

Using Empowerment and Social Inclusion For Pro-poor Growth: A Theory of Social Change

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Background Paper for the Social Development Sector Strategy Paper

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Using Empowerment and Social Inclusion For Pro-poor Growth: A Theory of Social Change

Section 1: Introduction

This paper is an abridged version of a longer paper which is being prepared as a contribution to the Sector Strategy Paper for the Social Development group¹. The longer paper will seek to clarify the ways in which poverty is a social phenomenon -- and to suggest how social development thinking and practice can offer traction on some aspects of the poverty reduction challenge which have been the most difficult for the Bank to tackle. In its concluding chapters the longer version lays out Social Development's core competencies: participatory practice and social analysis. It outlines a set of Social Development tools and approaches which draw on these core competencies and can be combined in different ways to produce custom products and services that respond to the specifics of regional and country context. Both versions of the paper draw from PREM's Empowerment Sourcebook², from the Issues Paper for the SD Strategy, the concept note on *Institutional and Organizational Analysis*³, the writing on Community Driven Development, Conflict Prevention, Participation and Civic Engagement as well as the on-going work to develop the OP and Guidelines on Social Analysis and the Poverty and Social Impact Assessment tools.

This short version has been prepared for the PREM, ESSD, WBI Empowerment Retreat (May 7-8, 2002). It offers Social Development's operational definitions of empowerment and social inclusion⁴ as two key processes which focus on the relation between people and the institutions and organizations which affect them. Building from these definitions, the paper presents a framework for poverty reduction through institutional and social change at multiple levels. The framework builds on the Sustainable Livelihoods⁵ approach, but places more emphasis on power relations as defined by social identity and economic status and mediated by institutions and organizations. **It focuses particularly on the inter-related processes of empowerment and social inclusion as the means of shifting these relations – and the institutions and organizations which embody them -- towards greater equity.**

After this brief introductory section, sections 2 and 3 present a Social Development perspective on institutions and lay out the key elements of a framework for understanding how the processes of empowerment and social inclusion can work to bring change. Section 3 concludes with a discussion of the concept of pro-poor growth as defined by Ravallion and others and its relevance to our understanding of social inclusion. Section 4 offers a theory of social change based on actions from below and from above that work to restructure the distributional 'rules of the game' in a given country so that economic growth is widely shared and poverty is reduced.

It is expected that empowerment and social inclusion will reduce inequality, but what will it do to growth? Section 5 examines some of the current thinking on the relationship between inequality and growth. This section also explores Stern's concept of the investment climate and finds that empowerment and social inclusion are in many ways integral to the systems of good governance which provide the foundation of a good investment climate. This suggests that empowerment which Stern sees an important element in the Bank's strategy for poverty reduction, may actually work, not *parallel* to growth, but *through* growth as force that helps to create specifically *pro-poor growth* and thus, more rapid poverty reduction.

Section 2: Empowerment, Social Inclusion and Security: The Social and Institutional Foundations of Sustainable Development

2.1 Individuals, Institutions and Organizations

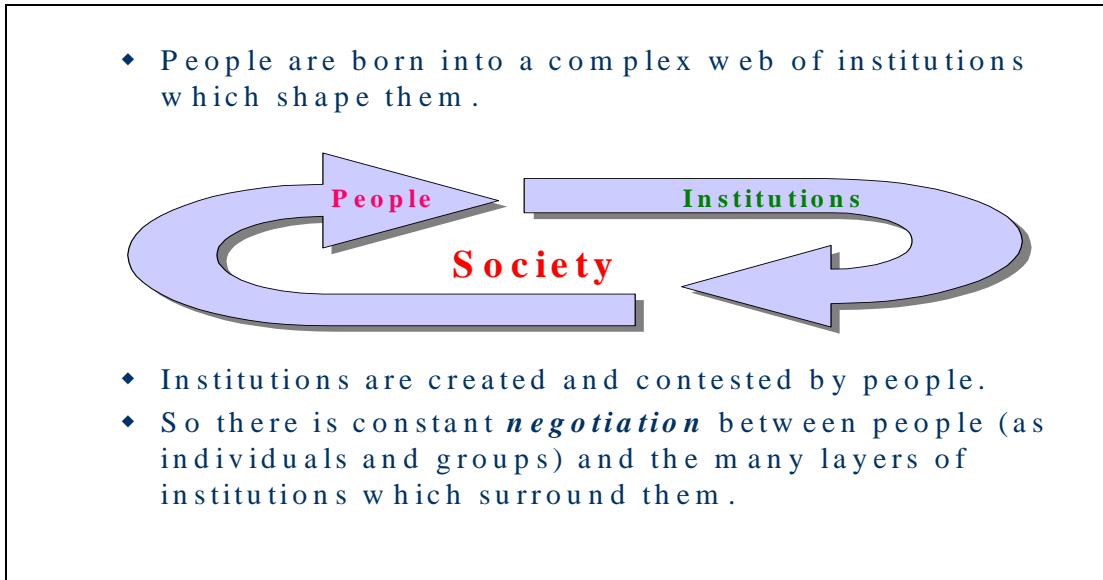
In simple terms, this paper sees *social development as development that enables poor people to take actions to help themselves*. This implies that development strategies begin with poor people's aspirations and needs and focus on supporting institutions (including markets) that are inclusive not only of those with money and power, but also of the poor and marginalized. We see institutions as critical to poverty reduction because they establish the distributional rules of the game; they structure access to the assets, capabilities and opportunities that allow people to meet their needs, manage risks and make progress towards achieving their aspirations. But in most of the world today the distributional rules of the game vary for diverse individuals and groups on the basis of their social identity and this has negative effects on poverty outcomes and prospects for sustainable growth⁶.

This may sound discouraging; but our knowledge of the reciprocal relationship between people and their institutions gives us hope. People are born at a certain time and place into the complex web of institutions which not only determine their initial asset endowments, but also shape their thinking and behavior. Yet, these same institutions have themselves been created by people – and are continually contested by other people. The fluidity of the situation is what opens the way for change.

Just as an individual's social identity has many overlapping layers, so institutions also overlap. As an individual, one is a *citizen* of one's country⁷, a speaker of one's native tongue and perhaps several other languages as well. One is also a *consumer* of market goods and services, a *producer* of goods and services as an employee in a large firm or perhaps in one's own small business. In addition to membership in state and market institutions, individuals also belong to many *civil society institutions* or organizations. In the US for example, one would likely belong to or at least identify with one of the two main political parties; one might be a member of a labor union, or a Rotarian, and also member of a religious group and perhaps also an archery club. The

list of institutions and organizations to which each individual “belongs” is a long one and the state, market and civil society institutions with which each individual interacts, is even longer.

Figure 1



Many of these overlapping institutions *reinforce* each other – sometimes in negative ways. The WDR 2000/1 notes that, “values, norms and social institutions may reinforce persistent inequalities between groups in society – as with gender-based prejudice throughout much of the world, the caste system in India and race relations in South Africa and the United States.”⁸ However, institutions also *compete* with each other for legitimacy and power, thus opening up space for structural change. Individuals and groups who are disadvantaged in some way by the prevailing distributional rules under one institution continually use these competing institutions selectively to negotiate ways to meet their own needs and aspirations. No matter how inequitable the distributional rules established by a particular institution or set of interlocking institutions may be, the fact that they are *socially constructed* also means that they are dynamic and subject to negotiation and change.

For example, take even something as seemingly rigid as the Hindu caste system which ranks all individuals with respect to the relative “purity” of the occupation traditionally practiced by their social group. This identity comes at birth and can be changed only through a life of merit which would bring re-birth in a higher, “purer” caste group. Yet ethnographic and historical observations show us that this system can actually be quite fluid on the ground. Groups and even individuals who theoretically were born into the permanent impurity of a low status caste, can and do use many strategies to re-negotiate their position. Sometimes it is through migration – exiting the whole system and taking on a new name and identity in a more anonymous urban setting or a new country. But sometimes groups stay within the system and use its own rules to redefine their status – through changing their eating or worship behaviors or, if they have gained enough wealth,

moving up through hypergamous marriage with women from a slightly higher caste group, but a poor family.⁹

A focus on institutions helps us to see poverty as a *dynamic process* rather than a *static situation*.¹⁰ Impoverishment is seen as the social process that results in loss of assets and capabilities of individuals and groups. Social mobility is the process of accumulation by which individuals and groups create assets and capabilities. Institutions are key to accumulation because they establish the “rules of the game”. These rules reflect and reproduce the power relations among groups; they structure the authorizing environment and the organizational mechanisms for the exercise of voice and influence and for holding institutional actors accountable. In other words, institutions can either help the poor and socially excluded move up, or keep them down. The Bank’s strategic focus on empowerment, social inclusion and security works towards supporting institutions and organizations that enable the poor to seize and create opportunities to move up.

2.2 Three Social Development Outcome Goals in Support of Sustainable Development

The Social Development agenda supports the Bank’s overarching goals of poverty reduction and equitable growth by seeking three specific outcomes in line with the Bank’s corporate advocacy priorities of *empowerment, social inclusion and security*¹¹. These are:

- For Empowerment – **Citizen’s with Agency and Voice**
- For Social Inclusion – **Inclusive and Accountable Institutions**
- For Security – **Societies that are Resilient to Conflict**

Each of these outcomes is at a different level, yet all are interdependent and essential to social sustainability. Without a wide range of empowered citizens who can speak out and influence the behavior of the institutions and organizations that determine their access to public services and livelihood resources, institutions will not be inclusive and accountable to the interests of citizens from all socio-economic groups. And without institutions that are seen to be legitimate and are thus able to mediate the conflict and competition that is a natural and inevitable part of social life, society will break down as groups who feel powerless and unheard resort to violence.

Empowerment and Social Inclusion: Complementary Approaches

Figure 2. presents one way of visualizing the main ingredients of “Socially Sustainable Development”. In this view, empowerment and social inclusion are conceived as complementary and mutually reinforcing approaches to changing the institutional environment in ways that foster pro-poor growth. *Empowerment* is used to characterize approaches based on *social mobilization*. A key element in most social mobilization approaches is helping poor and socially excluded individuals realize the power they gain from collective action. Often social mobilization approaches work “from below” to create voice and demand for change among diverse groups of poor and socially excluded citizens. But social mobilization can also stimulate the formation of

coalitions for change between excluded groups and other better-off citizens who also want a more equitable society –or share other interests with the excluded.

Figure 2.



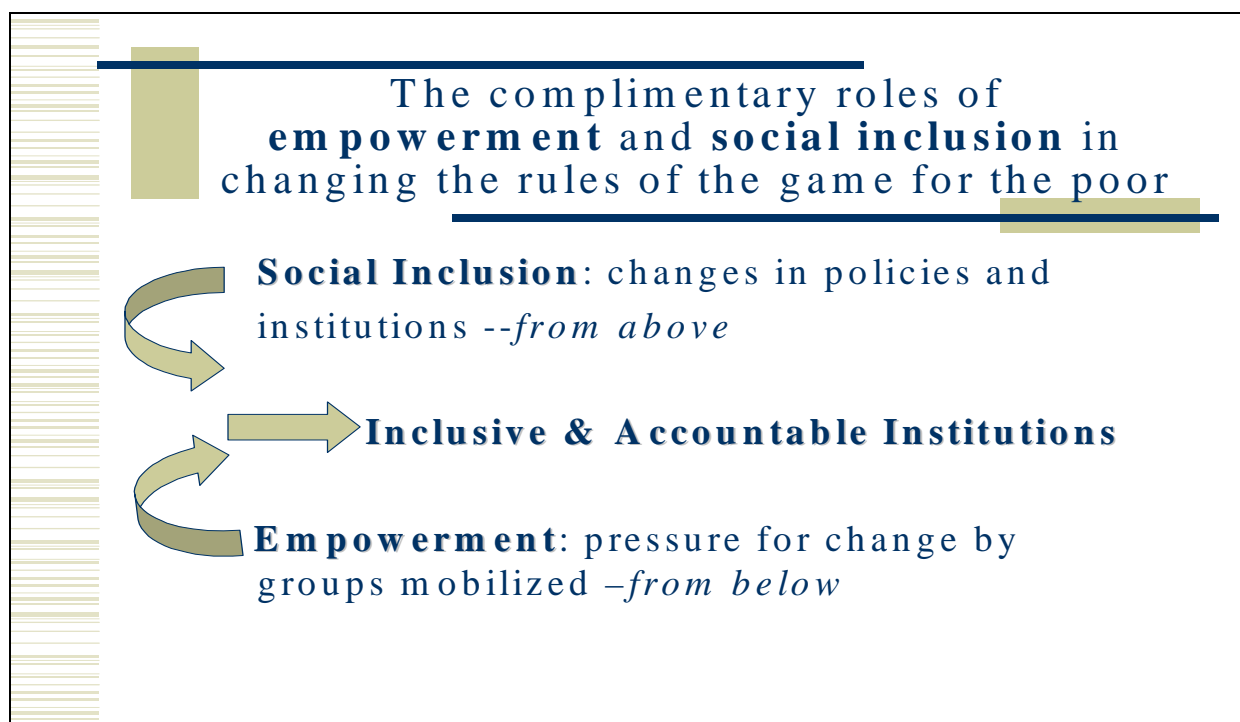
Social Inclusion is used to describe the complementary approach which seeks to bring about system-level institutional reform and policy change to remove inequities in access to assets, capabilities and opportunity. While the social inclusion dimension of the social change process may be responding to pressure from below created through empowerment, it is often instigated from positions of relative power within the existing institutional framework. (See Figure 3)

Social inclusion is aimed at building the incentives and capacity within institutions that will enable these institutions to respond effectively and equitably to the demand of **all** citizens – *irregardless of social identity*. In socially inclusive **markets** each individual operates as a consumer or a supplier of goods and services on the proverbial *level playing field* where only their ability to pay and to produce are taken into consideration. Similarly, in the socially inclusive **state**, the individual's identity *as a citizen* trumps all other identities (in terms of gender, ethnicity, caste, religion, etc.) as a basis for claims from the state for whatever the state has committed to provide its citizens (e.g. justice, social service provision, investment in public infrastructure, police protections, etc.) through its constitution and legal system¹².

This distinction between empowerment and social inclusion is strategically important for the Bank because although we have some opportunities to support social mobilization/empowerment

indirectly by insuring that they are integral to our investment lending (particularly through Community Driven Development projects), the Bank's comparative advantage is at the system/policy level. Increasingly our role will be in supporting governments to change the rules of the game to make institutions and policies more equitable and socially inclusive – not only on paper or in theory but throughout the implementation process as these policies are translated into operational mechanisms and ultimately into impacts on diverse socio-economic groups.

Figure 3.



Defining Social Inclusion

The European concept of social exclusion encompasses the failure of people's social, economic and political relationships. It includes 1) **social isolation** resulting from the lack of or breakdown of meaningful ties to the family, local or national community associations, etc. and 2) **lack of legal rights** and/or the inability to defend them. The socially excluded individual or group is unable to participate fully in the economy, in social life or in political life and the existence of such individuals or groups is seen as reducing solidarity, increasing social tensions and holding back social development.¹³

The Bank has articulated its own view of appropriate "policies for social inclusion/equity" in part C of the rating criteria for the Country Policy and Institutional Assessment (CPIA) 2000. Part C has five sections on gender, equity of public resource use, building human resources, social protection and labor and poverty monitoring and analysis. Except for the section on building

human resources which mainly focuses on issues of quality, the other four sections under this heading taken together are quite clear about the importance of **equitable policies and pro-poor revenue and expenditure patterns**. A “good” rating in these areas requires that the country to clearly identify social and economic groups that are either vulnerable or structurally excluded and to actively seek ways to overcome the barriers these groups face in getting access to basic services and economic opportunities.

Section 12 of the CPIA on “Equity of Public Resource Use” presented in Box 1 is a good place to begin in defining social inclusion and what it means in operational terms. It is important to note that the 5 rating for “good” country performance specifies that programs targeted to the poor should be designed “with their participation”¹⁴. Similarly, Section 14 on “Social Protection and Labor” also explicitly seeks evidence of government support for “community driven initiatives” rather than exclusive reliance on “centralized programs”. However, it is only Section 11 on “Gender” that explicitly calls for an assessment of the gap between “adequate policies” to promote gender equity and the existence of adequate “institutions to implement these laws fairly and enforce them effectively.”

Box 2.

| |
|--|
| <i>Equity of Public Resource Use</i> |
| <p>This item assess the extent to which the overall development strategy and the pattern of public expenditures and revenues favors the poor. National and sub-national levels of government should be appropriately rated.</p> <p>2* The overall development strategy and the incidence of public expenditures benefits the better-off more than the poor, or the incidence is unknown. There are few or no policies and programs to address disparities among individuals, groups or geographic areas in their access to public services or outcomes. The overall incidence of public revenues is regressive.</p> <p>5* Public expenditures for social services benefit the poor more than the better-off. The government has identified individuals, groups or localities that are poor, vulnerable or have unequal access to services and opportunities and is designing, with their participation, appropriate targeted programs. The overall incidence of revenues is progressive.</p> |
| <p>* The ratings are done on a six point scale as follows: 1 = Unsatisfactory for an extended period of time; 2 = Unsatisfactory; 3 = Moderately unsatisfactory; 4 = Moderately Satisfactory; 5 = Good; 6 = Good for an extended period of time.</p> |
| <p>Source: Country Policy and Institutional Assessment 2000, (Assessment Questionnaire), World Bank</p> |

This is the all too familiar “implementation gap” between policy and programs and their intended outcomes. Social Development uses institutional and organizational analysis of the situation on the ground to expose this gap and to help key stakeholders develop strategies and concrete implementation mechanisms to overcome it. Without such attention, it is likely that even a country that has promoted pro-poor and socially inclusive policy reform will have little to show in terms of actual impact on the lives of poor people. According to Ghani and Lockhart, “ when

government organizations are not aligned, a policy goal cannot be translated into its intended outcomes. A policy reflects an equilibrium among a set of interest groups. Policy reform disrupts this equilibrium and requires that a coalition of interests is rearranged". The authors explain that the required transformation of institutional relationships must begin with an understanding of the situation "as is" – with "an understanding of existing institutions and organizations (and) the dynamic between the formal and informal."¹⁵

Social Inclusion and Pro-Poor Growth

The CPIA is quite clear that countries which are judged to use public resources well are those which target public resources to the poor and where policies and programs clearly reduce disparities in access to services and opportunities. But how do we know whether a given country's policies and institutions are pro-poor? Ravallion has proposed a powerful tool for allowing us to do just that by tracking not just the extent of growth and poverty reduction a country has achieved, but by measuring the extent to which the growth itself is pro-poor.

It is well established that growth is poverty reducing. But the WDR 2000/01 and a series of papers produced more recently by the Poverty and Inequality group in DEC show that the effectiveness of a given pattern of growth in achieving rapid poverty reduction depends a great deal on where the growth takes place – in which geographic region, which sector of the economy and among which economic quantile of the population.

Ravallion makes a compelling case that in order to be called "pro-poor", *growth must occur at a faster rate for the poorest deciles than for the richest*. He cites the pattern in China over the past decade where aggregate growth has averaged 7 percent a year, but for the poorest, income rose by 3 percent while for the richest it rose by 11 percent per year¹⁶. There is nothing shabby about even a three percent annual income growth rate for the poor and in much of the world, especially in Africa where many countries have actually experienced economic contraction over the past several decades, leaders would be happy to see the incomes of their poorest raised by this much.

But the "distribution corrected rate of growth"¹⁷ is important -- especially if the international development community is going to meet its core IDG of reducing poverty in half by 2015. In another paper, Ravallion notes that "a one percent rate of growth in average household income or consumption will bring anything from a modest drop of 0.6 percent to a more dramatic 3.5 percent annual decline in the poverty rate"¹⁸ –depending on how growth interacts with distribution in a given country. This suggests that the rapid reduction of poverty required to meet the IDG goal is much more likely to happen if countries consciously seek pro-poor growth.

One way to help concretize what Social Development means by "social inclusion" is to think of it as **the set of policies and institutions (broadly conceived to include organizations, norms and codes of behavior) that support pro-poor growth and social equity**. Research on precisely what these pro-poor policies and institutions are is in its early stages, but there are already some suggestive empirical findings on what seems to work. One of the first conclusions is that initial conditions matter, especially with respect to *asset inequality*¹⁹. We will return to the

inequality issue later, but at this point we can say that targeted government investment in quality education seems to make a big difference in the degree to which the poor share in growth. This critical “leg” of the 1990 WDR approach to poverty reduction remains a solid one. Broadly comparing the performance of certain East Asian countries with those in Latin America, it looks as though land reform can also help – though the way that this is carried out appears to also make a big difference and in many contexts what seems to make the most sense is land market reforms that strengthen rather than undermining property rights and the long term security of tenancy and thus create incentives for productive investment.

Besides the initial endowment of physical and human capital, Ravallion also suggests that “location, social exclusion and exposure to uninsured risk” may be factors that can reduce the extent to which the poor share in aggregate income growth.²⁰ In a separate paper he and Datt look at a specially designed data set for India’s 15 main states to understand why growth has been more pro-poor in some states than in others.²¹ They find that the sectoral composition of growth is important. Growth in rural areas is more poverty reducing than in urban area; growth in the primary and tertiary sectors helps more than growth in the secondary sector and where there is less labor market dualism (as measured by wage differentials between the formal and the informal sectors) there will not only be more growth, but what growth does occur will deliver more benefit to the poor.²²

Their most interesting finding however, is on the marked differences in the extent to which growth in the non farm sector has benefited the poor in different states. Ironically but understandably, in the states where poverty is deepest, growth in the non farm sector has had the least impact on poverty reduction with “poverty effects ... (varying) from a low of 0.26 in Bihar to a high of 1.08 in Kerala and 1.24 in West Bengal”²³. Consistent with the observations above on the importance of the initial distribution of human and physical capital, these turned out to be the most salient variables determining the poverty impact of non farm rural growth in the 15 states. Physical capital was measured by the share of landless in the rural population and human capital was measured by state level infant mortality and female literacy rates. Given the nature of the type of job opportunities that are likely to be available in the non-farm sector, it is not surprising that differences in literacy levels between the states was by far the most powerful factor explaining the differences in the poverty impact of non-farm growth.

What is clear from this study and a host of others is that there are important interaction effects between the various elements of pro-poor policy and institutional reform. As Ravallion notes, it is not just a matter of ticking off as many things as possible from the emerging list of poverty reducing actions. It looks as though pro-poor policies are not just additive, but multiplicative.²⁴ Investment in the non-farm sector – through better rural infrastructure and connectivity, improved rural financial markets, etc., -- needs to be accompanied by investment in better quality education if it is to have its full potential impact on poverty reduction. And though this dimension is not dealt with in the paper, we are tempted to wonder whether factors such as the nature of local level governance (the way in which decentralization has been approached and the extent to which Panchayati Raj institutions are inclusive and accountable to the broad range of their constituents) in the different states may have also played a role in the extent to which each state can

be said to have followed a pro-poor or socially inclusive path of development. (*Check with Ruth for literature*)

Security and Social Sustainability

Social Development's contribution to the third corporate advocacy priority, *security*, comes through its efforts to help clients ensure that the development they undertake is *socially sustainable*. As noted above, competing and sometimes conflicting ideas, values and identities are an integral part of social, economic and political life. The constant competition and negotiation between ideas and between the institutions that embody them is what makes change and the hope of greater equity, possible. But without political and market mechanisms, without robust and credible institutions and organizations that permit differences to be voiced, negotiated and (at least temporarily) resolved, society loses its *resilience*. Normal, healthy differences can turn to violent conflict. As the WDR 2000/1 notes,

*ethnicity can become a basis for competition for political power and for access to material resources. Unless institutions of the state and civil society offer forums for mediating inter-group rivalries and forging cross-cutting ties among diverse ethnic groups, these ethnic cleavages can lead to conflicts, tearing a society and community apart and leaving everyone vulnerable to poverty.*²⁵

Although the Conflict Prevention and Rehabilitation Unit's work in support of social sustainability is the most prominent example, it is clear that Social Development's work on participation and civic engagement, social safeguards, social analysis and community driven development are also critical – as are the contributions of other networks (notably Social Protection, PREMPO, Economic Management, Public Sector Management and Private Sector Development) and the IMF. There are few events that hurt the poor as much as war or civil conflict. But hyperinflation, public sector downsizing or forced resettlement can also lead to insecurity and greater poverty.(see secton 3) Good political and economic governance that provides a framework for political disagreement, that regulates market competition and provides some social insurance for when that competition or other shocks create temporary hardship, is fundamental to socially sustainable development. And from this perspective empowerment and social inclusion can be seen as not only a national but also a global public goods because they are critical to security and social sustainability.

Section 3: A Conceptual Framework

3.1 Definitions

Social Development's theory of social change is implicit in two key definitions -- of empowerment and social inclusion -- which have been articulated in the draft OP on Social Analysis²⁶. These two definitions are as follows:

- **Empowerment** is the enhancement of assets and capabilities of diverse individuals and groups to engage, influence and hold accountable the institutions which affect them.
- **Social Inclusion** is the removal of institutional barriers and the enhancement of incentives to increase the access of diverse individuals and groups to assets and development opportunities.

(Add a discussion here of alternative definitions such as Naila Kabeer's definition of empowerment as "enhancing the capacity to make strategic life choices of people to whom this was previously denied." Explain that SD chose its definitions because they are operational in that they outline a process not an outcome and thus provide a guide to action rather than a description of an end point..)

3.2 Elements in the Framework

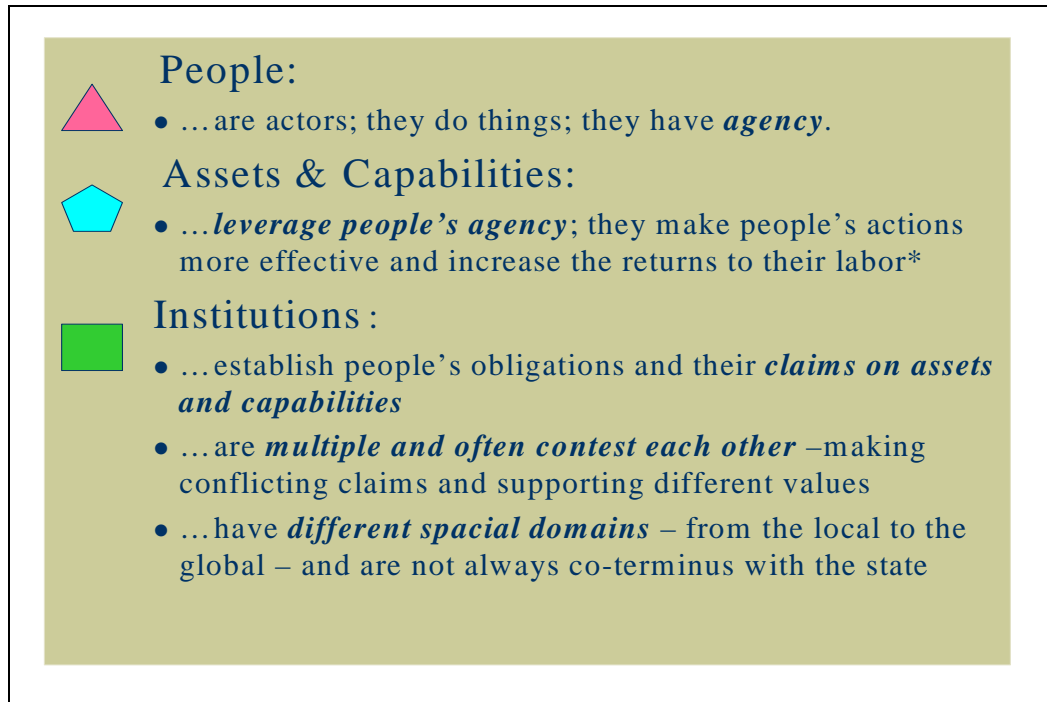
There are three basic elements in the conceptual framework behind these definitions: people, their assets and capabilities, and the institutions and organizations²⁷ which structure their interactions and express their beliefs and values. This framework shares a great deal with the Sustainable Livelihoods Framework²⁸ including these three main elements and also the idea of a *vulnerability context* which impacts on each of these three elements and which in turn, can be either mitigated or exacerbated by the institutions and organizations that have developed in a given society.

People, represented in the figures which follow by a triangle, are the starting point. In very simple terms, *people are actors*: they do things; they have agency. Also in every society *people are stratified* to greater or lesser degree on the basis of their social identity (gender, ethnic group, caste, religion, etc.) and their economic status. Low social and economic status usually reinforce each other. Hence, people in their social relationships are represented by the triangle based essentially on economic status with the rich (and powerful) at the apex and the poor (and disempowered) at the base.

Second, are people's **assets and capabilities**. They leverage people's agency by making people's actions more effective and increasing the returns to their labor. Here we have adopted the pentagon used in the DFID presentation of its Sustainable Livelihoods framework to show the five types of "capital": financial, physical, natural, human and social²⁹. The first three capitals are traditional "assets" while human and social capital are perhaps best thought of as "capabilities". These assets and capabilities are combined in different *strategies* that people use to produce and sustain their livelihoods.

The third element are the **institutions** defined as the formal and informal rules of the game or "the humanly devised constraints on human interaction"³⁰. In recent years the Bank has become increasingly aware of the importance of institutions. Much of the concern with improving the "investment climate" for growth is a concern with promoting good governance and the rule of law so that there is greater predictability in business and other social interactions and less dependence on personal connections to get things done through an unresponsive or corrupt state

Figure 4.



bureaucracy. We know that the type of *livelihood strategies* that people chose to pursue is greatly influenced by the type of institutional environment in which they work : when the institutional setting is weak or unpredictable, poor people especially, tend to stick with low risk/low productivity strategies.

Related to this issue of risk is the final element in the SD framework which is the **vulnerability context**. It is closely linked with the third social development outcome goal, security and with the central goal of the Sustainable Livelihood framework which is livelihood security. Understanding the vulnerability context also helps us to clarify just what is meant by socially sustainable development which is the core goal of the ESSD network.

People – and especially the poor – are vulnerable to two broad categories of risk. At every level of social, political or economic organization, there are some risks which are exogenous or *generated from outside the system*, while others are endogenous, *generated by the system itself*. (see Figure 7) For example, at the level of the nation state, externally generated threats to livelihood security include degradation of the international environmental commons (which could lead to desertification, reduction in fish populations, etc.), transmittable diseases such as the HIV/AIDs pandemic, war, international financial shocks, hurricanes, volcanic eruptions, etc. Although strong country level institutions can help cope with such events, individual countries have only limited control over these external threats and must depend on broad international cooperation to prevent and deal with them.

However, citizens face many kinds of risks to livelihood security that the state and other private sector and civil society institutions can either mitigate – or exacerbate. For example, good

public social protection systems combined where feasible with private insurance, can help deal with some of the more predictable risks such as old age, illness, unemployment, seasonal or periodic droughts or floods³¹. Through good environmental policies, governments can create incentives for equitable and sustainable management of both private and common property natural resources, increasing livelihood security for all and reducing the vulnerability of the poor who often depend on common property resources³².

Government and international development agencies can reduce risk and ensure sustainable development by enabling the development of inclusive and accountable institutions that give equal access to all social and ethnic groups. This includes sound financial systems, equitable laws and effective and independent judicial systems, democratic political structures and responsive, high quality social services. When these are not in place citizens are more vulnerable to irreversible declines as they try to deal with exogenous shocks. There is also greater threat of internally generated shocks as excluded groups resort to civil conflict and violence to achieve the access and dignity they feel they have been denied.

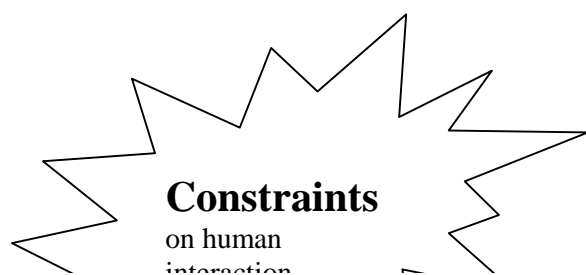
3.3 Institutions from a Social Development Perspective

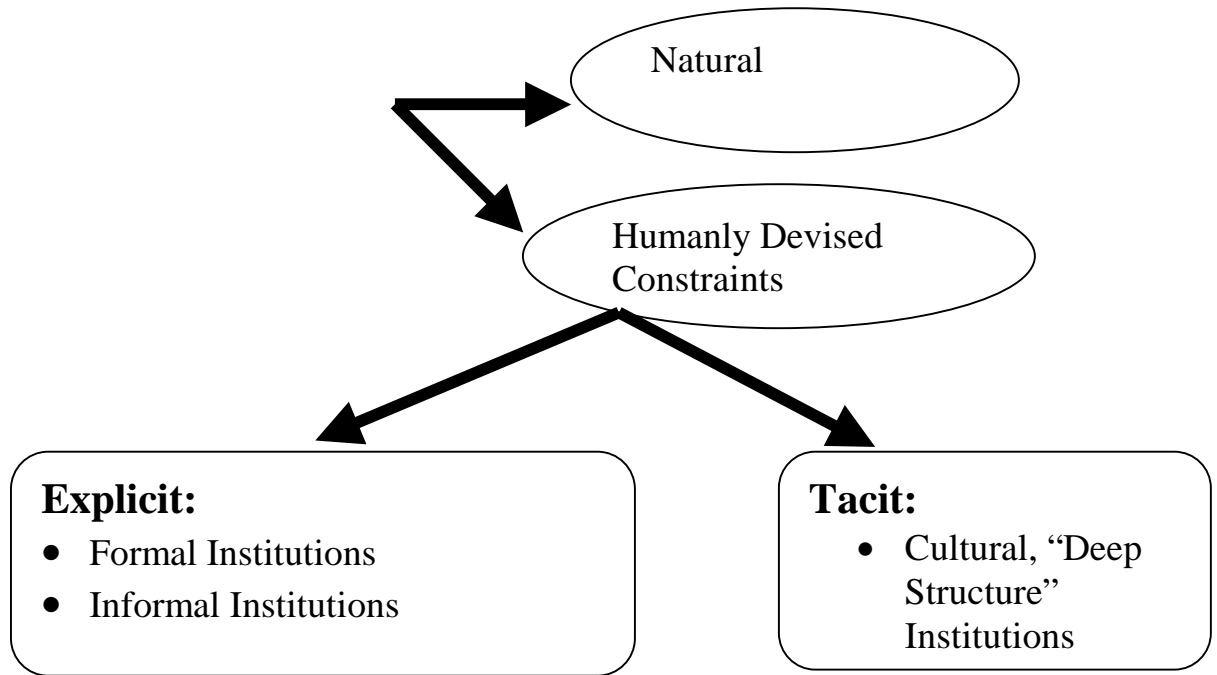
The Bank's recognition of the importance of institutions has begun to expand beyond its traditional focus on "economic" institutions such as the market and the formal institutions of state administration, to encompass the whole range of institutions -- including those such as kinship, local networks of exchange and reciprocity, etc. which are defined as specifically "social". What has not yet been fully recognized is that in fact, all institutions are social, just as kinship and local networks are also economic and political.

Social Development's understanding of institutions and organizations is based on the classic "rules of the game"/ "players of the game" definitions³³, *but with special attention to implementation and how things actually work in practice*. The focus on practice leads to a focus on *people*, how they play the game in the most creative way they can in order to win and how they make and contest the rules. Institutions are really about the power to shape human interaction and the distribution of obligations and entitlements among different social and economic groups. This perspective is well captured in North's definition of institutions as *humanly imposed constraints on human interactions, constraints that establish fields of opportunities with boundaries*.³⁴

Looking at the constraints on human interaction we see a cascade beginning with *natural* constraints (see figure 5) like weather shocks or other natural calamities -- or like the biological life span over which humans have little or no control. Below these natural constraints come a series of different levels or categories of *humanly imposed* constraints or institutions. The category of institutions which have been the primary field of development intervention are the *formal institutions* of the state and, through the state's legal and regulatory power, formal market and civil society institutions. These institutions are familiar to development practitioners. They have

Figure 5.





Less visible are a host of *informal institutions* that operate at all levels and in all sectors. Some, like informal savings and credit groups or traditional systems of natural resource management, work outside the formal system, but are fairly easy to identify and often already well aligned with the development goals of poverty reduction and pro-poor growth. However, informality, like social capital, is not necessarily good in itself. For every formal institution or set of rules that is established to achieve a certain purpose, there are also informal norms and codes of behavior which we call the “institutional culture”. Institutional culture has a profound affect on the way institutions actually work and the outcomes they actually achieve. It tends to reflect the actual incentive structures underpinning that institution – incentives that sometimes produce behavior completely contrary the formally stated purpose of the institution.

Informality is the space of human agency. It is the realm of practice where individuals and groups playing the “game” use the inevitable space around the rules to make them work in their favor. It is the realm of strategy that keeps the outcome of the game from being entirely predictable even when we know the rules. It’s the difference between knowing the rules of poker and being a good poker player. Or to put it another way, it’s the difference between the government’s published budget document and the way the funds actually get spent.

The most difficult set of “rules” or institutions to understand and factor into development practice are the often *tacit* rules of what Graham and Naim have called “meta” institutions. These institutions “represent rules (formal and informal) which are not expressed in an organizational hierarchy, and that mediate exchanges among and within economic sectors, cities, villages, cultures and societies.”³⁵ These deep structure institutions operate at the cognitive and emotional level where values and beliefs are formed. These are the institutions like kinship, gender, caste and

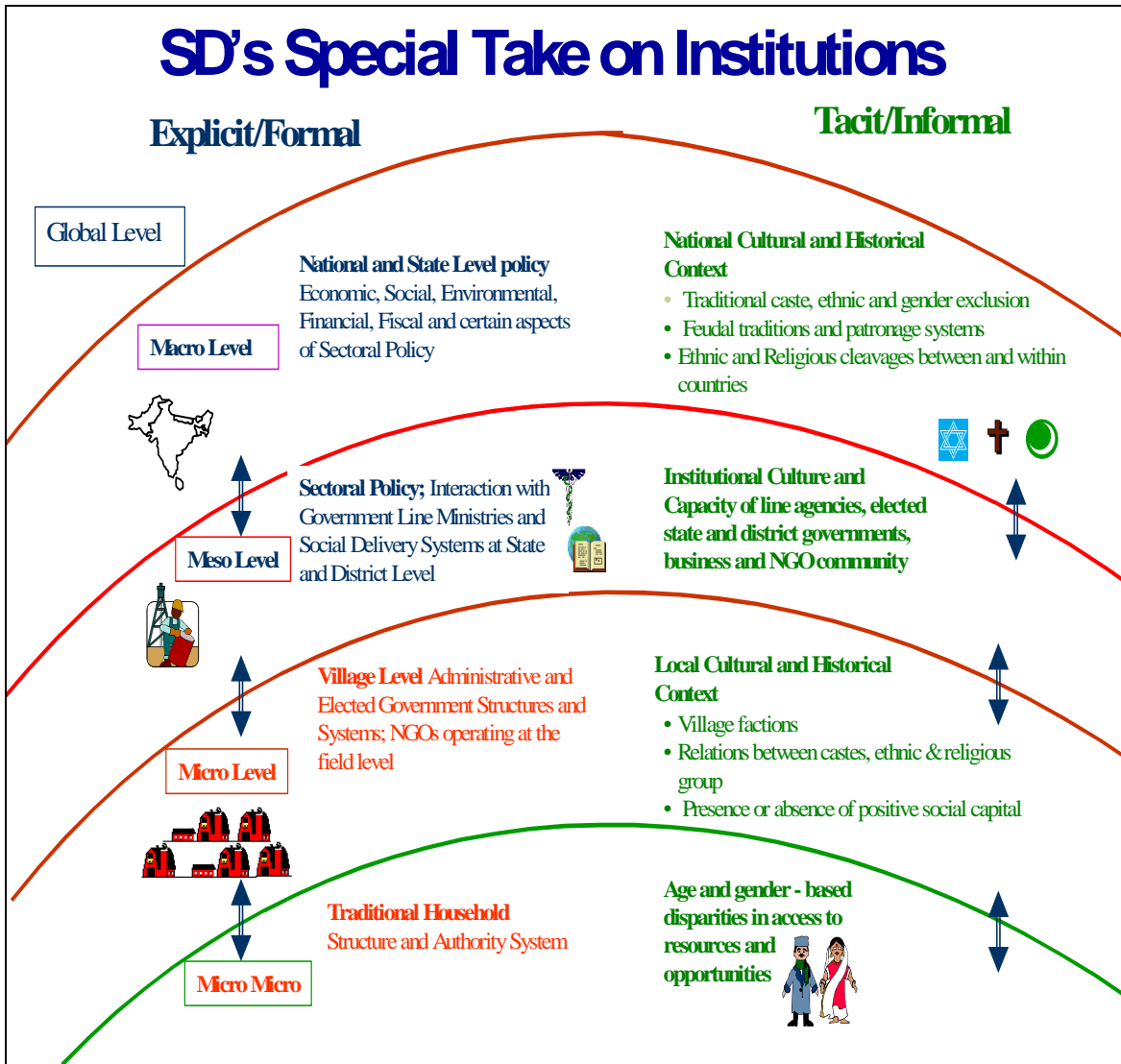
patron-client systems which shape individual and group identity. Such institutions are usually difficult for those outside them to “read” because they are embedded in the specific cultural and historical context of a particular country or region. For those born and socialized within them, much that is most important and powerful about these norms and codes of behavior is *tacit* or unspoken because it is axiomatic. It needs no explanation. Yet even as outsiders, Bank staff intuitively know that these structures and the norms and values they express have profound influence on the way that the more visible formal public and private sector institutions in a given country actually work and hence, on the development outcomes which flow from them.

Figure 6. presents a schematic view of these different levels and domains that need to be drawn into our analysis because they affect the outcomes of Bank-supported investments. In the top left quadrant on the “explicit/formal” side are the macro and meso level domains that occupied the Bank’s attention for most of its first 40 years. Indeed, its earliest history was preoccupied with action at the sectoral or meso level, building roads, health posts or agricultural extension systems. Only in the 80’s did the Bank turn its focus to broader policy and structural issues. Increasingly in the 90’s we began to pay more systematic attention to the bottom left quadrant as it became more and more evident that village level (micro) and intra-household (micro-micro) systems and relationships can critically affect project outcomes. This was the period during which participatory approaches began to be recognized as necessary to project effectiveness and greater attention began to be given to the gender dimension of development.

But only in the last five years has the Bank begun to look at the right half of the figure -- the informal and tacit systems of meaning and value in which the formal institutions and explicit rules of the left half of the of the figure are rooted. As the use of the term “rooted” suggests, the informal/tacit domain is far more influenced by the particularities of history and place than the more “generic” public policies and institutions that populate the left side of the diagram -- especially those in the top left quadrant. And yet we know that behavior even in formal institutions can be powerfully influenced by the deep seated values and systems of social organization such as caste or gender systems.

Figure 6. also illustrates that institutions have different spatial domains – from the local to the global. And although we are used to thinking in terms of countries, many influential institutions are not co-terminus with the state. Decentralization is occurring as more and more countries across the world seek to shift certain types of government obligations and powers to lower levels that are (hopefully) more accessible and accountable to the people they serve. In the other direction we are increasingly aware that not only do trans-national business entities, the UN system, the Bank and other MFIs operate across borders, but so do a growing number of civil society networks and “movements” as well as “deep structure” institutions such as religion. At least some part of the discomfort that many voice about globalization arises from the sense that while it is difficult enough to build and maintain accountability, social equity and good governance *within* the

Figure 5



boundaries of a single nation state, it is exponentially more difficult to do so *across* those boundaries.

3.4 Institutions and Social Capital

When we say that institutions are “the rules of the game” we mean that they establish people’s **claims on assets and capabilities** and also their **obligations** to others. In a sense every institution is based on either formal or informal, explicit or tacit sets of expectations between people. When these expectations are formal, backed by the rule of law we speak of “rights” and contractual obligations; when they are not so codified we sometimes speak of “trust” or “social capital”.

In its broadest definition **social capital** can be seen as a means of solving collective action problems – reducing uncertainty about whether claims and obligations will be honored, facilitating the sharing of knowledge and the management of commonly held resources and generally lowering

the transactions costs of human interaction. If institutions are the “rules of the game”, then social capital is something like the collective agreement to play by those rules. From this perspective social capital can encompass both the formal laws and the power of coercion vested in government as well as the voluntary cooperation found in informal social networks and associations³⁶. Collier’s distinction between “public” social capital³⁷ and “civil” social capital captures this difference in both the *nature* of the agreement established (backed by the formal authority of the state or backed by informal social sanctions) and also the *source* of the social capital. Public social capital is generated by government and manifest in “the institutions of government that facilitate private activity”³⁸. Civil social capital is generated by the community and manifest in the form of “trust which lowers transactions costs, knowledge (shared) through social networks and enhanced capacity for collective action”³⁹.

Pursuing this distinction, Knack⁴⁰ defines public social capital as “governmental institutions that influence peoples ability to cooperate for mutual benefit – enforceability of contracts, the rule of law and the extent of civil liberties that are permitted by the state”. Civil social capital by contrast, “encompasses common values, norms and informal networks and associational memberships affecting the ability of individuals to work together to achieve common goals”. Both types of social capital improve the gains to cooperation within the group.

Collier and Knack both appear to see public social capital primarily as a *macro* phenomenon (where the “group” in question is the nation) and civil social capital as a *micro* phenomenon (where the group could be the household, the community, or other local or meso level aggregations). While Knack sees the *economic* effects of civil social capital as occurring only at the micro level, he does concede that its *political* effects can be manifest at the macro level as “social cohesion and civic engagement”. He cites a number of studies which suggest that civil social capital can “strengthen democratic governance (Almond & Vertan, 1963), improve the efficiency and honesty of public administration (Putnum, 1993) and improve the quality of economic policies (Easterly & Levine)”. Added to this the evidence available from Social Development’s own Participation and Civic Engagement group on the results of public accountability mechanisms pursued by civil society groups in India, Philippines, Brazil and elsewhere and their effects on public expenditure and service quality, makes it difficult to confine the economic effects of civil social capital to the micro level.⁴¹

Ideally public and civil social capital complement one another, together providing what Fukiyama describes as the “high trust society”. In such societies there is “less need to spell things out in lengthy contracts; less need to hedge against unexpected contingencies; fewer disputes and less need to litigate if disputes arise”⁴². He cites Japan, Germany and the US as high trust societies and China and France as low trust societies. The main difference he sees is that in the latter countries is their reluctance to trust people outside the family. Trust in these societies is “specific” between people one already knows and has links with rather than “generalized” trust in strangers. It is this generalized trust or “spontaneous sociality” that Fukiyama sees as supporting more flexible and productive economies where new ideas and technologies can be taken on and corporations can hire professional managers rather than keeping all the managerial positions “in the family”.

Knack⁴³ notes that although Fukiyama's book is largely descriptive, an empirical study carried out by La Porta⁴⁴ provides support for his conclusions. Using an index of trust measuring the percentage of a sample survey who think that "most people can be trusted" to "you can't be too careful in dealing with people"⁴⁵, the study found that regardless of income levels, countries where there is high generalized trust grew faster than countries where people's trust was confined to family members.

There is a good deal of evidence that civil social capital – often generated within more local level groups where face to face contact and personal relations can be maintained – comes in to fill the "trust" or "contract enforcement" vacuum left by the absence of good governance. Knack and Keefer⁴⁶ found that the impact of trust on growth is significantly higher for poorer countries – where legal and financial markets are less well developed.

The discussion of public and civil social capital is useful in elucidating the connection between social inclusion and empowerment. While public social capital and social inclusion manifest themselves primarily through policies, laws and formal institutions at the national, civil social capital and empowerment tend to be most visible at the local level and in the tacit, unwritten codes of behavior. Just as policies, laws and government institutions can either be inclusive and pro-poor or not, so civil social capital and the norms and behaviors that support it can either support and empower the poor and marginalized -- or it can be repressive, locking them into perpetual poverty and exclusion.

This is where the *agency* of individuals and groups manifests itself. As we noted earlier, even for a single individual, the number of institutions which may shape his or her identity and values is myriad. So are the accompanying claims that individuals can make on others and the obligations he or she has towards others by virtue of membership in these various institutions. And while some of these institutions present mutually reinforcing claims and obligations, other institutions affecting the individual present very different – and often competing – sets of claims and obligations. Some of these claims and obligations empower her and increase her freedom while others restrict and confine her. This is the seemingly chaotic field upon which social change takes place. This is where individuals and groups act by accepting, rejecting or combining in new and creative ways some of the "humanly devised constraints on human interaction" which institutions present to them.

Section 4: A Theory of Social Change

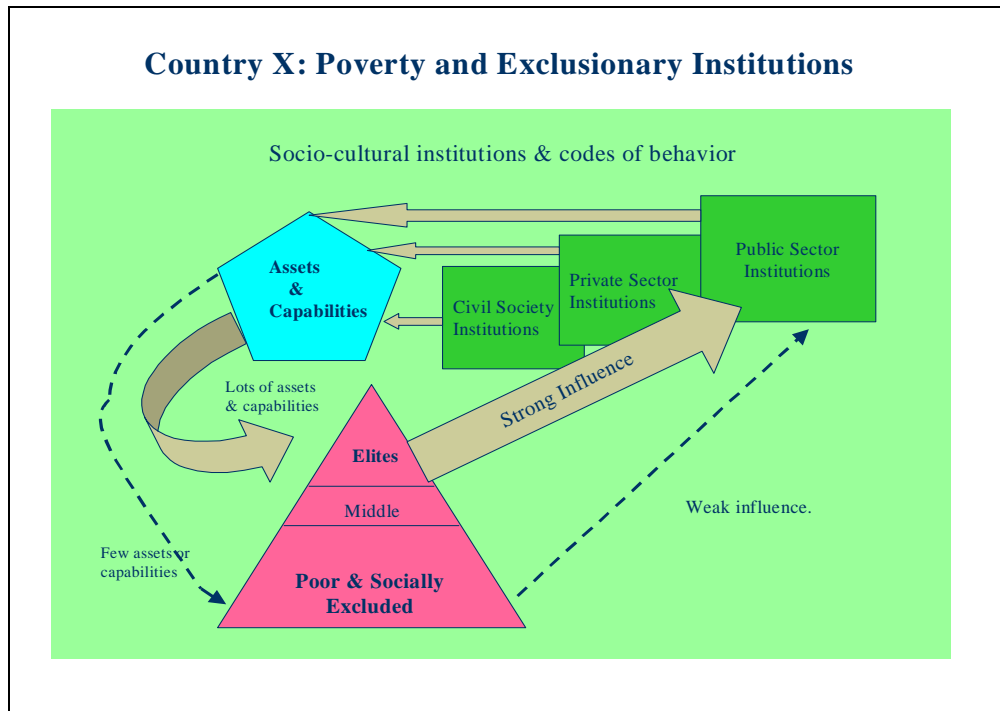
4.1 Initial Conditions of Poverty and Inequity

Figure 7 shows a hypothetical country X where the "initial conditions" are high levels of poverty and inequitable distribution of the assets and capabilities in the livelihood assets pentagon. The income pyramid has a small tip of elites who control most of the assets and capabilities and maintain their strong influence over the set of interlocking and highly exclusionary social, business and government institutions. The way these institutions operate is heavily influenced by underlying hierarchical norms and codes of behavior based on social identity. In other words, this is a country

where each individual’s social identity in terms of gender, racial, linguistic or ethnic background, determines his or her access to good employment, good schools, health care, political influence and so on. The poor and socially excluded who make up more than half of the citizens of this country are disempowered. Despite their great numbers, they have very little voice or control over the institutions in their country and must make do with the thin flow of assets and capabilities that come their way.

From the perspective of this paper, empowerment and social inclusion are viewed as two closely linked dimensions of the process of social change needed to loosen the elite group’s lock on the assets and institutions in country X. How do these two dimensions of the change process work? And how are they related to each other? At present, we have no clear answers to the second question. There does not appear to be any necessary starting point or linear sequence for the empowerment and social inclusion dimensions of the change process. The two are intertwined and **opportunities for action will be different in each socio-political context and at each historical moment.**⁴⁷ Even in cases where the absence of pro-poor policies and institutions suggests that action must begin at the grass roots level with empowerment, it is important to recognize that action “from below” also requires some minimum degree of an enabling institutional and policy environment. So this “social inclusion” or structural dimension of the change process can never be ignored.

Figure 7.



4.2 Two Dimensions of Empowerment

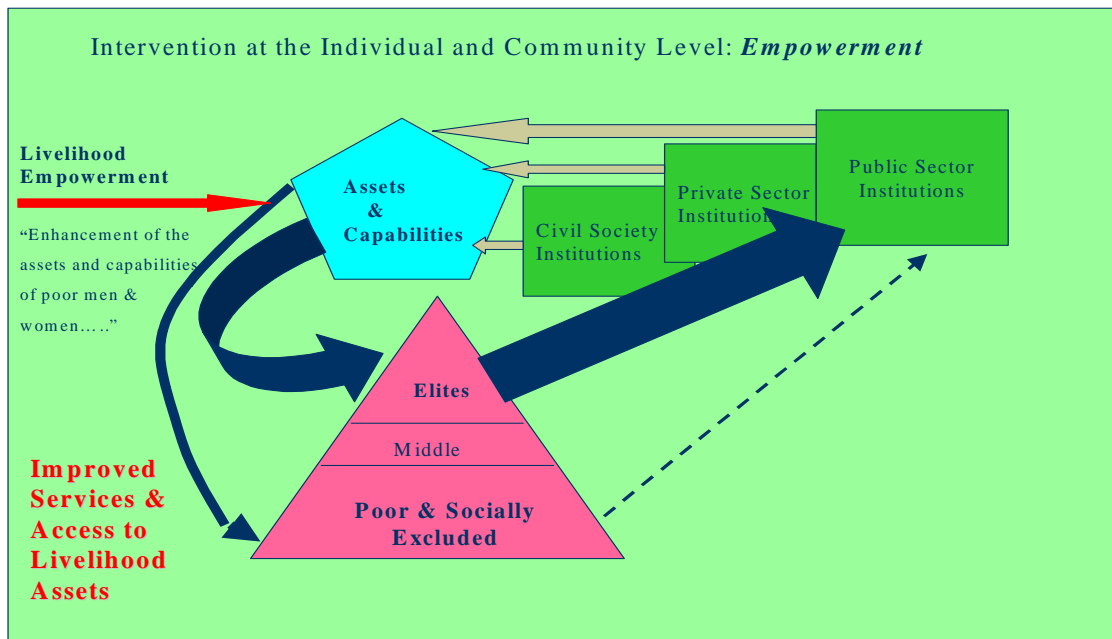
As defined in the draft Social Analysis Policy, the process of empowerment seems to fall naturally into two parts: 1) *Enhancement of the assets and capabilities of diverse individuals and*

groups...2) so that they can engage, influence and hold accountable the institutions which affect their well being. While there is no absolute necessity that the process proceed in this sequence, attaining sufficient assets and capabilities to earn a secure livelihood (what Friedman calls “life space”⁴⁸) is the foundation for everything else. Social mobilization of the poor, political awakening, grass roots organizing, consciencization: whatever we call the second aspect of empowerment, it can rarely be sustained unless some attention is paid to improving access to services and livelihood assets. At the same time, it has been found that unless the poor are mobilized to take some responsibility for improving their own situation while they also learn to hold those delivering services accountable and to continue demanding better access to livelihood resources, even the most well-intended top down systems rarely deliver.

The **two aspects of the empowerment process** are illustrated in Figures 8 and 9. In operational terms, the first aspect (shown in Figure 8) is **improving access to services and livelihood assets**. We call this “livelihood empowerment” and it can be initiated by outsiders (governments, donors, NGOs) and involves increasing access to the assets and capabilities that can sustain at least a minimum base of livelihood security and create the human capital foundation for upward mobility.

Figure 8

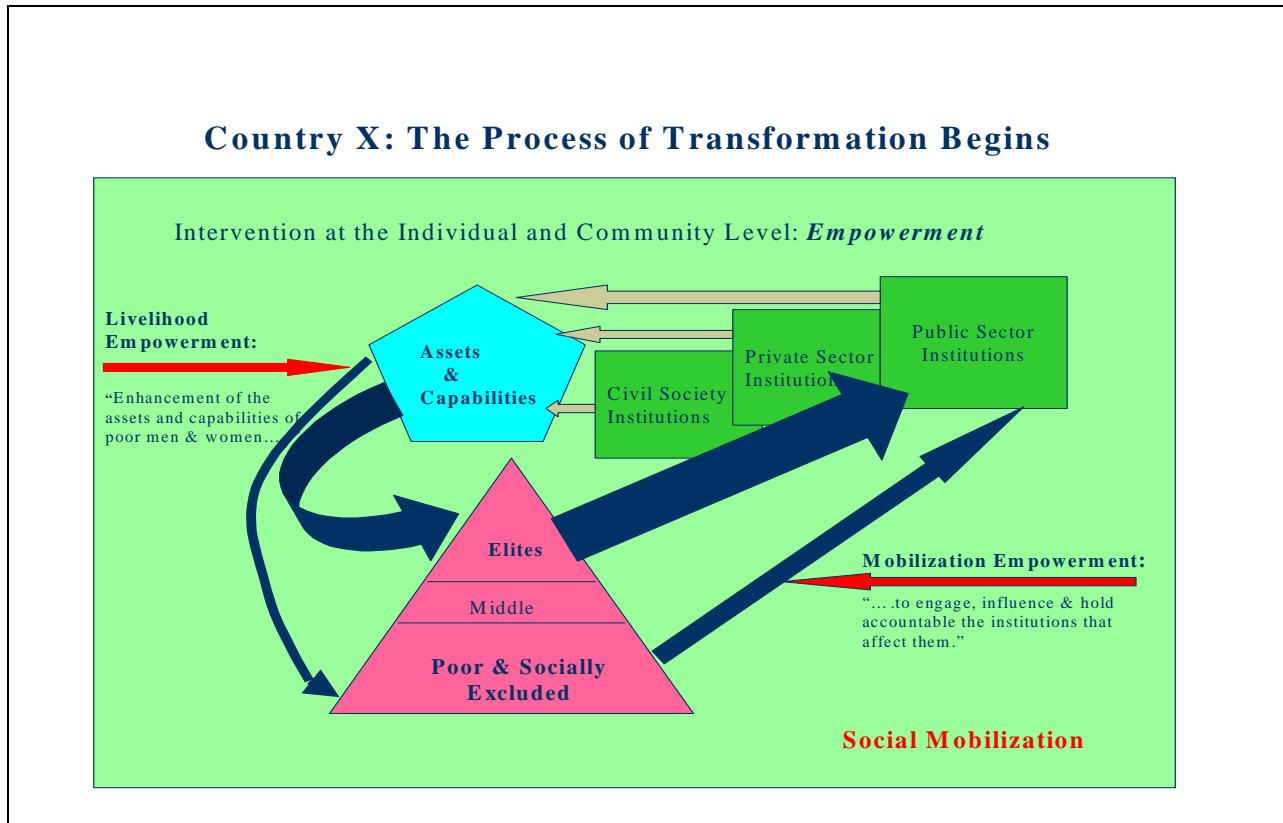
Country X: The Process of Transformation Begins



The second aspect of empowerment – which can be initiated from outside, but in the end can only be done by poor people themselves – is **social mobilization** (shown in Figure 9). This is “mobilization empowerment” and it builds on the very skills, information and linkages (human and

social capital) needed for livelihood empowerment. Mobilization empowerment can lead to new self understanding, solidarity and capacity for collective action. Organizations emerge that can influence and change the encompassing institutional environment – or the “rules of the game” that are used to distribute assets and opportunities to different individuals and groups in Country X.

Figure 9.

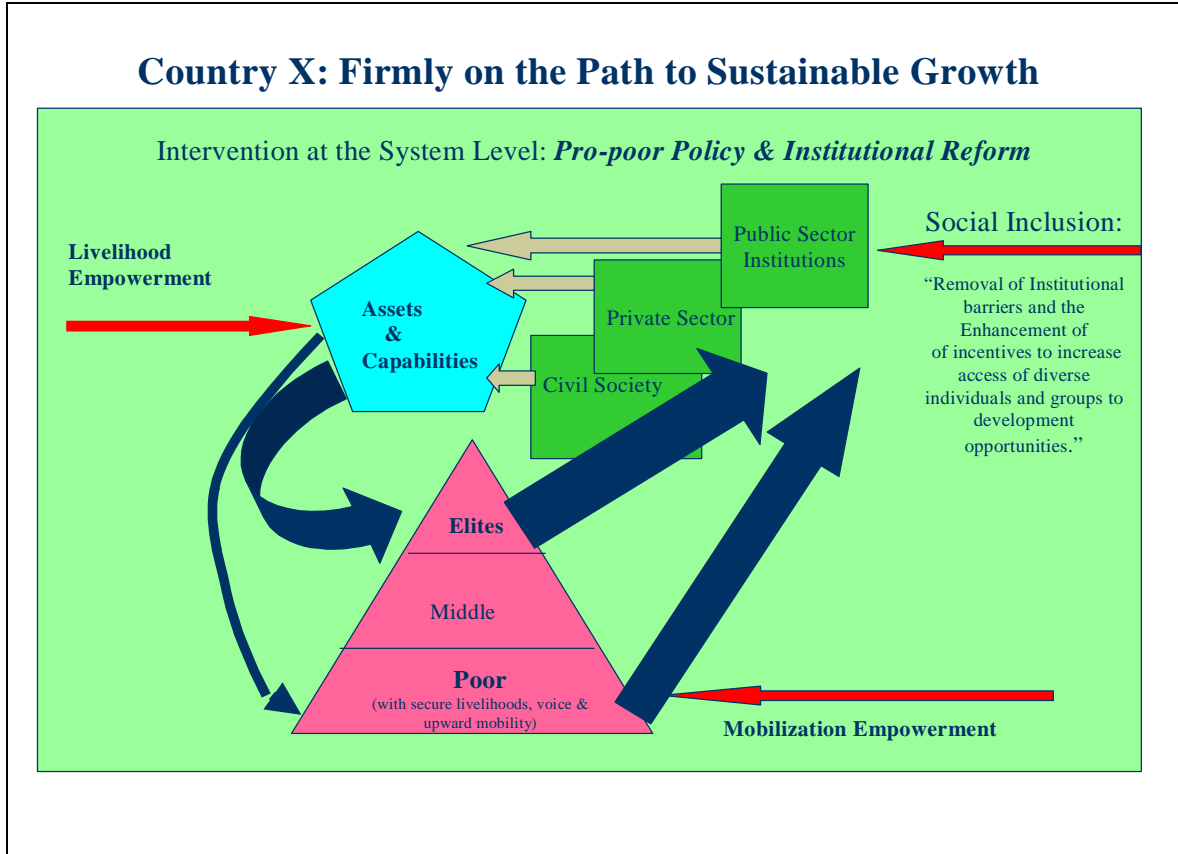


4.3 Social Inclusion

This leads us to **social inclusion** which is about the institutions and the policies that must be changed (see Figure 9). Once again, we are guided by the definition in the draft Social Analysis OP: “*Social inclusion is the removal of institutional barriers and enhancement of incentives (through good policies?) to increase the access of poor men and women and other excluded groups to assets and development opportunities.*” The route to an inclusive society is through **pro-poor policy and institutional reform**.

While empowerment focuses on the individual or group and hence the micro level, social inclusion is about changing institutions at the system level. However, both are about increasing access for the poor to assets and capabilities and as mentioned earlier, both are closely intertwined.

Figure 10



To borrow the terms used by Moser⁴⁹ and Molyneux⁵⁰ in their various writings on changing gender systems, empowerment tends to begin by mobilizing poor and excluded people around meeting their immediate *practical*, survival needs. Livelihood empowerment process begins to address those needs. Then over time through social mobilization, this energy can be turned to creating the awareness and building the organizations of the poor that can address their longer term *strategic* needs. Social inclusion too, is aimed at meeting the *strategic* needs of the poor. **Like the social mobilization aspect of empowerment, social inclusion seeks to change the overall system within which the needs of the poor are to be satisfied.** But as it is used here, social inclusion refers to action which is initiated not “from below” like empowerment, but from a position of power – usually within the system that is to be changed.

At the micro level individuals and groups use assets (including their civil social capital) and capabilities to empower themselves to be able to influence institutions and negotiate a better “deal” in terms of the flow of assets and opportunities dispensed by these institutions. So micro level change (and the development intervention that seeks to catalyze it) *can* lead to system change. But other than cases of violent revolution, the process of change from below is halting and frustratingly

slow for poor people, for concerned better-off fellow citizens who want to help from within the system and for development agencies who want to help from outside.

The reason that the needed social transformation is so slow is the same reason that empowerment from below needs to be supported by complementary efforts at the system level to make institutions and policies more inclusive. After all, the institutions which control the rules of distribution are themselves controlled by those who benefit from the current patterns. As the WDR 2000/01 observes, the greater the social and economic inequality in the “initial conditions”, the more difficult it is for economic growth to translate into poverty reduction.

Figure 10 illustrates country X after it has made important structural changes fostering empowerment/civil social capital and social inclusion/public social capital. Here, poor and wealthy citizens alike have significant influence on formal public, private and civil society institutions – and the underlying socio-cultural institutions do not privilege one gender over another or certain religious or ethnic groups over others. Hence, access to the assets needed for sustainable livelihoods are broadly available. The rule of law prevails and there are both strong formal regulatory systems as well as high levels of generalized trust – all of which lower the transactions costs of doing business.

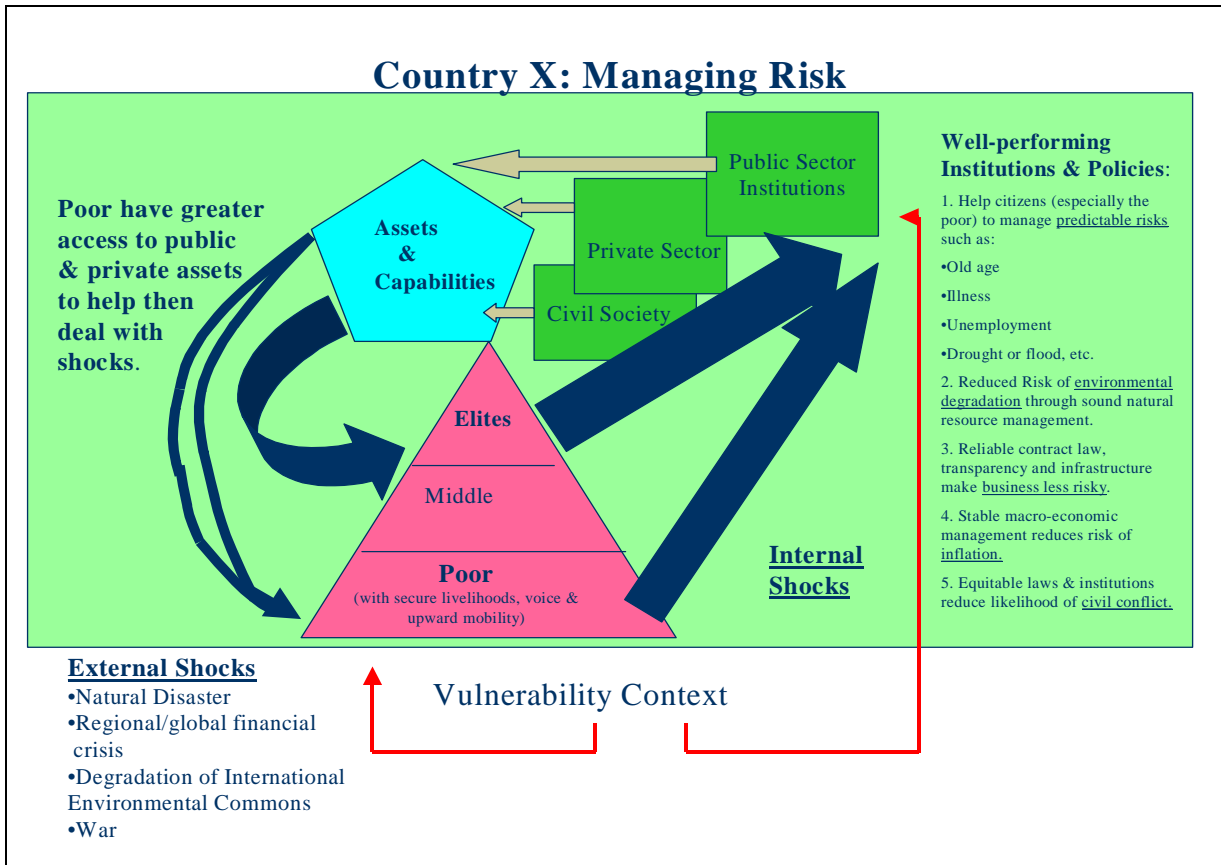
4.4 Managing Risk

Figure 11 expands this picture to show improvements in the **vulnerability context** of country X. Earlier, when its institutions served only the interests of a small group of elite, most of the ordinary citizens of country X had little help in dealing with the predictable risks such as old age, unemployment, natural disasters, etc. Without clear contract enforcement and transparent accounting norms, business risks were high. Street violence and even armed civil unrest was a constant threat. While this situation affected rich and poor alike, its impact on the poor was the

most harsh. In the transformed country X however, the government has established social protection systems for old age and unemployment security. Now even the poor have some assets to cushion them from adverse shocks and safe savings and even insurance services are available to them to help with consumption smoothing.

In the WDR *Attacking Poverty*, several of the actions proposed for “making state institutions more responsive to the poor and removing social barriers” involve bottom up actions which we would describe as *empowerment*. “Facilitating the growth of poor peoples’ associations and increasing the political capacity of poor people” (WDR 01:99) are two examples which prepare and mobilize individuals and groups of people so that they can be effective in changing the “the system” from below. These two examples both involve fostering civil social capital and civic engagement. However, most of the approaches discussed in the WDR involve efforts at *system level change* that result in what we have called *social inclusion*. The approaches mentioned include public sector reform, pro-poor decentralization, financial sector reforms to support the delivery of market based financial services to the poor, improving the legal system to make it more equitable and accessible to excluded groups, etc. Clearly, these reforms must be led by government and involve the creation of public social capital.

Figure 11.



However, since government is itself part of the system that is to be changed, the pressure from below created by empowered citizens are essential. Barraclough gives a powerful example of the complementarity between empowerment and social inclusion:

While not a sufficient condition for needed reforms, peoples ability to articulate their demands and mobilize for collective action (or the fear that this may happen) are usually indispensable for bringing about reforms. Popular mobilization leading to collective action may provoke violent repression and other anti reform measures, but in the long run it is usually essential. Look at South Africa, for example. If there had been no collective and articulated protests by the victims, would official apartheid have ended in the 20th century? One doubts it⁵¹.

Section 5: The Link to Economic Growth

5.1 Distribution and Growth

But a lingering concern remains. Does the picture of our “ideal” reformed society in Figures 10 and 11 show us *sustainable poverty reduction*, or is it just a picture of *redistribution*?

Evidence from countries across the world tells us how important growth is for sustainable poverty reduction. In a recent study tracing the sources of the decline of poverty in India, Ravallion found that 87 per cent of the improvement was due to the growth component rather than changes in distribution⁵². So we must ask whether the new, more equitable institutional relationships between people in this reformed country X will actually contribute to *growth* and help to increase the overall size of the assets pentagon or is this just a case of changing the allocation of a fixed pie?

For many development economists, more equitable distribution has been seen as a tradeoff with growth. Redistribution through populist transfers could lead to fiscal destabilization – or if the transfers were paid for by high taxation, it could reduce incentives for investment and entrepreneurship. Either way growth would stagnate. The World Bank’s first WDR on poverty in 1980 put its faith in the growth process itself -- “the rising tide that lifts all boats” -- to reduce poverty⁵³. Indeed, Hollis Chenery and others held that the growth process itself would bring redistribution⁵⁴.

The debate continues and some recent studies have found a positive and significant relationship between inequality and growth – at least in the short and medium term⁵⁵. But there is growing evidence that inequality – especially with respect to the distribution of *assets* – actually slows growth. A number of empirical studies based on what is called endogenous growth theory⁵⁶ have found a negative correlation between the average rate of growth and a number of measures of inequality in cross country regressions⁵⁷. The general theory used to explain the observation is that the lower growth performance of high inequality countries reflects the differential access of the poor to productive assets in these countries. This under-investment in the poor leaves large numbers of workers less productive than they could be and thus reduces the aggregate efficiency of the economy. Birdsall and Londono suggest that for Latin America, at least half of increase in poverty in the 1980s can be accounted for by the deterioration in income distribution relative to the previous decade. They calculate that “if the economies of Latin American had maintained the same income distribution throughout the 1980s as in 1970, the increase in poverty would have been smaller by almost half⁵⁸ in the years 1983-1995.”

There are a number of direct channels through which high levels of inequality are thought to dampen growth. Alesina and Rodrik trace the link through the “median voter theorem” which holds that (at least in a democracy) the median voter will determine the tax rate. Thus the lower the average individual’s share of capital income (relative to his labor income), the higher his ideal tax and the lower his ideal growth rate. As long as income is being transferred to him through a tax on capital, he has no incentive to accumulate capital himself.⁵⁹ Another channel is imperfect credit markets: because of the inability of the poor to offer collateral, and the difficulty of reaching many disbursed and often illiterate clients with small loans, lenders fail to make potentially productive loans to the enterprising poor⁶⁰. A third route by which inequality hampers growth is through the instability and social unrest that it is expected to create. Deininger reports that in Latin America where inequality is highest, crime leads to an average loss of 7.5 percent of the annual GDP.⁶¹

5.2 Investment Climate: Improving the Link between sowing and reaping.

Although he does not refer directly to distributional issues, Nicholas Stern does cite instability and high levels of violence among the factors which he sees as detrimental to the investment climate.⁶² Understanding what makes a good investment climate is another way to help us to understand why empowerment and social inclusion – and the higher levels of equality they create -- can actually be good for growth. A careful reading of Stern’s writing on the investment climate suggests that the policies, institutional arrangements and behavioral norms that promote empowerment, social inclusion and security are very similar to those needed to attract investment and stimulate the entrepreneurial creativity which leads to economic growth.

When Stern writes about the Bank’s role in helping countries to improve their investment climate, he uses the language of business and finance. He sees this as the “structural” or growth agenda and outlines the need for macroeconomic stability, good governance (in terms of sound regulation to promote competition, overcoming bureaucratic delay and inefficiency, fighting corruption) and improved infrastructure.⁶³ But integral to the success of the “structural” reform is what he sees as the “social” or poverty reduction agenda. They are not in his view, separate agendas:

Some may be tempted to think of the structural agenda as for (hard-headed) growth and the social agenda for (soft-hearted) poverty reduction, but this is the wrong way to view these issues. The social agenda of delivering public services, providing effective social protection, and empowering the poor to participate can contribute strongly to growth. And the structural agenda – although aimed directly at improving the investment climate – is vital for poverty reduction.⁶⁴

While in part, he still uses the word “social” here in the more limited sense to refer to the state’s welfare obligations, it is clear that when he brings in empowerment and participation he is actually using “social” in a “structural” way that refers to institutions and the power relationships they establish between people.

Stern’s strategy for development has two pillars:

- Investment climate → Growth → Poverty Reduction
- Empowerment → Poverty Reduction

Considerable evidence is presented to show that the *results* of a good investment climate are good for the poor: more jobs in a growing economy (especially jobs in SMEs which tend to be more accessible to the poor), higher productivity, higher wages, deeper financial markets that can offer consumption smoothing and risk management products even to low end customers and so on. This is familiar territory, but Stern points beyond the usual growth/poverty linkages when he describes the institutional and behavioral *foundations* of a good investment climate as **“a more reliable link between what you sow and what you reap”⁶⁵**.

From the business point of view this reliable link between investment and profits may mean, the rule of law that guarantees enforceable contracts and equal treatment, sound monetary policy, regulation of key industries to insure open competition, a banking system that observes international accounting standards, a stable, democratically accountable government with well paid civil servants who do not expect bribes to perform their functions – and who can expect negative repercussions if they do not perform. Such institutional and behavioral foundations do not remove the risk inherent in investment, but they greatly reduce it.

These same foundations also reduce risks faced by the poor and the arbitrary “taxes” imposed on them by predatory bureaucrats and criminal gangs . The volumes of the *Voices of the Poor*⁶⁶ and Moser’s writing on violence in Latin America⁶⁷ give powerful evidence that the absence of the rule of law and accountable, transparent public and private sector institutions affects the poor more harshly than anyone else. Demands for bribes, police harassment and street violence all increase the vulnerability of the poor and constrain their ability to participate in the market economy and in the civic life of their communities. Added to the failure of the state to provide basic protection, is the failure to provide basic services and infrastructure⁶⁸ such as education, health care, water and sanitation, energy, communication and transportation. If they are available at all to the poor they are likely to be unreliable, poor quality and/or high cost. Or, as De Soto shows us, many of these services such as water, lighting and transportation, may be provided to the poor by other poor – the entrepreneurial “informals” who are forced to operate illegally outside a formal government system controlled by the elite⁶⁹. In such situations the formal state bureaucracies not only fail to deliver services to citizens living in illegal slums, but refuse to even officially recognize the existence of these decades old slums and place formidable bureaucratic barriers in the way of recognizing the small businesses that do provide basic services in these areas.

If we return to Figure 11 on the vulnerability context, we see that many of the things governments would need to do to improve their investment climate would also greatly reduce the risks of what we labeled the “internal shocks” that affect all citizens, but are especially threatening to the poor. As pointed out by Holzmann and Jorgensen⁷⁰, social protection systems that help people deal with unemployment or loss of livelihood through old age, illness or during a drought are fundamental to enabling the poor to take the necessary risks involved in planting a new higher yielding crop or opening a new business. In addition to the risk aversion which traps the poor in low return activities, the absence of public or affordable commercial risk management systems can also force the poor into traditional informal risk sharing arrangements which have “high transaction costs and hidden opportunity costs”⁷¹. An example that comes to mind here is the practice in Bangladesh where even though the law mandates that daughters get some share of the paternal property, sisters feel obliged to turn over their shares to their brothers. They do this not just out of “affection” (which may also be a factor), but because they view such gifts as a way to insure their right to return to their brother’s house should they be expelled or widowed. In a setting where land markets are “sticky” and buying and selling land requires time and sophistication to maneuver through the rent seeking legal bureaucracy, and in a male dominated society where it is difficult for women to productively manage property, it may be difficult for a woman to gain much direct benefit from such an inheritance. So giving it away in exchange for this informal “insurance policy” with the brother is a rational choice. However there is no guarantee that the policy will pay off, and several authors have noted that in recent times with the greater fluidity of rural Bangladeshi

society and the frequent weather related economic shocks, brothers are less and less willing or able to take in their destitute sisters even when they have benefited from their share of the family land.(get refs)

In addition to reducing risk through the provision of social protection, good governments also support policies and institutions that provide the stability that both businesses and citizens (rich and poor alike) need to thrive. Just looking at the items mentioned in Figure 11 we see the many ways a well functioning government can simultaneously reduce vulnerability and attract growth promoting investment and entrepreneurship:

- A **stable macroeconomic environment** that reduces the likelihood of rapid inflations which hurts business and the poor.
- **Environmental and natural resource management policies with a long term view** – especially those that recognize local community ownership – encourage a healthy environment, a balanced and sustainable flow of renewable natural resources. Both the positive health impacts and the sustainable management of natural resources are important to all citizens – but especially to the poor who suffer the most from polluted air and water and who are often dependent on natural resources for their livelihoods.⁷²
- A **sound financial and banking system** is clearly good – indeed essential -- for a vibrant and growing business economy which provides employment opportunities for the poor. But beyond that is the even more direct benefits of a financial system that is deep enough to provide not only working capital and investment credit to the working poor, but savings and insurance products that can help them – and even the ultra poor who cannot borrow – to smooth consumption and manage risk.
- The **rule of law and an effective legal system** are clearly important to business which needs contract enforcement, etc. and to both rich and poor citizens who need to be free from the arbitrary use of power whether by the private sector, the public sector or by civil society.
- Related to the rule of law are **civil liberties** and an **inclusive political system that makes government democratically accountable to all citizens**.
- Where such institutions are not in place to negotiate differences and resolve conflicting interests among different groups, there is **increased likelihood of violence and civil conflict**. Even the threat of such conflict puts a chill on legitimate business investment. The actual outbreak of violence directly threatens both the physical and the economic security of all citizens – but especially the poor who are often the least able to leave the war zone.

5.3 The African Example

Collier and Gunning⁷³ offer a particularly rich and empirically grounded example of what a poor investment climate means and how it manifests itself at both the aggregate and the micro level in the African context. The authors review the aggregate data for the region from a number of growth regression studies that have sought to understand why Africa has suffered a decline in per capita GDP over the last decades. They then look at micro data to see how agents (households and

firms) and markets have responded to the constant risks and uncertainties they face in this hostile setting to see whether macro and micro level explanations are consistent.

The section on agents is particularly useful because the data on households gives us a sense of the “vulnerability context” in which the poor must operate to earn a livelihood and how they have responded, while the data on firms gives us the business point of view and helps us understand why the “investment climate” is so important to growth. While the authors conclude that households have actually coped better than firms, it is clear the same public sector institutions which have failed business have also failed the poor – for many of the same reasons. In Stern’s terms, both households and firms in Africa suffer because *they cannot be sure of a reliable link between reaping and sowing* and this has had disastrous impact on economic growth and on welfare indicators in the continent.

Part of the uncertainty is because of the harsh physical environment in Africa⁷⁴, but Collier and Gunning convincingly demonstrate how, instead of reducing the uncertainty through the kinds of policies and institutions discussed above, most African governments have only compounded it with frequent policy changes and reversals. The authors’ conclude that along with the high risk posed by Africa’s hostile environment, a major cause of economic stagnation in the continent has been “inadequate social capital -- particularly dysfunctional government”⁷⁵.

The distinction between public and civic social capital discussed earlier in section 2 is important to the analysis. *Public* social capital defined as “the institutions of government that facilitate private activity” seems to fit well with Stern’s idea of the investment climate. *Civic* social capital is embodied in more informal social networks. As we recall, it includes Putnum’s horizontal associations -- the choirs, guilds, bowling groups, etc. -- as well as more vertical networks such as kinship systems and various hierarchical relationships. These networks, in addition to whatever social or physic benefits they provide, also “build trust which lowers transactions costs, (offer) .. knowledge externalities... and ... enhance capacity for collective action”⁷⁶.

In the authors’ view civic social capital is important to growth because civic organizations put pressure on governments to produce public social capital, or in other words, a more socially inclusive governance system that is responsive to a much broader segment of society – rather than serving the interests of a small select group. In the African context the absence of civic social capital has contributed to economic stagnation,

*because governments were captured by a narrow elite that undermined markets and used public services to deliver employment patronage. These policies reduced the returns on assets and increased the already high risks private agents faced. To cope, private agents moved both financial and human capital abroad and diverted their social capital into risk-reduction and risk bearing mechanisms.*⁷⁷

This picture of public, private sector and even most civic institutions captured by the elite – and used to set the “rules of the game” to favor themselves in the distribution of assets and capabilities, is very much the picture we see of Country X in Figure 7. The institutions which control the access to (and even to some extent the returns on) assets and capabilities are

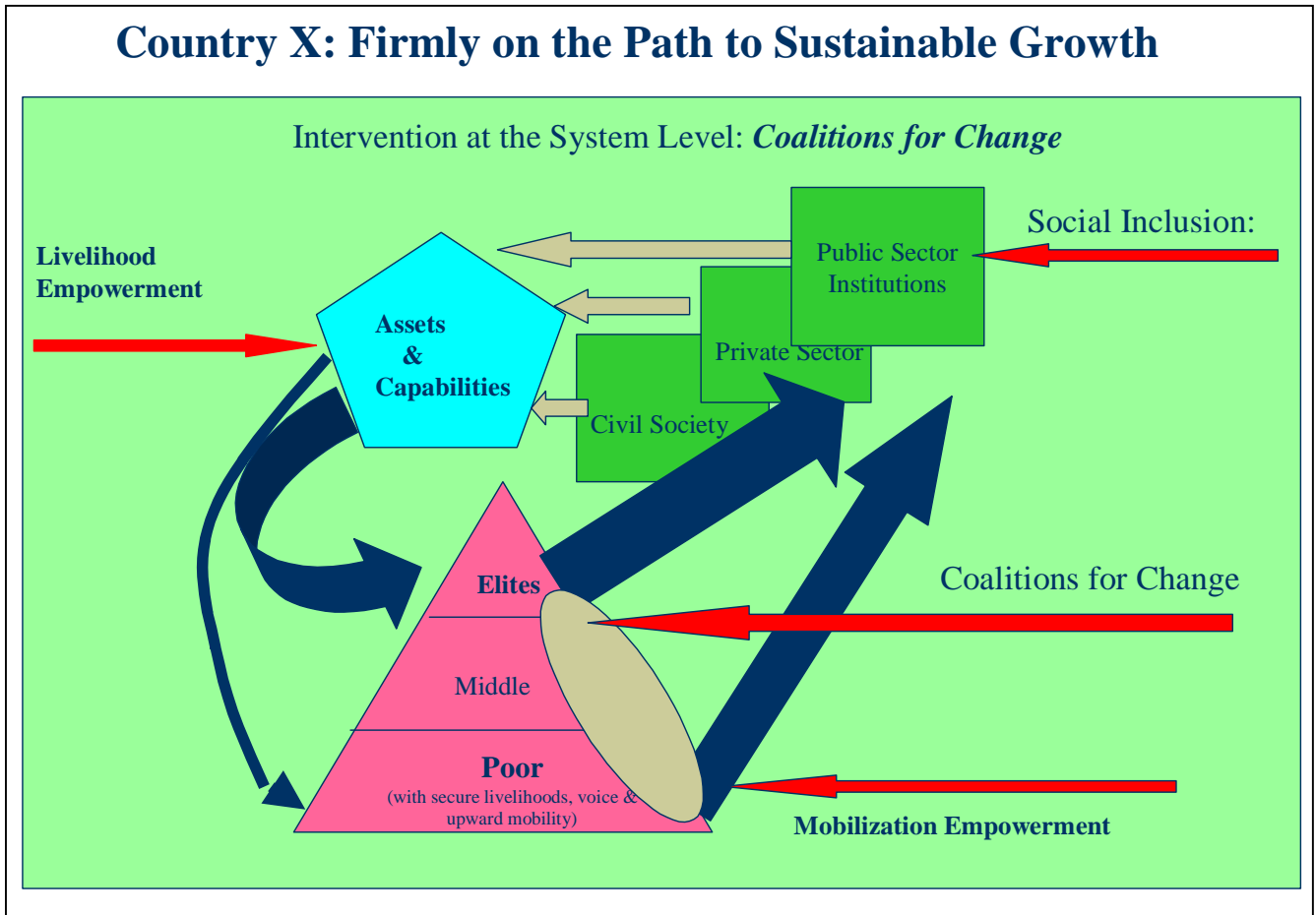
exclusionary. Neither the middle class, nor the poor have the influence or voice they need to make either public or private sector institutions accountable to them.

What Figure 7 does not show is that over time in the absence of any reliable accountability mechanisms, the tight little circle of elites who control the institutions of Country X (and through them, the lion's share of wealth), breeds corruption and inefficiency and ultimately in the case of Africa, negative growth. The asset and capabilities pentagon in African countries has actually contracted as both foreign investors and the elite themselves found high risks and low returns in their own economies and sought to invest their assets (financial and human) elsewhere. The poor governance situation in country X and in so many African countries is also highly likely to lead to violent conflict. While Africa is highly fractionalized⁷⁸, an earlier study by Collier⁷⁹ found that **high ethnic diversity only has negative growth effects in societies lacking in political rights** – as has been the case with so many African countries until recently. The negative effects are not limited to economic stagnation. X out of sub-Saharan Africa's xx countries, xx have undergone or are currently in the throws of violent conflict. (*Check with Ian and Conflict group for data*).

The lack of accountability to the broader public which initially seems to leave political leaders free to do as they wish, ultimately makes them more vulnerable to discontented factions within their own small group of elites. Collier and Gunning cite this as one reason that early attempts at reform in Africa proved short lived and were soon reversed: “Being insulated from the mass of the rural population and having only limited legitimacy, governments were acutely exposed to pressures from their own base of supporters”⁸⁰. When inefficient businesses owned by the elite began to suffer from competition caused by removal of trade barriers and price controls, the majority of the population who stood to benefit, had little influence or voice to prevent a return to the status quo.

The ray of hope for Africa's return to higher growth which Collier and Gunning offer us is very similar to the mechanisms of empowerment – especially empowerment through social mobilization – shown in Figure 9. They point to the “wave of democratization in Africa during the 1990s (which has) weakened the power of the old elites and so paved the way for politically sustainable reforms”⁸¹. The new-found civil liberties should enhance the level of civic social capital which has been so weak in Africa. This will enable a much broader group of citizens to protest the legacy of low public social capital -- the poor government services, lack of physical and institutional infrastructure, corruption and favoritism. Rather than the “quiescent majority” who long remained without voice or influence over the workings of government, there is now scope for broad based “coalitions for change” between the poor and the middle and upper classes (see Figure 12). Such coalitions can arm themselves with information that can be widely spread through a more open press. They can mobilize public opinion to demand an overhaul of the inefficient, narrow and often brutal institutions and policies of the past. The authors don't foresee a quick and easy transformation to economic dynamism in Africa, but they are clear about the important role that empowerment through the resurgence of civic social capital will play in the process.

Figure 12

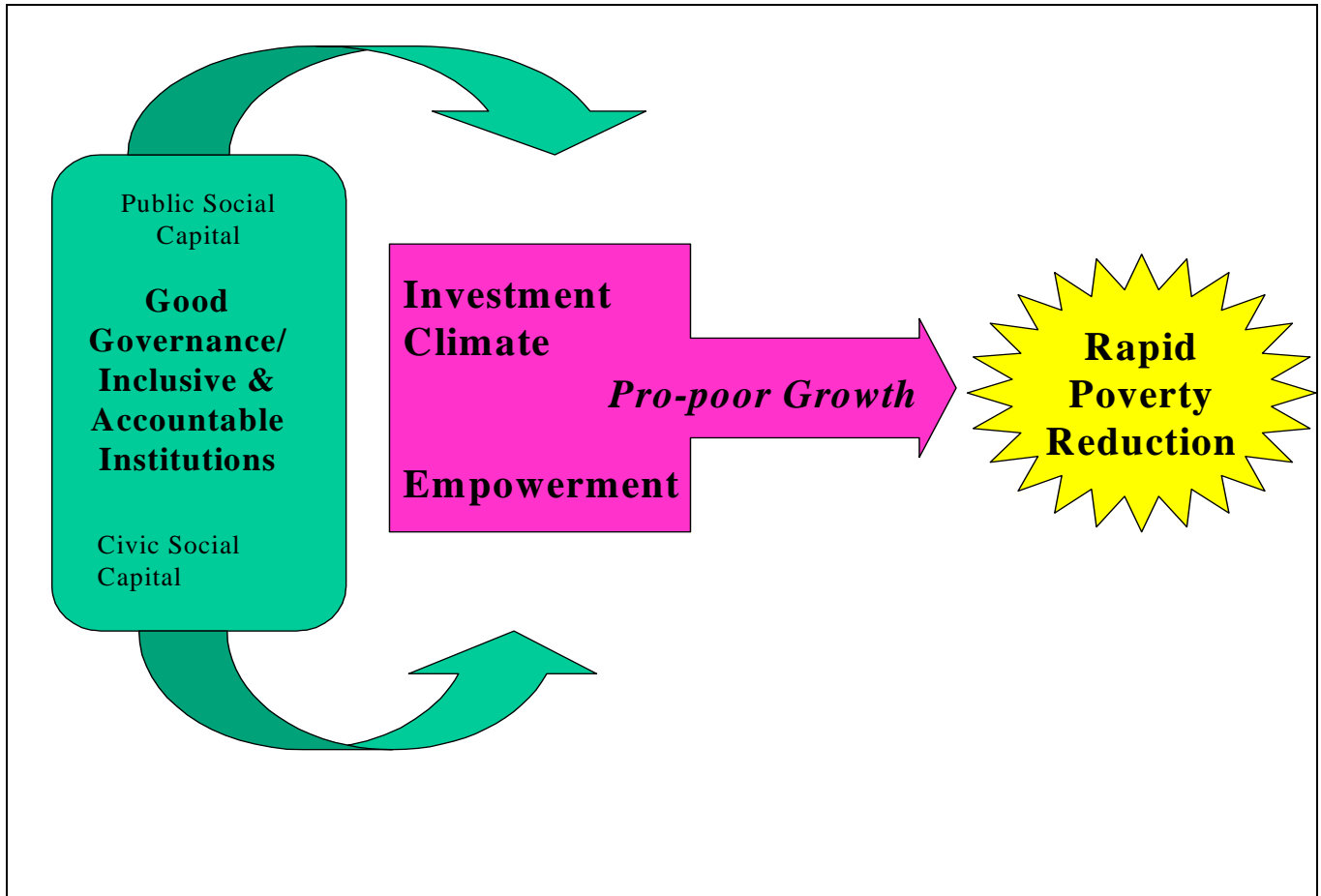


5.4 Good Governance: The Foundation of Growth and Empowerment

The African account suggests a way to expand on Stern’s strategy for development by visualizing the common foundation of good governance/inclusive and accountable institutions that underpin both the growth and the empowerment pillars. It turns out that civil liberties which empower a wide cross section of society to speak out and protest unequal treatment and poor service delivery is also critical for a good investment climate – and therefore to growth itself.

Figure 13 presents a new visualization of Stern’s strategy for development where instead of *parallel* paths to poverty reduction through investment climate and growth on the one hand and empowerment on the other, we show **investment climate and empowerment both emerging as two complementary outcomes of good governance and jointly producing pro-poor growth and rapid poverty reduction**. The positive impact of public and civil social capital on growth is seen to operate through the creation of a good investment climate on the one hand and on the other, through empowered citizens who can make sure it stays that way. A good investment climate allows markets to work by offering enforceable contracts and transparent, predictable business dealings where no special treatment is given. But the very rule of law that creates this enabling

Figure 12.



environment for business also empowers citizens so that they can continuously insist on transparent, inclusive and accountable institutions rather than institutions which favor one group of citizens over another. Citizen empowerment then becomes a means of ensuring the checks and balances between public and private sector are maintained and makes it more likely that the type of growth which occurs will be pro-poor.

The link posited here between empowered citizens and growth is not the same as positing a straight forward link between democracy and growth. It is well known that some of the East Asian countries where there has been rapid growth and poverty reduction over the last several decades have not been highly democratic. It is also well known that there are important variations in the degree of influence which the average citizen actually has within the general set we call democracies. However, Bueno de Mequita et al⁸² have suggested a way of measuring the size of the group to which government leaders must respond if they are to stay in power rather than simply categorizing countries as democracies or autocracies. The authors look at two institutions which they believe determine the degree to which leaders will be concerned with the production of public goods rather than private goods which get distributed to a small group of their supporters. One institution is *selectorate*: “the set of citizens who have a chance of becoming members of the winning coalition”. In a genuine democracy this includes all

adult citizens who have the vote. In an autocracy it would include a much smaller group of elite families or perhaps members of a certain favored ethnic group. The second institution of concern is the *winning coalition*: “that portion of the selectorate who keep the incumbent in office and who get privileges not available to non-members”. Again, in a democracy the winning coalition would include all the members of the winning party while in an autocracy it would be whichever of the ruling families had chosen to back the current holder of power. The authors explain that for autocrats bad policy is often good politics:

When the winning coalition is small, leaders are more inclined to provide private benefits, rather than public goods because such an allocation better serves their desire to stay in office. When the winning coalition is large, leaders must be more concerned with provision of public goods, not out of civic mindedness, but because providing such goods is compatible with their desire to stay in office. Thus large winning coalitions, such as exist in democracies, encourage attention to the quality of public policy.⁸³

Using the size of the winning coalition as a continuous variable the authors examine the growth rates of 176 of the most democratic and 176 of the most autocratic leaders since 1952 . The results show an average growth rate of 3.04 per cent per annum for democratic leaders as compared to 1.78 percent for the average autocrat. This difference can be significant over the long term. Beginning with an average real income of \$500 per year in 1950, citizens under the autocrat would be earning \$1,200 by 2000 and \$2,910 by 2050. In a democracy an annual income of \$500 in 1950 would have grown to \$4,480 by 2000 and \$10,035 by 2050⁸⁴.

Political leaders who are accountable to a large group of citizens to remain in power are forced to pay much more attention to good public policy than those who must only keep a small group happy by providing them special privileges. And although the danger remains that the outcome could be the “over production” of public goods through populist policies which create disincentives for capital accumulation and entrepreneurship, it looks as though this is not necessarily what happens. It looks as though the creation of public goods such as infrastructure, education, social protection and the rule of law which help the poor *also* serves to improve the investment climate and stimulate pro-poor growth.

End Notes

¹ Social Development is one of the three groups (along with Environment and Rural Development) which make up the Network Vice Presidency for Environmentally and Socially Sustainable Development (ESSD) in the World Bank.

² Deepa Narayan, August 14, 2001 Draft

³ Asraf Ghani and Clare Lockhart, "A Repertoire: Techniques in Institutional and Organizational Analysis", draft note, June 21, 2001

⁴ Draft Operational Policy 10.05 on Social Analysis, October 10, 2001. The definition of empowerment in the Social Analysis policy also forms the basis for Deepa Narayan's most recent version (Oct 28) of her Staff Guidance Paper on Empowerment.

⁵ The Sustainable Livelihoods (SL) framework grew out of the work of Robert Chambers and others at the University of Sussex and has been nurtured and further refined with support from DFID. See *Sustainable Rural Livelihoods*, Diana Carney, ed., DFID, 1998; also DFID SL website.

⁶ Evidence for this assertion is presented in Chapter 4.

⁷ And these days quite possibly, a resident in another country or even a new citizen in a country other than one's country of origin.

⁸ Op cit.p117

⁹ Draw in specific examples from Woolcock and Rao's on going study of mobility in the Delhi slums.

¹⁰ This paragraph is largely taken from Ashraf Ghani's presentation on Organizational and Institutional Analysis

¹¹ Strategic Framework Paper, Feb 2001

¹² The framework is focused on citizens rights rather than human rights. Since the Bank's owners and clients are nation-states this seems to be the most practical approach. However, we do recognize the importance of the Human Rights framework as a platform for building a broad consensus over time and also for strengthening the claims of some groups of citizens whose voices may not be heard in their own country. See Norton and Moser (2001) for a full discussion of the human rights dimension of social development.

¹³ Loskin, get full ref.

¹⁴ "Voice and participation in public activities" for the "general public" is also explicitly mentioned in Part D, Section 20 "Transparency, Accountability and Corruption in the Public Sector".

¹⁵ Ghani and Lockhart, op.cit. page 2-3.

¹⁶ Martin Ravallion and Shaohua Chen, "Measuring pro-poor growth", World Bank Policy Research Working Paper n. 2666, Aug 2001, p.6.

¹⁷ Ibid, p.16.

¹⁸ Martin Ravallion. "Growth, Inequality and Poverty: Looking Beyond Averages", p.10. This is a December 2001 revision of a paper by the same title published in November 2001 in *World Development*.

¹⁹ See Nancy Birdsall and Juan Luis Londono, 1997, "Asset Inequality Matters: An Assessment of the World Bank's Approach to Poverty Reduction" in *American Economic Review, Papers and Proceedings* 87(2):32-37; Klaus Deininger and Pedro Olinto, "Asset Distribution, Inequality and Growth", June 2000, Policy Research Working Paper no. 2375, World Bank.

²⁰ Martin Ravallion, 2001, "Growth, Inequality and Poverty" op.cit., p.24.

²¹ Martin Ravallion and Gaurav Datt, "Why has economic growth been more pro-poor in some states in India than others?" in *Journal of Economic Growth*, fourthcoming.

²² Ibid, pp 3-8.

²³ Ibid, p.14.

²⁴ Ibid, p.4.

²⁵ Op cit. p127

²⁶ Draft OP 10.05 on Social Analysis, December 14, 2001

²⁷ Add footnote on distinction between institutions and organizations

²⁸ The Sustainable Livelihoods (SL) Framework grew out of the work of Robert Chambers and others at the University of Sussex and has been nurtured and further refined with support from Dfid. Both the SL and the SD frameworks share the same elements – people, assets and institutions. The principal difference is the SD focus on power differentials. See Figure x in Annex y which shows the basic SL framework and suggests where the Bank's concern with empowerment, social inclusion and security can be integrated into various parts of the model.

²⁹ There are different versions of the “capitals”, some include cultural or political capital as well, but in our view social capital can encompass both political and cultural capital and hence we have adopted the five as presented here and in the WDR *Attacking Poverty*.

³⁰ Douglas North cited in Ghani and Lockhart, op.cit

³¹ Cite Social Protection Sector Strategy

³² Cite Environment Sector Strategy

³³ The draft note on “Institutional and Organizational Analysis” written by Ashraf Ghani and Claire Lockhart (Oct 16, 2001) draws on Douglas North to offer the following definitions: “*Institutions* are the formal and informal rules of the game in a society, or the humanly devised constraints that shape human interactions. *Organizations* are groups of individuals, bound by a common purpose, involving a definite set of authority relations, and dedicated to achieving objectives within particular rules of the game.”

³⁴ Ibid,p.4.

³⁵ Carol Graham and Moises Naim, “The Political Economy of Institutional Reform in Latin America”, in *Beyond Tradeoffs: Market Reforms and Equitable Growth in Latin America*, Nancy Birdsall, Carol Grahman and Richard Sabot, eds., (Washington D.C.: The Brookings Institution Press/InterAmerican Development Bank, 1998)

³⁶ This is not to say that traditional non-state institutions are without the power to sanction those who do not stay within the norms. The “honor killings” where women may be killed by their own relatives if they are believed to have threatened the “izat” or honor of the patrilineal family or larger clan group through illicit sexual behavior are an extreme example of such sanctions. While most “post enlightenment” thought holds that only the state may hold the power of imprisonment and physical punishment, there is not universal agreement on this and the issues of whether secular or religious power is preeminent and whether the two kinds of power should be kept separate is one of the sources of tension in the world today.

³⁷ Collier first made this distinction in “Social Capital and Poverty”, 1998, Working Paper No. 4 of the Social Capital Initiative, World Bank. In his more recent article “Explaining African Economic Performance” in *Journal of Economic Literature*, Vol. XXXVII, (March 1999) he uses the term public social capital instead of government social capital and we have adopted the latter term .

³⁸ Collier, 1999 Op.cit. p.65

³⁹ Ibid. p.65.

⁴⁰ Stephan Knack, “Social Capital, Growth and Poverty: A Survey of Cross Country Evidence”, Social Capital Initiative Working Paper No. 7, May 1999, World Bank, p.1.

⁴¹ Cite Civic Engagement literature from Parmesh and William. (e.g. Samuel Paul’s report cards, Philippine Social Weather stations; Porto Alegro. Etc.)

⁴² Fukiyama, 1995, *Trust*. P.

⁴³ Stephan Knack, 2001, op.cit. pp.16-17.

⁴⁴ La Porta *et al* , 1997

⁴⁵ Responses on this scale ranged from 60% positive in Norway to only 8% positive in Brazil.

⁴⁶ Knack and Keefer, 1997

⁴⁷ This point is frequently stressed in *Empowerment and Poverty Reduction: A Sourcebook for World Bank Staff* by Deepa Narayan, PREM World Bank, February 13, 2002 draft.

⁴⁸ John Friedman, *Empowerment: The Politics of Alternative Development*, 1992, Blackwell Publishers, UK

⁴⁹ Caroline Moser, *Gender Planning and Development: Theory, Practice & Training*, Routledge, London , 1993, p.,38-40.

⁵⁰ Maxine Moyneux, “Mobilization without emancipation? Women’s interests, state and revolution in Nicaragua”, *Feminist Studies*, 11 (2)

⁵¹ Solon L. Barraclough, *Toward Integrated and Sustainable Development?*, UNRISD, Feb. 2001, p 37.

⁵² Ravallion get ref.

⁵³ Nancy Birdsall and Juan Luis Londono, 1997, “Asset Inequality Matters: An Assessment of the World Bank’s Approach to Poverty Reduction”

⁵⁴ Hollis Chenery; Montek Ahluwalia; C.L.G. Bell; John Duloy; Richard Jolly, 1974 *Redistribution with Growth*, Oxford University Press

⁵⁵ Kristin.J. Forbes, 2000, ‘A Reassessment of the Relationship Between Inequality and Growth’, *American Economic Review*, 90 (4):869-887.

⁵⁶ Paul Romer, 1994, “The Origins of Endogenous Growth”, *Journal of Economic Perspectives* 8(1):3-22.

⁵⁷; Nancy Birdsall, Carol Graham, and Richard H. Sabot eds, *Beyond trade-offs: Market reforms and Equitable Growth in Latin America*, Washington, InterAmerican Development Bank ,1998;Klas Deininger and Pedro Olinto, 2000, “Asset Distribution, Inequality and Growth”, Policy Research Working Paper no. 2375, World Bank.

⁵⁸ Op.cit. pp34.

⁵⁹ Alberto, Alesina and Dani Rodrik, 1994, “Distributive Policies and Economic Growth”, *The quarterly Journal of Economics* 109:465-490

⁶⁰ Joseph Stiglitz, 1969, “Distribution of Income and Wealth Among Individuals”, *Econometrica* 37 (3):382-397;

⁶¹ Op.cit. p.9

⁶² Nicholas Stern, *A Strategy for Development* , 2001, World Bank

⁶³ Ibid, 52

⁶⁴ Ibid, 153

⁶⁵ Ibid, p 145

⁶⁶ Deepa Narayan, 2000, *Can Anyone Hear Us?* World Bank, Washington D.C.; Deepa Narayan, Robert Chambers, Meera k, Shah & Patti Petesch, 2000, *Crying Out for Change*, World Bank, Washington, D.C.

⁶⁷ Caroline Moser, 2000, *Urban Perceptions of Violence and Exclusion in Columbia*, Washington D.C. World Bank Publications

⁶⁸ It is useful here to make the distinction between public *provision* of these services and public *production*. While the state has the responsibility to provide these services, it is not always in the best position to actually produce them so the most efficient solution is often a situation where the state is responsible for regulating and contracting competing private producers to provide these services either as public goods paid for by general taxes, private goods paid for by user fees or some combination with subsidies available for those too poor to pay.

⁶⁹ Hernado De Soto, *The Other Path: The Invisible Revolution in the Third World*, 1989, Harper & Row.

⁷⁰ Robert Holzmann and Steen Jorgensen, “Social Risk Management: A new conceptual framework for Social Protection and beyond”, page 7, World Bank, Feb 2000

⁷¹ Ibid, p

⁷² cite Environment strategy paper and background paper on Environmental Health

⁷³ Paul Collier and Jan Willem Gunning, “Explaining African Economic Performance”, *Journal of Economic Literature*, Vol. XXXVII (March 1999) pp. 64-111.

⁷⁴ E.g. Low rainfall and poor soil over much of the continent limit agricultural productivity; population density is low and many countries are land locked which increases transportation costs and many areas are prone to Malaria and other diseases. High reliance on natural resource exports have also made many countries vulnerable to fluctuations in world commodity prices.

⁷⁵ Ibid, p.65

⁷⁶ Collier and Gunning, op. cit. p.65

⁷⁷ Ibid. p.100.

⁷⁸ Fractionalization is measured in terms of the probability of two randomly drawn citizens being from different ethnolinguistic groups. Collier and Gunning report the aggregate score for Africa is 67.6 (with 100 being the highest diversity) compared with 32.7 for other LDCs.

⁷⁹ Paul Collier, 1998, “The Political Economy of Ethnicity” in *Proceedings of the Annual World Bank Conference on Development Economics*, Boris Pleskovic and Joseph E. Stiglitz, eds, World Bank

⁸⁰ Op.cit 1999, p.68.

⁸¹ Ibid, p.106

⁸² Bruce Bueno de Mesquita, James D. Morrow, Randolph Siverson and Alastair Smith, “Political Competition and Economic Growth” in *Journal of Democracy*.

⁸³ Op.cit. p.63.

⁸⁴ Op.cit. p.66