions, these newly unemployed workers have generally not been able to find jobs in other sectors. In part, their skills are not appropriate, and in part, the fastest-growing firms are the large, technologically sophisticated ones that are capital-, not labor-intensive. The smaller firms, which employ the largest number of workers, have been growing much more slowly.

This brings us to the issue of job quality and the relationship between the formal and informal sectors. The informal sector is defined in several different ways. The spirit of the concept is that, since informal firms are not legally registered, their workers lack access to various kinds of benefits. They also tend to be poorly remunerated, have low productivity, and endure sometimes dangerous working conditions. In other words, job quality is poor. In practice, this concept is difficult to measure, so economists have tended to use a proxy that equates the informal sector with work in small firms (5-10 workers, depending on the country) and the self-employed (subtracting out professionals); sometimes domestic workers are also included in the definition.

During the 1990s, the informal sector has grown much faster than its formal-sector counterpart. According to some recent data, informal employment as a share of the total rose from 51.6 percent in 1990 to 57.4 percent in 1996. An average of 80 out of 100 jobs created in the 1990s were in the informal sector.[5] The idea of work in small firms per se is not a problem; the problems derive from the low quality of employment: long hours, low pay, and few benefits.

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[4] An overview of employment trends can be found in Jurgen Weller, "La evolución del empleo en América Latina en los años noventa," ECLAC Working Paper on Economic Reforms, 1998.

[5] Eduardo Lora and Gustavo Márquez, "The Employment Problems in Latin America: Perceptions and Stylized Facts?" Paper presented at Annual Meeting of IDB, March 1998.

Wages and Wage "Gaps"

Real wages—for those who have jobs—have generally increased in Latin America during the 1990s. Important exceptions are Argentina (where real wages have been flat during the decade) and Mexico (where they increased rapidly until the "tequila crisis" but have not yet recovered); in Venezuela, real wages have fallen throughout the decade. In some cases, especially the three just mentioned plus Peru, median wages are still below their 1980 level.[6]

Within this somewhat mixed picture for overall wage patterns, two "gaps" illustrate particular problems in Latin American labor markets. One is the difference between incomes of skilled and unskilled workers. Incomes of skilled workers have generally been growing faster than those of the unskilled, or the gap has remained constant. In the nine countries of the ECLAC project, the skill differential has increased in four (Argentina, Colombia, Mexico, and Peru), remained the same in two (Brazil and Costa Rica), and fallen in only three (Bolivia, Chile, and Jamaica).

The skill differential has not been reduced in more countries for two basic reasons. First are longstanding problems in the education systems in Latin America, which tend to produce a small group of highly qualified people at the same time that the large majority does not finish secondary school. This situation, which contrasts with that in Asia and Eastern Europe, makes it possible for scarce, skilled workers to obtain a wage premium. In addition, the economic reforms of the 1980s and 1990s have almost universally led to a rise in the capital-labor ratio. That is, capital has become cheaper with respect to labor (as tariff barriers have fallen and the value of local currencies has appreciated), and capital intensity has risen. With greater use of machinery comes the need for more skilled workers and fewer unskilled.

A second "gap" produced or exacerbated by the labor markets is that between urban and rural incomes. For lack of adequate wage data, we will rely here on poverty trends. During the 1980s, the urban sector bore the brunt of rising poverty; over 70 percent of the increase in poverty during that decade was urban. Since 1990, the situation appears to have been reversed in most countries, in that poverty reduction has been primarily in the urban sector. In seven of our nine countries, there has been a smaller reduction in rural than urban poverty. In some cases, such as Mexico and Jamaica, the differences are striking.

The exceptions to this trend are Chile, Costa Rica, and Peru. In Peru, rural poverty fell between 1985 and 1994, but at the same time a large flow of rural to urban migration took place, so that rural poverty seems to have been transferred to the urban sector.

There could be two, possibly overlapping, explanations for why the rural sector seems to be lagging behind the urban in poverty reduction. In the first place, it could be that the cycles in economic activity primarily affect the modern, urban sector of the economy. If that were the case, recession in the 1980s would have been expected to increase urban poverty. Likewise, the recovery in the 1990s would sim-

[6] ECLAC, *Economic Survey of Latin America and the Caribbean, 1997–98.*

ply reverse the process, with the rural sector being somewhat insulated from these cyclical changes.

In addition, macroeconomic variables may have been at work as well. To the extent that rural economies produce traded goods, their welfare will be affected by the real exchange rate. Real depreciation of local currencies (typical of the 1980s) will boost the fortunes of the rural traded goods sector, while real appreciation (typical of the 1990s) will do the opposite.

Conclusions

The principal problem of labor markets in Latin America at the present time is that not enough jobs are being produced. For a given rate of growth, fewer jobs are being produced than in earlier decades, mainly because growth is concentrated in a small group of large, capital-intensive firms. Those jobs that are being created tend to be in the informal sector, with the associated lack of benefits and poor working conditions.

With respect to wages, the picture is slightly more mixed. Real wages have generally been rising in the 1990s, but the increases have been unequally distributed. Skilled workers have been gaining at the expense of the unskilled, and urban workers have been gaining at the expenses of their rural counterparts. In some cases, this has increased rural-urban migration.

The impact of these trends on poverty and inequality, however, is not as direct or obvious as might be expected. We know more about the causes and remedies for poverty than we do about inequality. Poverty has generally been declining in the 1990s, because of the increase in the growth rate and because of the fall in inflation (especially the elimination of hyperinflation), but it remains unacceptably high.

Inequality is much more difficult to analyze. Despite the widely held view that inequality has increased in the 1990s, this is only partially true. For example, inequality among income recipients (excluding the unemployed) appears to have declined in many countries. Even the increased skill differential has not been directly reflected in increased inequality of total income because other things have been happening at the same time.

The most important countertrend is that, in a number of countries, the profit share has been falling as a result of increased international competition or other factors. If that happens, the overall distribution of income may improve despite an increased skill differential. Also, the process of job creation and destruction may be more positive than we think. Some evidence in the Chilean case, for instance, suggests that poor-quality jobs are being destroyed and better-quality jobs are being created. In general, we need much more information and analysis on the causes of inequality.

Despite declines in poverty and some much more modest gains with respect to inequality, Latin America clearly has a long way to go in these areas. Labor markets must play a key role in improving the quality of life for citizens of the region. If this is to happen, some important policy steps need to be taken to strengthen labor

markets. These involve second-generation institutional changes. Especially important are (1) improving access to, and quality of, secondary education; (2) increasing the resources dedicated to worker training; (3) providing special assistance to small and medium-sized firms to increase their access to credit and technology; and (4) simplifying the legal procedures to bring more firms into the formal sector so as to extend benefits to their workers. Only with better-functioning labor markets can real gains be made with respect to poverty and inequality.

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