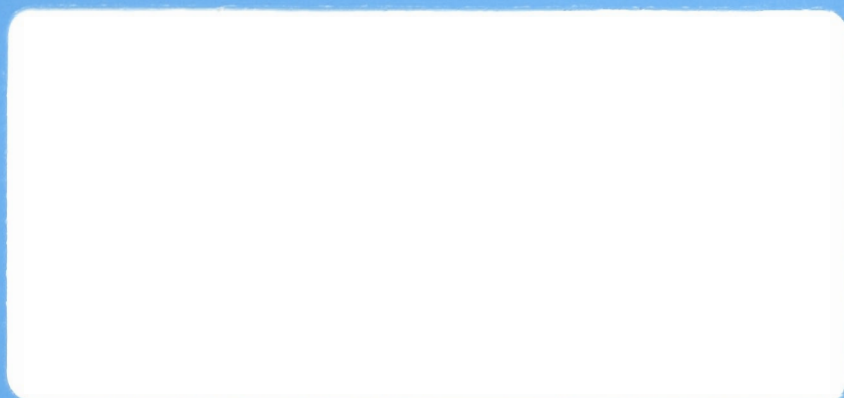




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**MACROECONOMIC POLICY, POVERTY ALLEVIATION
AND LONG-TERM DEVELOPMENT:
LATIN AMERICA IN THE 1990s**

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The views expressed in this paper are those of the author. They do not necessarily represent the views of the UNICEF International Child Development Centre.

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I. THE INITIAL CONDITIONS: LATIN AMERICA IN THE LATE 1970s

A. Economic Growth and Poverty Trends Before 1980

Despite radical reassessment of the merits of Import Substituting Industrialization (ISI) in the course of the last ten years, it is beyond question that this strategy and, more generally, the efforts of the Latin American *Desarrolismo* brought important results during the first three postwar decades in terms of the evolution of the productive structure, technological development, expansion of the industrial base as well as in terms of a growth rate which was among the most rapid in the developing world. Between 1950 and 1980, GNP per capita in the region rose 2.7 per cent (with peaks of 4.2 per cent and 3.3 per cent in Brazil and Costa Rica). GNP per capita therefore doubled during this period, a significant rise given that the population increased by similar proportions (Table 1).

Table 1: GNP PER CAPITA AND GROWTH RATES IN LATIN AMERICA

	Population (% of total)	GNP/Capita (1975 \$)		Annual Growth Rate GNP/Capita			Cumulative Drop/Rise in GNP/Capita
	1980	1950	1980	1950-80	1981-90	1991-93	1981-90
Brazil	35.6	637	2,152	4.2	-0.6	-0.2	-5.2
Mexico	20.2	1,055	2,547	3.0	-0.7	0.2	-6.4
Argentina	8.0	1,877	3,209	1.8	-2.3	6.6	-20.2
Colombia	7.5	949	1,882	2.3	1.7	1.6	17.9
Venezuela	4.3	1,811	3,310	1.5	-2.1	3.0	-19.0
Peru	5.1	953	1,746	2.1	-3.5	-0.2	-28.9
Chile	3.2	1,416	2,372	1.8	1.5	5.6	12.2
Uruguay	0.8	2,184	3,269	1.4	-0.3	3.5	-2.8
Ecuador	2.3	683	1,556	3.1	-0.7	0.9	-6.6
Guatemala	2.0	842	1,422	1.8	-2.1	1.1	-18.2
Domin. Rep	1.7	719	1,564	2.6	-0.4	0.5	-2.9
Bolivia	1.6	762	1,114	1.3	-2.4	1.0	-21.2
El Salvador	1.3	612	899	1.3	-1.5	2.1	-13.5
Paraguay	0.9	885	1,753	2.4	0.0	-0.2	0.5
Costa Rica	0.6	819	2,170	3.3	-0.6	2.4	-5.8
Panama	0.5	928	2,157	2.9	-1.5	5.5	-13.6
Nicaragua	0.7	683	1,324	2.3	-4.4	-4.0	-34.5
Honduras	1.0	680	1,031	1.4	-0.9	0.8	-8.2
Haiti	1.6	363	439	0.7	-2.3	-10.0	-20.6
Total L.A.	--	--	--	2.7	-0.9	1.4	-8.9

Sources: Dornbusch and Edwards (1991), ECLAC (1993).

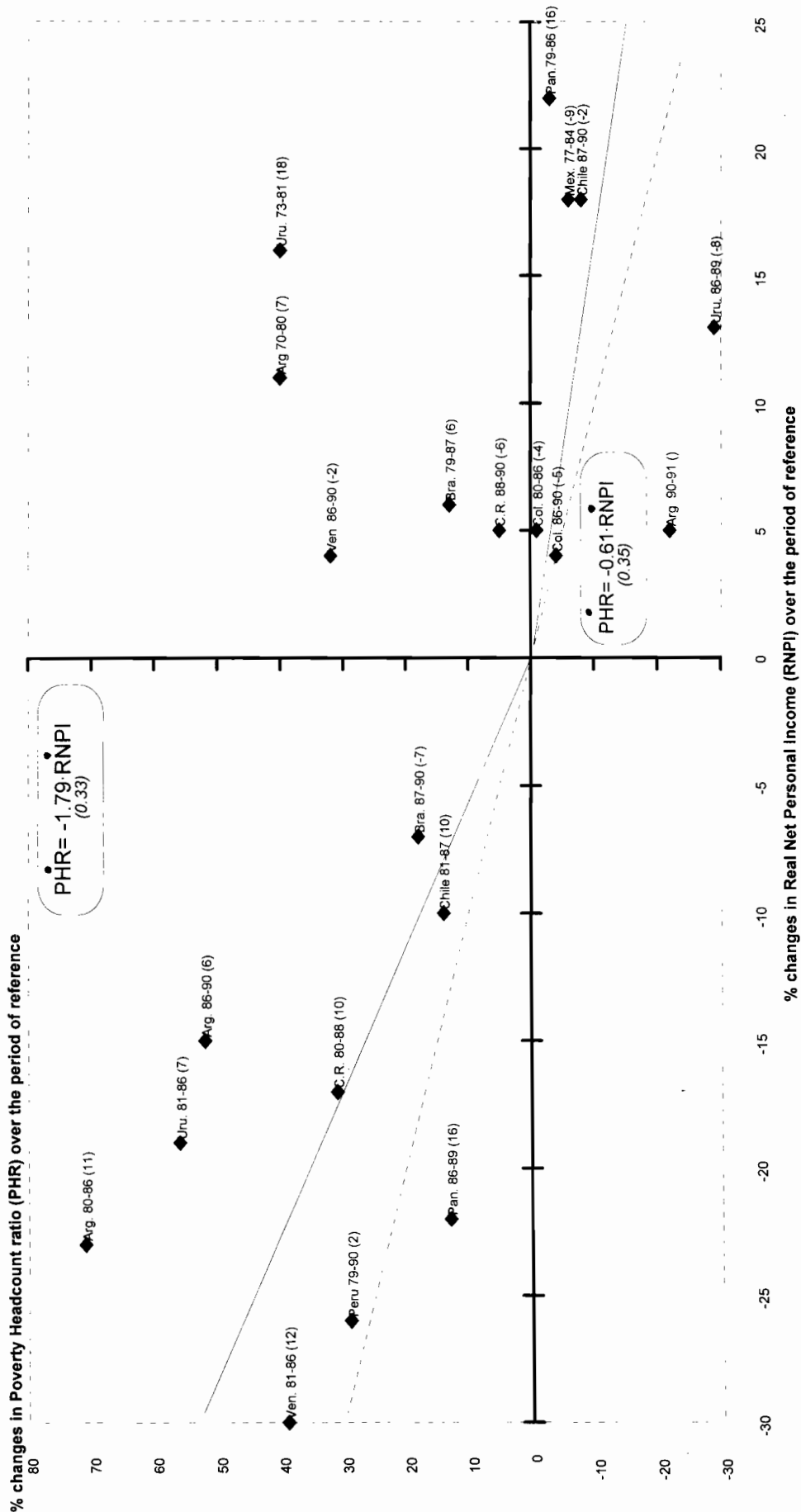
The process of industrialization and growth was accompanied in several countries by massive migration toward cities, the emergence of a Western-style middle class and a gradual, if slow, improvement in social conditions. Between the early 1950s and the early 1980s, for instance, the infant mortality rate (IMR) fell from 126 to 63 per 1,000 live births and average life expectancy increased by 13 years. By 1980 primary and secondary school enrolment rates had reached almost 100 and 40 per cent, respectively.

Despite these improvements, however, Latin American development during the first three postwar decades was marked by profound contradictions. The remarkable industrial development of the 1950s, 1960s and 1970s was only partially able to narrow the technological gap with Western economies. The external balance remained largely dependent on exports of raw materials, the prices of which were subject to notable fluctuations and to a gradual but continual decline in real terms. Furthermore, the insistence on ISI, even when its limitations had become fully manifest, not only contributed to the gradual weakening of growth and export performance but also made recourse to foreign borrowing and to growing deficit financing unavoidable, particularly after the first oil shock.

The limits of Latin American development were even more obvious in the social sector. With few but important exceptions (Chile, Costa Rica, Cuba and, to some extent, Uruguay), welfare improvements were inferior to those achieved in other developing regions or obtainable on the basis of financial and technical resources available. After 30 years of efforts, a large section of the population was still excluded from the most essential health care, potable water and social assistance services.

While it is difficult to give an accurate estimate of the extent of poverty in Latin America in the first two postwar decades, available sources indicate that between 1970 and 1980 the proportion of households living in poverty in the region only declined from 40 to 35 per cent. Similarly, the poverty gap fell marginally from 5.3 per cent of GDP in 1970 to 3.6 per cent in 1981 (ECLAC 1990c; Molina 1982). In a few extreme cases, such as during the military dictatorships of the 1970s in Chile, Argentina and Uruguay, the poverty headcount ratio increased substantially, despite a positive and significant growth in per capita incomes (see Figure 1). Though the pace of poverty reduction was extremely slow in most countries and remained an acute problem at the end of the 1970s, particularly in rural areas, these phenomena showed considerable intercountry variations. In 1980, for instance, poverty affected only between 9 per cent and 11 per cent of the population in Argentina and Uruguay (mostly urban families with unemployed or underemployed heads of household) and

Figure 1: ELASTICITY OF REAL NET PERSONAL INCOME (RNPI) vs. POVERTY HEADCOUNT RATIO (PHR) DURING PERIODS OF EXPANSION (1ST AND 2ND QUADRANT) AND RECESSION (4TH QUADRANT)*



* The dots over the variables $\dot{P}HR$ and \dot{RNPI} indicate growth rates over time; the figures in parenthesis under the coefficients indicate the standard error of estimate; the figures in parenthesis next to each country observation indicate the growth rate of the Gini coefficient over the period of reference.

indigence had practically been eradicated. In contrast, in countries such as Guatemala, El Salvador, Bolivia and Peru poverty affected as much as 65 per cent of the population in 1980. These rates were even higher in rural areas. In addition, close to 30 per cent of the population was still living in extreme poverty (termed 'indigence' in this paper).

Thirty years of almost uninterrupted growth was therefore unable to substantially modify the marked dualism, absence of democracy and technological dependence typical of Latin American society. Thus, countries of the region entered the difficult decade of the 1980s with a highly polarized economic and social structure. A new urban middle class had to coexist with traditional social groups, such as the agrarian oligarchy, the bureaucracy, the military and the *burghesia compradora*, on the one side and the rural landless, small farmers and a rapidly expanding urban lumpenproletariat on the other.

B. Main Causes of Poverty Prior to 1980

1. Insufficient capital accumulation and labour market dualism

In the 1950s and early 1960s, it was widely held that capital accumulation and economic growth would swiftly eradicate the widespread poverty and unemployment which prevailed then in nearly all Latin American countries. Yet, despite two decades of sustained GDP growth, a fairly rapid capital accumulation and a respectable 3.7 per cent growth in formal sector non-agricultural employment between 1950 and 1980, unemployment and underemployment still affected a considerable share of the labour force in 1980. In addition, differences in employment status remained a major source of social differentiation; that is, poverty rates were generally much lower among modern-sector workers than for the self-employed, the underemployed and the unemployed. During this period the proportion of labourers partially or totally unemployed only fell from 46 to 42 per cent, and the overall index of labour underutilization declined marginally, i.e. from 23 per cent of the economically active population in 1950 to 20 per cent in 1980. Three factors contributed to these unsatisfactory trends: to start with, the small size of the modern sector in 1950 meant that even relatively high growth rates could have, at least in the initial years, only limited effects in terms of employment creation; second, the 'technological dualism' and 'technological dependence' typical of ISI reduced the employment creation potential of a fairly rapid capital accumulation; third, rapid population growth (oscillating between 2-3 per cent per year)

contributed to a rapid increase in labour supply, to persistent labour market imbalances and to very slow growth in informal-sector wages (Curiel 1984).

2. Income inequality

Despite the popularity this thesis enjoyed in the 1960s, it does not fully explain the persistence or slow decline of poverty up to the late 1970s in both urban and rural areas. Indeed, already in the 1960s, most Latin American countries had reached **average** levels of labour productivity that were sufficient to eradicate all forms of destitution and the most severe aspects of poverty; a respect in which Latin America differed from the poor countries of Africa and Asia. However, the persistence of an extremely polarized distribution of income presented a major obstacle to the attainment of even minimal poverty alleviation and distributive objectives, particularly in rural areas. Overall income inequality remained well above levels observed in other developing areas over these three decades. For instance, in the late 1960s-early 1970s the decile ratio in Latin America was on average 2.5 times greater than in the developing nations of East and South-East Asia (Table 2). In extreme cases (Peru and Ecuador, for instance), it was four to five times greater.

Table 2: INCOME DISTRIBUTION IN LATIN AMERICA AND EAST ASIA*
(late 1960s and early 1970s)

	Lowest Decile	Highest Decile	Ratio		Lowest Decile	Highest Decile	Ratio
Argentina	4.4	50.3	11.4	China	7.0	39.0	5.6
Brazil	2.0	66.6	33.6	Hong Kong	6.0	49.0	8.2
Chile	4.5	51.3	11.4	South Korea	6.6	49.4	7.5
Colombia	2.8	59.4	21.2	Malaysia	3.5	56.0	16.0
Ecuador	1.8	72.0	40.0	Philippines	3.9	53.0	13.6
Mexico	4.2	63.8	15.1	Singapore	6.5	49.2	7.6
Peru	1.9	61.0	32.1	Taiwan	8.8	37.2	4.2
Uruguay	4.4	47.5	10.8	Thailand	5.6	49.8	8.9
Venezuela	3.0	54.0	18.0				
<i>Average</i>	3.2	57.7	21.1	<i>Average</i>	6.0	47.5	8.7

Source: Kaufman and Stallings (1991).

* Based on data from family income surveys carried out in the late 1960s and early 1970s.

These acute distributive imbalances were deeply rooted in pervasive market failures as well as in a highly unequal distribution of land, other assets and educational opportunities which benefited a tiny agrarian, mining and commercial oligarchy. In addition, modification of this highly unequal income distribution could not be sought through redistributive fiscal policies because of the capacity of this oligarchy and other high-income groups to resist any type of direct taxation. More specifically, high income inequality in the region could be traced to the following factors:

i) *Land concentration and factor market distortions.* Due to the long colonial history of the region, the rural sector in Latin America was traditionally dominated by a highly polarized distribution of land (well illustrated by the coexistence of latifundia and minifundia), widespread landlessness, lopsided sharecropping and tenancy arrangements, and agrarian institutions among the most inequitable in the world. In the 1950s and 1960s, the Gini coefficient of land distribution oscillated between 0.6 and 0.8 (as opposed to 0.3-0.5 in Asia and Africa). In extreme cases, such as Bolivia, Chile and Peru, the top 20 per cent of rural households respectively controlled 98.7, 90.4 and 94.4 per cent of farmable land (Jazairy et al. 1992). As highlighted by a substantial number of analyses (see, for instance, El-Ghonemy 1990), the extent of rural poverty was closely related to the incidence of landlessness, capital and insurance market imperfections and distortions in the marketing of agricultural products. In Brazil and Colombia, for instance, the incidence of poverty in the 1960s was highest among landless farmers, while in Peru it was most pronounced among small-scale subsistence farmers with limited access to both land and credit (Cardoso and Helwege 1991, Jazairy et al. 1992).

Access to the land was, and still is, the most serious problem faced by the rural poor in most Latin American countries (highly urbanized, land-abundant countries - such as Argentina - may be an exception.) Thus, despite a greater average availability of land per agricultural worker (see the first column of Table 3) and higher average per capita incomes (including in rural areas), a land concentration close to the theoretical maximum caused the incidence of landlessness and rural poverty to rise to much higher levels than elsewhere (Table 3).

Table 3: LAND CONCENTRATION AND RURAL POVERTY
(Circa 1980)

	Hectare per Farm Worker (1981-4)	Gini Index of Land Concentration	Landless in Total Rural Families (%)	Per Capita GDP (\$, 1982)	% of Rural Population in Poverty	Year
Pakistan	1.4	0.539	31	190	39	1978
Thailand	0.8	0.460	10	213	34	1978
Indonesia	0.7	0.620	36	254	44	1980
Egypt	0.5	0.430	24	282	18	1982
Honduras	1.4	0.780	33	283	58	1980
Philippines	1.2	0.530	37	413	42	1982
Jamaica	0.8	0.815	41	546	51	1981
Panama	2.8	0.840	20	564	30	1978
Brazil	6.0	0.859	39	658	67	1980
South Korea	0.4	0.301	4	806	10	1980
Paraguay	11.4	0.939	27	1,161	63	1980
Venezuela	5.1	0.920	27	1,553	56	1980

Sources: Column 1: Alexandratos (1988), Columns 2-5: El-Ghonemy (1990).

It is important to underscore that an unequal distribution of land affects poverty over both the short and the long term. In the short term, poverty increases because of the appropriation of an excessive share of agricultural output by the landlords. Over the long term, a high degree of land concentration contributes to the persistence of high levels of poverty, or to its increase, due to the generally slower growth of agricultural production than would be the case with smallholder agriculture. Indeed, as shown in numerous studies (Griffin 1976, Berry and Cline 1979, Cornia 1985), in **economies with surplus labour**, the higher transaction costs borne by large farms and the dualism prevailing on factor markets (entailing substantially lower labour costs on small-scale, family-run farms than on large farms) mean that small-scale farms exhibit higher yields per hectare and greater total factor productivity than large farms (which are characterized by a lower intensity of cultivation and labour inputs per hectare). Because of this 'inverse relationship' between farm size and land productivity, a more egalitarian distribution of land tends to be accompanied not only by a lower income inequality over the short term but also by a faster growth of output over the medium term.

ii) *Policy biases.* A discussion of the impact of past policy biases on income distribution and overall poverty should be carried out within the wider context of the 'urban bias paradigm'. It would therefore require an extensive analysis of past exchange rate policies, pricing policies for inputs and products, taxation and public expenditure, and saving and investment flows. While such an extensive review is outside the scope of this study, available evidence on pricing biases prior to the 1980s points to moderate distortions in the ratio of producer to border prices and to much larger distortions in the foreign trade area. Indeed, overvaluation of the exchange rate and protectionism which were typical of ISI severely depressed rural incomes and incentives. Even the reformist regimes of Velasco and Cardenas, who promoted agrarian reforms in Peru and Mexico, followed price and credit policies that favoured the urban sector, including high minimum urban wages, price controls on food and protectionist policies (Cardoso and Helwege 1991).

The evidence is even more conclusive in the field of taxation and public expenditure. With the exception of Mexico and a few other countries, the share of agriculture in total government expenditure in the 1960s and 1970s generally oscillated around 5 per cent of the total, even though agriculture accounted for between 30 and 40 per cent of total output (Jazairy et al. 1992). Similarly, the proportion of overall government expenditure of any type allocated to rural areas oscillated between 11 and 18 per cent, though rural population accounted for 45 to 80 per cent of the total (ibid). Furthermore, the pattern of public expenditure in rural areas reinforced inequalities associated with ecological factors, location and control over resources. By and large, public expenditure on road and transport infrastructure, input subsidies, extension and R&D, irrigation and human resource development favoured large-scale farmers at the expense of the peasantry. For instance, despite the fact that smallholders represented the overwhelming majority of the rural population, they received only one third of rural public expenditure in Brazil and a quarter in Mexico and Jamaica in the 1970s (Jazairy et al. 1992). Only in Costa Rica did smallholders receive a share of rural public expenditure (about 60 per cent) commensurate to their numbers.

Institutional distortions and market failures, particularly pronounced in the case of credit and technology, contributed to a high incidence of poverty in both urban and rural areas. Small farmers and informal-sector enterprises typically functioned in conditions of more limited access to and substantially higher costs of credit, intermediate inputs and support services (in the field of training, R&D and commercialization) than large farmers and

modern-sector enterprises. For instance, small urban-based businesses were subject to average real interest rates (on informal credit markets) which were two to three times higher (in Colombia and El Salvador) or even eight times higher (in Mexico) than those prevailing in the modern sector (Haggblade et al. 1990).

3. Inadequate and inequitable access to education

The high incidence of poverty and unequal income dynamics of the 1950s and 1960s can also be traced to the inadequacies and biases of public policy in the field of education. While insufficient public expenditure on education influenced the overall level of labour productivity over the medium term, its distribution among levels of education, areas, sexes and income groups affected average productivity, income inequality and the risk of poverty of specific social groups.

Particularly in urban areas, low productivity, low earnings and a high risk of poverty were, and still are, closely correlated (after controlling for other variables) to the level of education of the head of household. Thus, a nine-country study on the relative impact of various factors in explaining income inequality and the risk of poverty found that differences in educational achievements dominated over other characteristics of the labour force, such as employment category, sector, age and gender (Altimir and Pinera 1979). Similarly, a study on income distribution in Brazil showed that differences in educational achievements in 1960 explained 35 per cent of income inequality, while the employment sector and age accounted for only 17 and 13 per cent respectively (Langoni 1973). In 1970 education explained an even larger proportion (46 per cent) of total income inequality.

In rural areas, in contrast, the level of education of the head of household was found to be positively correlated with labour productivity and negatively correlated with poverty only in those areas where modern inputs and farming practices were being introduced (Cotlear 1989). Finally, both in urban and rural areas, women's level of education showed a negative correlation with the risk of poverty faced by the household, as more highly educated women not only tended to have greater earnings but also had lower fertility and better skills for managing family resources.

With the increase of primary and secondary enrolment rates in the 1960s and 1970s, it is likely that the importance of education as a cause of poverty decreased, although

differentials in educational achievement continued to play a key role in the determination of inequality.

II. CHANGES IN THE EXTENT, NATURE AND CAUSES OF POVERTY IN THE 1980s

A. Poverty Dynamics in the 1980s

Contrary to the situation of most developing regions, national household surveys, offering a relatively accurate picture of the dynamics of poverty, have been available in Latin America for several years and for 19 countries, representing about 95 per cent of the population of the region (Altimir 1987). Though not all of these surveys provide national coverage of income formation and expenditure, they are generally considered sufficiently reliable. Moreover, they are subject to regular adjustments to correct for the underreporting of income and other biases (ECLAC 1990c). The data they provide unambiguously indicate that the slow decline in poverty observed between 1950 and 1980 was abruptly reversed at the beginning of the 1980s. During this decade, nearly all countries in the region registered a rise in the proportion, as well as the absolute number, of poor families. For the region as a whole, the proportion of **poor households** in the total grew from 35 per cent in 1980 to 37 per cent in 1986 and 39 per cent in 1990. As poor households are on average larger than middle- and higher-income households, the proportion of **poor persons** grew from 41 per cent in 1980 to 43 per cent in 1986 and 46 per cent in 1990. Population growth during this period meant that the increase in the absolute number of poor people was even more marked, climbing from 136 million in 1980 to 196 million in 1990 (Tables 4 and 6). The number of indigents (that is, individuals living in extreme poverty) jumped from 62 million to 93 million.

This phenomenon did not affect all countries, sectors and segments of the population in the same way. Indeed, poverty became far more heterogeneous in the 1980s than it had previously been. Firstly, those nations which were less affected by recession, including Colombia, Panama and, to some degree, Mexico, were able to sustain the downward trend in the incidence of poverty that had been recorded during the earlier postwar years (Tables 4 and 6).

Second, with few exceptions, the incidence of poverty in rural areas continued to decline, although at a slower rate than previously. This should not be surprising since

Table 4: THE INCIDENCE OF POVERTY AND THE ABSOLUTE NUMBER OF THE POOR^a

	1970	1980	1986	1990
<i>A. Poverty Incidence among Households (percentages)</i>				
Rural areas	62	54	53	53
Urban areas	26	25	30	34
Total	40	35	37	39
<i>B. Number of Poor Individuals (in millions)</i>				
Rural areas	71	73	76	80
Urban areas	42	63	94	116
Total	113	136	170	196

Source: ECLAC (1990c), Tables 10 and 11, and ECLAC (1992).

^a Including indigents.

most of the adjustment programmes of the 1980s aimed at correcting some of the earlier anti-rural policy biases by introducing price incentives for agricultural products, devaluing the real exchange rate and eliminating implicit subsidies for foodstuffs; that is, measures which modified the internal terms of trade in favour of agriculture and *ceteris paribus* raised farm incomes relative to urban incomes. In addition, the structural adjustment programmes generally succeeded in boosting the export of non-traditional agricultural products. At the same time, however, rural incomes were affected by the fall in international prices for traditional exports. Sugar, coffee and cacao prices plummeted by 42-53 per cent between 1980 and 1990, while an average slump of around 20 per cent was recorded for the prices of wheat, maize, soya, fishmeal, wool and cotton (ECLAC 1990a).

The above policies on poverty reduction would have had a more positive impact if the distribution of land and other assets had been more equitable and the dependence on traditional raw material exports less pronounced. Indeed, the extent to which the rural poor have benefited from these policies remains uncertain. The limited evidence available for Chile, Costa Rica, Mexico and Uruguay shows, in fact, that real agricultural wages declined over the 1978-87 period (Jazairy et al. 1992). As a result of these trends together with the continued migration toward the cities and the adverse poverty dynamics in urban areas, the absolute number of the poor in urban areas surpassed that in rural areas in the 1980s. However, the percentage incidence of poverty remained vastly more alarming in the

countryside. This tendency can be seen even more markedly in the case of indigents, whose absolute number and relative incidence remained much higher in rural areas than in cities. Small-scale subsistence farmers, landless labourers, small-scale sharecroppers and farmers renting their farmland under unfavourable conditions were, and still are, among these 'wretched of the earth'.

Third, particularly during the first half of the 1980s, the incidence of poverty rose significantly in urban areas where the formal sector, more heavily struck by the austerity measures, was more developed. This rise in poverty was dramatic in Chile, Guatemala, Peru, Venezuela, and even Argentina. As a result of this trend and the increasing urbanization, poverty, in absolute terms, became a predominantly urban phenomenon. In 1986, 55 per cent of the poor were living in urban centres, and by 1990 this figure had reached 60 per cent (ECLAC 1991).

Fourth, the crisis deeply affected low income groups through employment, incomes and relative price effects. Thus, the thesis that "the poor were so poor that they did not even have access to the recession" was proven incorrect. However, unlike in the first three postwar decades, poverty in the 1980s also affected important segments of the lower-middle and middle classes in cities, including blue-collar workers in the modern sector, white-collar workers, small-businessmen and professionals. At the end of the 1980s, for instance, approximately 10 per cent of the professionals and skilled workers of Brazil, Chile and Mexico were living in poverty (ibid). Even more surprising is the fact that in the 1980s the incidence of poverty among formal-sector workers was similar to that of the self-employed and underemployed. In contrast, and despite the severity of the crisis, the incomes and consumption of the richest 5 per cent of the population continued to climb in nearly all countries of the region during this decade.

Fifth, with the exception of Argentina, the decline in urban poverty during the period of expansion was much slower (in relation to the increase in net income per capita) than its increase during the recession. The average regional elasticity of the poverty headcount ratio *vis à vis* the net income per capita was in fact equal to 1.78 during the years of recession (broadly corresponding to the 1980-87 period) and to only 0.61 during the years of recovery. This suggests that future economic expansion will have to be three times as pronounced to reabsorb the surge in poverty which occurred during the recession (see Figure 1).

In a few extreme cases, such as in Venezuela, Costa Rica and Brazil, the poverty headcount ratio grew even during the recovery (see Table 5 and Figure 1). This asymmetry

is most likely the result of structural changes involving the labour market, the distribution of assets and the redistributive role of the State during the 1980s (see later).

Table 5: ELASTICITY OF THE POVERTY HEADCOUNT RATIO *Vis À Vis* NET INCOME Per Capita (urban areas)

Country	Period	Economic Phase	Elasticity
Argentina	80-86	Recession	-3.09
	86-90	Recession	-3.47
	90-91	Expansion	-4.40
Brazil	79-87	Rec-Exp	2.17
	87-90	Recession	-2.14
Colombia	80-86	Expansion	0.00
	86-90	Expansion	-0.75
Costa Rica	80-87	Recession	-1.82
	87-90	Expansion	1.00
Chile	81-87	Recession	-1.40
	87-90	Expansion	-0.44
Panama	87-90	Expansion	0.14
	79-86	Expansion	-0.59
Uruguay	81-86	Recession	-2.95
	86-89	Expansion	-2.23
Venezuela	81-86	Recession	-1.30
	86-90	Expansion	8.00

Source: Author's estimates based on Altimir (1993).

Sixth, an examination of indigence trends reveals changes similar to those observed for poverty. Thus, there was a sharp reversal of earlier tendencies beginning in 1980, with a relatively more rapid rise in the proportion of indigents in urban areas. Nonetheless, at the end of the 1980s this phenomenon was still more widespread in rural areas (Table 6). In addition, while with few exceptions rural poverty declined or stagnated, rural indigence grew steadily, thereby revealing the limitations of the poverty alleviation policies followed in the 1980s for the rural sector.

Table 6: THE INCIDENCE OF POVERTY AND INDIGENCE IN SELECTED COUNTRIES*
(In Percentages)

Country	Year	Poor Families			Indigent Families		
		Urban	Rural	Total	Urban	Rural	Total
Argentina	80	7	16	9	2	4	2
	86	12	17	13	3	6	4
Bolivia	90	50	-	-	-	-	-
Brazil	79	30	62	39	10	35	17
	86	34	60	40	13	34	18
	90	39	56	43	17	31	20
Chile	70	12	25	17	3	11	6
	86	37	45	38	13	16	14
	90	34	36	35	11	15	12
Colombia	80	36	45	39	13	22	16
	86	36	42	38	15	22	17
	90	35	-	-	12	-	-
Costa Rica	81	16	28	22	5	8	6
	86	21	28	24	6	10	8
	90	22	25	24	7	12	10
Guatemala	80	41	79	65	13	44	33
	86	54	75	68	28	53	43
	90	-	72	-	-	45	-
Honduras	86	53	81	71	28	64	51
	90	65	84	75	38	66	54
Mexico	77	--	--	32	--	--	10
	84	23	43	30	6	19	10
Panama	79	31	45	36	14	27	19
	86	30	43	34	13	22	16
	90	34	48	38	15	25	18
Paraguay**	86	46	-	-	16	-	-
	90	37	-	-	10	-	-
Peru	79	35	65	46	12	37	21
	86	45	64	52	16	39	25
Uruguay	81	9	21	11	2	7	3
	86	14	23	15	3	8	3
	89	10	23	15	2	8	3
Venezuela	81	18	35	22	5	15	7
	86	25	34	27	8	14	9
	90	33	38	34	11	17	12

Source: ECLAC (1990c) and ECLAC (1992).

* According to the definition adopted by ECLAC, 'indigents' are those individuals whose income is inadequate to satisfy minimum daily nutritional requirements (estimated by FAO and WHO to be approximately 2,200 calories and 35 grammes of protein for an adult). On the other hand, a 'poor' individual is one whose income is inadequate to meet minimum daily nutritional requirements and other basic needs, such as sufficient hygiene, clothing, education, transportation, and so on. The value of the poverty line is around twice the value of the threshold used for indigents in urban areas and is about 60 per cent higher in rural areas. ** Refers only to metropolitan areas.

B. Causes of the Surge in Poverty in the 1980s

1. The persistence of old causes of poverty

Few of the structural biases and problems responsible for the high incidence of poverty in the region in the past were eliminated or lessened in the 1980s. This decade even witnessed some deterioration in these structural biases. For instance, radical changes in asset ownership were not initiated over this period, except in revolutionary Nicaragua. In Mexico, the recent reform of the *ejido* system is likely to have uncertain or even adverse distributive effects (Heath 1992).

While, as noted, improvements in the terms of trade of agriculture and a more balanced allocation of public expenditure in favour of the rural sector may have reduced the anti-rural bias of earlier policies in most countries, the persistence over time of highly unequal agrarian structures, the considerable dependence on a few agricultural exports and the still high rate of increase of rural labour supply sharply reduced the distributive and efficiency gains of these measures.

At the same time, labour market dualism has become more accentuated, access to education has remained as inequitable as in the past (though school enrolments have not, on average, worsened) and the skill level of a person still exerts a significant influence on his or her risk of becoming poor. A ten-country study, for instance, found that differences in educational achievements still represented the single most important contribution to income inequality in 1989. In the same year, the probability of an illiterate person belonging to the bottom 20 per cent of the income distribution was 2-3 times greater than that of a person who had completed primary education and five to 13 times greater than that of people with 12 years of schooling (Fiszbein and Psacharopoulos 1992).

2. Cyclical factors affecting poverty during the 1980s

i) *Economic stagnation and recessionary adjustment.* The sharp recession of the first half of the 1980s and the stagnation which followed severely depressed incomes per capita and exerted a strong upward pressure on poverty rates. As indicated in Table 5, the poverty headcount ratio in urban areas increased during the years of recession, with elasticities *via à vis* income per capita ranging between 0.6 for Panama and 3.4 for Argentina. Only few

countries, including Colombia, Paraguay and, since 1987, Chile, were able to escape the region-wide recession and avoid a negative performance in terms of GNP per capita (Table 1) and poverty alleviation.

In view of the policy mistakes of the past and the exogenous shocks which affected the demand for Latin American exports in the early 1980s, their terms of trade, the interest rates on the Latin American debt and capital flows to the region, the downturn of the 1980s and the parallel increase in poverty were, according to many analysts, unavoidable.

Several observers contend, however, that theoretical flaws inherent to the adjustment policies pursued in the 1980s were an important contributory factor to the surge of poverty during that period. While macroeconomic adjustment was certainly desirable and unavoidable, the features of both orthodox and heterodox stabilization as well as the erratic modalities with which these reforms were often carried out (with costly and failed stabilization attempts followed by expansionary policies which led to high inflation and further recession) meant that poverty rose faster than it would have as a result of the exogenous shocks alone of the early 1980s.

Without exception, the **orthodox stabilization programmes** (see Table 7) introduced in the first half of the 1980s were characterized by short duration (one year, as in the case of most IMF programmes); the predominance of highly restrictive fiscal, wage and monetary measures; and limited attention, because of their supposed short-term nature, to distributive and poverty problems. In approximately 40 per cent of cases, orthodox programmes included measures, such as exchange rate devaluations, price incentives and other inducements, designed to raise the relative prices of traded goods *vis à vis* those of non-traded goods in order to stimulate their production and export.

During the second half of the 1970s and the first half of the 1980s a few countries (such as Argentina and Chile) adopted an extreme version of this type of programme which was characterized by a total liberalization of external trade and capital flows, a highly restrictive credit and fiscal policy and the absence of any attention whatsoever to the social side-effects of these measures. Such an approach was generally taken up by military regimes which were anti-democratic, often openly repressive and responsible for the rapid growth of external debt in the 1973-80 period. The total lack of control on capital flows, accompanied by a fixed nominal exchange rate or a phased devaluation and high interest rates, which were typical of this approach, favoured enormous speculation and capital flight, thereby laying the groundwork for the debt crisis of the 1980s.

During the same period a more modest number of longer-term programmes were undertaken, usually with the support of the World Bank (see Table 7). These programmes included interventions aimed more at the supply side, such as financial-sector reform, the restructuring of key economic sectors, savings incentives, price incentives (particularly in agriculture) and import liberalization. Although they also included monetary and fiscal measures and shared the liberal philosophy of the stabilization approach, these programmes, like the structural and sectoral adjustment programmes (SAL and SECAL) of the World Bank, differed from those of the IMF in their greater emphasis on the elimination of the structural causes of macroeconomic imbalances through supply- and efficiency-enhancing measures.

Table 7: ADJUSTMENT PROGRAMMES IN THE 1980s
(by year)

	In Cooperation with the IMF	In Cooperation with the World Bank	Total
Argentina	83 84 85 86 87	86 87 89	8
Barbados	82 83		2
Bolivia	80 86 87	80 86 87 88	7
Brazil	83 84 88	84 86 88	6
Chile	83 84 85 86	85 86 87 88	8
Colombia		85 86 88	3
Costa Rica	80 81 82 85 87 88	83 85 89	9
Ecuador	83 85 86 88	86 88	6
El Salvador	82		1
Guatemala	83 88		2
Guyana	80 81	80 81	4
Haiti	82 83	87	3
Honduras	80 81	89	3
Jamaica	81 82 83 84 85 86 87 88	80 81 82 83 85 87	14
Mexico	82 83 84 85 86 89	83 86 87 88 89	11
Panama	80 81 82 83 84 85	84 87	8
Peru	80 82 83 84		4
Uruguay	83 85 86	84 87 89	6
Venezuela	89	89	2
Total L.A.			107

Source: Stewart (1991).

The monetary approach to balance-of-payments stabilization proved to be particularly recessionary as it tended to achieve macroeconomic balance mainly through demand management measures. For instance, the Economic Commission for Latin America and the Caribbean (ECLAC 1990b, page 50) estimates that:

...in order to improve the trade balance by \$100 billion in three years [1981-4], the region sacrificed a total of some \$250 billion in lost product: that is to say, two and a half dollars of domestic production were sacrificed in order to save one dollar of foreign exchange. This means that any efficient combination of tariff surcharges or special export subsidies which saved or generated one dollar of foreign exchange at a lower cost than that amount of lost production would have been preferable to the adjustment policy which was actually followed.

In addition, as evidenced by the allegedly 'successful' Chilean and Mexican experiences, the monetary approach to the control of inflation generated a number of unexpected monetary and fiscal side-effects which required that austerity measures be kept in place for a number of years (up to seven years in at least one instance) in order to bring inflation down to below the accepted threshold of 20 per cent per year (Solimano 1992). Moreover, the fiscal cuts part of the orthodox approach and the transfer abroad of a large amount of resources (equivalent to 5-6 per cent of GDP each year) to meet higher debt servicing obligations led to a severe contraction in public investments (Solimano 1992, Servén and Solimano 1993). Contrary to the expectations of the proponents of the 'crowding out' hypothesis, the drop in public investments had, in turn, a negative effect on private-sector investment, particularly when the decline of the former was not accompanied by an easing of monetary restrictions to the private sector. This was the case of Chile in the early 1980s, when the drop in public investment was accompanied by a surge of real interest rates to 37 per cent. As a result, the overall investment rate for the whole region fell from 22.6 per cent in 1973-81 to 17.3 per cent in 1982-89 and down to 15.7 per cent in 1990 (ECLAC 1991; see also Table 12).

The **heterodox adjustment programmes** adopted in 1985-6 in Argentina, Brazil and Peru (Taylor 1988) did not lead to better medium-term results. Such programmes were implemented immediately after the failure of orthodox stabilization programmes, which, while usually leading to serious recessions and to a massive underutilization of the labour

force and installed capacity, had also cut fiscal deficits and improved the level of foreign exchange reserves, thereby setting the stage for more expansionary policies.

In the words of Dornbusch and Edwards (1991, p. 9) - two of the most severe critics of what they have termed 'macroeconomic populism' - "[The heterodox approach] is an approach to economics that emphasizes growth and income redistribution and deemphasizes the risks of inflation and deficit finance, external constraints and the reaction of economic agents to aggressive nonmarket policies [such as wage and price freezes]." Reactivation and redistribution were to be achieved through increases in real wages and public expenditures which were supposed to boost aggregate demand and supply. As stressed by the debate on 'multiple real equilibriums', the inflationary and balance-of-payment pressures which might otherwise have resulted from this fiscal stimulus were to be restricted by the drop in average and marginal production costs and in the profit rate per unit of value added. This was to be made possible by the ample excess capacity available as well as by the concurrent freeze on prices, tariffs and wages, the stability of the nominal exchange rate, a swift reduction in interest rates and by the high level of foreign reserves.

The heterodox approach emphasized little direct redistribution. However, while fiscal policies were neutral or only moderately progressive, the poor were to benefit from lower inflation and from the reactivation of the economy. This was expected to generate more jobs, higher wages and more demand for the goods produced in the informal sector or by small farmers.

For the first two years after their introduction, the Austral, Inti and Cruzado Plans led to a more satisfactory growth in GDP and decline in inflation than those achieved under the orthodox approach. Nonetheless, heterodox adjustment has come under fire for several reasons: because of its inability to control inflation over the medium term as aggregate demand increased far more rapidly than supply; because of the difficulties encountered in boosting investments and the supply of wage goods; and because wage and price freezes met with unsatisfactory results. Indeed, in the medium term, the supply of various goods shrank and inflation began to rise once more because of a large public deficit financed by an expansion in the money supply. In addition, the heterodox model did not succeed in increasing exports, nor could it avoid a drop in foreign reserves and capital flight.

Perhaps the most serious criticism levelled at the heterodox approach concerns the fleeting nature of the improvements achieved in redistribution in favour of wages and agricultural incomes, even though improvements in these areas were one of the principal

goals of the approach. While wage increases and agricultural price incentives substantially boosted real incomes among the low- and middle-income groups and enhanced the agricultural terms of trade over the short run, a weak fiscal and monetary policy and the inability to control inflation generated a rapid erosion in the real value of wages, agricultural incomes and social expenditures over the medium run. In Peru, for instance, real wages, which had grown by almost 50 per cent during the first two years of the Inti Plan, lost 70 per cent of their value over the following 18 months (Mesa Lago 1991).

ii) *The instability of recovery.* The prospects for poverty alleviation during the latter part of the decade were also affected by the peculiar characteristics of the adjustment process in Latin America. More specifically, the huge drop in investment and the narrow scope of fiscal policy, which were typical of the adjustment process in the region, caused a severe growth instability during the recovery phase of the economy.

As noted above, stabilization was accompanied by a drop in investment expenditure which was far greater than that recorded for other components of aggregate demand. This investment slump, in turn, negatively affected the creation of new installed capacity, opportunities for technological innovation and the duration of recovery at the end of each downturn phase (Serven and Solimano 1993, French-Davis n.d.). Indeed, growth was often quickly paralysed by the inadequacy and obsolescence of installed capacity. While an excessive drop in public investments was at the root of this 'stop-go process', balance-of-payments problems also played an important role in the decline of the overall investment rate. Indeed, imports of investment goods were sharply reduced by the limited success of the policies undertaken to stimulate non-traditional exports, by the deterioration of the terms of trade of traditional exports and by the high cost of debt servicing.

In addition, the difficulties encountered in reducing inflation added to the 'stop-go' problems induced by a weak capital accumulation. The serious drain on public funds due to debt servicing, as well as the absence of an effective tax reform aiming at increasing government revenues, fuelled the tendency toward deficit spending and the monetization of the deficit, despite drastic cuts in public expenditure. The recurrent episodes of inflation and fiscal crises which followed from these decisions thus called for further stabilization measures. These, in turn, exacerbated the halting pace of recovery. This syndrome highlights the limitations on the scope for lowering primary public spending and the problems linked

to the closure of the fiscal deficit mainly through interventions on the expenditure side (Reisen and Van Trostenburg 1988).

3. Worsening income distribution

Contrary to the claim that '....in the 1980's, [the] Latin American countries exhibited virtually constant inequality' (Fields 1992) or to the view held by the proponents of the 'immiserizing growth theory', according to which the 'fast growth - greater inequality' relation which had prevailed in the region in the past would be reversed by the severe recession of the 1980s, there is incomplete but important evidence that income distribution worsened during this period in several countries, thus compounding, in some cases permanently, the poverty impact of declining GDP per capita. Indeed, while a detailed analysis of changes in income distribution during the 1980s is rendered difficult by the limited availability of annual household income surveys (which are usually conducted every three or four years in most countries, and even less frequently in some), available evidence points to a generalized deterioration in income inequality during the recessionary periods and to various tendencies during the periods of recovery and expansion. In particular, Table 8, which provides 52 observations of urban, rural and overall changes in income inequality over the 1980s, shows that:

- only Colombia shows a definite improvement in both urban and rural income distribution;
- in the rural sector of Costa Rica and the urban sector of Uruguay, income inequality rose during the recession and declined by broadly the same amount during the recovery;
- in the urban sector of Costa Rica, Chile and Venezuela, the increase in income inequality recorded during the periods of recession and adjustment was followed by a more limited decline during the recovery, so that income inequality was more pronounced at the end of the 1980s than at its beginning; and
- in Argentina, Brazil and Mexico (between 1984 and 1989), Peru (between 1986 and 1990), Panama and Venezuela (rural sector), income inequality appears to have increased throughout the decade, both during the contraction and the expansion of the economy.

Another study on changes in income inequality during the 1980s broadly confirms these findings while showing that income inequality also worsened in Bolivia and remained broadly unchanged in Honduras and Guatemala (Fiszbein and Psacharopoulos 1992).

Table 8: PERCENTAGE CHANGES IN INCOME INEQUALITY IN 10 LATIN AMERICAN COUNTRIES IN THE 1980s

Country	Period	Phase	Urban Sector* Gini	10/40**	Rural Sector Gini	10/40	Overall Gini	10/40
Argentina	80-86 85-90	Recession Recession	11 6	27 33	- -	- -	- -	- -
Brazil	79-87 87-90	Recess-Exp. Recession	4 2	32 9	7 1	9 53	7 -	28 -
Colombia	80-86 86-90	Recess-Exp. Expansion	-3 -2	-16 -1	-5 -9	0 -2	- -	- -
Costa Rica	81-88 88-90	Recession Expansion	7 -6	22 -13	14 -6	3 -15	- -	- -
Chile	78-88 87-90	Recess-Exp. Expansion	- -2	23 -3	- -2	- -3	- -	- -
Mexico	84-89	Recess-Exp.	-	-	-	-	28	
Peru	86-90	Rec Exp Recession	2	5	-	-	-	-
Panama	79-89	Exp-Recess	-	-	-	-	16	66
Uruguay	81-86 86-89	Recession Expansion	7 -9	20 -19	- -7	- -12		
Venezuela	81-86 86-90	Recession Expansion	8 -4	19 -7	18 0	46 3	- -	- -

Source: Author's estimates based on Altimir (1993).

* In several cases data refers to metropolitan areas; ** data corresponds to the income of the richest 10 per cent of the population divided by that of the poorest 40 per cent of the population.

What were the causes of this fairly widespread increase in income inequality? The factors that have contributed to a temporary or structural change in income inequality are reviewed hereafter.

- i) *Structural changes on the labour market.* Given the sharp devaluations and wage restraint policies implemented during the adjustment phase of 1980-86, it is no surprise that the 'labour share' in national income declined in all countries of the region, with the exception

of Uruguay, Honduras and Brazil. Such decline continued in subsequent years (Sainz and Calcagno, 1992 Table 8). By the end of the decade the fall in the 'labour share' had exceeded 5-6 percentage points in Argentina, Chile and Venezuela and 10 percentage points in Mexico. Four structural changes underlie this trend and, possibly, explain the permanent surge in income inequality discussed above.

First, the number of jobs created between 1980 and 1985 was four million short of the number predicted on the basis of the rhythm of job creation during the 1970s. The number of the unemployed and underemployed therefore rose dramatically (ECLAC 1991). This trend was partially reversed during the second half of the 1980s, and in a few countries like Chile and Mexico the gradual reintegration of the unemployed into the labour force was nearly complete by the end of the decade.

Second, the labour market recorded a considerable 'informalization' as a large portion of new jobs created was in the informal sector, where lower productivity and wages tend to be the rule. Even during the recovery of the late 1980s, the proportion of modern-sector jobs in the total did not increase significantly, pointing therefore to a permanent shift in labour market conditions and income distribution.

Third, during the 1980-86 recession, average wages declined faster than GDP per capita for the region as a whole (Tokman 1986), while in the latter part of the 1980s they grew more slowly than GDP per capita, even in those countries where capacity utilization had returned to pre-recession levels. Thus, as may be seen in Table 9, with the exception of Chile, Colombia, Costa Rica and Paraguay, real minimum and average wages were substantially lower in 1991 than in 1980 (ECLAC 1990a and 1991). In Colombia, instead, there is evidence that the steady increase in the minimum wage was one of the main factors behind the decline in income inequality (World Bank 1990).

Fourth, there is evidence that wage differentials by skill and educational level widened during the 1980s. Over the 1980-85 period, for instance, the drop in earnings was more pronounced among minimum-wage workers (-11.4) and informal-sector workers (-27.0) than it was among industrial workers (-8.4) (Tokman 1986). Evidence given by Sainz and Calcagno (1992) confirms that this trend continued in the latter part of the decade. Barros et al. (1992) argue that in the case of Brazil this trend can be explained mainly by a surge in wage differentials by level of education. Indeed, between 1980 and 1985 the ratio between the average earnings of illiterate workers and workers with lower primary education declined

Table 9: INDEXES OF PER CAPITA GDP AND OF THE AVERAGE AND MINIMUM WAGES
(1980 = 100, 1982-91)

Country	Index	1982	1984	1986	1988	1989	1990	1991
Argentina	GDP/capita	85	87	86	83	78	75	78
	Average wage	80	129	108	96	80	76	76
	Minimum wage	98	168	111	96	--	--	--
Brazil (Rio de Janeiro)	GDP/capita	92	89	99	99	100	94	93
	Average wage	121	105	121	103	102	88	84
	Minimum wage	107	87	89	69	72	53	62
Chile	GDP/capita	90	89	92	101	109	109	113
	Average wage	109	97	95	101	103	105	110
	Minimum wage	117	80	74	74	79	87	95
Colombia	GDP/capita	99	100	107	113	114	116	116
	Average wage	104	118	120	118	119	118	117
	Minimum wage	103	113	114	110	111	108	108
Costa Rica	GDP/capita	86	90	90	92	94	95	94
	Average wage	71	85	98	85	86	87	--
	Minimum wage	86	104	119	115	119	120	--
Ecuador	GDP/capita	99	97	100	99	96	95	96
	Average wage	--	--	--	--	--	--	--
	Minimum wage	76	63	65	53	47	39	35
Mexico	GDP/capita	102	97	92	90	91	92	94
	Average wage	102	75	71	72	75	78	77
	Minimum wage	93	72	65	54	51	45	42
Paraguay	GDP/capita	101	95	93	97	100	100	100
	Average wage	--	--	--	--	--	--	--
	Minimum wage	102	94	108	135	137	132	127
Peru	GDP/capita	102	89	92	86	75	70	70
	Average wage	110	87	98	76	41	43	39
	Minimum wage	80	62	56	52	25	23	17
Uruguay	GDP/capita	88	80	86	93	93	93	94
	Average wage	106	71	72	76	76	70	73
	Minimum wage	104	89	88	84	78	69	62
Venezuela	GDP/capita	92	81	82	87	79	80	85
	Average wage	--	--	--	--	--	--	--
	Minimum wage	78	66	90	89	65	51	47

Source: Compiled by the author on the basis of ECLAC (1990a and 1991).

from 0.63 to 0.59 and the ratio between college-educated workers and workers with secondary education rose from 2.36 to 2.42.

While no conclusive analysis of the causes of the differential declines in wages and greater informalization of the economy has, to the best of our knowledge, been carried out, there is some evidence that these trends are due to the long-term impact of past educational policies (Barros et al. 1992); to an increase in labour supply, particularly pronounced among low-skilled women and adolescents, following an income drop for heads of household (Albanez et al. 1989); and to changes in labour legislation, such as the abolition of minimum wages and limitations to the activities of trade unions.

ii) *The effects of hyperinflation.* In countries which experienced very rapid increases in the price level, hyperinflation has altered the distribution of income and assets. Firstly, inflation has reduced the real wages and salaries of those segments of the population with fixed money incomes, or with incomes which are indexable only partially or over the long run, as well as of those who are unable to raise the prices of the goods they produce in line with the general increase in prices. The impact of inflation was negligible only for those who operate outside the monetized sector, a relatively small group in most of the region (except in some of the Central American and Andean countries).

Less obviously, the poverty impact of hyperinflation has been shown to be substantial even for those incomes which are regularly subject to full indexation. Assuming, for instance, that the rate of inflation is 20 per cent a year, that workers get paid monthly, that indexation occurs once a month and that outlays are spread evenly during the month, the yearly inflation tax is equal to a negligible 0.75 per cent of the workers' yearly incomes. The inflation tax grows to 2.8 per cent if inflation rises to 100 per cent, and shoots up to 9.1 and 16 per cent respectively if inflation reaches 1,000 and 10,000 per cent, i.e. inflation rates which have been experienced in several Latin American countries. While these losses could be contained if wage payments were made on a weekly basis and if workers changed their spending habits, it is evident that under conditions of high inflation like those that prevailed in the region in the 1980s, and remain dominant in Brazil, no system of perfect indexation is feasible.

Second, the decline in real incomes during the 1980s was generally much greater than discussed above because the effective rates of indexation proved to be substantially lower than the rate of inflation. In addition, indexation took place at irregular intervals and to

varying extents for different groups of workers. Generally speaking, it was found that wage indexation better protected higher wages, thus impacting negatively on both the distribution of income and the level of poverty (Cardoso 1992).

Third, hyperinflation has a strong impact on asset distribution as it reduces the real value of the monetary savings of those without access to fixed assets, foreign exchange or other edges against inflation. At the same time, hyperinflation allows those with a better capacity to operate on the financial market to realize large financial gains and it also provides considerable 'seignorage' revenue to governments. In Argentina and Mexico, for instance, the government revenue from the inflation tax on time and savings deposits reached 4.8 and 6.4 per cent of GDP respectively in 1983 (Reisen and van Trostenburg 1988). According to some authors (Cardoso 1992), hyperinflation had a limited effect on the assets of the poor because of their limited cash holdings, whereas it wiped out the monetary savings of the middle class. The limited evidence available (see, for instance, Gil Díaz 1987, Cardoso 1992) suggests, however, that the incidence of the overall inflation tax was also substantial among low-income groups. The redistribution of assets from the middle class and the poor to the upper part of the income distribution is likely to have permanently affected income inequality.

iii) *The erosion of the redistributive role of the State.* Though subject to a number of methodological limitations, past studies of the net fiscal incidence of government tax and expenditure operations in Argentina, Brazil, Colombia, Guatemala and Panama (De Wulf 1975) showed that the State played a positive, though generally limited, role in redistributing income from the upper to the lower income groups. This redistribution was the result of the broad proportionality of taxation and the relative progressivity of public expenditure.

Though no comprehensive empirical analysis of this phenomenon is available for the 1980s, changes in the level, composition and incidence of public expenditure have likely reduced, or even reversed, the redistributive role of the State, thus contributing to the worsening of the distribution of income after taxes and transfers. First of all, the share of interest payments on total public expenditure increased massively. For the region as a whole, interest payments increased from 9 per cent to 19.3 per cent of total expenditure between 1980-81 and 1985-87. In Brazil they rose from 11 to 42 per cent over the same period and in Mexico they climbed from 13 to 49 per cent (Cornia and Stewart 1990, Ebel 1991). Though a considerable share of these interest payments accrued to foreign banks, they also accrued to nationals in the latter part of the decade, particularly in those countries (such as Argentina,

Brazil, Mexico and Chile) which had developed a sizeable domestic bond market. Though no empirical evidence is available to us, it is plausible to assume, following De Wulf (1975), that the receivers of this growing flow of interest payments (generally financed with proportional taxes) were the top two deciles of the income distribution. In this way, a non-negligible share of national income was being transferred from the low- and middle-income deciles to the upper part of the income distribution.

Second, a growing share of social security payments was financed out of the state budget in the 1980s (Grosh 1990, Table II.B.2). Available evidence, however, shows that social security pensions (which typically absorb the lion's share of total social security expenditure) were highly regressive, with the top 20 per cent of the income distribution receiving over 40 per cent of the pensions, and the bottom 40 per cent receiving between 15 and 20 per cent (ibid). Therefore, also in this case the distribution of that part of public expenditure affecting the final distribution of cash income has evolved in a regressive way.

III. POSSIBLE REMEDIES: MACROECONOMIC POLICIES AND TARGETED INTERVENTIONS FOR THE 1990s

A. The End of the Decade: Some Positive Results

Favourable changes over the last three years have led to a widespread recovery in Latin America (see Table 1) and to improved prospects for poverty alleviation for the remainder of this decade. Many countries have benefited from a series of powerful 'external counter-shocks' which contributed to the stabilization of their economies and to the recovery of investments. As a result, GDP per capita has risen steadily (Table 1); inflation has fallen (except in Brazil) to its lowest level since 1986; and for the first time since 1981 the net transfer of resources to the region became positive. Although slight, these gains are relevant, given the fact that they have occurred in a context of world recession. Among the factors which contributed to this improved performance, the following three should be mentioned.

1. The repatriation of capital flights and fresh bank credits

To a considerable extent, the transfer of resources abroad that occurred during the 1980s was caused by an increase in interest rates on international markets and a decline in lending by

international banks. However, the situation began to change in 1989. Data elaborated by ECLAC show that the total value of net capital flows from abroad, including direct investments, bank loans and bond issues on international financial markets, jumped from around \$6 billion in 1988 to \$13 billion in 1990 and \$40 billion in 1991 (Table 10). For the five main countries in the region, these capital flows represented a considerable portion of their GDP in 1991, namely 2.7 per cent in Brazil, 5.8 per cent in Chile, 6 per cent in Mexico, 7.6 per cent in Argentina and 10 per cent in Venezuela.

Table 10: NET CAPITAL FLOWS TO LATIN AMERICA
(In billions of Dollars, 1989-91)

	1989	1990	1991
Argentina	1.4	0.5	5.1
Brazil	0.2	0.4	11.6
Chile	1.1	2.0	1.7
Mexico	0.7	8.4	16.1
Venezuela	1.0	1.8	4.8
Rest of the region	0.6	0.2	0.8
Total	5.0	13.4	40.1

Source: Salomon Brothers (1992).

However, it must be pointed out that this phenomenon mainly involved five countries and that two of these, Brazil and Mexico, accounted for about 70 per cent of the overall flows to and from the region. For the most part, these flows consisted of new bond issues on international markets and foreign direct investments. Only to a limited extent were they composed of fresh lines of credit opened by international banks. Of special relevance was the return of capital flights which, according to some sources, accounted for about half of the new foreign direct investments. If this substantial flow of capital continues and if it spread to the rest of the region, an alleviation of the constraints on the balance of payments would become more likely as well as new and more effective investments and a recovery in economic growth.

External phenomena (which could indeed be reversed in the future) doubtless contributed to this financial inflow. Among these were the rapid growth and internationalization of financial markets that facilitated the trade in shares of 'healthy' Latin American companies as well as the US monetary policy which, by massively and quickly slashing real interest rates, encouraged the shift of enormous amounts of capital toward more

profitable investments abroad. Internal factors also played a role in fostering positive net transfers of capital toward Latin America. In some countries, such as Mexico, steps taken to solve the external debt problem (thanks to the Brady Plan and other swap schemes) encouraged additional capital flows. The return to positive real interest rates, competitive exchange rates and less restrictive legislation on foreign investment also contributed to the change in attitude among economic agents, even in those nations, such as Argentina and Brazil, which were, or still are, suffering macroeconomic imbalances.

2. The launch of social emergency and social investment funds

Toward the end of the 1980s, the increasing awareness of the impoverishment of ever larger segments of the population, the erosion of public-sector infrastructure and the deterioration of public health care services, education systems and water utilities led to the creation of Social Emergency Funds (SEF) and, subsequently, Social Investment Funds (SIF) in a growing number of countries (Bustelo 1993). Frequently implemented as a result of pressure from the international community, the SEF were originally devised to offset the 'social cost of adjustment', particularly among those categories of the workforce that had been affected in a direct way by the new austerity measures, such as the employees of enterprises which had been closed or public-sector employees who had been laid off.

Although Chile and Costa Rica had previously introduced similar measures, the first true SEF was undertaken in Bolivia in 1987. In general, these programmes were countercyclical in nature, though they eventually came to resemble more general anti-poverty programmes and thus focused on the 'old' as well as the 'new' poor. Their main purpose was to transfer resources to groups at risk and to create temporary jobs through highly labour-intensive public works projects. As economic recovery took hold, the SEF were to be replaced by the SIF programmes, which were designed to accelerate economic growth through human capital development.

In both cases, the administration of these funds was to bypass normal management and budgetary channels, particularly by relying on non-governmental organizations and other private entities or enterprises that were to be established to run the funds, thereby avoiding wastage, delays and bureaucratic bottlenecks. In low-to-medium income countries, around 80 per cent of the assets needed to finance these funds was provided by international assistance, while in medium-income countries the assets came largely from domestic sources

or from capital freed up through debt-for-development swaps. In some countries, such as Bolivia, Jamaica, Mexico and Peru, considerable financing was allocated to the SEF. In Bolivia it was supported to the tune of 2 per cent of GDP, while the Pronasol in Mexico benefited from the equivalent of \$1.8 billion per year.

While the programmes in some countries are limited in terms of financing and duration, at least 13 (and probably more) nations are currently carrying out SEF or SIF programmes. These include all the countries of Central America, plus Bolivia, Chile, Paraguay, Peru and Uruguay. Only Argentina and a few other nations have not implemented either an SEF or SIF.

Although the SEF and SIF proved unable to compensate for the cuts in public spending that were part of orthodox adjustment programmes and although they were also criticized on other grounds (see later), they averted a severe drop in the standard of living of some segments of the population. In any case, they clearly highlighted the distributive and social costs associated with orthodox adjustment.

3. The growth of non-traditional exports

First the decline and then the stagnation of the value of exports, due not so much to a fall in the volume of exports as to a drop in export prices, played a crucial role in making a contractionary adjustment inevitable during the 1980s (Table 11). Export prices and exchange rates began to stabilize in 1987, while the growth in the volume of exports markedly accelerated (from an annual average of 2 per cent during 1980-6 to more than 8 per cent in 1987-91). The value of exports in current dollars shot up from \$80 billion in 1986 to \$128 billion in 1991.

Table 11: THE TRADE BALANCE
(1980-91)

	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Trade balance ^a	-3	7	29	38	33	17	19	23	29	30	12
Exports: value ^a	101	91	92	101	96	80	91	105	116	128	126
volume ^b	108	105	114	122	123	116	128	138	148	155	160
Imports: value ^a	104	84	63	64	64	63	72	82	87	98	114
volume ^b	102	84	65	67	66	69	71	76	77	82	95
Exchange rate ^b	94	89	86	89	87	78	74	73	73	72	68
Volume of world trade ^b	101	99	102	111	114	120	127	138	148	154	159

Source: IMF (1989 and 1992). ^a In billions of current dollars. ^b Index: 1980 = 100.

The improvement in 1987-91 was the result of two conflicting trends. On the one hand, the value of traditional exports, like meat, wool and grain in Argentina and Uruguay, tin in Bolivia, copper in Chile and Peru, coffee in Brazil and Colombia, bananas and sugar in the Central American countries and so on, were stagnating or falling because of the low level at which international market prices had stabilized, market saturation, the weak price elasticity of demand for many of these products and expansion in the global supply of these products. On the other hand, non-traditional exports, including primary goods, fruits and vegetables, wood products, flowers and shrimps as well as a wide array of manufactured consumer products, were expanding at a steady pace in an increasing number of countries which had already moved towards the 'new export model'.

These opposing trends were very clear-cut in many nations. For example, the value of total exports in Colombia climbed 6 per cent in 1991, while that of non-traditional exports jumped 30 per cent. In Mexico in 1991 overall exports rose by barely 2 per cent, while exports of non-petroleum products increased by 14 per cent. In Uruguay total exports fell by 5 per cent over the same year, while the value of non-traditional exports maintained a steady rise. Although in a few cases, such as that of Peru, both traditional and non-traditional exports dropped, empirical evidence indicates that the general trends outlined above were also apparent in Chile, the Dominican Republic, Ecuador, El Salvador and many other countries.

B. Possible Policy and Programmatic Responses to Poverty

Hereafter we illustrate the policy measures needed to tackle the traditional, cyclical and new distributive problems discussed in Parts I and II above and to substantially reduce poverty over the next two decades. These measures fall into two categories. First, they contemplate the adoption of a broad-based development model conducive to a gradual fall of poverty in the medium and long term. More specifically, they envisage the introduction of measures aiming to:

- favour the adoption of labour-intensive production techniques through appropriate factor pricing policies and other measures;
- increase the productive assets of the poor and correct those market failures which prevent their access to credit, intermediate inputs and modern technology;
- improve the productivity of the poor through investments in their human capital; and
- raise the price of goods produced by the poor.

Second, the proposed approach comprises targeted interventions for those whose incomes cannot be increased through an employment-based strategy. It also includes short- and medium-term interventions to tackle the considerable poverty problems that even the development model described in more detail below would leave unresolved.

C. A Broad-based and Equitable Development Model

The evolution of economic theory over the last two decades has provided useful insights for the development of a new model of growth and political economy that would avoid the inefficiencies of ISI and of the monetarist-liberal approach. The new model is based on the positive elements of earlier approaches, but also on fresh ideas which have emerged from advances in theory over the last 15 years, especially the 'new growth theory' and the 'optimal taxation theory'.

The model proposed in this paper is characterized by a longer policy-making horizon, a more equitable distribution of land, other productive assets and opportunities, a search for competitiveness through the recovery of capital accumulation, sustained investment in technology and human capital, the promotion of labour- and skill-intensive exports and specific measures to correct distributive imbalances through institutional reforms. These measures must be implemented within the context of a macroeconomic policy which is at once sensible and socially sensitive. The State plays an important role in this approach, though it is a fundamentally different one from that which it played in the past. The State must assure not only the implementation of realistic macroeconomic policies, the creation of an enabling environment and the provision of public goods, but it must also stimulate the recovery of investments, adopt key institutional reforms and actively confront the problem of urban and rural poverty.

The country in Latin America that has so far most faithfully adhered to this 'third path', similar in many ways to the development model adopted in the nations of East and South-East Asia, is Chile under Presidents Alwyn and Frei. Elements of this new approach are also evident in policies which have been undertaken in Costa Rica, Colombia and a few other nations.

1. A stable macroeconomic policy

The pursuit of monetary and budgetary goals should not aim at an unattainable absolute price stability or at fiscal balance *strictu sensu*, but should rather focus on a steady reduction of inflation and budget deficits to below 20 per cent and 3-4 per cent of GDP a year respectively, as well as on the financing of such deficit through measures which are non-inflationary and avoid an increase in the public debt/GDP ratio to above the critical threshold of 0.75.

However, in the attempt to reach these goals, it is necessary to avoid the two biases typical of the monetarist approach. First, public deficits must not be reduced too rapidly (in most cases, by no more than 2-3 per cent of GDP per year). Greater reductions would in many cases cause a large recessionary impact requiring additional, and equally depressionary, measures because of the endogenous drop in tax revenues and increase in public expenditure that generally accompany severe deflation. Except in the case of large random shocks, it is thus better to opt for smaller cuts in spending and for the financing of the remaining deficit through non-inflationary methods. Second, in trying to reduce the fiscal deficit, it is necessary to avoid the tendency to focus exclusively on expenditure cuts (Cornia and Stewart 1990). Traditional Keynesian analysis suggests that expenditure cuts have a negative multiplier effect which is greater than that of an increase in taxation. Aside from these macroeconomic motivations, the decline of the expenditure/GDP ratios over the 1980s and the extensive tax evasion and tax elusion problems prevailing in the region make it desirable to close part of the deficit through a increase in the tax pressure on the richest 20 per cent of the population and, particularly, on the top 5 per cent.

During the high inflation of the 1980s, the difficulties encountered in maintaining positive real interest rates imposed large efficiency and distributive costs on most economies. Negative real interest rates encouraged significant reliance on bank credits (often for speculative purposes), which in turn caused a massive redistribution of wealth and the adoption of highly capital-intensive production techniques. In addition, they discouraged savings and fostered capital flights. Parallel with the reduction of inflation, it is therefore necessary to re-establish positive real interest rates. Empirical evidence shows that this would have a modest impact on the formation of savings, but a greater effect on the composition of the demand for credit. However, while 'long-run' real interest rates of 3-4 per cent may contribute to greater monetary stability, to a more efficient allocation of credit and to the

adoption of more labour-intensive production techniques, higher interest rates and an excessive 'credit squeeze' would have a negative effect on capital formation, aggregate demand and poverty.

A macroeconomic policy consistent with the goal of improving economic efficiency and promoting non-traditional exports also requires that the exchange rate reflects the economic fundamentals of the economy and, in particular, the purchasing power parities of the country. While the benefits deriving from a one-off devaluation of the real exchange rate will vary substantially across countries (with small 'monocultural' primary commodities exporters likely reaping smaller gains than higher-income and more diversified economies), it is important to avoid successive competitive devaluations (that would have large inflationary and poverty effects and divert the attention from the 'real economy' improvements needed to increase exports) or a policy of broadly fixed nominal exchange rate (as currently practised by Argentina and Mexico, for instance). While the latter approach may favour a faster decline of inflation, it tends to penalize export performance. It is thus better to opt for a managed exchange rate which would remain broadly fixed in real terms. The series of mini-devaluations implicit in this approach should not have an excessive effect on inflation and, in any case, is preferable to these other two solutions, particularly if it is accompanied by a prudent monetary and fiscal policy.

Finally, a macroeconomic policy aiming at the long-term reduction of poverty in the region should avoid a new accumulation of debt. At present, while a consistent portion of the new capital flows to the region is composed of foreign investments and repatriated capital flights (Griffith-Jones, Marr and Rodriguez 1992), another portion is composed of new lines of credit. Although borrowing conditions are generally favourable, fresh debts could lead to a further increase in the debt stock as, until now, only a handful of countries have succeeded in lowering their total debt stock. The majority, in contrast, is still facing the risk of fuelling another debt crisis through additional borrowing. For all of these reasons, although a 'positive net transfer' represents a precondition for the recovery in investments, this goal ought to be sought through reductions in the capital stock and interest rates or through foreign direct investment, rather than through the opening of new lines of credit.

In those countries where capital inflows have now reached substantial proportions, inflationary pressures and the appreciation of the exchange rate now pose an additional challenge because of the expansionary effect they have on money supply. While 'sterilization' through open market operations of the central bank should not be excluded, these normally

entail a considerable cost to the treasury and higher interest rates which, in turn, deter productive investment and encourage further capital inflows. A solution to this problem consists in keeping flexible exchange controls in place, a policy successfully enforced, for instance, by Chile in 1992-94.

2. The recovery of investment

Although the return to and preservation of macroeconomic stability is a necessary condition for the success of development policies, sustained growth and rapid poverty alleviation will be difficult to achieve without a rapid recovery in investments. While it is true that some of the past declines in capital accumulation were due to the elimination of inefficient investments and while it may also be said that many nations in the region still have some unutilized capacity (estimated at 15 per cent of potential production in 1992), it nonetheless seems clear that sustained growth in the coming years will be very difficult to achieve without a rapid rise in investments in infrastructure and in the industrial sector. In view of the sharp decline in capital accumulation during the 1980s (see Table 12), the need for new investments and for increased expenditure to enable the maintenance of the existing capital stock is extremely acute in those nations, like Chile, Colombia and Uruguay, where the installed capacity is being fully employed and in those, like Argentina and Peru, where the obsolescence of the capital stock and the deterioration in transport, communications and marketing infrastructures is such that not even the minimum efficiency necessary for recovery is assured. In this last group of nations, even a boost in the expenditure on capital maintenance and repairs would have a significant impact on overall efficiency.

The UN Economic Commission for Latin America and the Caribbean (ECLAC 1990b) estimates that the investment rate for the entire region must rise at least from 16 to 22 per cent. This would represent additional annual investments of around \$70 billion (at 1990 prices). Other components of aggregate demand, especially private- and public-sector consumption (except for that in human capital) will therefore have to be increased at a slower pace. However, a recovery in investments depends even more on a substantial reduction in the cost of debt servicing (the main cause of the decline in investments and the high level of the net transfer of resources from the region to the rest of the world). This must be (and, to a considerable extent, is being) achieved through a large 'exogenous' reduction in international interest rates and through a more energetic application of the Brady Plan and

other schemes for the conversion or forgiveness of debt. In view of the high share of public debt in total debt, this would permit important fiscal savings and a rise in public savings and public investments in infrastructure.

Table 12: GROSS INVESTMENT RATES AND NET TRANSFERS
(In Percentages Of GDP, 1980-9)

	Investment Rate			
	1980	1983	1986	1989
Latin America	22.7	16.6	16.8	16.4
Argentina	22.2	14.0	11.8	9.9
Bolivia	14.2	11.0	9.5	10.1
Brazil	22.9	16.9	19.0	17.7
Chile	16.6	12.0	14.1	17.2
Colombia	16.8	17.6	15.8	14.9
Costa Rica	23.9	15.1	19.0	18.6
Dominican Republic	23.6	19.7	20.4	--
Ecuador	23.6	15.7	14.5	12.9
Mexico	24.8	16.6	16.4	17.8
Paraguay	27.2	20.6	20.0	19.8
Peru	23.5	20.5	17.7	--
Uruguay	16.7	10.8	7.6	9.0
Venezuela	25.2	19.9	18.4	14.5

Source: ECLAC (1990a).

A rapid recovery in investments in public-sector infrastructure would act as a strong stimulant on investments in the private sector. For instance, estimates for Ecuador show that each dollar of public-sector investment brings in another \$0.70 in private-sector investment (Yepes 1992). Thus, the current reduction in the cost of servicing the foreign debt should indeed facilitate the recovery of both public and private capital formation. The promotion of private investments should not be pursued through fiscal incentives (which have only a limited impact on investment, while causing considerable revenue losses to the treasury), but rather through a policy of macroeconomic stability that favours the formation of savings, maintains real interest rates within acceptable limits and encourages the return of capital from abroad and fresh investments by foreign investors through a liberalization of regulations on foreign investments. Through such an approach, some countries, such as Chile,

have been able to attract investments from abroad over the last few years amounting to up to 5-6 per cent of GDP.

3. The development of human capital and of non-traditional exports

The decline in public expenditure on health care, education and research which took place in the 1980s (see Table 13) aggravated the risk of poverty for many and at the same time exacerbated one of the main paradoxes of the Latin American economy, i.e. the continued dependence on exports of raw materials despite an intermediate level of development and a significant share of industrial value added in GDP. Regional-level data show that the **level** of public expenditure on the first two of these areas fell from 24.4 per cent of overall public expenditure in 1980-1 to 18.4 per cent in 1985-7 (see Table 15). Other analyses confirm that between 1980 and 1986 **per capita public expenditure** on health care, education and social security shrank by 20 per cent in the nine countries, including Argentina, Brazil and Venezuela, for which comparable data are available (Grosh 1990). The slump in expenditure was more apparent in health care and education than it was in social security (which covers only workers in the formal sector).

Table 13: HUMAN CAPITAL, R&D AND THE LEVEL OF EXPORTS
(mid-1980s)

	Latin America	Mediterranean Basin	Asia	G-7
Secondary school enrolment rate	45.6	--	65.0	--
University enrolment rate	17.8	--	18.4	--
University graduates per 100,000 inhabitants	1,560	1,910	4,780	5,920
Engineering & technology graduates/total graduates	17.2	17.6	20.2	15.5
Engineers & scientists per 100,000 working-age persons	690	1,190	1,450	5,810
R&D expenditure/GDP	0.6	0.9	1.3	2.7
Per capita R&D expenditure	120	240	180	3,460
Total exports/GDP	15	21	-	-

Source: ECLAC (1990b).

Continuation of a policy of limited investment in human capital would certainly hamper attempts to reduce poverty and to boost and diversify exports through macroeconomic measures. It would also hinder an increase in investments and a shift in the trade regime. Indeed, it is now clear, not least through the contributions of the 'new growth

theory' and 'new trade theory', that some of the lag of the region relative to the economies of East Asia and a few Mediterranean countries (used here as comparators) has been due to the region's limited investment in human capital and scientific research together with its narrow capacity to absorb or generate technical progress.

The adoption of a competitive and stable real exchange rate, a shift in trade regime from high tariffs and quotas to low uniform tariffs and other measures designed to raise exports (such as subsidies or fiscal incentives for 'infant export industries') will therefore need to be accompanied by private and public initiatives to boost the absorption of technical advances in all sectors, but particularly in the strategic and new export sectors. Measures will be needed which promote basic research and improvements in the absorption of new technical advances by enterprises as well as in the field of training, education and research, health and nutrition (which strongly influence cognitive development, learning ability and overall welfare). Priority interventions include:

i) *Initiatives to promote basic research and improvements in the absorption by enterprises of technical advances.* This will require:

- the establishment within key sectors, including agriculture, of basic research centres which are appropriately independent in terms of management and financing. Such an approach has been taken up, with some success, in biotechnology and genetic engineering in Cuba and in plant genetics in agricultural technology institutes in Argentina, Brazil and Colombia.
- the strengthening of specialized, mixed-economy consortiums with the aim of generating research which can be used by a vast array of users. The Centre for Technological Innovation of Mexico City (jointly established by the National Autonomous University of Mexico and a group of construction companies) as well as the related Centre for Electronics and Computer Processing and other similar initiatives undertaken in Brazil and Colombia are positive examples of such an approach.
- incentives for research within enterprises on new products and processes through the provision of *ad hoc* subsidies, fiscal incentives or the preferential distribution of foreign exchange.

ii) *Measures to strengthen the education system.* These include a rapid expansion in kindergartens as an appropriate stimulus for the development of children's cognitive

capacities; the attainment of net enrolment rates in compulsory schooling of 100 per cent; focus on the maximum number of pupils per teacher and the minimum level of public expenditure per student for course materials; a gradual rise in the graduation rate for secondary and higher school institutions. At all levels, it is essential that science and technology benefit from greater emphasis.

4. Institutional reforms

The efficiency and poverty alleviation goals set by the new model cannot be achieved without a thorough reform of agrarian structures, credit and labour market institutions and government tax and expenditure systems. Failure to do so would condemn the Latin American countries to a situation of slow growth, persistent poverty, latent or open social conflict as well as to permanent temptations to use macroeconomic instruments for distributive purposes. As will become clear in the course of the following discussion, therefore, the case for institutional reforms rests on solid efficiency and credibility arguments as much as on distributive and welfare arguments.

i) *Agrarian reform.* No fewer than 27 land reform programmes were carried out in developing countries in the postwar period. Agrarian reforms of this type, consisting of the redistribution of large farms, plantations and state-run farms to the landless and to small marginalized farming families, were undertaken, among others, in China (beginning in 1978), Egypt, Iraq, Japan, South Korea, Taiwan, the Indian state of Kerala and other nations. In each of these cases, the results were positive in terms of higher output, labour absorption, rural development and the reduction of poverty, even though over the short run a drop sometimes occurred in the marketing of food surpluses in urban areas.

Despite an extremely high degree of land concentration, the reforms implemented in Latin America during this period have been limited in number and scope (Table 14). Apart from reforms of a special nature, such as the 1971 expansion of the *ejidos* in Mexico and land collectivization in Cuba and Nicaragua, the only noteworthy land redistribution programmes have been those carried out in Bolivia and Chile in the 1950s and 1960s and, particularly, that implemented in Peru in the 1970s (where, however, lack of support measures in the areas of credit and fertilizer supply led to the failure of the reform). In the other cases, reforms involved only a relatively modest proportion of the available land, benefited only a small

share of all landless families, often redistributed land of inferior quality and mainly aimed at pacifying some segments of the population or at nurturing a positive public image abroad. Finally, in some of the nations with the highest incidence of landlessness and rural poverty, like Brazil, Guatemala and Paraguay, land redistribution programmes have never been undertaken. For example, the 1985 National Plan for Agrarian Reform in Brazil, envisaging the redistribution of 80 million hectares of private land among 1.4 million landless families, has never been implemented because of the opposition of the agricultural oligarchy.

Table 14: AGRARIAN REFORMS IN LATIN AMERICA

	Year of Reform or Modification	Beneficiaries/ All Farm Families	% Land Area Redistributed	New Form of Ownership*
Cuba	1959, 1963	70 (1963)	--	SRF, SPF, C
Mexico	1917, 1971	69 (1917)	--	<i>ejidos</i>
		43 (1970)	43 (1970)	
Peru	1963, 1969	30 (1975)	39 (1982)	C, some SPF
Bolivia	1952, --	74 (1977)	83 (1977)	SPF
Nicaragua	1979, 1981	30 (1983)	--	SRF, SPF, C
Chile	1962, 1970	9 (1982)	10 (1982)	<i>asentamientos</i>
Venezuela	1960, --	31 (1979)	19 (1979)	SPF, C
El Salvador	1980, --	23 (1985)	22 (1985)	SPF, C
Colombia	1961, 1973	10 (1975)	--	SPF, C
Costa Rica	1961, --	5 (1980)	7 (1980)	SPF, C
Honduras	1962, 1975	8 (1978)	--	SPF, C
Ecuador	1964, 1973	10 (1983)	9 (1983)	SPF, C
Dominican Republic	1962, --	8 (1983)	14 (1983)	SPF, C
Panama	--	13 (1977)	22 (1977)	SPF

Sources: Deere (1985), Thiesenhusen (1989).

* SRF = state-run farms, SPF = small private farms, C = cooperatives.

Land reform, painfully absent from the policy agenda of both orthodox and heterodox reformers in the 1980s, will therefore be urgently needed in the years ahead in order to revitalize the rural economy and confront the deep-seated problem of rural poverty, a problem that, as recent analyses confirm (Lipton 1988 and 1993, de Janvry and Saudolet 1992), still depends crucially on access to the land and other assets. In view of the persistently high incidence of landlessness in the region - which still affected 31 per cent of farm households in 1988, with peaks of over 40 per cent in Brazil, Costa Rica and El Salvador

(Jazairy et al. 1992) - the medium-term impact of land reform on the alleviation of rural poverty is therefore expected to be very large. Only in few countries, such as Argentina and Uruguay such measures would have a limited impact. Although the specific measures which should be adopted will obviously differ from country to country, they should be guided by common principles.

To start with, land reform should give priority attention to the redistribution of public and private landholdings in parcels above agreed ceilings (varying according to the quality of the land) to landless rural residents or to farmers with plots which are insufficient to keep them out of poverty. Market and tax incentives can also be used together with more traditional methods to trigger a more market-based redistribution of land. For instance, the taxation of land, particularly if left idle, and the desubsidization of inputs would make the divestiture of land more feasible from an economic perspective. In parallel, improvements in the legal framework for sharecropping and tenancy contracts should be introduced, so as to guarantee sharecroppers and tenants reasonable returns for their labour, sufficient time to cultivate the land and a more equitable distribution of agricultural outputs.

Land reform should be carried out in an '**incentive compatible**' way. In this regard, land redistribution should be accompanied by the removal of those factor, insurance and credit market failures which penalize small-scale landholders as well as by 'collective action' for those activities, such as tractorization, storage and commercialization of farm products, for which economies of scale do exist (Lipton 1993). Whenever these distortions and market failures cannot be fully corrected, land redistribution should allow for the survival of a few large-scale farms which can play a second-best, but positive, role as intermediaries-providers of services (credit, fertilizers, technical innovation, and so on) to small farms.

Land reform should also be carried out in a '**power compatible**' way. Policy makers should explicitly address the problem of the distribution of the fiscal and political costs of the agrarian reform among all groups in society, and particularly among large-scale landowners, urban consumers (who might have to pay higher food prices in the short run) and high-income urban settlers. The original owners of expropriated lands should be compensated, if partially, through the issuance of government bonds or similar methods. At the same time, the new owners should be required to reimburse the government over a reasonably long time period at rates which are within their means but also in proportion to the expected land yields. In order to respect the principle of 'horizontal equity', the burden of land reform should be shared, in particular, among all high-income groups in society. For

instance, part of the resources to be utilized for compensating the landlords should be mobilized through the taxation of high-income urban settlers. Under traditional land reform, this group would not suffer any loss. A combination of incentives, such as partial compensation for expropriated landlords, improved public services for the urban working class and better growth opportunities for the urban entrepreneurial class, together with sanctions for all of these groups, would certainly make the reforms more credible from the political-economic perspective.

ii) *Correcting market failures.* As noted in Part II, the 1980s witnessed a sharp increase in unemployment and underemployment as well as a sizeable transfer of labour from the formal to the informal sector of the economy. Though the number of jobless people has diminished in these early years of the 1990s in a few countries (most notably, Bolivia, Chile, Panama and Venezuela), unemployment and underemployment are still an unresolved problem and remain a major cause of poverty. At the end of 1993, for instance, more than 8 million people were unemployed in the large cities of Brazil alone. Unemployment and poverty reduction prospects appear even less promising if one considers that the labour force is expected to grow during the rest of the 1990s at an annual average rate of 2.7 per cent and that the modern sector will be able to absorb no more than 30 or 40 per cent of new entrants, even assuming a rapid recovery in investments. A massive rise in labour supply is therefore to be anticipated on the informal labour market where, given widespread market failures, labour productivity and real incomes can be expected not only to remain well below those in the modern sector, but to often fall below the poverty line. An important element of the fight against poverty will therefore consist in raising labour productivity in the *Economía Popular*, that is, among micro-, small- and medium-sized businesses outside the modern sector.

In those sectors where technology allows for ample substitutability between production factors, small businesses generally rely on labour-intensive technologies and exhibit a total factor productivity and labour absorption that are **higher** and a capital and import intensity per unit of output that is **lower** than those of larger enterprises (Stewart 1987). The full realization of these efficiency advantages and the further growth of such informal-sector enterprises, however, are hampered by institutional bottlenecks and market failures in the areas of credit and technology (see Part II). To raise productivity and incomes in these small enterprises and thereby help reduce poverty will thus require a series of measures, notably institutional and legal interventions aimed at removing those obstacles

which prevent an efficient functioning of product or factor markets; support to 'collective actions' undertaken by small producers (as in the case of the *comercializadoras* which simultaneously market the output of several small companies); state interventions to ensure equal access to training, new technologies and physical infrastructure (for instance, through the establishment of industrial parks offering space, utilities and other essential services at market prices to small businesses and workshops); and measures to facilitate access to credit at market interest rates.

This last objective, usually the most difficult to fulfil, will mean not so much the provision of credit at lower rates through the normal banking system, as it will the creation of financing institutions which can meet the particular needs of small companies. These generally include the carrying out of a large number of small transactions at low cost per transaction and with uncomplicated procedures, the granting of unguaranteed loans often involving the joint responsibility of several people and the parallel provision of some technical support (as in the case, for instance, of the financial and technical assistance programme for small-scale enterprises in Colombia and of the Banco Popular in Costa Rica and the Dominican Republic). In each of these cases, the usual indicators of performance (percentage of bankruptcies, repayment rates, growth in deposits, rates of return, and so forth) of these banking institutions were often found to be more satisfactory than in the traditional banking sector.

iii) *Public expenditure and tax reform.* The recovery in public-sector investments, the return to adequate levels of current expenditure in health care, education and other priority areas, the launching of public works projects, the redistribution of income towards marginalized groups, the establishment of incentives for non-traditional exports and other such interventions implicit in the development model proposed in this paper call for the elimination of the biases currently affecting public expenditure, an increase in tax revenue and a thorough reform of the tax system inspired by the optimal taxation theory (Newbery and Stern 1987).

Public expenditure reform should aim, in particular, at a better allocation of resources, at a more equitable distribution of the benefits of public expenditure and at increasing the microeconomic efficiency of most expenditure programmes. Because of the policies adopted during the ISI period, the military dictatorships of the 1970s and the debt crisis of the 1980s, a large share of public expenditure in most Latin American countries has been, and still is,

absorbed by subsidies to private and parastatal enterprises producing goods for the protected domestic market, by military and internal security spending and, in particular, by interest payments on the public debt. In 1987, for instance, this last expenditure item ate up nearly half of the public expenditure of Brazil and Mexico (Ebel 1991).

Table 15: THE SECTORAL DISTRIBUTION OF PUBLIC EXPENDITURE
(In Percentages, 1980-1 and 1985-7)

	Health Care & Education		Economic Services		Interest on the Debt		Defence		Administration		Social Security	
	1980-1	1985-7	1980-1	1985-7	1980-1	1985-7	1980-1	1985-7	1980-1	1985-7	1980-1	1985-7
Bolivia	28.6	20.1	12.6	17.1	25.3	5.0	11.1	6.0	15.6	9.7	1.0	24.8
Brazil	11.2	11.0	23.4	12.1	11.3	42.0	3.7	3.4	16.1	12.5	33.6	23.3
Chile	21.6	18.8	11.5	9.2	1.9	6.6	12.0	10.9	11.2	8.8	36.9	37.1
Mexico	18.2	11.1	30.8	18.8	13.0	48.8	2.1	2.0	12.7	4.9	13.7	8.2
Peru	22.1	23.6	20.9	17.3	18.8	17.4	22.0	19.5	6.2	9.7	--	--
Uruguay	12.0	11.1	10.4	8.2	2.1	8.8	14.2	10.4	10.7	11.0	51.4	49.0
Latin America	24.4	18.4	19.3	13.6	9.0	19.3	7.7	6.8	13.1	9.6	29.4	33.6

Sources: Ebel (1991), Cornia and Stewart (1990).

With the new development approach, a considerable proportion of public expenditure will have to be reallocated from these sectors to others, such as investments in infrastructure, health care, education and training, water utilities, support for exporting companies and social safety nets, which have higher social rates of return and a greater impact in terms of poverty alleviation. In a few countries and sectors such reallocation has already begun. Thus, military spending fell in Argentina, Uruguay and a few other countries between 1982 and the end of the decade. Steady reductions could well be achieved over the short run in Chile, El Salvador and all other countries where civilian governments have recently been elected. Similarly, interest payments on the public debt have begun to decline as a result of the Brady Plan, the repatriation of capital flights (which, by lowering the pressure on the exchange rate, contribute to a fall in inflation and to better control of the cost in local currency of servicing external debt) and, above all, the lowering of interest rates on international markets since 1991. These 'exogenous counter-shocks', which have already allowed considerable fiscal and foreign exchange savings, must be accompanied by internal measures designed to reduce the cost of servicing the domestic debt, as well as by a reduction of the subsidies to parastatal enterprises and any other sectors with low social rates of return.

Within each sector, considerable opportunities are generally available to improve the distribution of public expenditure among income groups. For instance, public spending on tertiary education is usually to the advantage of the children of better-off families, which can bear the opportunity cost and direct private costs (for tuition, course materials, food and lodging) of higher education. On the other hand, public expenditure on elementary schooling tends to favour lower-income families with children who only attend public schools (Selowsky 1979) (See Table 16).

Table 16: THE DISTRIBUTION OF PUBLIC EDUCATION SPENDING IN COLOMBIA
(In Percentages By Income Quintile, Mid-to-late 1970s)

Income Quintile	Income Share	Distribution of Public Expenditure by Level of Education		
		Primary	Secondary	Tertiary
First	5.2	32.1	16.8	0.8
Second	9.1	26.7	21.8	4.6
Third	12.6	20.5	21.2	10.7
Fourth	18.7	14.5	24.6	23.5
Fifth	54.4	6.2	15.6	60.4

Source: Selowsky (1979).

Similar considerations are valid for health care services (where preventive care and basic services tend to benefit the poor more than proportionately, while hospital care in cities is more often to the advantage of higher-income groups), transportation and many other public services. Despite a growing awareness of the more equitable distributive effects and higher social returns of outlays on basic social services, public expenditure in most cases still favours high-income groups and contributes in this way to the persistence of poverty. For instance, in 1988, university education received between 35 and 40 per cent of public spending on education in Costa Rica and Venezuela and between 20 and 25 per cent in Bolivia, Chile, Colombia, Panama and Paraguay; this, despite the fact that university students represented only one-twentieth of the number of students in secondary schools and one-sixtieth of elementary school pupils and that, furthermore, elementary education had higher rates of return in all these countries.

A radical reallocation of public expenditure is therefore necessary and desirable both on equity and efficiency grounds, even within sectors with high social rates of return. Cost-recovery measures (allowing for exemptions for pupils from poor families) could, for instance, be introduced for university enrolment to recoup a significant portion of the cost of services provided to high-income families. This will allow part of the public expenditure on hospitals, university education, expensive urban water utility projects and global food subsidies to be shifted towards elementary and secondary education, rural health care clinics, community water systems, infant nutrition programmes and other initiatives which in large measure benefit lower-income groups.

Finally, considerable efficiency improvements will be necessary in most sectors through better staff deployment; greater balance among expenditures for investments, wages, inputs and subsidies (thereby guaranteeing that a minimum sum per user is spent on intermediate inputs such as teaching materials, drugs and fuel); greater decentralization in service provision; the introduction in some instances of 'nominal user fees' (equal to, say, 5-10 per cent of the cost of services) to inhibit the excessive use of certain services and encourage greater competition among public, private and voluntary providers (even if the financing of services remains the responsibility of the State); and, finally, the adoption in the public sector of work contracts similar to those in the private sector. As these measures normally encounter considerable resistance, their application should be accompanied by adequate compensation for the costs they may induce and should be staggered over a reasonable amount of time.

A radical tax reform will also be needed. Despite the reforms undertaken in the 1980s (Carciofi 1994), in several Latin American countries the pursuit of non-inflationary poverty alleviation and development policies is still hampered by archaic and inequitable tax systems which generate modest revenues and impose substantial distortions on the economy. Though primary income distribution in Latin America is among the most inequitable in the world, the low yields and limited progressivity of tax systems (and the low efficiency of public expenditure) have greatly reduced the redistributive role of fiscal policy and have thus contributed to the persistence of unnecessarily high levels of poverty. This is all the more surprising given the enormous impact that a modest redistribution of income would have on the incidence of poverty. Indeed, with the exception of Guatemala and Peru and, presumably, of Bolivia, El Salvador and Honduras where a more radical shift in income distribution would be required, a rise in the tax pressure on the better-off population of around 0.8 per cent of GDP in the case of Argentina and Uruguay and between 4 and 6 per cent of GDP for

Brazil, Colombia, Costa Rica, Mexico, Panama and Venezuela would enable the total elimination of poverty and indigence (ECLAC 1987).

Theoretically, tax systems in Latin America are very progressive, with rates of direct taxation on the highest income brackets standing at around 60 per cent in the mid-1980s. However, they also rely heavily on indirect taxes and administrative and registration fees (Tanzi 1992). For instance, over 100 kinds of taxes exist in Costa Rica today (ibid). Tax yields, however, remain modest relative to theoretical rates because of significant tax avoidance (due to countless exemptions and deductions) and massive tax evasion.

The data in Table 17 hint at the extent of the inequity in the tax systems in Latin America. They clearly show that, while the share of GDP going to the richest 20 per cent of the population between 1985 and 1987 fluctuated between 51 and 62.6 per cent, the total revenue from direct taxes represented only 1 to 3.7 per cent of GDP. Though the situation improved over the last seven years, the changes intervened have not fundamentally altered this situation.

Table 17: THE INCIDENCE OF DIRECT TAXES ON THE RICHEST 20 PER CENT OF THE POPULATION
(In Percentages, 1985-6)

	GDP Received by Richest 20% of the Population	Direct Taxes/ GDP	Direct Tax Incidence on Richest 20% of the Population
Argentina	54.5	1.6	2.9
Brazil	62.6	3.7	5.9
Colombia	53.0	2.7	5.1
Peru	51.9	1.0	2.0
Uruguay	51.0	1.8	3.5

Source: Author's estimates based on World Bank (1991), ECLAC (1990c).

Economic efficiency, labour supply and export promotion are also negatively affected as a substantial proportion of tax revenue originates from taxes on foreign trade and broad-based consumption as well as from administrative fees, rather than from income taxes, wealth taxes and progressive indirect taxes. Finally, the Latin American tax systems suffer from acute problems of horizontal equity (in view of the narrowness of the tax base for direct taxes and, to a lesser extent, indirect taxes) and vertical equity (in view of the limited progressivity of most indirect taxes and the regressivity of the 'inflation tax') (De Wulf 1975, Carciofi 1994 and Gil Diaz 1987).

In a large number of Latin American economies, it would thus be desirable and efficient to raise the tax/GDP ratio by a few percentage points. Furthermore, in nearly all these economies the tax load should be distributed more equitably, tax laws should be simplified, and tax administration strengthened. In concrete terms, it would be necessary to streamline direct taxation through reductions in the number of income brackets, a lowering of maximum tax rates to around 40-45 per cent, a rise in the minimum taxable income level, the inclusion in the tax base of those incomes (such as agricultural incomes and financial rents) which have been excluded to date, the introduction of presumptive taxation in those sectors where tax evasion has been high (such as the service sector and small-scale enterprises) and the elimination of a large number of deductions and exemptions. In Ecuador, a drastic cut in the tax exemptions and deductions on the profit tax generated additional revenue equal to about 0.5 per cent of GDP in 1990 (CEIS 1991).

In addition, a moderate real estate and land tax should be introduced, and sales taxes should be replaced by the more efficient value added tax. Also in this case, it would be preferable to reduce the number of tax brackets (to two or three) and eliminate exemptions, except those for essential food items, basic drugs and other key products which weigh heavily on the budgets of poor families. At present, indirect taxes still absorb 10-14 per cent of the income of households in the lowest income decile in Colombia and Mexico (Thirsk 1990). At the same time, it would be necessary to raise excise tax rates on those products with inelastic demand, which are mainly consumed by middle- and high-income groups and which generate negative externalities. Similar considerations are valid for tariffs on those public services, including communications, electricity and some types of transportation, consumed mostly by upper-income people. Duty stamps as well as administrative and licence fees should be drastically streamlined or eliminated.

Some of these measures have already been implemented in a few countries over the last five or six years (Carciofi 1994). These changes now need to be consolidated and extended to the rest of the region. Furthermore, in most instances the reforms have focused more on improving the efficiency rather than the equity and yields of the tax systems. One exception is the reform undertaken in Chile between 1990 and 1992 (Schkolnik 1992). This reform involved a surcharge of 2 per cent on income taxes and a temporary rise in the value added tax on a wide range of products. Tax revenue rose by two percentage points of GDP, the distribution of the tax burden improved and the redistributive effect of public

expenditure increased. Concurrently, the growth rate of the economy and of exports, especially non-traditional ones, increased markedly.

iv) *Labour market reform.* In the latter part of the 1970s and in the 1980s labour market relations were influenced by the repressive political climate of the time and by lopsided labour legislation. These factors contributed to a much greater drop in average and minimum wages than would have been expected on the basis of the contraction of the economy and the changes in labour supply and demand (see Part II). As noted (see Table 9), the minimum urban wage in the early 1990s in Brazil, Uruguay and Venezuela stood at 50-60 per cent of the 1980 levels, while in Ecuador and Mexico it was around two-fifths of the corresponding levels, and in Peru it down to one-sixth, i.e. falls between 1980 and 1991-2 that were between 2.7 and 16 times greater than that of GDP per capita (ECLAC 1993).

Two main types of reforms are needed to restore the proper functioning of the labour market and to eliminate existing biases. First, legal and institutional barriers to the achievement of a healthy balance of power between labour and management must be removed and stability in labour contracts reestablished (although the obstacles represented by the proper functioning of an open, competitive market must be appreciated). This means that discrimination of any type against workers' organizations, union representation or collective bargaining must be eradicated in line with the recommendations of the International Labour Office. Measures along these lines were introduced in Chile in 1991 (Sckolnick 1992). Until the promulgation of two new laws in Chile in 1991, the freedom of workers to organize and be represented by unions was not recognized (the only exception being for the Central Unitaria de los Trabajadores, which represented only a few categories of workers whose special status had been legally recognized earlier): This inevitably influenced wage negotiations in key ways. These new laws should be extended to those sectors, such as agriculture, some service industries and companies with fewer than 100 employees, which have traditionally been excluded. Moreover, norms on working conditions, dismissals of employees, the payment of social security premiums, social security in general, and so on should be reassessed and made compatible with ILO recommendations in this area.

Second, active labour market policies designed to foster the entry or reintegration into the workforce of those segments of the population facing special problems in this area should be implemented. In a certain sense, Latin America is at the forefront in introducing such

policies, among which are professional training initiatives for young people in search of a first job (such as the programmes adopted in Colombia and Costa Rica or Chile where various apprenticeship courses aim at integrating half of the 200,000 unemployed or underemployed youth), as well as retraining programmes for workers who have been laid off.

D. Targeted Interventions to Halt Mass Pauperization

In most Latin American countries, a rapid check on and subsequent lowering of poverty will not follow automatically from the implementation of the development strategy outlined above. Thus, without special interventions, it is probable that any reduction in the incidence of poverty will be slow and, in the worst cases, almost imperceptible. Targeted initiatives will therefore be necessary, particularly in the short to medium term, if the elimination of poverty is to be taken seriously as a goal. Among such interventions, two stand out most conspicuously.

1. Public works programmes

Several theoretical arguments justify in most instances the adoption of public work schemes over other income transfer programmes. To start with, public work programmes not only permit the achievement of specific poverty alleviation objectives in the short run, but also contribute to the growth of productivity and to poverty alleviation over the long term by speeding up capital formation. In addition, they are less affected by the 'labour supply' and 'adverse selection' problems associated with other income transfer programmes. In Latin America, the case for public work schemes acquires particular significance in view of the acute *descapitalisation* which took place in the 1980s together with the related need to renovate a significant proportion of the public infrastructure (roads, clinics, schools, water and sanitation systems, and so on). Public works projects can also be very useful in the development of rural roads, irrigation canals, agricultural markets and so on, particularly in densely populated rural areas affected by limited off-farm employment opportunities and excess labour supply. Usually scarce, especially in remote rural areas, such infrastructure would have a strong positive impact on agricultural productivity over the medium term

while contributing to the generation of employment and the struggle against rural poverty in the short run.

The success of public work schemes generally depends on the existence of a well-analysed portfolio of projects which fulfil a specific role in the local economy, promise a satisfactory return on investments, entail a relatively modest cost per job created, have a wage bill to total programme expenditure ratio above 0.7, offer wages which will not attract workers already employed but which nonetheless can assure the livelihoods of hired workers, have a clear impact on poverty alleviation and, finally, can be adequately financed by the government budget, foreign grants or by fees for the use of the newly created infrastructure. While these programmes can offer the occasion for political patronage and often suffer the delays and wastage typical of public bureaucracies, their implementation can effectively be entrusted to NGOs and other private entities established for this purpose.

Although with varying degrees of success, projects of this type have already been undertaken in Latin America, beginning in the 1960s with the Frentes de Trabalho in the rural areas of north-east Brazil. In the 1980s, large-scale interventions were carried out in Chile (where the Programa de Empleo Mínimo and the Programa de Ocupación de Jefes de Hogares absorbed a staggering 13 per cent of the labour force in 1983 and an average of 5-6 per cent between 1982 and 1987), Peru (where the Programa de Apoyo de Ingreso Temporal involved 3.5 per cent of the workforce in 1988) and a few other countries.

The Social Emergency Funds (SEF), introduced in a large number of countries in the 1980s (see above), helped avert even greater drops in the standard of living of some segments of the population. Furthermore, in the case of Chile, Peru, Jamaica and, perhaps, Bolivia and Mexico (where the success of these programmes remains highly controversial), they absorbed sizeable amounts of resources (varying between 2 and 4-5 per cent of GDP per year) and effectively provided an important safety net for large sections of the vulnerable population. The majority of the SEFs, however, remained limited in scope, financing and duration and appeared broadly inadequate in relation to the growing needs of the population, especially in those countries such as Argentina, Bolivia, Ecuador, Guatemala, Venezuela and others where economic recession, drops in investments and increases in income inequality had been particularly severe. In the 1980s these nations registered a decline in per capita GDP of 15 to 35 per cent, a drop in the investment ratio of between 6 and 12 percentage points, cuts in per capita social spending of 30 or more per cent and substantial increases in income concentration.

Furthermore, design and implementation problems have meant that these schemes were often unable to satisfy the efficiency and equity criteria outlined above, especially those relating to the unit costs of the programmes, the level of the wage rate and the targeting on the poorest groups and regions or on those most affected by the adjustment programmes. For the future, microeconomic improvements will have to be realized in order to raise the efficiency of these projects.

2. Income transfer programmes for the poor

Public work programmes are not able to reach all the poor and particularly those unable to participate in labour-based programmes (such as the elderly, the handicapped, the sick, orphans, heads of lone-parent families and widows) or those who can be excluded from such programmes for political motives (such as certain ethnic minorities). They are also unable to address the specific needs of other groups who are particularly vulnerable for demographic, biological or other reasons (such as under-5 year olds or pregnant women in low-income families or families with a large number of dependents relative to those in the labour force). With the possible exception of Chile, Costa Rica, Uruguay and very few other countries, the number of marginalized individuals not covered by formal social security programmes may reach as high as 20 per cent of the total population. It is thus necessary to institute a system of income transfers that will guarantee these people access to a minimum amount of resources. In many cases, the programmes which have been most effective in this light are those involving the targeted distribution of food stamps (carried out successfully in Jamaica, for instance), the provision of nutrition supplements to infants and young children (undertaken with promising results in many countries), or those designed to reduce the cost of some basic foods (as in experiments in the PAN programme in Colombia, particularly in low-income areas of the country).

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