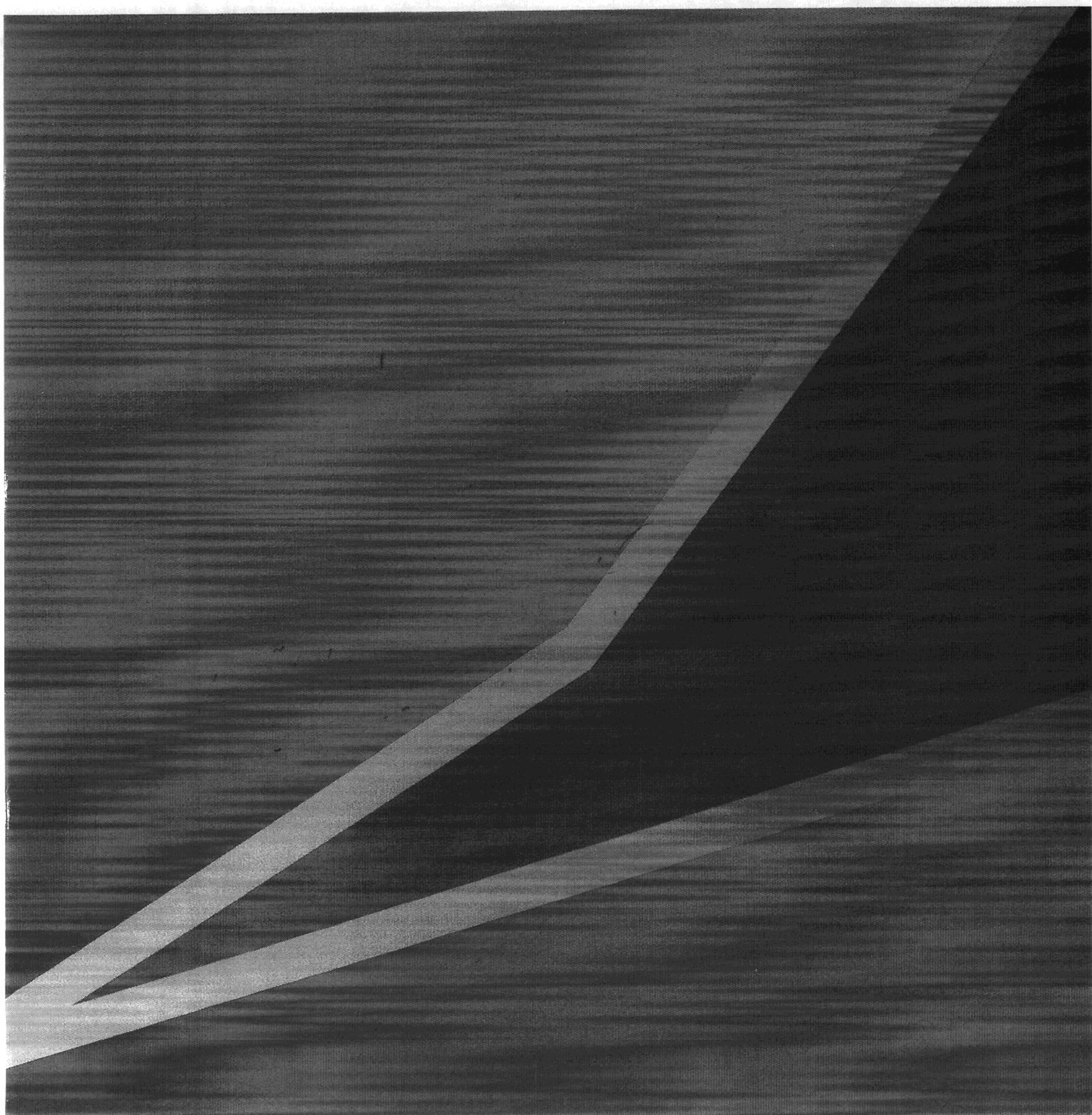
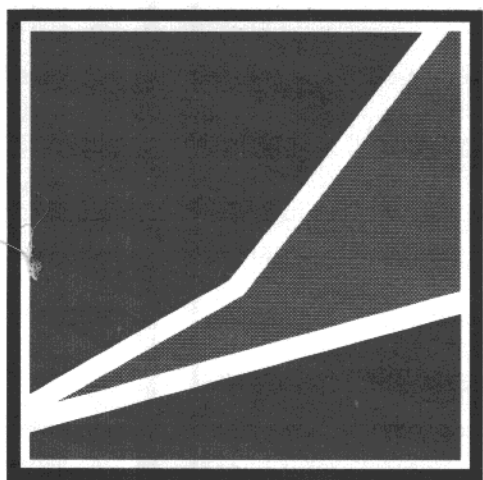


# HUMAN DEVELOPMENT REPORT 1993





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## Foreword

The past decade has been a decade of the people. The forces of democracy are spreading across many lands. New markets are springing up in former command economies, unleashing the creativity and productivity of their people. With free enterprise winning out over central planning, and the courageous voices of democracy quieting the terrors of authoritarianism, people everywhere are asserting their right to determine their own destiny.

But democracy is more than drawing up constitutions, designing new election procedures or holding elections as one-time events. Democracy is a way of life. It is a long-term process of reorganizing the institutions of a civil society. For some countries, the process is painful—involving political unrest, civil strife, even war. And many of today's struggles are more than struggles for access to political power. They are for access to the ordinary opportunities of life—land, water, work, living space and basic social services.

What is impressive is the great determination of people to participate in the events and processes that shape their lives. No more impersonal commands from above. Instead, a search for participatory patterns of development. No more directives from a distant centre. Instead, a demand for decentralization of power. No more stifling regulations from an all-powerful state. Instead, an urge to liberate human enterprise.

What is even more impressive is that even the severest hardships are not turning people away from their newly won econom-

ic and political freedoms. Just look at the sheer determination of the people in the newly independent states of the former Soviet Union—in the face of high inflation, falling output, rising unemployment, and the removal of long-enjoyed subsidies. And look, too, at the determination of people throughout the developing world to go through their own democratic and economic transitions, to scale back their overextended public sectors, to meet their human development needs.

The challenge for the development community in all this is to identify practical and pragmatic options. The best route is to unleash people's entrepreneurial spirit—to take risks, to compete, to innovate, to determine the direction and pace of development.

It is fitting, therefore, that this year's *Human Development Report* has people's participation as its special focus. As the Report stresses, we have to redefine our concept of security as security for people, not security for land. We have to weave development around people, not people around development. And we have to ensure that development cooperation focuses directly on people, not just on nation-states.

The *Human Development Report* has, since its introduction in 1990, become a tradition in contributing to the international development debate. For this, I must thank the Report team and especially Mahbub ul Haq, my Special Adviser and the Report's chief architect.

The views set forth in this Report have emerged from the team's professional,

frank and candid analysis of the issues. They do not necessarily reflect the views of UNDP, its Governing Council or other member governments of UNDP. The usefulness of a report such as this continues to depend on its professional indepen-

dence and intellectual integrity.

I am confident that this year's Report will again make a major contribution to the development dialogue by offering a new vision for the future of human development.



New York  
March 17, 1993

William H. Draper III

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## ABBREVIATIONS

DAC	Development Assistance Committee
EC	European Community
FAO	Food and Agriculture Organization of the United Nations
HDI	Human development index
IDA	International Development Association
ILO	International Labour Organisation
IMF	International Monetary Fund
ODA	Official development assistance
OECD	Organisation for Economic Co-operation and Development
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNEP	United Nations Environment Programme
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNFPA	United Nations Fund for Population Activities
UNHCR	Office of the United Nations High Commissioner for Refugees
UNICEF	United Nations Children's Fund
UNIDO	United Nations Industrial Development Organization
WHO	World Health Organization
WIDER	World Institute for Development Economics Research

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## Overview

People's participation is becoming the central issue of our time. The democratic transition in many developing countries, the collapse of many socialist regimes, and the worldwide emergence of people's organizations—these are all part of a historic change, not just isolated events.

People today have an urge—an impatient urge—to participate in the events and processes that shape their lives. And that impatience brings many dangers and opportunities. It can dissolve into anarchy, ethnic violence or social disintegration. But if properly nurtured in a responsive national and global framework, it can also become a source of tremendous vitality and innovation for the creation of new and more just societies.

The dangers arise as the irresistible urge for participation clashes with inflexible systems. Although the achievements in human development have been significant during the past three decades, the reality is continuing exclusion. More than a billion of the world's people still languish in absolute poverty, and the poorest fifth find that the richest fifth enjoy more than 150 times their income. Women still earn only half as much as men—and despite constituting more than half the votes, have great difficulty securing even 10% representation in parliaments. Rural people in developing countries still receive less than half the income opportunities and social services available to their urban counterparts. Many ethnic minorities still live like a separate nation within their own countries. And political and economic democracy is still a reluctant process in several countries. Our world is still a world of difference.

But many new windows of opportunity are opening. Global military spending is be-

ginning to decline for the first time since the Second World War. The cold war in East-West relations is over, and there is a good chance of phasing it out in the developing world. The ideological battles of the past are being replaced by a more pragmatic partnership between market efficiency and social compassion. The rising environmental threat is reminding humanity of both its vulnerability and its compulsion for common survival on a fragile planet. People are beginning to move to centre stage in national and global dialogues. There are times in history when the human voice has spoken out with surprising force. These past few years have marked just such a watershed.

Humanity must choose between these dangers and opportunities. But there really is no choice, for the future of our planet depends on grasping the opportunities.

Many old concepts must now be radically revised. Security should be reinterpreted as security for people, not security for land. Development must be woven around people, not people around development—and it should empower individuals and groups rather than disempower them. And development cooperation should focus directly on people, not just on nation-states.

Many of the old institutions of civil society need to be rebuilt—and many new ones created. And because future conflicts may well be between people rather than between states, national and international institutions will need to accommodate much more diversity and difference—and to open many more avenues for constructive participation.

All this will take time, for participation is a process, not an event. It will proceed at different speeds for different countries and

*People today have an impatient urge to participate in the events and processes that shape their lives*

*New concepts of security must stress the security of people, not only of nations*

regions, and its form and extent will vary from one stage of development to another. That is why it is necessary to address not only the levels of participation, but also whether participation is increasing. What is important is that the impulses for participation be understood and nurtured.

The implications of widespread participation are profound—embracing every aspect of development. Markets need to be reformed to offer everyone access to the benefits they can bring. Governance needs to be decentralized to allow greater access to decision-making. And community organizations need to be allowed to exert growing influence on national and international issues.

This Report explores these themes in some detail. But it is not the details that matter. It is the overall vision of societies built around people's genuine needs. This calls for at least *five new pillars of a people-centred world order*:

- New concepts of human security
- New models of sustainable human development
- New partnerships between state and markets
- New patterns of national and global governance
- New forms of international cooperation.

**1. New concepts of human security must stress the security of people, not only of nations.**

The concept of security must change—from an exclusive stress on national security to a much greater stress on people's security, from security through armaments to security through human development, from territorial security to food, employment and environmental security.

The world has already made a good start:

- Global military expenditures have declined cumulatively by around \$240 billion since 1987.
- Nuclear warheads will be cut by two-thirds by the year 2003 as a result of the recent US-Russia agreement.
- More than two million people have been demobilized from the armed forces

since the beginning of the 1990s.

- Defence industries are expected to have cut nearly a fourth of their workforce by 1998.

This is a beginning, but a formidable agenda still awaits policy-makers.

- *Use defence cuts to finance human development*—Despite major reductions in arms expenditure, the expected peace dividend in industrial countries has yet to materialize. A close link must be created between defence cuts and the unfinished social agendas in these countries.

- *Ease the transition from defence to civilian production*—Industrial countries need to plan the transition to a peace economy by retraining defence workers and creating more jobs for them in the civilian sector. Unless this is done, there will be pressures to give further export subsidies to the arms industries—pressures that several industrial countries have already succumbed to. This way of easing the adjustment problems of today's defence industry is bound to lead to enhanced conflict and deferred human progress in the developing world. It is irresponsible to entice poor countries to buy expensive military toys at the same time they are advised to reduce military spending. For developing countries, even partial demobilization of their standing armies will require large-scale job creation.

- *Accelerate disarmament in the developing world*—Although the cold war has ended between the East and the West, it remains to be phased out in the developing world. If developing countries merely froze their military spending at the 1990 level during the next decade, this would release nearly \$100 billion for their essential human development agendas—which, combined with the restructuring of aid allocations proposed later, will be enough for universal literacy, primary health care and safe drinking water by the year 2000. This will also require some major initiative from industrial countries. Needed especially are time-bound targets to phase out military bases and military assistance, internationally monitored restraints on military shipments, and an enlightened donor-recipient policy dialogue on reductions in military spending.

- *Forge new regional and international alliances for peace*—Preventive diplomacy is

needed to diffuse tensions around the globe *before* there are blowups. This demands a new role for the United Nations, not just in peacekeeping but in peacemaking and peacebuilding. After all, an ounce of prevention is better than a ton of punishment. During 1992, the UN had to intervene in several internal conflicts, from Bosnia to Somalia, and the number of UN soldiers quadrupled to more than 50,000. With conflicts in countries displacing those between them, the time has probably arrived for the UN to have a permanent military force, mainly for the new goal of peacemaking. But military force is only a short-term response. The long-term solution is faster economic development, greater social justice and more people's participation. The new concepts of human security demand people-centred development, not soldiers in uniform.

**2. New models of sustainable human development are needed—to invest in human potential and to create an enabling environment for the full use of human capabilities.**

The purpose of development is to widen the range of people's choices. Income is one of those choices—but it is not the sum-total of human life.

Human development is development of the people *for* the people *by* the people. Development of the people means investing in human capabilities, whether in education or health or skills, so that they can work productively and creatively. Development *for* the people means ensuring that the economic growth they generate is distributed widely and fairly. Earlier *Human Development Reports* (1990–92) concentrated on these first two components. This Report advances the argument by concentrating on development *by* the people—on giving everyone a chance to participate.

The most efficient form of participation through the market is access to productive and remunerative employment. So, the main objective of human development strategies must be to generate productive employment. It has long been assumed that pursuing economic growth through increas-

ing output would necessarily increase employment. This clearly has not happened. Over the past three decades, the growth rate for employment in developing countries has been about half that for output. And as output rose in many OECD countries in the last decade, employment lagged behind. ILO projections for the next decade hold no comfort. On present trends, employment's growth will continue to lag far behind that of both output and the labour force.

We are witnessing a new and disturbing phenomenon: *jobless growth*. And policy-makers the world over are searching for development strategies that combine economic growth with more job opportunities. No comprehensive programme has yet emerged, but governments can do several things to increase employment. Governments can:

- *Invest* generously in basic education, relevant skills and worker retraining.
- *Liberate* private enterprise and make markets more accessible to everyone.
- *Support* small-scale enterprises and informal employment, mainly through reform of the credit system and fiscal incentives.
- *Create* an efficient service economy for the future by investing in the new skills required.
- *Encourage* labour-intensive technologies, especially through tax incentives.
- *Extend* employment safety nets through labour-intensive public works programmes in periods of major economic distress.
- *Reconsider* the concept of work and the duration of the work week, with a view to sharing existing work opportunities.

Policy-makers are searching not only for development models that are people-centred. They also want development to be more sustainable—to protect the options of future generations. This means that the conventional definition of capital must be broadened beyond physical capital to include human and natural capital.

The supposed choice between economic growth and sustaining the environment is false and dangerous. Growth is imperative if poverty is to be reduced. But the distribution of growth must change, and it must become less wasteful of natural resources in

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both rich and poor nations. The new models of development must also recognize that poverty is one of the greatest threats to the environment. That is why it is as important to address the "silent emergencies" of poverty (water pollution, land degradation, environmental diseases) as it is to focus on the "loud emergencies" (global warming, ozone depletion) that usually dominate the headlines.

In short, the new models of sustainable development must be much more sensitive to people and to nature.

**3. New partnerships are needed between the state and the market to combine market efficiency with social compassion.**

Heated ideological discussions have often marred an objective analysis of the relative roles of markets and the state. Some believe in the benevolence of the state and the need for constantly correcting the ill effects of the market. Others glorify the virtues of the market-place and argue that the economy should be liberated from the dead hand of state bureaucracy. Both groups assume, to a large extent, that the state and the market are necessarily separate and even antagonistic—that one is benevolent, the other not. In practice, both state and market are often dominated by the same power structures.

This suggests a more pragmatic third option: that people should guide both the state and the market, which need to work in tandem, with people sufficiently empowered to exert a more effective influence over both.

If people's interests are to guide both the market and the state, actions must be taken to allow people to participate fully in the operations of markets and to share equitably in their benefits. Markets should serve people—instead of people serving markets. After all, markets are only the means—people the end.

Changing markets to make them more people-friendly would start by maintaining the dynamism of markets but adding other measures that allow many more people to capitalize on the advantages that markets offer.

- *Preconditions*—People need the education and health standards to take advantage of market opportunities. Also needed is a reasonable distribution of productive assets (particularly land) so that people do not come to the market with totally unequal buying or selling power. Since poorer people often have very little access to credit, governments need to reform their credit systems to give access to the poor. In addition, governments have to ensure that markets are open to all—irrespective of race, religion, sex or ethnic origin. Other preconditions for effective people-friendly markets include adequate physical infrastructure (particularly in rural areas), a free and rapid flow of information, a liberal trade regime and a legal system that encourages open and transparent transactions.

- *Accompanying conditions*—are needed to ensure that markets work as freely and efficiently as possible. One of the most important is a stable macroeconomic environment—especially to ensure stability in domestic prices and external currency values. But markets would also benefit from a comprehensive incentive system, with correct price signals, a fair tax regime and an adequate system of rewards for work and enterprise. Markets should also be able to work untrammelled by arbitrary and unpredictable government controls.

- *Corrective actions*—When markets do not produce a desirable outcome, the state needs to regulate and correct. This would include protecting competition through antimonopoly laws, consumers through regulations on product standards, workers through adequate and well-enforced labour legislation, and such vulnerable groups as children and the elderly. It would also include protecting the environment, by banning certain types of pollution and ensuring that polluters pay.

- *Social safety nets*—must be in place to catch the victims of the competitive struggle. Sometimes, this support need only be temporary, for the short-term unemployed, for example. But there will always be those excluded wholly or partially by the market: the very young, the very old, the disabled

and those with heavy domestic commitments. In several developing countries, such social safety nets include employment schemes for the unemployed, pension schemes for the old, feeding programmes for malnourished children and mothers, and free basic health and education for all low-income groups.

The need to create people-friendly markets is all the greater now that so many countries have embarked on strategies of economic liberalization and privatization. Many developing countries have already undertaken bold programmes to liberalize trade and finance, reform their taxation systems, deregulate the labour market and reform or privatize public enterprises. The countries of Eastern and Central Europe and the former Soviet Union have been undergoing an even more dramatic transition—from command economies to market economies. The experiences of 11 developing countries and transition economies—Argentina, Brazil, China, Egypt, Ghana, India, Kenya, Malaysia, Poland, Russia and Viet Nam—are analysed in this Report.

One of the most significant aspects of economic liberalization has been privatization. Between 1980 and 1991, nearly 7,000 enterprises were privatized, around 1,400 of them in the developing world, chiefly in Latin America. As one element in a coherent private sector development strategy, privatization can greatly stimulate private enterprise. But mistakes are already being made in the process of privatization. The Report lists “seven sins of privatization”: maximizing revenue without creating a competitive environment, replacing public monopolies with private ones, using non-transparent and arbitrary procedures, using the proceeds to finance budget deficits, simultaneously crowding the financial markets with public borrowings, making false promises to labour, and privatizing without building a political consensus.

For economic transitions to be guided by the interests of the people—and for markets to be made people-friendly—requires new patterns of governance centred around the rising aspirations of the people.

#### **4. New patterns of national and global governance are needed to accommodate the rise of people's aspirations and the steady decline of the nation-state.**

Pressures on the nation-state, from above and below, are beginning to change traditional concepts of governance. On the one hand, globalization on many fronts—from capital flows to information systems—has eroded the power of individual states. On the other, many states have become too inflexible to respond to the needs of specific groups within their own countries. The nation-state now is too small for the big things, and too big for the small.

National governments must find new ways of enabling their people to participate more in government and to allow them much greater influence on the decisions that affect their lives. Unless this is done, and done in time, the irresistible tide of people's rising aspirations will inevitably clash with inflexible systems, leading to anarchy and chaos. A rapid democratic transition and a strengthening of the institutions of civil society are the only appropriate responses. Among the many specific steps that must accompany such a transition, the two main ones are to decentralize more authority to local governments and to give much greater freedom to people's organizations and non-governmental organizations (NGOs)—instruments of people's participation discussed at length in this Report.

The decentralization of power—from capital cities to regions, towns and villages—can be one of the best ways of empowering people, promoting public participation and increasing efficiency. Many industrial countries delegate 25% or more of total government spending to the local level. But the governments of developing countries remain much more centralized, delegating only 10% or less of budgetary spending and giving local governments few opportunities to raise funds through taxation or borrowing.

Where decentralization has taken place, it has often been quite successful, encouraging local participation, reducing costs and increasing efficiency. This is evident from

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*Democracy is unlikely to be so obliging as to stop at national borders*

experiences all over the developing world—from the Rural Access Programme in Kenya to the *gram sabhas* in the Indian state of Karnataka and the local bridge construction in the Baglung district of Nepal.

Decentralization also increases the pressure on governments to concentrate on human priority concerns. Given a fair chance, local people are likely to choose ready access to basic education and health care rather than the construction of distant colleges or hospitals.

One danger of financial decentralization is that the richer regions can raise more through local taxation and so will get better services. But experience shows how to overcome this. Brazil allows states to collect taxes but then redistributes them so that the richer states in the South and South-East get back only a quarter of the taxes collected from them, while the poorer states in the North get back more than twice what is collected there.

Decentralization can, however, end up empowering local elites rather than local people. So, there can never be effective local participation in developing countries without a redistribution of power—if decentralization is to promote human development, it must be accompanied by genuine democracy at the local level.

Another major instrument for people's participation is their organization into community groups. Indeed, people's organizations and NGOs have grown dramatically in recent years, offering a powerful means of correcting the failures of both markets and governments. People's organizations tend to be formed in response to a felt need or a common interest. People might simply form self-help groups to pool their labour, obtain credit or buy goods in bulk. Or they might be responding to a failure by government to provide infrastructure or social services or to a failure of markets to protect vulnerable groups.

Although NGOs have increased in number and financial clout, there have been few systematic evaluations of their effectiveness. In broad terms, they have had a clear impact in four main areas:

- *Advocacy on behalf of the disadvantaged*—On such issues as human rights, the

environment, women, poverty alleviation and indigenous peoples, NGOs have organized powerful advocacy groups that have changed the thinking of national and international policy-makers.

- *The empowerment of marginalized groups*—In most developing countries, poverty is often caused less by an absolute shortage of resources than by their skewed distribution. NGOs' emphasis on empowerment and their support of people's organizations have often enabled marginalized groups to resist local elites and claim their rights. In many countries, particularly in Asia and Latin America, they have been pressuring governments to provide land for the landless and embark on agrarian reform.

- *Reaching the poorest*—NGOs often manage to reach groups that governments find the most difficult to help, particularly the poorest 20% of the population and those in the rural areas, where government services may be thin or non-existent. It is doubtful, though, that they reach the very poorest—most NGOs probably miss the poorest 5–10%.

- *Providing emergency assistance*—One strength of NGOs is the ability to respond quickly and effectively to emergencies. Their network of contacts allows them to give advance warning of disasters and urge international action. And their independence means that they can operate in circumstances that are politically difficult for official organizations.

Although NGOs are effective in these and other respects, it is important to keep the scale of their operations in perspective. In the early 1980s, one estimate suggested that NGOs touched the lives of about 100 million people in developing countries—60 million in Asia, 25 million in Latin America and some 12 million in Africa. Today, the figure is probably nearer 250 million and rising—but that is still only a fifth of the 1.3 billion people living in absolute poverty in developing countries.

The small impact of NGOs is also evident at the national level. In Bangladesh, the Grameen Bank, one of the most internationally renowned NGOs providing credit for the poor, accounts for a mere 0.1% of total national credit.

This is not a criticism of NGOs—it is a reminder of a stark reality: NGOs can supplement government but never replace it.

The decentralization of government authority and the emergence of NGOs are powerful processes for greater participation by people. But they can be effective only if the overall framework of national governance changes—to become genuinely democratic and participatory.

Let us also recognize that the forces of democracy are not likely to be so obliging as to stop at national borders. This has major implications for global governance. States and people must have the opportunity to influence the global decisions that are going to affect them so profoundly. This means making the institutions of global governance much broader and more participatory. There should, in particular, be a searching re-examination of the Bretton Woods organizations. And the United Nations must acquire a much broader role in development issues. To contribute effectively to sustainable human development will probably require some form of Economic Security Council within the UN, where all nations can participate on the basis of geographical representation—with none holding a veto—to provide a new decision-making forum.

**5. New forms of international cooperation must be evolved—to focus directly on the needs of the people rather than on the preferences of nation-states.**

The new emphasis on human security coupled with sustainable development will have to be matched by a fresh approach to international development cooperation.

So far, the basic motivation for donors to give aid has been to win friends in the cold-war confrontation between socialism and capitalism. Some bilateral donors did place greater emphasis on developmental and humanitarian concerns, and so did the multilateral agencies. But in general, the dominant objectives have been political.

More than half of US bilateral assistance in 1991 was earmarked for five strategically important countries: Israel, Egypt, Turkey, the Philippines and El Salvador. With five million people and a per capita in-

come of \$1,000, El Salvador received more US assistance than Bangladesh, with 116 million people and a per capita income of only \$210. And the strategic significance of Egypt has been such that it received aid of \$370 per poor person in 1991. Compare that with just \$4 per poor person for India—even though Egypt has nearly twice the income of India.

Bilateral official development assistance (ODA) is badly allocated, showing the considerable potential for beneficial restructuring:

- Twice as much ODA per capita goes to high military spenders as to more moderate spenders.
- Only a quarter of ODA goes to the ten countries containing three-quarters of the world's poor.
- Less than 7% of ODA is earmarked for human priority concerns.
- Most of the \$15 billion in technical assistance is spent on equipment, technology and experts from industrial countries—rather than on national capacity building in developing countries.

Aid is allocated this way because it suffers from the scars of the cold war, from a focus on nation-states rather than on people, from a bias towards the public sector and from a reliance on western development models.

The changed circumstances of the 1990s demand an entirely new approach to ODA:

- *Focus aid on human priority issues*—Aid should be directed at human priority issues, such as health and basic education, and at environmental security and reducing population growth. Clear and specific goals in these areas—identified, implemented and monitored—would obtain greater public and legislative support in donor nations. At least 20% of total aid should be allocated to human priority concerns, three times the present 6.5%.
- *Base ODA allocations on levels of poverty*—ODA should be allocated to people rather than to countries, and it should go where the need is the greatest, to the poorest people wherever they happen to be. For example, the ten countries containing three-quarters of the world's poorest peo-

*At least 20% of total aid should be allocated to human priority concerns*



*Poverty anywhere  
is a threat to  
prosperity  
everywhere*

ple should get around three-quarters of ODA, not the present one-quarter.

- *Link ODA with mutual concerns*—ODA must be in the mutual interest of recipients and donors. Recipients would be justified in insisting that ODA allocations be guided by their priorities in the fields of human development, poverty alleviation, employment creation and accelerated economic growth. Donors, by contrast, could legitimately link their ODA policy dialogue with their concerns on such matters as human rights, reducing international migration pressures, pollution, nuclear proliferation and drug trafficking—as well as the control of terrorism. Perhaps as much as 3% of aid funds could be earmarked for spending within donor nations to prepare public opinion for these post-cold-war realities and to increase public awareness of the interdependence of the North and the South.

- *Adopt a new people-centred policy dialogue*—ODA should be accompanied by a new form of policy dialogue based on the real interests of people, rather than those of the developing country governments that negotiate aid. This means putting much more pressure on governments to improve the distribution of income and assets, to direct spending away from military towards social concerns and to attend to the larger issues of better national governance.

- *Use technical assistance for national capacity building*—Technical assistance should be used increasingly to hire national experts, to invest in local institutions and to accelerate human development in the recipient countries. The ultimate criterion for judging the success of any technical assistance programme must be that it has built adequate national capacity and phased itself out over a predefined period.

- *Place ODA in a larger framework of sharing global market opportunities*—ODA can make a significant contribution to developing countries, but it must also be conceived in a larger framework. As the 1992 Report pointed out, developing countries are being denied market opportunities worth ten times the annual flows of ODA. The long-term solution to poverty is not charity. It is more equitable access for poor nations to global market opportunities.

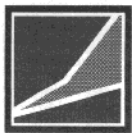
- *Create a new motivation for aid*—The old motive of fighting the cold war is dead. The new motive must be the war against global poverty, based on the recognition that this is an investment not only in the development of poor nations but in the security of rich nations. The real threat in the next few decades is that global poverty will begin to travel, without a passport, in many unpleasant forms: drugs, diseases, terrorism, migration. Poverty anywhere is a threat to prosperity everywhere.

\* \* \*

The implications of placing people at the centre of political and economic change are thus profound. They challenge traditional concepts of security, old models of development, ideological debates on the role of the market and outmoded forms of international cooperation. They call for nothing less than a revolution in our thinking. This Report touches on only a few aspects of a profound human revolution that makes people's participation the central objective in all parts of life. Every institution—and every policy action—should be judged by one critical test: how does it meet the genuine aspirations of the people? A simple test, vast in its reach.

This is the vision national and global decision-makers must consider if the 1990s are to emerge as a new watershed in peaceful development—and if the 21st century is to see the full flowering of human potential all over the world. The process of change ushered in by the events of the past few years must now be carried forward—with great courage and resolution. There are no engraved milestones on this road. There are no decorated heroes. It is a process of change led by people—and a promising journey we all must join.

An opportunity for this will arise fairly soon. All nations are committed to meet in 1995 at a World Summit on Social Development. It is a chance to focus on the building blocks for a new people-centred world order. It is a time to agree on a concrete agenda of national and global actions. That agenda will be the theme of the 1994 *Human Development Report*.



# Trends in human development

The 1980s were, in many ways, a decade of the people. All over the world, people had an impatient urge to guide their political, economic and social destinies. The democratic transition in developing countries, the collapse of socialist regimes and the world-wide emergence of people's organizations—all were part of a restless wave of human aspirations. Frustrated at times, in many places still in chains, the human spirit soared in the past decade.

At first sight, this may appear too sanguine an interpretation. This was, after all, a decade that shattered many lives and many hopes—with mounting external debt, faltering economic growth, increasing unemployment, growing civil strife, rising ethnic tensions, threats to the environment and the persistence of abject poverty.

But amid these disturbing and painful trends is an undoubtable resurgence of the human spirit. There are times in history when the human voice has spoken out with surprising force. These past few years have marked just such a watershed.

Now that the cold war is over, the challenge is to rebuild societies around people's genuine needs. The world has already made a positive start. For the first time since the Second World War, global military expenditures are beginning to decline—between 1987 and 1990, they fell cumulatively by some \$240 billion. Most of this reduction has been by the United States and the former Soviet Union. But the developing countries also cut expenditure, with a cumulative reduction of \$11 billion, chiefly in the Arab States and South Asia. This happened despite the fact that the poorest nations in Sub-Saharan Africa have yet to reduce military spending, and for many

poor countries, the ratio of military spending to social spending remains far too high (figure 1.1). But in 1991, military spending in developing countries rose back to its previous level, mainly because of the Gulf War.

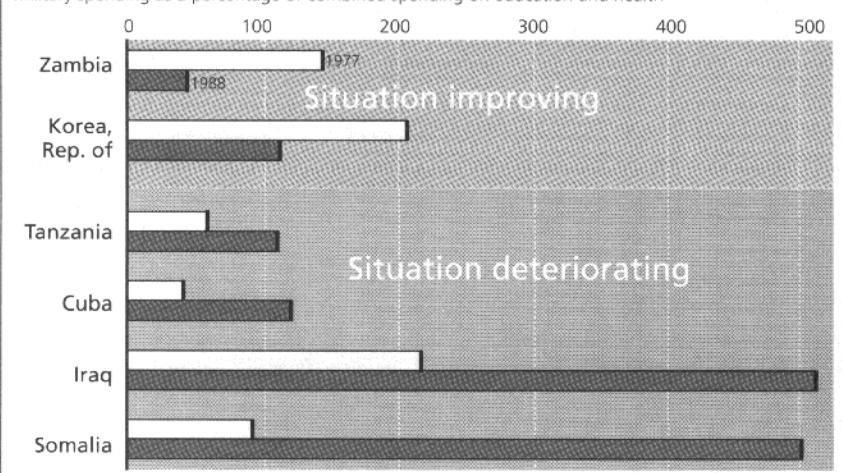
Detente and disarmament negotiations between East and West have considerably diminished the threat of nuclear war. As a result of the Strategic Arms Reduction Treaties (START I and II), the number of strategic nuclear warheads is likely to decline from 24,000 at the end of the 1980s to about 7,000 by 2003 (figure 1.2). And since the beginning of the 1990s, more than two million men and women have been demobilized, two-thirds of them in industrial countries and one-third in developing (figure 1.3). Further demobilizations on a similar scale are expected in the next few years.

This represents considerable progress, but the nuclear threat is far from gone, and conventional weapons continue to take many lives. So, greater emphasis must be

FIGURE 1.1

## Military and social priorities

Military spending as a percentage of combined spending on education and health



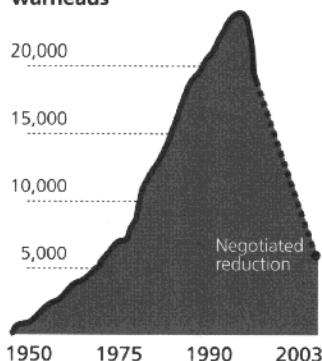
placed not just on peacekeeping but on peacemaking and peacebuilding, demanding a new role for the United Nations (box 1.1).

Employment in the arms industry is beginning to fall. Having employed around 15 million workers at the end of the 1980s—90% of them in the former Soviet Union, China, the United States and the European Community (in descending size)—the industry will lose an estimated three to four million jobs (20–25%) by 1998.

As military threats have lessened, other dangers have surfaced—such as the ethnic and religious conflicts in Bosnia, India, Iraq, Liberia, Somalia and Sri Lanka. And many industrial countries have seen violent conflicts between different racial groups—from riots in Los Angeles to neo-Nazi attacks on immigrants and asylum-seekers in Germany. The world is entering a dangerous period: future conflicts may well be between groups of people rather than states.

All these changes highlight the urgent need to focus on human development, the concept defined in the first *Human Development Report* in 1990 as a process of widening the range of people's choices.

FIGURE 1.2  
Strategic offensive nuclear warheads



#### BOX 1.1

##### An agenda for peace

Worldwide, there have been more than 100 major conflicts in the past four decades, taking the lives of some 20 million people. The United Nations was often powerless to deal with these conflicts—paralysed by vetoes by major powers on both sides of the East-West divide.

Since May 1990, however, no such vetoes have been cast, and there has been a growing demand for UN support in dealing with such conflicts. In July 1992, responding to a request of the first-ever meeting of the Security Council at the level of heads of state and government, the UN Secretary-General prepared a report, *Agenda for Peace*, setting forth the organization's objectives for peace and security, quoted here:

- To seek to identify, at the earliest possible stage, situations that could produce conflict, and to try through diplomacy to remove the sources of danger before violence results.

- Where conflict erupts, to engage in peacemaking aimed at resolving the issues that have led to conflict.

- Through peacekeeping, to work to preserve peace, however fragile, where fighting has been halted and to assist in implementing agreements achieved by the peace-makers.

- To stand ready to assist in peace-building in its differing contexts: rebuilding the institutions and infrastructures of nations torn by civil war and strife; and building bonds of peaceful mutual benefit among nations formerly at war.

- And in the largest sense, to address the deepest causes of conflict: economic despair, social injustice and political oppression. It is possible to discern an increasingly common moral perception that spans the world's nations and peoples, and which is finding expression in international laws, many owing their genesis to the work of this Organization.

## Assessing human development

The first *Human Development Report*, in introducing the concept of human development, argued that the real purpose of development should be to enlarge people's choices. Subsequent Reports have developed the basic concept, looking in particular at how human development could be financed and at its international dimensions—through trade, official development assistance and international migration flows. Each Report has also presented balance sheets for human development, for both industrial and developing countries (see boxes 1.2 and 1.3 for this year's balance sheets).

To quantify and clarify the process of human development, the 1990 Report also introduced a new yardstick of human progress: the human development index (HDI). By combining indicators of real purchasing power, education and health, the HDI offers a measure of development much more comprehensive than GNP alone.

The second Report, in 1991, took up the question of financing human development—and the role of governments. It looked at the potential for restructuring national budgets away from wasteful expenditure on the military and on loss-making public enterprises, for example—and towards more relevant priorities, such as basic education and primary health care.

The analysis used four ratios to highlight government spending priorities. These showed that developing countries spend more than 25% of their GNP through the budget, yet devote less than one-tenth of this to human development priorities. The 1991 Report also discovered similar imbalances in international aid: less than 7% of total aid is spent on human priority areas. It concluded that the world had an enormous opportunity to increase investments in human development—even with existing resources.

The 1992 Report extended the analysis by adding an international dimension. It focused specifically on global markets and on how they meet—or fail to meet—human needs. The Report discovered that global markets make developing countries lose

economic opportunities worth around \$500 billion annually—ten times what they receive in foreign assistance. No wonder that the global income disparity has doubled during the past three decades: the richest 20% of the world's people now receive more than 150 times the income of the poorest 20%.

That Report suggested two priority areas for future action. First, developing countries should invest massively in their people to sharpen their competitive edge in international markets. Second, there should be a radical dismantling of trade barriers and a major reform of international institutions, including the United Nations and the Bretton Woods institutions, to establish a new vision of global co-operation for the 21st century.

The HDI has attracted much attention from the academic community and from policy-makers. Technical note 1 explains its construction, and our intention is to continue to refine the methodology of the HDI in the light of comments and to steadily improve the database. Technical note 2 presents a detailed discussion of the HDI's methodology, the criticisms received, the refinements contemplated and the methodological options for dealing with some of the issues raised. We include this note to elicit further comments so that a much improved methodology can be devised for the 1994 Report. This Report introduces no changes in the method of HDI measurement, enabling a comparison of country rankings with the 1992 Report.

This year's country rankings show that Japan has displaced Canada at the top because of its significant increase (23%) in real GDP per capita during 1989–90 (table 1.1). For the countries with the lowest levels of human development, there has not been much change in ranking (table 1.2 and figure 1.4).

An analysis of the HDI country rankings brings out some interesting policy conclusions:

1. *There is no automatic link between income and human development*—Several countries—such as Chile, China, Colombia, Costa Rica, Madagascar, Sri Lanka,

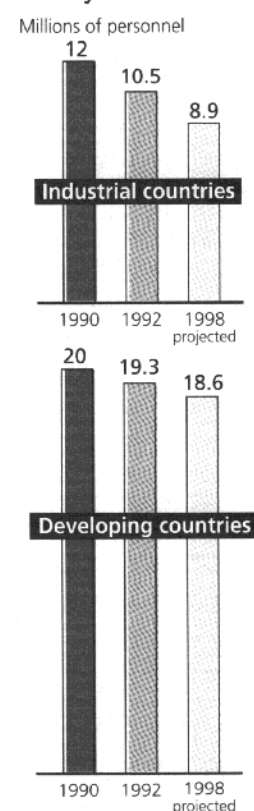
Tanzania and Uruguay—have done well in translating their income into the lives of their people: Their human development rank is way ahead of their per capita income rank (figure 1.5). Other societies—such as Algeria, Angola, Gabon, Guinea, Namibia, Saudi Arabia, Senegal, South Africa and United Arab Emirates—have income ranks

TABLE 1.1  
HDI ranking for industrial countries

Country	HDI value	HDI rank	GNP per capita rank	GNP per capita rank minus HDI rank <sup>a</sup>
Japan	0.983	1	3	2
Canada	0.982	2	11	9
Norway	0.978	3	6	3
Switzerland	0.978	4	1	-3
Sweden	0.977	5	5	0
USA	0.976	6	10	4
Australia	0.972	7	20	13
France	0.971	8	13	5
Netherlands	0.970	9	17	8
United Kingdom	0.964	10	21	11
Iceland	0.960	11	9	-2
Germany	0.957	12	8	-4
Denmark	0.955	13	7	-6
Finland	0.954	14	4	-10
Austria	0.952	15	14	-1
Belgium	0.952	16	16	0
New Zealand	0.947	17	23	6
Luxembourg	0.943	18	2	-16
Israel	0.938	19	27	8
Ireland	0.925	21	29	8
Italy	0.924	22	18	-4
Spain	0.923	23	28	5
Greece	0.902	25	35	10
Czechoslovakia	0.892	26	49	23
Hungary	0.887	28	52	24
Malta	0.855	39	33	-6
Bulgaria	0.854	40	67	27
Portugal	0.853	41	38	-3
Poland	0.831	48	80	32
Romania	0.709	77	84	7
Albania	0.699	78	90	12
<i>Other countries</i>				
Lithuania	0.881	29	51	22
Estonia	0.872	34	42	8
Latvia	0.868	35	43	8
Russian Fed.	0.862	37	47	10
Belarus	0.861	38	50	12
Ukraine	0.844	45	58	13
Armenia	0.831	47	63	16
Georgia	0.829	49	72	23
Kazakhstan	0.802	54	55	1
Azerbaijan	0.770	62	82	20
Moldova, Rep.	0.758	64	61	-3
Turkmenistan	0.746	66	81	15
Uzbekistan	0.695	80	92	12
Kyrgyzstan	0.689	83	85	2
Tajikistan	0.657	88	94	6

a. A positive figure shows that the HDI rank is higher than the GNP rank, a negative the opposite.

FIGURE 1.3  
Military demobilization





## Balance sheet of human development—developing countries

### PROGRESS

### DEPRIVATION

#### LIFE EXPECTANCY

- Average life expectancy increased by over one-third during the past three decades; 23 countries have achieved a life expectancy of 70 years and more.

- Of the 300 million people above the age of 60, only 20% have any form of income security.

#### HEALTH AND SANITATION

- In the developing world, more than 70% of the population has access to health services.
- Nearly 60% of the population has access to sanitation.

- About 17 million people die every year from infectious and parasitic diseases, such as diarrhoea, malaria and tuberculosis.
- More than 80% of the 12–13 million HIV-infected people are in the developing world, and the cumulative direct and indirect cost of AIDS during the past decade was around \$30 billion.

#### FOOD AND NUTRITION

- Between 1965 and 1990, the number of countries that met their daily per capita calorie requirements doubled—from about 25 to 50.

- Some 800 million people still do not get enough food.

#### EDUCATION

- Primary school enrolment increased in the past two decades—from less than 70% to well over 80%. In the same period, secondary enrolment almost doubled—from less than 25% to 40%.

- Nearly one billion people—35% of the adult population—are still illiterate, and the drop-out rate at the primary level is still as high as 30%.

#### INCOME AND POVERTY

- In South and East Asia, where two-thirds of the developing world's population live, the GNP growth averaged more than 7% a year during the 1980s.

- Almost one-third of the total population, or 1.3 billion people, are in absolute poverty.

#### CHILDREN

- During the past 30 years, infant and under-five mortality rates were more than halved.

- Each day, 34,000 young children still die from malnutrition and disease.

#### WOMEN

- The secondary enrolment ratio for girls increased from around 17% in 1970 to 36% in 1990.

- Two-thirds of illiterates are women.

#### HUMAN SECURITY

- With the end of the cold war, developing countries no longer have to serve as proxies for superpower rivalry, and in 1990, about 380,000 refugees returned to their homelands in Asia, Africa and Latin America.

- Internal conflicts afflict some 60 countries, and about 35 million people are refugees or internally displaced.

#### ENVIRONMENT

- The percentage of rural families with access to safe water has increased from less than 10% to almost 60% during the past two decades.

- More than 850 million people live in areas that are in various stages of desertification.
- The rate of tropical forest destruction is about the equivalent of one soccer field per second.

## Balance sheet of human development—industrial countries

### PROGRESS

### DEPRIVATION

#### LIFE EXPECTANCY AND HEALTH

- In 1960, life expectancy was more than 70 years in only 12 countries. Now, it is more than 70 years in all industrial countries.

- Nearly two million people are HIV-infected, and the direct and indirect cost during the 1980s was \$210 billion.

#### EDUCATION

- The tertiary enrolment ratio more than doubled between 1965 and 1990.

- More than one-third of the adults lack any upper-secondary or higher education.

#### INCOME AND EMPLOYMENT

- The per capita GNP grew at an annual rate of 2.4% between 1965 and 1990.

- The average unemployment rate is about 7%, and a quarter of the more than 30 million unemployed have been out of work for more than two years.

#### SOCIAL SECURITY

- Social security expenditures now account for just under 15% of GDP.

- About 100 million people live below the poverty line.

#### WOMEN

- Women now account for more than 40% of total employment.

- Women hold fewer than 10% of parliamentary seats.

#### SOCIAL FABRIC

- There are now five library books and more than one radio for every person, and more than one telephone and one TV set for every two people. One in three people reads a newspaper.

- There are more than 15 suicides, more than 100 drug crimes and more than 15 deaths from road accidents per 100,000 people.
- The number of divorces is now one-third the number of marriages contracted, and well over 5% of households are single-parent homes.

#### POPULATION AND ENVIRONMENT

- Energy requirements per unit of GDP fell by 40% between 1965 and 1990.

- People in industrial countries make up about one-fifth of world population but consume ten times more commercial energy than people in developing countries, and they account for 71% of the world's carbon monoxide emissions and 68% of the world's industrial waste.



far above their human development rank, showing their enormous potential for improving the lives of their people.

Several countries enjoying similar incomes per capita have very divergent human development experiences. Five countries with a GNP per capita of around \$380 in 1990 had human accomplishments that could not be more dissimilar: Guyana, Kenya, Ghana, Pakistan and Haiti. Of this group, Guyana has the highest HDI value (0.541, rank 105), Haiti the lowest (0.275, rank 137). Ghana's average life expectancy

is ten years shorter than Guyana's, and Pakistan's infant mortality rate is twice as high as Guyana's—and its illiteracy rate 16 times higher. Income alone is obviously a poor indicator of human development.

2. *The change in human development is as significant as its level*—Many countries started at a low level of human development three decades ago but have since made very rapid progress, particularly the Gulf States, whose real economic prosperity came in the mid-1970s after the steep increase in oil prices (figure 1.6). It clearly

TABLE 1.2  
HDI ranking for developing countries

Country	HDI value	HDI rank	GNP rank	Country	HDI value	HDI rank	GNP rank	Country	HDI value	HDI rank	GNP rank
Barbados	0.928	20	34	Ecuador	0.646	89	108	Ghana	0.311	131	140
Hong Kong	0.913	24	24	Paraguay	0.641	90	97	Pakistan	0.311	132	136
Cyprus	0.890	27	30	Korea, Dem. Rep.	0.640	91	103	Cameroon	0.310	133	107
Uruguay	0.881	30	54	Philippines	0.603	92	114	India	0.309	134	146
Trinidad and Tobago	0.877	31	46	Tunisia	0.600	93	88	Namibia	0.289	135	98
Bahamas	0.875	32	25	Oman	0.598	94	36	Côte d'Ivoire	0.286	136	113
Korea, Rep. of	0.872	33	37	Peru	0.592	95	95	Haiti	0.275	137	143
Chile	0.864	36	75	Iraq	0.589	96	73	Tanzania, U. Rep. of	0.270	138	172
Costa Rica	0.852	42	76	Dominican Rep.	0.586	97	112	Comoros	0.269	139	129
Singapore	0.849	43	26	Samoa	0.586	98	109	Zaire	0.262	140	158
Brunei Darussalam	0.847	44	19	Jordan	0.582	99	91	Lao People's Dem. Rep.	0.246	141	161
Argentina	0.832	46	62	Mongolia	0.578	100	104	Nigeria	0.246	142	153
Venezuela	0.824	50	56	China	0.566	101	142	Yemen	0.233	143	124
Dominica	0.819	51	70	Lebanon	0.565	102	87	Liberia	0.222	144	127
Kuwait	0.815	52	15	Iran, Islamic Rep.	0.557	103	59	Togo	0.218	145	135
Mexico	0.805	53	60	Botswana	0.552	104	69	Uganda	0.194	146	167
Qatar	0.802	55	22	Guyana	0.541	105	141	Bangladesh	0.189	147	159
Mauritius	0.794	56	68	Vanuatu	0.533	106	96	Cambodia	0.186	148	168
Malaysia	0.790	57	66	Algeria	0.528	107	65	Rwanda	0.186	149	151
Bahrain	0.790	58	32	Indonesia	0.515	108	122	Senegal	0.182	150	115
Grenada	0.787	59	71	Gabon	0.503	109	44	Ethiopia	0.172	151	170
Antigua and Barbuda	0.785	60	41	El Salvador	0.503	110	102	Nepal	0.170	152	166
Colombia	0.770	61	93	Nicaragua	0.500	111	133	Malawi	0.168	153	162
Seychelles	0.761	63	39	Maldives	0.497	112	131	Burundi	0.167	154	160
Suriname	0.751	65	48	Guatemala	0.489	113	110	Equatorial Guinea	0.164	155	147
United Arab Emirates	0.738	67	12	Cape Verde	0.479	114	116	Central African Rep.	0.159	156	139
Panama	0.738	68	77	Viet Nam	0.472	115	156	Mozambique	0.154	157	173
Jamaica	0.736	69	86	Honduras	0.472	116	118	Sudan	0.152	158	138
Brazil	0.730	70	53	Swaziland	0.458	117	99	Bhutan	0.150	159	163
Fiji	0.730	71	78	Solomon Islands	0.439	118	121	Angola	0.143	160	126
Saint Lucia	0.720	72	64	Morocco	0.433	119	106	Mauritania	0.140	161	128
Turkey	0.717	73	83	Lesotho	0.431	120	123	Benin	0.113	162	145
Thailand	0.715	74	89	Zimbabwe	0.398	121	117	Djibouti	0.104	163	125
Cuba	0.711	75	101	Bolivia	0.398	122	119	Guinea-Bissau	0.090	164	165
Saint Vincent	0.709	76	79	Myanmar	0.390	123	152	Chad	0.088	165	164
Saint Kitts and Nevis	0.697	79	45	Egypt	0.389	124	120	Somalia	0.087	166	171
Syrian Arab Rep.	0.694	81	105	São Tomé and Príncipe	0.374	125	137	Gambia	0.086	167	148
Belize	0.689	82	74	Congo	0.372	126	100	Mali	0.082	168	154
Saudi Arabia	0.688	84	31	Kenya	0.369	127	144	Niger	0.080	169	150
South Africa	0.673	85	57	Madagascar	0.327	128	157	Burkina Faso	0.074	170	149
Sri Lanka	0.663	86	130	Papua New Guinea	0.318	129	111	Afghanistan	0.066	171	169
Libyan Arab Jamahiriya	0.658	87	40	Zambia	0.314	130	134	Sierra Leone	0.065	172	155
								Guinea	0.045	173	132



## COMPARATIVE PERFORMANCE IN HUMAN DEVELOPMENT

FIGURE 1.4  
**Human development varies by region**

Human development index weighted by population  
1.00

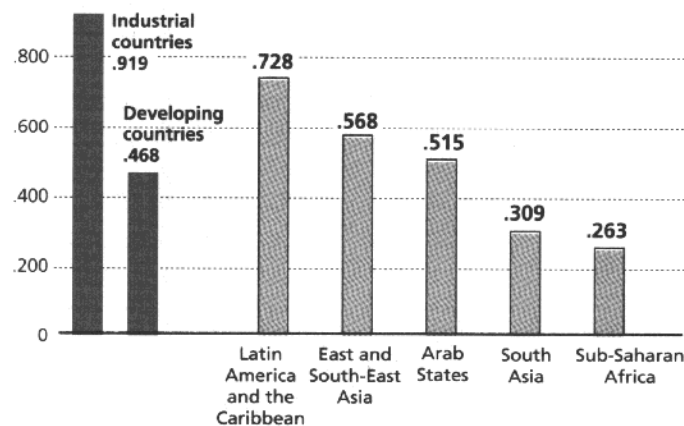


FIGURE 1.5  
**There is no automatic link between income and human development**

GNP per capita rank minus HDI rank

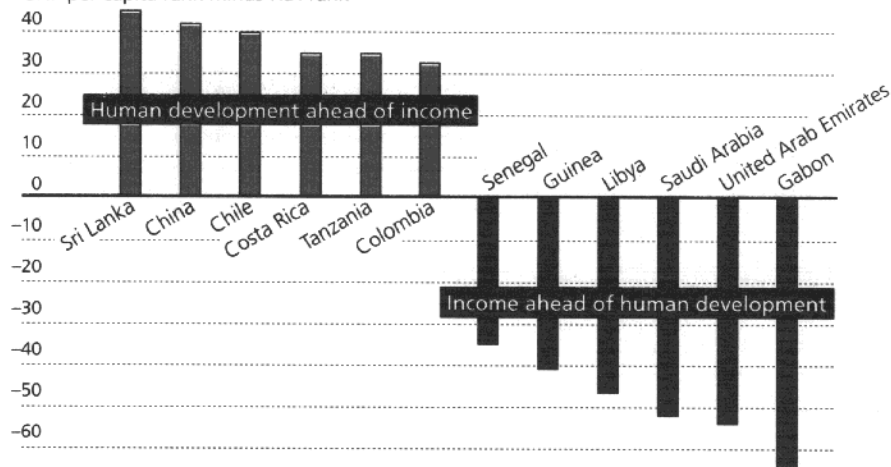


FIGURE 1.6  
**Human development progress in the Gulf States**

■ Gulf States  
● All developing countries

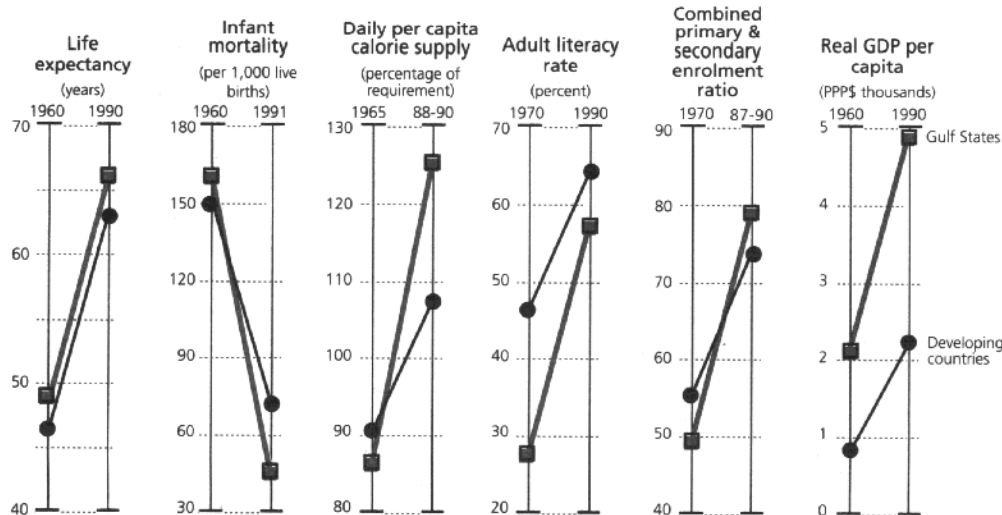


FIGURE 1.7  
**HDIs have diverged for countries with similar starting points**

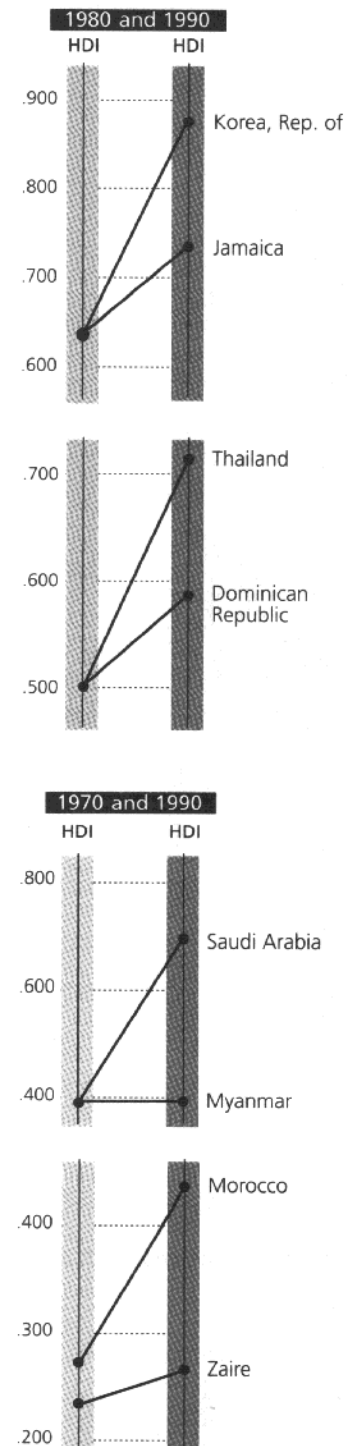
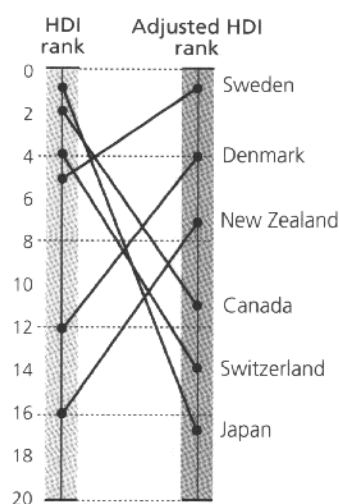


FIGURE 1.8  
Changes in rank with a  
gender-disparity-adjusted HDI



Ranks are for the 33 countries in table 1.3.

TABLE 1.3  
Gender-disparity-adjusted HDI

Country	HDI value	Gender-disparity-adjusted HDI	Difference between HDI and gender-disparity-adjusted ranks
Sweden	0.977	0.921	4
Norway	0.978	0.881	1
France	0.971	0.864	5
Denmark	0.955	0.860	8
Finland	0.954	0.859	8
Australia	0.972	0.852	1
New Zealand	0.947	0.844	9
Netherlands	0.970	0.826	1
USA	0.976	0.824	-3
United Kingdom	0.964	0.818	0
Canada	0.982	0.816	-9
Belgium	0.952	0.808	3
Austria	0.952	0.782	1
Switzerland	0.978	0.768	-10
Germany	0.957	0.768	-4
Italy	0.924	0.764	3
Japan	0.983	0.763	-16
Czechoslovakia	0.892	0.754	4
Ireland	0.925	0.720	-1
Luxembourg	0.943	0.713	-3
Greece	0.902	0.691	0
Portugal	0.853	0.672	3
Cyprus	0.890	0.656	0
Costa Rica	0.852	0.632	2
Hong Kong	0.913	0.618	-5
Singapore	0.849	0.585	1
Korea, Rep. of	0.872	0.555	-3
Paraguay	0.641	0.546	1
Sri Lanka	0.663	0.499	-1
Philippines	0.603	0.451	0
Swaziland	0.458	0.344	0
Myanmar	0.390	0.297	0
Kenya	0.369	0.241	0

A positive difference shows that the gender-disparity-adjusted HDI rank is higher than the unadjusted HDI rank, a negative the opposite.

FIGURE 1.9  
Difference between HDI and gender-disparity-adjusted HDI



took time to invest the new income in people, but during the past 20 years, the Gulf States have made much faster progress than the average developing country. Saudi Arabia had the greatest change in its HDI value—from 0.386 in 1970 to 0.688 in 1990.

Several countries with similar HDIs in 1970 have since had dissimilar experiences. Myanmar and Saudi Arabia, for example, started with similar HDIs in 1970, as did Zaire and Morocco. For Myanmar and Zaire, the world has stood still in terms of human development—a factor which no doubt has contributed to the countries' present problems. But Saudi Arabia has since nearly doubled its HDI, and Morocco has raised its HDI by 60% (figure 1.7).

3. *The economies in transition have very high levels of human development*—Two-thirds of the 15 newly independent states of the former Soviet Union fall into the category of high human development, the other third into the medium. The formerly socialist countries have already made major investments in the education and health of their people—and thus have considerable human capital available for the transition ahead. The average life expectancy for these economies is 70 years, and the population per doctor is around 300, compared with 63 years and 5,000 respectively for developing countries.

4. *When the HDI is adjusted for gender disparity, no country improves its HDI value*—The meaning: no country treats its women as well as it treats its men, a disappointing result after so many years of debate on gender equality, so many struggles by women and so many changes in national laws (table 1.3 and figures 1.8 and 1.9). But some countries do better than others, so adjusting for gender disparity makes a big difference to the rankings: Japan falls from number 1 to 17, Canada from number 2 to 11 and Switzerland from number 4 to 14. By contrast, Sweden improves its rank from number 5 to 1, Denmark from number 12 to 4 and New Zealand from number 16 to 7.

In industrial countries, gender discrimination (measured by the HDI) is mainly in employment and wages, with women often

TABLE 1.4  
Income-distribution-adjusted HDI

Country	HDI value	Income-distribution-adjusted HDI value	Difference between HDI and income-distribution-adjusted ranks
Japan	0.983	0.981	0
Netherlands	0.970	0.966	7
Switzerland	0.978	0.958	1
Sweden	0.977	0.958	1
Norway	0.978	0.956	-2
Canada	0.982	0.947	-4
Belgium	0.952	0.946	6
United Kingdom	0.964	0.945	2
USA	0.976	0.943	-3
France	0.971	0.938	-2
Australia	0.972	0.934	-4
Finland	0.954	0.932	0
Denmark	0.955	0.925	-2
Israel	0.938	0.912	1
New Zealand	0.947	0.909	-1
Ireland	0.925	0.908	0
Spain	0.923	0.898	1
Italy	0.924	0.892	-1
Korea, Rep. of	0.872	0.885	2
Hungary	0.887	0.873	0
Hong Kong	0.913	0.871	-2
Singapore	0.849	0.836	3
Costa Rica	0.852	0.829	1
Chile	0.864	0.818	-2
Portugal	0.853	0.802	-2
Argentina	0.832	0.791	0
Venezuela	0.824	0.771	0
Mauritius	0.794	0.745	1
Mexico	0.805	0.737	-1
Colombia	0.770	0.734	1
Malaysia	0.790	0.732	-1
Thailand	0.715	0.672	4
Panama	0.738	0.654	-1
Turkey	0.717	0.650	1
Syrian Arab Rep.	0.694	0.644	2
Jamaica	0.736	0.643	-3
Sri Lanka	0.663	0.634	1
Brazil	0.730	0.627	-4
Tunisia	0.600	0.583	1
Philippines	0.603	0.575	-1
Iran, Islamic Rep.	0.557	0.519	0
Indonesia	0.515	0.519	0
El Salvador	0.503	0.488	0
Honduras	0.472	0.419	0
Egypt	0.389	0.377	0
Kenya	0.369	0.344	0
Pakistan	0.311	0.303	1
Zambia	0.314	0.291	-1
India	0.309	0.289	0
Côte d'Ivoire	0.286	0.246	0
Bangladesh	0.189	0.172	0
Nepal	0.170	0.138	0

A positive difference shows that the income-distribution-adjusted HDI rank is higher than the unadjusted HDI rank, a negative the opposite.

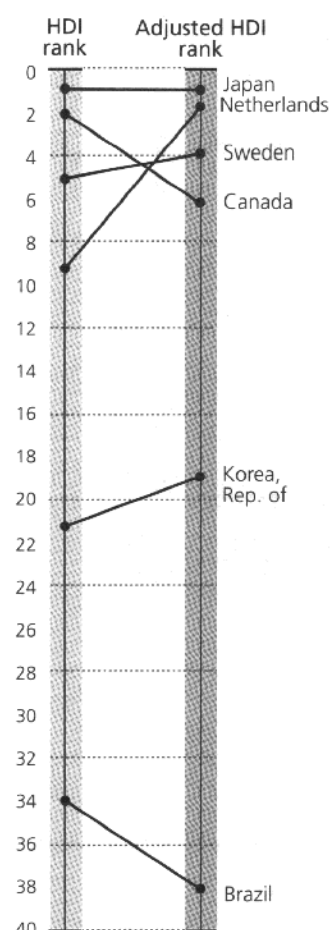
getting less than two-thirds of the employment opportunities and about half the earnings of men.

In developing countries, the great disparities, besides those in the job market, are in health care, nutritional support and education. For instance, women make up two-thirds of the illiterate population. And South and East Asia, defying the normal biological result that women live longer than men, have more men than women. The reasons: high maternal mortality and infanticide and nutritional neglect of the girl-child. According to one estimate, some 100 million women are "missing".

5. *The poor distribution of income has a major impact on human development*—Income disparities are wide in many countries, particularly in the developing world. Brazil has one of the most unequal distributions of income—the richest 20% of the population receives 26 times the income of the poorest 20%. When the income component of its HDI is reduced to reflect this maldistribution, its HDI falls by 14% (figure 1.10). The same correction also causes a major drop in the HDI of many other countries, including Jamaica, Malaysia, Mexico, Panama and Turkey (figure 1.11). Table 1.4 gives the income-distribution-adjusted HDI for 52 countries having data. Among the industrial countries, the largest adjustments downwards are for Portugal, New Zealand, Australia, Canada, France, Italy and the United States.

6. *When the HDI is disaggregated by calculating the specific HDI for groups or regions in a country, there can be startling divergences*

FIGURE 1.10  
Changes in rank with an income-distribution-adjusted HDI



Ranks are for the 52 countries in table 1.4.

FIGURE 1.11

#### Difference between HDI and income-distribution-adjusted HDI

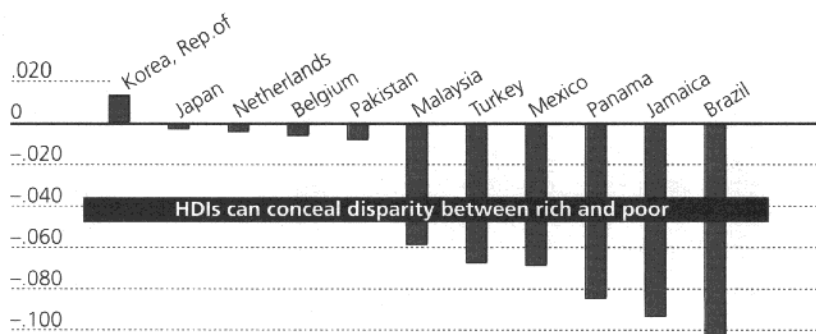
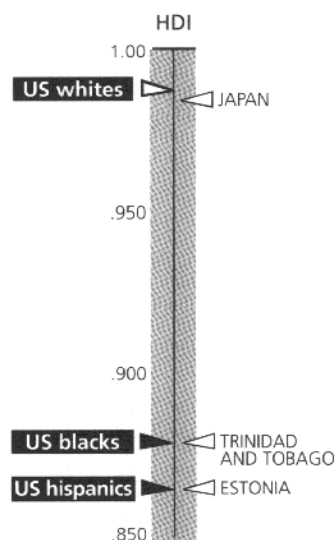


FIGURE 1.12  
HDI is higher for whites than for blacks and hispanics in the United States



from the national average—Disaggregating HDIs provides a group-specific or region-specific human development measure, whereas the gender-adjusted and income-distribution-adjusted HDIs are still national averages incorporating the extent of inequality. Five countries that have readily available data to undertake such a disaggregation: the United States, India, Mexico, Turkey and Swaziland. More countries should launch efforts to gather such data.

In the United States, with the HDIs of white, black and hispanic populations separated, whites rank number 1 in the world (ahead of Japan), blacks rank number 31 (next to Trinidad and Tobago) and hispanics rank number 35 (next to Estonia). This, even despite the fact that income levels are considerably discounted in the HDI calculations. So, full equality is a distant prospect in the United States (figures 1.12 and 1.13).

Similar disparities are obvious elsewhere. In India, the HDI in Uttar Pradesh is a third lower than the national average and 60% lower than that in Kerala (figure 1.14). In Mexico, the state of Oaxaca has an HDI 20% lower than the national average (figure 1.15). In Turkey, the HDI for rural females is 25% lower than that for rural males (figure 1.16). By contrast, Swaziland, with a smaller population of less

than one million, is a more homogeneous society.

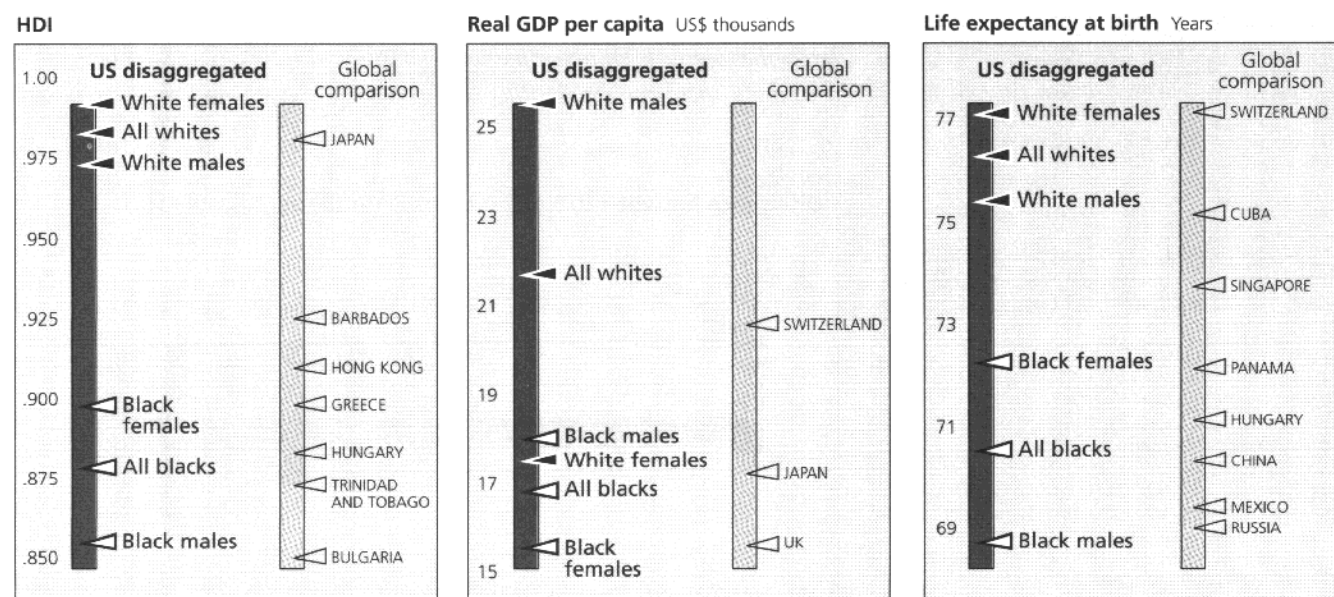
With so many inequalities in multiethnic and otherwise divided societies, a disaggregated HDI profile is essential to eventually understanding the underlying sources of tension and potential causes of future trouble.

The HDI is thus a useful and informative tool for analysing and assessing development. But it probably is still too early to use the HDI to evaluate a country's performance, or to allocate aid funds. That kind of application must await further improvements to the HDI.

### A human development agenda

Since the *Human Development Report* appeared, it has attracted a great deal of international attention and debate. And many countries, going beyond discussions and policy statements, are putting human development ideas into practice. Bangladesh, Colombia, Ghana and Pakistan have already prepared comprehensive human development strategies, and more than 20 other countries are—with UNDP assistance—undertaking different types of human development initiatives. These efforts are likely to include ten significant steps.

FIGURE 1.13  
Disaggregated human development indicators for the United States

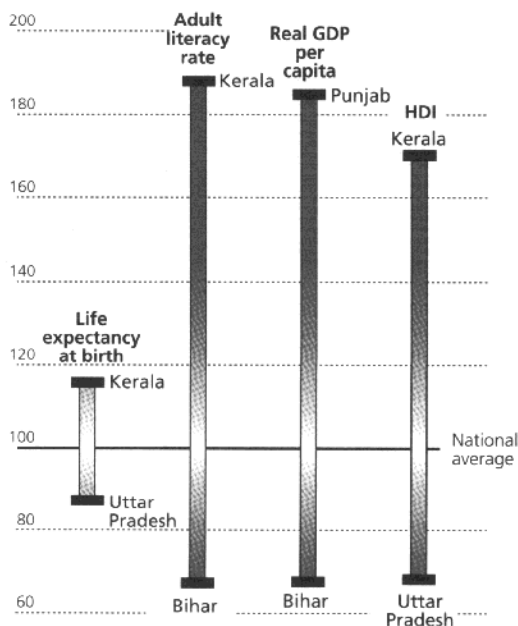


1. *Prepare a national human development report*—Since the *Human Development Report* must publish internationally comparable data, it often cannot use the most recent or most relevant information for countries. Some—including Cameroon, Côte d'Ivoire and Paraguay—have therefore produced their own reports reflecting their own circumstances, statistics and policy concerns.
2. *Prepare a human development country profile*—As a part of the national report, or as a separate initiative, a short statistical profile of human development can be prepared, showing the progress achieved and the distance yet to be travelled. This has already been done in Mozambique, Thailand, Papua New Guinea and elsewhere.
3. *Improve human development statistics*—Most countries put a lot of effort into publishing statistics on economic growth, but much less into those on the human condition—how many people are below the poverty line, for example, or are homeless. Often, the data are collected but not collated into usable form because of an apparent lack of demand. Priorities need to be re-established to ensure that data on human development are collected and made available to policy-makers, as has been found in Kenya, Mexico and the Philippines, among others.

FIGURE 1.14

### Disparity among India's states

Percentage of national average



4. *Set human development targets*—Human development targets are seldom quantitative—again because the underlying data are missing. The best progress in targeting has, often with UNICEF's assistance, been in the area of children's development, health and education. This experience needs to be extended to other areas to establish just what is to be achieved by which group—and when. To be kept in mind, though, is that human development objectives cannot be limited to quantifiable targets. Many important aspects of human development escape quantification and can be analysed only in qualitative terms. For example, people's education depends both on years of schooling and on the type of knowledge imparted.

5. *Cost the targets*—While the construction costs of roads or industrial plants are frequently estimated (if not very accurately), human development targets rarely are (even tentatively). This makes social expenditure vulnerable to economic cutbacks—since if nobody knows what good health costs, it is difficult to defend in the budget.

6. *Clarify who does what*—National strategies need to consider the most appropriate roles for central, regional and local governments—and for the private sector and NGOs. To be considered above all is how people can best participate and take charge of their own lives and the interests of their families and communities.

7. *Establish who will pay*—In some cases, the state will need to make the investment—in basic education or health. In oth-

FIGURE 1.15

### Disparity among Mexico's states

Percentage of national average

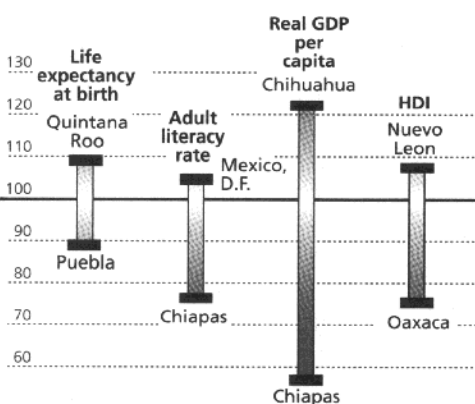
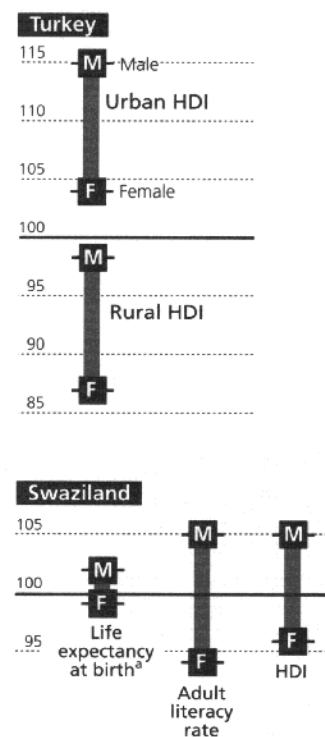


FIGURE 1.16  
Gender differences in Turkey and Swaziland

Percentage of national average



a. Adjusted to account for the biological differential.



ers, some segments of the population could be asked to pay for services through user charges. Or it might be better to concentrate on providing more employment and

income-earning opportunities that would enable people to become more self-sufficient and independent.

8. *Design a national strategy*—To ensure that all the activities link together naturally, it might be useful to formulate a comprehensive country strategy for human development—a strategy concerning all the steps from the identification of priority areas to the implementation of policies and programmes and a monitoring of progress.

9. *Seek external cooperation*—Most governments of developing countries can improve levels of human development with the resources they already have. But more substantial achievements will also depend on international cooperation—through fairer access to international markets and through more effective technical assistance and financial aid (box 1.4). They should establish areas of common interest and common priority with industrial countries. For Bangladesh and Pakistan, human development has been an agenda item of consultative group meetings.

10. *Build political alliances*—Human development accelerates where people understand the benefits from a healthier and better-educated population. Governments can assist this process by working with natural allies, such as doctors and teachers, to promote these ideas. They can also target media campaigns at small businesses, for example, to extol the virtues of educating children better so that they can one day help manage businesses—or at men, to explain how all society benefits when women have better opportunities. To broaden support for human development country strategies, it is often useful to ensure full participation of all interested partners right from the start—of all concerned government entities, as well as the private sector, NGOs and people at large.

These ten steps are only schematic, and each country will decide on its agenda. The steps nevertheless highlight the value of approaching human development systematically. Remember that the struggle for human progress in the industrial countries is a continuous process (box 1.5). Clearly, reorienting development towards people—although doable—is a complex challenge.

#### BOX 1.4

##### Technical cooperation's high cost in Africa

Technical cooperation is an important way for developing countries to acquire skills, build up their capacity and pursue self-reliant development. About a quarter of all development assistance to Africa has been in this form—more than \$3 billion a year. But this technical cooperation is under attack for being expensive and outmoded—serving the priorities of the donors rather than building up national capacity.

Such programmes often rely heavily on expatriate personnel. A study of ten African countries showed that around 75% of the resources are spent on personnel—as opposed to equipment and operating expenses. Relatively little use is made of national experts. In Mali in 1990, donors employed some 80 foreign doctors and medical personnel, even though 100 qualified Malian doctors were unemployed.

Donors often impose experts on reluctant national governments who feel this to be the price of financial assistance. When the experts come, they often run the programmes, with control

over the purse strings. This is frustrating for African governments and for aspiring professionals in African institutions, who, using the expert-counterpart training system, find themselves “overshadowed” by a foreign expert.

Technical assistance is very expensive aid. Donor spending on technical cooperation is as large as the entire civil service bill—in Uganda, many times greater. The cost of one person-year of an expatriate expert can exceed a department's entire operating budget. In capital assistance projects, the situation may even be worse.

Proposals are beginning to be implemented that could help improve technical cooperation. One is to make greater use of local experts and to pass the management of programmes to recipient governments. Another is to include market elements in technical cooperation. If recipients were given the money—untied to any predetermined “package” from the donors—they would probably make very different decisions on how best to use it for human development.

#### BOX 1.5

##### Progress possible—though not inevitable—on three fronts

The more enlightened advanced societies have taken three centuries to achieve the civil, political and social dimensions of human development. The 18th century established *civil* rights: from freedom of thought, speech and religion to the rule of law. In the 19th century, *political* freedom and participation in the exercise of political power made major strides, as the right to vote was extended to more people. In the 20th century the welfare state extended human development to the *social* and *economic* spheres, by recognizing that minimum standards of education, health, nutrition, well-being and security are basic to a civilized life and to exercising the civil and political attributes of citizenship. These battles were not won easily or without resistance. Each

progressive thrust was followed by reactionary counterthrusts and setbacks.

The struggle for *civil* liberty was opposed, after the French Revolution, by those fearful that it would lead only to tyranny—that the fight for political participation would enslave the masses. We are now witnessing one of these counterattacks on the economic liberties of the welfare state, and on some fronts partial retreat. The argument again is that the opposite of the intended result is achieved. Just as civil liberty was said to lead to tyranny, and political liberty to slavery, so compassionate concern for the poor, it is now said, can lead only to their continuing poverty. The *Human Development Reports* show that human progress is possible, though not inevitable, along all three fronts.



## People's participation

Participation means that people are closely involved in the economic, social, cultural and political processes that affect their lives (box 2.1). People may, in some cases, have complete and direct control over these processes—in other cases, the control may be partial or indirect. The important thing is that people have constant access to decision-making and power. Participation in this sense is an essential element of human development.

Participation, certainly not a new term, has been a part of the development vocabulary since the 1960s, or even before. But it has generally referred only to people's involvement in particular projects or programmes. In this Report, the critical difference is that participation is an overall development strategy—focusing on the central role that people should play in all spheres of life. Human development involves widening their choices, and greater participation enables people to gain for themselves access to a much broader range of opportunities.

People can participate as individuals or as groups. As individuals in a democracy, they may participate as voters or political activists—or in the market as entrepreneurs or workers. Often, however, they participate more effectively through group action—as members of a community organization, perhaps, or a trade union or a political party.

People everywhere are certainly demanding much greater access to political, economic and social opportunities. They might not expect “full participation”—but they do want a steady advance towards it. Participation is, after all, a process, not an event.

Since participation requires increased influence and control, it also demands in-

creased empowerment—in economic, social and political terms. In economic terms, this means being able to engage freely in any economic activity. In social terms, it means being able to join fully in all forms of community life, without regard to religion, colour, sex or race. And in political terms, it means the freedom to choose and change governance at every level, from the presidential palace to the village council.

All these forms of participation are intimately linked. Without one, the others will be incomplete and less effective.

Any proposal to increase people's participation must therefore pass the empowerment test—does it increase or decrease people's power to control their lives? This test applies to all institutions that organize or affect human lives—whether markets, governments or community organizations. Each must advance the cause of people.

Participation, from the human development perspective, is both a means and an end. Human development stresses the need to invest in human capabilities and then ensure that those capabilities are used for the benefit of all. Greater participation has an important part to play here: it helps maximize the use of human capabilities and

### A checklist of effective participation

BOX 2.1

*Do people have:*

- Equitable access to health and other aspects of physical well-being?
- Equitable access to knowledge, skills, technology and information?
- Equal human rights?

*If there are obstacles, do they lie in:*

- The legal system?
- Administrative rules and procedures?
- Social norms and values?

*What should be the priority concern for a strategy to promote people's participation?*

- The distribution of income and assets?
- Increasing public expenditure on human development priorities?
- Dismantling market barriers?
- Improving democratic governance?
- Strengthening the elements of a civil society, such as people's organizations, NGOs and a free press?



*Participation in economic life affords people a basis for self-respect and social dignity*

is thus a *means* of increasing levels of social and economic development. But human development is also concerned with personal fulfilment. So, active participation, which allows people to realize their full potential and make their best contribution to society, is also an *end* in itself.

**Forms of participation**

Since participation can take place in the economic, social and political arenas, each person necessarily participates in many ways, at many levels. In economic life as a producer or a consumer, an entrepreneur or an employee. In social life as a member of a family, or of a community organization or ethnic group. And in political life as a voter, or as a member of a political party or perhaps a pressure group. All these roles overlap and interact, forming patterns of participation that interconnect with—and often reinforce—each other.

- *Household participation*—It is almost always women who rear the children and provide food and water, as well as ensure adequate health care for the family. And to fulfil such responsibilities, they also work outside the home, often in the informal sector.

This contribution of women to society remains unrecognized in economic statistics, and it does not give women even an equal say in decisions in the household. A survey in Uganda found that the management of household income was a joint responsibility for only a small minority. In most cases, the husband handed over only a small proportion of “housekeeping money” to the wife.

Where women do have control over household funds, they generally make much better use of them. In Malaysia, a case study of rubber tappers found that almost all income earned by women was directed to meeting household needs—while men tended to devote sums equivalent to 40% of household incomes to their personal requirements, such as tobacco. Most societies are still a long way from looking at household tasks as a shared responsibility of men and women.

The starkest example of gender discrimination in the household is revealed through child survival rates. In Bangladesh, nearly 15% more girls than boys die in the first few years of life. And under the age of five, the mortality rate for girls in many countries is higher than that of boys—5% higher in Nepal, 4% in Pakistan and India, and 2% in Bhutan—whereas, biologically, more girls should survive than boys.

- *Economic participation*—Most people spend a large part of their lives in economic activity. It is in the economic arena that people have a unique opportunity to use their capabilities and to gain a remunerative income, which in turn enables them, through increased purchasing power, to increase their range of choices. Participation in economic life also affords people a basis for self-respect and social dignity, attributes that are integral to participating in all dimensions of life.

The nature of economic participation can vary widely, from forms of drudgery to creative, productive and independent economic activity. Societies also vary greatly in the value they place on forms of work, ranging from the association of manual work with servitude to a respect for manual labour in more egalitarian societies. And closely related to this range of social attitudes is the nature of the work environment itself, which can be more or less participatory. But it is only in a democratic environment that people can derive full satisfaction from work and from the perception that they are making a valuable contribution to development.

- *Social and cultural participation*—All people, and all communities, have a right to create their culture in whatever way they wish—whether through language, through ritual, art, music and dance or through literature or storytelling—in any of the myriad forms of culture through which human beings the world over express themselves.

But globally there has been a tendency towards homogenization. The world today has around 4,000 languages, but thousands of languages have been lost over the past couple of centuries. In the 19th century, there were 1,000 Indian languages in South

America. Now there are fewer than 200. And dress has similarly become more uniform, with most traditional costumes being steadily replaced by a much smaller number of international styles.

Even the very form of expression can come under threat. Oral cultures are particularly at risk since the current trend is towards less emphasis on memory and more on literacy and mechanical reproduction—substituting books for the spoken word. This means, for example, that much traditional wisdom in health and medicine, not written down, has been lost.

Similarly, many communities have communicated from one generation to the next through such intricate skills as weaving and carving—skills constantly being eroded by mass industrial production.

Such changes are usually accepted, often welcomed, as “progress”. Only now—with the threat that some languages and skills might disappear altogether—is the world becoming more concerned about the wealth of valuable human information that might be lost.

Cultures need to be respected and constantly asserted or they die. Hence the determination of many groups, particularly indigenous peoples, to participate actively to preserve and reassert their identity. This is a form of cultural participation to which they have a right—and from which the whole world gains.

But if these valuable elements of the human experience are to survive, all parts of society have to contribute—including people’s organizations, non-governmental organizations (NGOs) and governments. Cultural riches must be available to all at reasonable prices, not limited to the wealthy or to tourists. UNESCO studies show how critical the decentralization of cultural institutions is for ensuring that they are readily accessible at the local level. And while new technologies can often diminish local cultures, used creatively they can also make them available to much wider audiences.

- *Political participation*—In recent years people have been struggling, individually and collectively, to have a much greater say in national life. In many cases, opposing au-

torocratic regimes has demanded great courage—as with those who opposed the regimes in Argentina, the Philippines and South Africa, as well as in Eastern Europe and the former Soviet Union. In other cases, as in Zambia, the rulers have themselves recognized that, in the long term, stifling people’s power and initiative would be counter-productive. And international pressures have also reinforced national forces for political change as ideas about human rights and democracy have spread around the globe.

Achieving meaningful and durable democracy is far from simple. It may include several aspects: guarantees of human rights, including freedom of speech and association; rule of law; free, fair and fully contested elections at periodic intervals; a multiparty system; orderly transition of government and elected representatives fully accountable to voters.

Democracy demands an effective and open political system, not just within governments but within political parties so that people have a real choice when nominating candidates for election. And if governments are to be kept free from undue influence from vested interests, democracy also demands strong institutions of civil society (such as a free press) and a diversity of non-governmental organizations (such as the environmental groups that have had such an impact in many countries in recent years).

Democracy cannot be achieved overnight. Just as economic growth means little unless it is translated into improvements in human lives, so democracy can be merely an empty ritual of periodic elections unless people participate, aware and empowered, in all the institutions of civil society. Elections are a necessary, but certainly not a sufficient, condition for democracy. Political participation is not just a casting of votes. It is a way of life.

### New openings

Despite a number of violent conflicts, the world seems to be going through a period of positive change: participation of all kinds

*Political participation is not just a casting of votes. It is a way of life*

**Markets exclude  
those whose  
poverty renders  
them  
uncreditworthy**

seems to be on the upswing—particularly in the formerly socialist countries and in the developing world.

- *Democracy*—has been extended to many parts of the world in the past decade. Close to two-thirds of humankind now live in countries that are moving towards, or are already enjoying, democratic forms of government.

- *The transition to market economies*—is also gathering pace all over the world as governments dismantle state controls and open new doors for participation and entrepreneurial activity. Most formerly socialist countries have by now committed themselves to more market-based strategies. And many developing countries are liberalizing their economies—removing restrictive regulations, establishing much greater transparency in business affairs and offering entrepreneurs greater opportunities for participation in economic activity.

- *Privatization*—is creating new avenues for participation in the economies of many countries. Since 1980, around 7,000 state-owned enterprises have been privatized, about 1,400 of them in developing countries.

- *The information revolution*—is bringing reports of global events to everyone's home. Now, through radio and TV, people have a much greater sense of participation in international events—as they happen. And people now have many different ways of communicating within their own countries, not just through broadcast media, but also through newer media, from fax machines to videocassettes, that are much less vulnerable to censorship—making it much harder for governments to monopolize the flow of information.

- *Non-governmental organizations*—have increased substantially in recent years. In 1990, there were an estimated 50,000 non-governmental organizations (NGOs) in developing countries working in many different fields, from health care to informal education. And they have taken on an important advocacy role on such issues as gender discrimination, human rights and environmental concerns.

These changes, rapid and complex, have taken different directions in different countries. In some, the impetus has come from the government in power. In others, it has been the outcome of popular rebellion. And the results have been as diverse as the events. Some countries have succeeded in strengthening democratic institutions and enjoyed steady increases in efficiency. Others have suffered economic crisis, social chaos, ethnic disruptions and even civil war.

### **The groups excluded**

Despite the accumulating forces for greater participation, large numbers of people continue to be excluded from the benefits of development: the poorest segments of society, people in rural areas, many religious and ethnic minorities—and, in almost every country, women. Also excluded are those millions, particularly children, whose preventable and premature deaths cut short their lives.

Many of these groups necessarily overlap but it is useful to identify some of them individually.

- *The poorest people*—find that their very poverty is a formidable barrier to entering many aspects of social, economic and polit-

#### **BOX 2.2**

##### **Children of the streets**

Millions of children live in the slums or on the streets of Third World cities, and their numbers grow daily as poverty in the rural areas drives people to the cities in the hope of a better life. Thirty years ago, the population of Brazil was 55% rural—now it is 75% urban. Around three-quarters of street children in Brazil are thought to be migrants.

Many street children do have homes and parents, but they may visit them only rarely, forced to earn their livelihood on the streets and driven from the squalor of one or two crowded rooms in the shantytowns. In Manila in the Philippines, three million people live in slums, about half of them children. Fewer than a quarter of families have piped water, and two-thirds have no sanitary facilities. Manila has about 75,000 street children.

India probably has the greatest number of street children. New Delhi, Bombay and Calcutta have around 100,000

street children each, and Bangalore about 45,000. There, as elsewhere, they must work to survive—collecting rags, shining shoes, selling newspapers, scavenging on rubbish dumps. Many also turn to crime. India's juvenile crime rate is 3.1 per 1,000 people.

Street children are also a growing problem in Africa. There, too, migration from the countryside is swelling the urban slums. Mathare Valley in Nairobi is the largest slum community in Kenya, with around 200,000 people. The majority are migrants and a high proportion are children. Four years ago, Nairobi had about 16,000 street children, today there are thought to be 25,000.

Street children are one of the most obvious signs of urban deprivation. Hungry, sick and often homeless children with little chance of a basic education are a sharp reminder of the human potential the world is wasting.

ical life. In many developing countries, income disparities are very wide. In Indonesia, the poorest 20% of the people receive only 8.8% of national income, in Sri Lanka 4.8%. And in many cases, the gaps between the poor and the rich are widening. In Chile between 1970 and 1988, the real income of the poorest 20% fell by 3%, while that of the richest 20% increased by 10%. Markets, in theory open to everyone, in practice exclude those whose poverty renders them uncreditworthy. In Bangladesh, the landless make up around half the rural households but receive only 17% of institutional credit.

Poverty has its greatest impact on children and is a denial to future generations. Infant mortality rates in the least developed countries are still 114 per 1,000 live births, and nearly 13 million children die each year before their fifth birthday. The HIV/AIDS pandemic will increase not only the number of child deaths but also the problem of orphans and hence child poverty.

And even children who do survive are deprived of the opportunity to participate fully in their countries' development. Some 200 million of today's children are having their potential for growth stunted by malnutrition. And well over 300 million children who should be in primary or secondary schools are missing their education, either because of the need to work or because schools are unavailable or too expensive. Many of these children spend their days at work in the fields or in the streets (box 2.2).

Poverty can also be harsh for the elderly. In the formerly socialist countries, the pensioners are among those who suffer most from the current reform process.

For millions of people all over the world, the daily struggle for survival absorbs so much of their time and energy that, even if they live in democratic countries, genuine political participation is, for all practical purposes, a luxury.

- **Women**—are the world's largest excluded group (box 2.3). Even though they make up half the adult population, and often contribute much more than their share to society, inside and outside the home, they are frequently excluded from positions of power. They make up just over 10% of the

world's parliamentary representatives, and consistently less than 4% of cabinet ministers or other positions of executive authority.

In many industrial countries, the female human development index is only around 80% that of males. Women participate inadequately in employment, and in some industrial countries, women's earnings are less than half those of men (box 2.4).

Many developing countries exclude women from both political participation and productive work—whether by tradition, discriminatory laws or withheld edu-

BOX 2.3

### Women—the non-participating majority

Women, a majority of the world's population, receive only a small share of developmental opportunities. They are often excluded from education or from the better jobs, from political systems or from adequate health care.

- **Literacy**—Women are much less likely than men to be literate. In South Asia, female literacy rates are only around 50% those of males. And in many countries the situation is even worse: in Nepal 35%, Sierra Leone 37%, Sudan 27% and Afghanistan 32%. Women make up two-thirds of the world's illiterates.

- **Higher education**—Women in developing countries lag far behind men. In Sub-Saharan Africa, their enrolment rates for tertiary education are only a third of those of men. Even in industrial countries, women are very poorly represented in scientific and technical study: in Spain, the ratio of female to male third-level students in these fields is 28%, in Austria 25% and in Canada 29%.

- **Employment**—In developing countries women have many fewer job opportunities: the employment participation rates of women are on average only 50% those of men (in South Asia 29%, and in the Arab States only 16%). Even when they do find work, they tend to get paid much less: in the Republic of Korea, women's wages are only 47% those of men. Wage discrimination is also a feature of industrial countries: in Japan, women receive only 51% of male wages.

Women who are not in paid employment are, of course, far from idle. Indeed, they tend to work much longer

hours than men. The problem is that the work they do, in domestic chores and caring for children and the elderly, does not get the recognition it deserves in national income accounts.

- **Self-employment**—Women's opportunities for self-employment can be restricted in a number of ways. In some countries they are still not allowed to own property, or to offer collateral for bank loans or even to drive.

- **Politics**—In some countries, women are still not allowed to vote. And women almost everywhere are underrepresented in government: in 1980, they made up just over 10% of the world's parliamentarians and less than 4% of national cabinets. In 1993, only six countries had women as heads of government.

- **Health**—Women tend on average to live longer than men. But in some Asian and North African countries, the discrimination against women—through neglect of their health or nutrition—is such that they have a shorter life expectancy. Indeed, comparing the populations who should be alive, based on the global mortality patterns, it seems that 100 million Asian women are "missing".

One of the greatest health risks for women in poor countries is childbirth. Maternal mortality rates in the developing world are more than 15 times higher than in the industrial countries.

- **National statistics**—Women are often invisible in statistics. If women's unpaid housework were counted as productive output in national income accounts, global output would increase by 20–30%.



## BOX 2.4

## Women in Japan

Japan, despite some of the world's highest levels of human development, still has marked inequalities in achievement between men and women. The 1993 human development index puts Japan first. But when the HDI is adjusted for gender disparity, Japan slips to number 17. Here's why:

In education, the tertiary enrolment ratio for females is only two-thirds that of males.

Similarly in employment, women are considerably worse off. Women's average earnings are only 51% those of men, and women are largely excluded from decision-making positions: they hold only 7% of administrative and managerial jobs.

Their representation is even lower in the political sphere. Women obtained the right to vote, and to be elected to parliament, only after the Second World War. Yet today, only 2% of parliamentary seats are held by women, and at the ministerial level there are no women at all (compared with the 9% average for in-

dustrial countries and 13% for the other countries of Asia). Nevertheless, one or two women have achieved important political positions, and a number of women were among the founders of the Social Democratic Party.

In legal rights in general, Japan's patrilineal society is only gradually changing to offer women greater recognition and independence. Only in 1980 were the inheritance rights of Japanese women raised from one-third to one-half of their late husbands' property (the rest goes to the children). And in other aspects the law is still not gender-neutral. Thus, the legal age of marriage is 18 for men, but 16 for women. And after divorce, a man can remarry immediately, but a woman has to wait six months.

Japan now has political and non-governmental organizations pressing for change. The League of Women Voters, for instance, is lobbying for a correction in the disparity of seat distribution in parliament, and for a greater participation of women in policy-making.

cation. In the countries for which relevant data are available, the female human development index is only 60% that of males. Indeed, for decades, life has changed very little for 500 million rural women in the developing world.

- *Minorities and indigenous peoples*—often find it difficult to participate fully in societies that consistently operate in favour of the dominant groups. Sometimes this discrimination is embedded in the legal framework—denying minority groups equal access to education, to employment opportunities or to political representation. But exclusion is generally less a matter of official policy than everyday practice. In the United States, where everyone is “created free and equal”, there is a marked difference between the white and black populations. As chapter 1 showed, if the US were divided into two “countries”, the one with only the white population would be in first place in the human development index, while the one with the blacks would be number 31 (box 2.5). In Guatemala, the Indian population has an infant mortality rate 20% higher than the rest of the population. And in South Africa, the blacks are a marginalized majority (box 2.6).

An extreme form of discrimination and exclusion is through violence. Since the Second World War, 40 ethnic groups around the world have been persecuted or massacred, suffering millions of deaths.

- *People in rural areas*—have very restricted participation in economic and social life in the developing world. The rural per capita income in many countries is around half that in towns and cities. And rural people have much less access to government services. Despite making up around two-thirds of the population, they receive on average less than a quarter of the education, health, water and sanitation services. In Ethiopia, 87% of the people live in rural areas but only 11% of them have access to safe drinking water, compared with 70% of the urban population. In Bangladesh, 84% of the population is rural but only 4% of them have access to sanitation facilities, compared with 40% of the urban population. And in India, school attendance for children aged 5–14 is much lower in rural areas: 55% for boys and

## BOX 2.5

## One country, two nations

Almost every country has one or more ethnic groups whose level of human development falls far below the national average. One of the clearest, and best documented, cases is that of blacks in the United States.

Their disadvantage starts at birth. The infant mortality rate for whites is 8 per 1,000 live births, but for blacks it is 19. And black children are much more likely than white children to grow up in single-parent homes—in 1990, 19% of white children were growing up in single-parent households, compared with 54% of black children.

Children in black families are also more likely to grow up in poverty. The real GDP per capita for whites in 1990 was around \$22,000, but for blacks it was around \$17,000.

As Andrew Hacker, the author of *Two Nations* (1992), graphically records:

*The statistics are daunting. Nearly two-thirds of black babies are now born out of wedlock, and over half of black families are headed by women. The majority of black*

*youngsters live only with their mother, and in over half of these households, she has never been married. At the last count, over half of all single black women have already had children, and among women in their mid to late thirties, less than half have intact marriages. These figures are from three to five times greater than for white households, and markedly higher than those recorded for black Americans a generation ago.... Black Americans are Americans yet they subsist as aliens in the only land they know. Other groups may remain outside the mainstream—some religious sects, for example—but they do so voluntarily. In contrast, blacks must endure a segregation that is far from freely chosen. So America may be seen as two separate nations.*

Indeed, if the United States were divided into two “countries”, the one with the white population would rank number one in the world, according to the human development index, while that with the black population would be only number 31.

35% for girls (compared with 74% and 52% in urban areas).

Urban biases are a predominant feature almost everywhere. But even when the parliaments of some developing countries are dominated by rural elites, this does not mean that they act on behalf of rural people. Most are composed of city-based absentee landlords with little personal interest in public services in rural areas. They often ensure their own access to electricity or water through private generators or tubewells, and send their children abroad for education. Meanwhile, rural people in developing countries remain a deprived and marginalized majority.

- *The disabled*—make up at least 10% of the world's population. They include all those who have experienced injury, trauma or disease that results in long-term physical or mental changes.

Disability is common to both industrial and developing countries, but the sources tend to be different: in the industrial countries, the principal causes are degenerative diseases associated with ageing, while in the developing world the causes are more likely to be disease, malnutrition and war. Of Cambodia's 8.5 million people, 150,000 have been disabled by mines.

Disability, even in industrial countries, is closely linked with poverty. In the United States, blacks and native Americans are twice as likely to be disabled as whites. And children in poor families are 13% more likely to be mentally retarded than those in middle- and upper-income families.

In developing countries, disability is more common in rural than in urban areas, and among the poor. In Bangladesh, those most likely to be disabled are the landless labourers.

TABLE 2.1  
**Share of poorest 20% of world population in global opportunities**  
(percentage of global economic activity)

	1960-70	1990
Global GNP	2.3	1.3
Global trade	1.3	0.9
Global domestic investment	3.5	1.1
Global domestic savings	3.5	0.9
Global commercial credit	0.3	0.2

The disabled face many barriers to participation. They tend, for example, to have less access to education: in Hong Kong in 1981, more than a quarter of the disabled population between 15 and 24 had received no schooling. And they are also more likely to be unemployed: in Japan in 1980, when 62% of the total population was employed, only 32% of the disabled were employed.

Some countries have taken measures to give the disabled greater opportunities. Germany has a quota for employment of the disabled of 6% in both government and private business. And the United States has far-reaching legislation: the 1992 Americans with Disabilities Act sets a large number of standards to be achieved in working life.

The disabled in the developing world have much more basic problems. In Zimbabwe in 1982, when 10% of the population was estimated to be disabled, only 2% had access to any kind of rehabilitation services. For most of the world's disabled, full participation is still a long way off.

- *Poor nations*—cannot participate on an equal footing in international markets or extend market opportunities to their own people. Poverty is a formidable barrier to participation, whether within or between nations. The very poverty of poor nations denies them international credit, and barriers on the movement of both goods and people cut their potential earnings. The 1992 *Human Development Report* estimated that poor nations are being denied \$500 billion of market opportunities annually—

BOX 2.6

### Blacks in South Africa—still a people apart

South Africa has officially abolished apartheid. Yet the country's black people continue to live in a world apart.

- *Assets*—The richest 5% of the population, mostly white, owns 88% of all private property.

- *Poverty*—Half the population, mostly black, lives below the poverty line.

- *Children*—Many poor black children are being stunted by malnutrition: 40% of rural children and 15% of urban children.

- *Literacy*—One-third of the black

population over 15 (some three million people) is illiterate.

- *Education*—Three-quarters of black teachers are either unqualified, or underqualified, for their job. The education system thus perpetuates a vicious circle of deprivation and discrimination.

For South African blacks, the achievement of full political rights would be a vital step towards greater participation. But unravelling apartheid completely will be a complex and difficult task in the years ahead.

*Participation is a plant that does not grow easily in the human environment*

about ten times the annual flow of foreign assistance they receive. The poorest 20% of the world's population now receives only 0.2% of global commercial credit, 0.9% of global trade and only 1.3% of global income (table 2.1).

It would be short-sighted to assume that the growing demands for increased participation will stop at national frontiers. Millions of workers from developing countries have already voted with their feet and migrated, legally and illegally, to industrial countries or to neighbouring developing countries. And the process has only just started. Unless more people can begin to participate in global economic opportunities, the 21st century may witness an unprecedented migration across national borders.

Increased participation at a global level will require a radical readjustment of the international order—in particular a dismantling of international trade restrictions and a much more democratic system of global governance.

Taking these and other excluded groups together, it seems likely that fewer than 10% of the world's people participate fully in political, economic, social and cultural life. For the vast majority, real participation will require a long and persistent struggle.

### **Obstacles**

Participation is a plant that does not grow easily in the human environment. Powerful vested interests, driven by personal greed, erect numerous obstacles to block off the routes to people's political and economic power. These obstacles include:

- *Legal systems*—Laws are often arbitrary and capricious and favour those with political influence or economic clout. In too many countries, legislation fails to measure up to ideals of transparency, accountability, fairness—and equality before the law. Some countries' laws exclude the participation of women, for example, or of religious or ethnic minorities, or deny certain rights to workers.
- *Bureaucratic constraints*—Many developing countries have shackled their people

with innumerable regulations and controls, demanding all sorts of permits and permissions for even the most modest business initiative. Fortunately, many governments have started to dismantle the most stifling of these controls and are opening new avenues for entrepreneurial activity.

- *Social norms*—Even when laws change, many old values and prejudices persist, whether against women or different tribes, castes or religious groups—and are often deeply embedded in everyday language and behaviour. Laws may promote equality, but it is usually left to the discriminated group to struggle against prejudice. Thus, working women, for example, even when they prove themselves better, are not given equal treatment.

- *Maldistribution of assets*—In developing countries, one of the most significant assets is land. A high proportion of the people struggle to make a living in agriculture, but their efforts are often thwarted by the dominance of feudal elites who exert an overwhelming control over land. In most Latin American countries, the land tenure systems are notoriously skewed in favour of the rich (table 2.2). Inequality is conventionally expressed by the "Gini coefficient", which varies from zero (equal assets for everybody) to 1 (one person owns everything). In most Latin American countries, the Gini coefficient for land distribution is around 0.8—in Panama 0.84, in Brazil 0.86 and in Paraguay 0.94.

Maldistribution of land is by no means confined to Latin America. In Egypt, the richest 20% of landowners still control 70% of the agricultural land. And in Bangladesh, small farmers (with less than 2.5 acres) account for 70% of farms but have only 29% of the land area.

In these countries, there can never be true participation in the rural areas without far-reaching land reforms—as well as the extension services, training and credit for smaller farmers that can help them become productive and self-reliant.

Whether in urban or rural areas, vested interests that currently enjoy economic, financial, political or social power are usually determined to defend their position—

either individually or through close-knit associations, well-financed lobbies and even violence.

Changing the power equation requires the organization of a countervailing force, or even a revolution. People's organizations—be they farmers' cooperatives, residents' associations or consumer groups—offer some of the most important sources of countervailing power. And they often exercise it most effectively through the sharing of information and ideas—it is ideas,

not vested interests, that rule the world for good or evil.

## Structure of the Report

Participation is an important element in these and many other aspects of human life. This Report concentrates on participation in development—through markets, government and community organizations.

Chapter 3 focuses on free and open markets as a dynamic form of participation for both producers and consumers, assessing the extent to which markets are accessible to wide popular participation—that is, whether they are “people-friendly”. It also analyses the participation of people through work, especially their participation in labour markets. It shows how current strategies result in output growth without employment and argues for a fundamental change in development thinking. This chapter also reviews the experiences to date in liberating private enterprise and explores how participatory human development requires a new balance between the private and the public sectors.

Chapter 4 is devoted to people's participation in governance. It looks at political participation and at how governments reach out to people, particularly through decentralization as a technique for opening governance up to greater popular participation—examining the conditions for successful participation as well as highlighting the potential pitfalls, including the risk of creating even firmer power bases for entrenched local elites.

Chapter 5 examines people's participation in civil society, particularly the role of non-governmental organizations. Considering them from both a national and an international perspective, it shows how these organizations can oppose existing power structures and engineer practical changes—and through their advocacy bring millions of the world's marginalized people into the mainstream of social and economic life.

*Changing the power equation requires the organization of a countervailing force*

TABLE 2.2  
**Inequality in the distribution of landholdings in selected countries**

Country	Year	Gini coefficient
<i>Very high inequality (Gini above 0.75)</i>		
Paraguay	1981	0.94
Brazil	1980	0.86
Panama	1981	0.84
Uruguay	1980	0.84
Saudi Arabia	1983	0.83
Madagascar	1984	0.80
Kenya	1981	0.77
<i>High inequality (0.51 to 0.75)</i>		
Colombia	1984	0.70
Dominican Rep.	1981	0.70
Ecuador	1987	0.69
Grenada	1981	0.69
Chile	1987	0.64
Honduras	1981	0.64
Yemen	1982	0.64
Sri Lanka	1982	0.62
Peru	1984	0.61
Nepal	1982	0.60
Uganda	1984	0.59
Turkey	1980	0.58
Jordan	1983	0.57
Pakistan	1980	0.54
Philippines	1981	0.53
<i>Medium inequality (0.40 to 0.50)</i>		
Bahrain	1980	0.50
Bangladesh	1980	0.50
Morocco	1982	0.47
Togo	1983	0.45
Ghana	1984	0.44
<i>Low inequality (below 0.40)</i>		
Malawi	1981	0.36
Mauritania	1981	0.36
Egypt	1984	0.35
Niger	1981	0.32
Korea, Rep. of	1980	0.30

The Gini coefficient is a measure of inequality in distribution. It ranges from zero to 1: the closer the value to 1, the greater the inequality.





## People and markets

*People-friendly markets allow people to participate fully in their operation and to share equitably in their benefits*

Free markets provide the most efficient mechanism yet devised for the exchange of goods and services—impersonally matching supply and demand, bringing together buyers and sellers, employers and workers, and constantly setting and resetting prices so that the economy works at peak efficiency. Free enterprise provides a mechanism for unleashing human creativity and entrepreneurial ability.

Three critical questions: Are the markets really free? Are they accessible to all the people? And what is their impact on the distribution of income and other development opportunities and benefits?

Most markets are stifled by barriers—many raised by government regulations and some by powerful interest groups. And markets are not automatically or inevitably people-friendly. They make no value judgments. They reward those who have either substantial purchasing power or valuable commodities or services to sell. But people enter markets as unequal participants and often leave with unequal rewards, even when markets operate neutrally.

So, for all their efficiency at matching buyers and sellers, markets can also be associated with increasing inequality and poverty, as well as large-scale unemployment.

Markets may also place very little value on environmental concerns and the needs of future generations. Soil, water, fossil fuels and minerals are important inputs to the production process. But their market prices often fail to reflect their true scarcity value—leading to overexploitation and depletion. Company profit and loss accounts seldom register the true costs of pollution—which are passed on to the rest of society. Similarly, national income accounts fail to register the constant depletion of nat-

ural capital—and thus hide from policy-makers the high cost of environmental neglect. Costa Rica during 1970–90 lost natural capital (such as soils and forests) amounting to more than 6% of its total GDP in that period. And in Indonesia during 1971–84, these losses were more than 9% of GDP. Yet their national income accounts were silent on this continuing haemorrhage.

Sustainable human development demands more of markets—that they continue to offer their advantages but that they do so in a more balanced way, combining efficiency, equity and sustainability. Markets are, after all, not an end in themselves. They are a means to human development. Markets should serve people—rather than people serving markets.

### **Making markets more people-friendly**

People-friendly markets allow people to participate fully in their operation and to share equitably in their benefits. Making markets more people-friendly will require a strategy that maintains their dynamism but supplements them with other measures to allow many more people to capitalize on the advantages they offer.

Most markets suffer from three types of distortions. First, there are distortions in the workings of the markets themselves. Some may be due to monopoly power as well as to short-term business considerations that make the markets less competitive, less efficient or less respectful of environmental concerns. Others are due to controlled prices, fiscal disincentives and constant government intervention in the market.

Second, there are distortions in the form of disparities among people who enter the market. Many people lack the educa-

tion, the assets, the credit or the skills to be competitive—or are excluded on the grounds of sex, race or ethnicity.

Third, markets often fail to reflect external costs and benefits—be it pollution (an external cost) or the prevention of communicable diseases (an external benefit). In addition, there are areas where markets are missing altogether. National income accounts do not, for example, include household work—nor do they measure the depreciation of natural capital assets over time. For both, a proper accounting should be made.

Traditional discussions of markets have focused more on their efficiency than on their equity aspects. But since markets are only a means towards human development, we must closely examine ways to build a bridge between markets and people—to make them more “people-friendly”. The measures that would make such a radical transformation possible can be divided into four groups (box 3.1):

1. Preconditions
2. Accompanying conditions
3. Corrective actions
4. Social safety nets.

#### 1. *Preconditions*

Certain conditions need to be met for markets to be kept free—and open to all those who seek to enter them.

- *Investment in people*—To compete effectively and to make a productive contribution, people need to have the health, the education and the skills to do so. The more dynamic developing countries have recognized the value of investing in their people. The newly industrializing countries of East Asia have sharpened their competitive edge, not just with lower-wage labour but with skill and entrepreneurship. Investments in human capital raise labour’s productivity—and, if matched by the kind of technology best suited to the skills of the workforce, can have a multiplier effect throughout the economy. These investments can also help reduce social and economic disparities.

Consider this: labour productivity increased by 11% a year in the Republic of

Korea between 1963 and 1979, and in Thailand by 63% between 1980 and 1985. Most of this increase came from a generous investment in the education and skills of people. And in Western Europe between 1970 and 1980, improvements in human capabilities accounted for 20–30% of the growth in income.

- *Access to assets*—If people are to participate freely in markets, they also need the physical and financial resources to do so. One of the greatest obstacles to a dynamic economy is an excessive concentration of land or business assets. But measures such as land reform may be only the start of the process. Many countries also have progressive fiscal regimes to ensure that income and wealth continue to be redistributed to the poorer members of society.

### Steps towards people-friendly markets

BOX 3.1

People-friendly markets allow people to participate fully in their operations and to share equitably in their benefits. Having markets serve people, rather than people serve markets, requires concrete steps:

#### 1. *Preconditions*

- Adequate investment in the education, health and skills of people to prepare them for the market
- An equitable distribution of assets, particularly land in poor agrarian societies
- Extension of credit to the poor
- Access to information, particularly about the range of market opportunities
- Adequate physical infrastructure, especially roads, electricity and telecommunications, and adequate support for R & D
- A legal framework to protect property rights
- No barriers to entry, irrespective of race, religion, sex or ethnic origin
- A liberal trade regime, supported by the dismantling of international trade barriers.

#### 2. *Accompanying conditions*

- A stable macroeconomic environment, especially ensuring stability in domestic prices and external currency values

- A comprehensive incentive system, with correct price signals, a fair tax regime and adequate rewards for work and enterprise
- Freedom from arbitrary government controls and regulations.

#### 3. *Corrective actions*

- Protection of competition, through antimonopoly laws and safeguards against financial malpractices
- Protection of consumers, especially through drug regulations, safety and hygiene standards and honest advertising
- Protection of workers, through regulated working conditions and minimum wage standards
- Protection of special groups, particularly women, children and ethnic minorities
- Protection of the environment, particularly through incentive systems and by banning pollution or making polluters pay.

#### 4. *Social safety nets*

- Adequate arrangements to look after the temporary victims of market forces to bring them back into the markets, primarily through human investment, worker retraining and access to credit opportunities—as well as more permanent support for groups such as the disabled and the aged.

*Information is power: denying people information is a sure way of disempowering them*

- *Extension of credit to the poor*—Much of the future growth in developing countries will have to come from small enterprises. But without adequate access to credit—and, where appropriate, to fiscal incentives and government contracts—small enterprises are unlikely to grow as rapidly as they might. So, the state should ensure, with private banks, that credit is available to smaller enterprises that can use it productively.
- *Access to information*—One of the essential characteristics of a people-friendly market is a good flow of information. The more widely information is available, the better the chances of fair competition and the equal sharing of benefits—information on global prices, efficient labour exchanges, transparent business contracts and honest advertising for consumers. Information is power: denying people information is a sure way of disempowering them and denying them equitable access to market opportunities.
- *Adequate infrastructure*—Private investment depends for its success on the existence of physical infrastructure such as roads and communications. Infrastructure is particularly important for rural areas, where roads, electricity and improved water supplies can enable people to participate in trade and industrialization and in increased employment opportunities. In many of the more successful developing economies, such as the Republic of Korea and Taiwan (province of China), the non-farm income of farm families now exceeds their income from agriculture.

There is also a need to ensure adequate funding for research and development (R & D) directed at human development. If R & D is left to the private sector alone, there may be little research directed at the needs of “excluded groups”—such as subsistence farmers and small-scale industries. There may also be too little funding for the development of more environment-friendly production technologies and alternative energy sources.

- *The rule of law*—Productive market participation demands clear and open transactions, primarily on the basis of mutual trust and respect but with the sanction of legal enforcement. At the same time, the

legal system needs to protect property rights, both from illegal forced seizure in civil society and from capricious nationalization by the state.

In too many developing countries, however, business is conducted on the basis of contacts rather than contracts—and directed less by open competition than by bribes and corruption. This saps initiative, reduces output and distracts from the real challenge of productive investment. Closed markets permit exploitation by the few, rather than unleash the creativity of the many.

- *No barriers to entry*—Many people are also excluded from effective participation in markets by political or social discrimination. Women, ethnic minorities and the disabled are often excluded either by legal fiat or by social practice. Many “low-caste” people have paid a heavy price, sometimes with their lives, when they dared to challenge the market barriers that their societies erected against them. Governments can play a major role in ensuring that markets are open to all—irrespective of race, religion, sex or ethnic origin.
- *A liberal trade regime*—All countries need to exploit their comparative advantages, keeping their economies open to international trade. But liberal strategies in the South can succeed only if the North keeps dismantling its protectionist barriers and opening its restricted markets.

## *2. Accompanying conditions*

Markets also need accompanying conditions to ensure that they are people-friendly and work as efficiently and equitably as possible.

- *A stable economic environment*—Markets function much better in a stable economic environment created by sound fiscal and monetary policies. High rates of inflation and violent fluctuations in exchange rates make it difficult for entrepreneurs to plan. Contracts entered into in good faith can become impossible to complete or enforce if conditions change drastically. Wild swings in exchange rates, although a delight to currency speculators, inhibit genuine entrepreneurs and restrict their decision-making to short-term visible horizons.

- *A comprehensive incentive system*—Correct price signals, a fair tax regime and adequate rewards for work and enterprise will ensure efficient resource allocation and utilization, including that of labour.

- *Freedom from arbitrary government actions*—Markets are greatly disturbed by sudden government intervention. Through changes in excise duties, tariffs or direct price controls, governments can distort markets such that prices reflect the interests of those in government, and their supporters, rather than the forces of the market. Government intervention is often essential to accelerate development. But it should follow three golden rules, as suggested by *World Development Report 1991*. First, intervene reluctantly: “let markets work unless it is demonstrably better to step in”. Second, “put interventions continually to the discipline of the international and domestic markets”: for instance, withdraw state subsidies when they are no longer needed. Third, intervene openly: “make interventions simple, transparent and subject to rules rather than official discretion”—preferring tariffs to quotas, for example.

### 3. Corrective actions

Where markets alone do not produce a desirable outcome, the state needs to regulate and correct. This should, of course, be done cautiously and only where necessary. But caution must not be confused with indecision. Corrective actions must be effective, though limited. This requires:

- *Protection of competition*—All governments need regulations to keep markets open and free. For instance, they need effective antimonopoly legislation—as well as regulations for banks and financial markets to ensure transparency and accountability in their operations. Such regulations are never villain-proof, as the savings and loan failures in the United States, the Recruit stock exchange scandal in Japan and the insider trading deals in the Bombay stock markets have shown. Regulations require energetic policing and swift reactions if the financially strong and powerful are not to reap unfair profits at the expense of the majority.

- *Protection of consumers*—The interests of responsible businesses, as well as those of consumers, are best served by clear sets of standards that the community expects producers to achieve. Regulations for the pharmaceutical industry, for example, require that drugs be tested over a certain period before they are released. Food manufacturers have to meet standards of health and hygiene. Car manufacturers must maintain standards of safety.

- *Protection of workers*—Less responsible employers are tempted to exploit their workers—among them, children (box 3.2). This requires action on two fronts. First, trade unions should be allowed to organize as a countervailing power to resist exploitation by employers. Second, governments need labour legislation to ensure good working conditions and minimum wages.

- *Protection of specific groups*—There are many cases where the natural workings of

BOX 3.2

#### Children without childhood

Child labourers are among the world's most exploited workers. Hundreds of millions of children work in fields and factories, on street corners and in garbage dumps all over the world. Most do some form of work from their earliest years, helping around the home or running errands. But the term “child labour” implies exploitation—that children are working long hours for low pay, sacrificing their health, their education and their childhood.

The largest numbers of child workers are in Asia, where in some countries they make up more than 10% of the labour force. But there are also large numbers in Africa, where several countries are reported to have up to 20% of their children working. And in Latin America, more than a quarter of children in some countries are thought to be working.

Industrial countries also have a substantial child workforce. In Europe, some of the largest numbers are in Italy and Spain. And there are believed to be large numbers in the United States, where between 1983 and 1990 there was a 250% increase in violations of child labour laws.

Poverty is the chief cause of child labour. When a family is poor, everyone

has to work, every extra contribution helps. But many children work because of lack of other opportunities: schools might be unavailable, inadequate or just too expensive.

Others are forced to work. Pakistan, according to some reports, has millions of bonded child labourers, working long hours each day in all sorts of activities, from agriculture to carpet factories to brick kilns. And in Thailand, children are bought and sold to work in private houses, restaurants, factories and brothels.

While the long-term objective must be to eliminate child labour, much needs to be done for children who currently have to work—providing them with support through health services, feeding programmes or informal education schemes that they can fit in around their work. And children should be removed immediately from the most hazardous environments.

Improving educational opportunities is one of the most important steps—to make schooling a real and practical alternative for today's working children. But in the ultimate analysis, child labour will be eliminated only through alleviation of poverty—the real cause of child labour.



*Stakeholders—  
consumers,  
workers, nature—  
should be given at  
least as much  
consideration as  
shareholders*

an impersonal market would still ignore the potential participation of particular groups—women and ethnic minorities. They may require strong affirmative action (see box 3.5 on page 45).

- *Protection of the environment*—Many companies find that they can maximize short-term profits at the expense of the environment, through pollution and other forms of environmental degradation. The pricing of environmental resources—or more effective regulation—can ensure that everyone works under the same rules, and that today's production does not pass on some of its costs to society in general or deplete resources that need to be conserved for future generations. Making the polluter pay—or banning certain types of pollution—are among the most effective ways of ensuring sustainable development. Domestically, this requires antipollution legislation, as well as taxes on the consumption of non-renewable energy. Internationally, this would require tradable permits for carbon emissions and other forms of international taxation on polluting nations. If resources were properly priced and polluters were paying for environmental costs, the incentive structure would tend to stimulate development of technologies required to ensure more sustainable development. In short: stakeholders—consumers, workers, nature—should be given at least as much consideration as shareholders.

#### *4. Social safety nets*

Every country needs to establish effective social safety nets to catch the victims of the competitive struggle—such as the temporarily unemployed—and to protect the lowest income groups, the young, the old and the disabled. In the United States and the United Kingdom, around 25% of GNP is committed to social safety nets in the forms of health care, unemployment and social security benefits. In the Scandinavian countries, the figure is roughly 40%.

But there is always a debate over just how substantial these safety nets should be. If they are too firm and reassuring, they may discourage people from working. If they are too open or flimsy, they may let the gen-

uinely deprived fall through. The latter has more often been the problem than the former in developing countries. Where the need is greatest, the safety nets are often weakest—amounting generally to no more than 5% of GNP. Millions of people live in absolute poverty and lack the most basic social services. Most countries have some form of health care, though the delivery is very uneven—and often inadequate in rural areas. But few developing countries offer widespread social security in the form of pensions, and almost none pay unemployment benefits.

Governments in developing countries do offer some relief to the poor, for example, through the distribution of food supplements for children, and they may organize labour-intensive public works programmes to provide income—especially in times of disaster. But in practice, most people in developing countries have to rely on support from their families or communities in times of difficulty.

It should be clearly understood that the purpose of people-friendly markets is not to invite governments to introduce more discretionary controls, which rarely work. The basic idea is to protect the interests of everyone who seeks to enter the market. Correct price signals and an efficient incentive system are usually much more effective than direct controls in achieving this.

#### **Encouraging participation through employment**

For most people, the best form of market participation is through productive and remunerative work and through self-employment and wage employment. This empowers them not just economically but also socially and politically.

Employment empowers people economically by giving them purchasing power for goods and services. It empowers them socially by offering a productive role that enhances their dignity and self-esteem. And it can empower them politically if they begin to influence decision-making in the workplace and beyond.

The measures that lead to people-friendly markets can make a major contri-

bution to employment creation. Land reform, for example, allows larger numbers of farmers to develop the land and results in more labour-intensive cultivation. And opening markets and credit to women and other so far excluded groups can help create many more small enterprises—and many more jobs, since smaller companies tend to be more labour-intensive. In Japan, small and medium-size businesses create 57% of value added to products but employ about 74% of the total industrial workforce.

### *Growth without employment*

The need for a fresh approach is evident from the high unemployment throughout the world. In OECD countries, unemployment stayed above 6% throughout the 1980s, reaching a peak of 6.9% in 1991, which means more than 30 million jobless. Unemployment in the European members of OECD increased threefold from 3% in the mid-1970s to about 10% in 1992.

The situation in the developing countries is much worse. In Sub-Saharan Africa, not a single country had single-digit unemployment figures throughout this period. In Latin America, urban unemployment has been above 8%. And in Asia, countries like India and Pakistan, despite respectable GDP growth rates (more than 6% a year), had unemployment rates above 15%. Only the East Asian countries had low unemployment rates—below 3%.

A comparison of the growth in GDP and employment in various regions of the

world during 1960–73 and 1973–87 shows that employment has consistently lagged behind economic growth (table 3.1). This is true in both industrial and developing countries. The industrial countries had fairly respectable GDP growth rates, but between 1973 and 1987, employment in countries like France, Germany and the United Kingdom actually fell (figure 3.1). The reason: three-quarters of the rise in output in these countries came from increases in total productivity, with the rest from increased capital investment—without creating new jobs.

The developing countries have had a similar problem, though they have experienced at least some employment growth. In 1960–73, GDP growth rates were fairly high (4–5% a year) but employment growth rates were less than half this. Less than a third of the increase in output in developing countries between 1960 and 1987 came from increased labour, more than two-thirds from increases in capital investment.

The pattern is similar for transnational corporations with subsidiaries in developing countries: they have made substantial investments without creating large numbers of jobs. In 1990, there were at least 35,000 transnational corporations with more than 150,000 foreign affiliates. Of the 22 million people they employ outside their home country, around seven million are directly employed in developing countries—less than 1% of their economically active population. In addition, probably an equal number are employed indirectly as

FIGURE 3.1  
GDP and employment growth in industrial countries, 1960–87  
(1960=100)

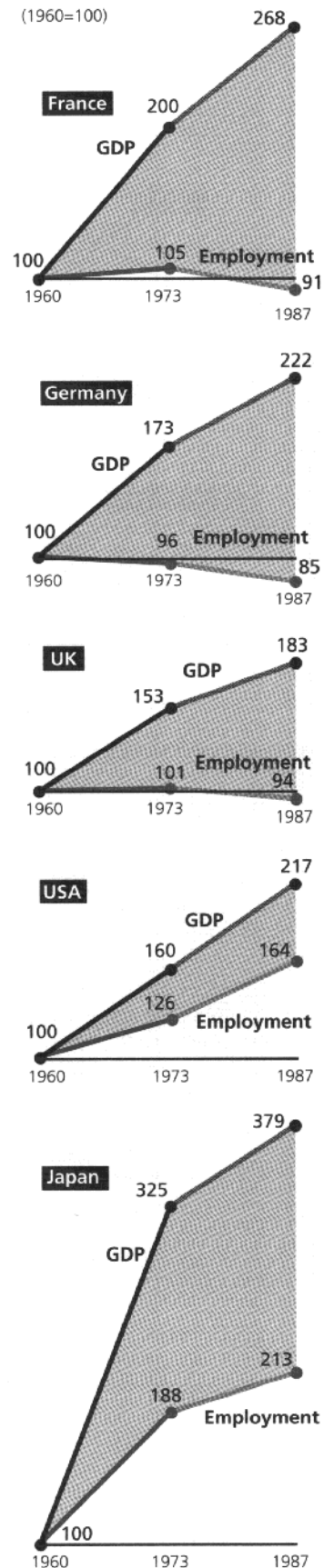


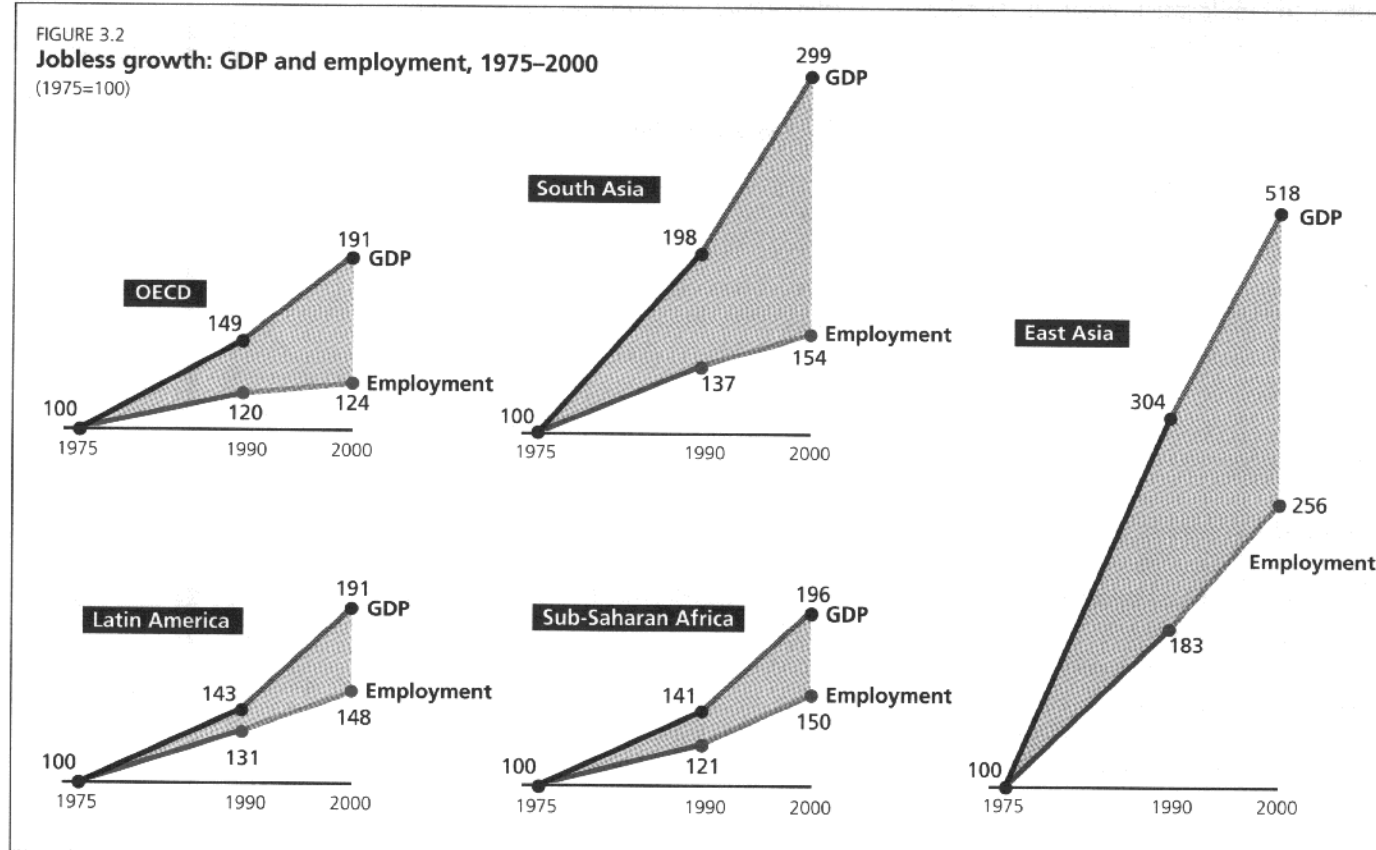
TABLE 3.1  
Growth in GDP and employment, 1960–87  
(percent)

Region or country	Average annual growth rate of GDP		Average annual growth rate of employment	
	1960–73	1973–87	1960–73	1973–87
<i>Selected developing regions</i>				
Africa	4.0	2.6	2.1	2.3
South Asia	3.8	5.0	1.8	2.3
Latin America	5.1	2.3	2.5	2.8
<i>Selected industrial countries</i>				
France	5.5	2.1	0.4	–1.0
Germany	4.3	1.8	–0.3	–0.9
Japan	9.5	4.6	1.2	0.9
United Kingdom	3.3	1.3	0.1	–0.5
USA	3.7	2.2	1.8	1.9

FIGURE 3.2

**Jobless growth: GDP and employment, 1975–2000**

(1975=100)



## BOX 3.3

**Jobless growth**

Many parts of the world are witnessing a new phenomenon—*jobless growth*. Even when output increases, increase in employment lags way behind.

- Developing countries experienced 4–5% growth in GDP during 1960–73, but employment grew only half as much.
- Industrial countries managed fairly respectable output growth during 1973–87, but in France, Germany and the United Kingdom, employment levels actually fell.
- Informal employment has increased sharply in developing countries, offering low-wage, non-permanent jobs, instead of remunerative employment.
- In the United States, the recent economic recovery has been a “jobless recovery”.

Policy-makers all over the world are searching for strategies that combine a high GDP growth rate with more job opportunities. No comprehensive programme has emerged, but there are several measures that can contribute to an increase in employment:

- Invest generously in basic education, relevant skills and worker retraining.

- Liberate private enterprise and make markets more accessible to everyone.
- Support small-scale enterprises and informal sector employment, principally through reform of the credit system, fiscal incentives and proper legal framework.
- Create an efficient service economy for the future by investing in the new skills required and removing international barriers.
- Encourage labour-intensive technologies, especially through tax breaks.
- Extend employment safety nets through labour-intensive public works programmes in periods of major economic distress.

These measures could greatly help in both developing and industrial countries, but nagging questions remain: if new technologies continue to increase human productivity at a sharply accelerating rate, do people need to work such long hours? Is it not time to redefine the concept of employment? Can there be work sharing? Should we not redefine work to include what are unpaid tasks today, such as housework, community work or even political work?

suppliers, for example, or through service companies. This total number is still relatively small, however, and the proportion of the world’s economically active population employed by transnationals appears to be falling.

Thus, in many parts of the world, we are beginning to witness a new phenomenon—*jobless growth* (figure 3.2 and box 3.3). In the United States, if job growth during the current recovery of the business cycle had matched the rate of eight previous recoveries, an additional 3.9 million jobs would have been created. In industrial countries, a major part of the output growth came from total productivity increases—primarily an outcome of labour-saving technological advancement.

There are four major causes of this phenomenon. First, the search for labour-saving technology was encouraged by the demographic situation of industrial countries, where stagnating population growth often led to growing labour shortages in the 1960s. Second, it was also enhanced by rising labour costs as well as an active trade union movement. Third, technological in-

novation in the civilian sphere often resulted as a by-product of military research and development, which usually has a preference for capital intensity. Finally, the prevalent technology reflects the existing pattern of income distribution—20% of the world's population has 83% of the world's income and, hence, five times the purchasing power of the poorer 80% of humankind. Clearly, technology will cater to the preferences of the richer members of the international society.

In developing countries, the total labour force increased by more than 400 million during 1960–90. This was due to rapid population growth (2.3% a year), an increase in the proportion of people of working age, and greater numbers of women joining the ranks of job-seekers.

Without substantial policy changes, the employment outlook for these people is bleak. The labour force in developing countries will continue to increase by 2.3% a year in the 1990s, requiring an additional 260 million jobs. Women's participation in the labour force is likely to increase. And there will be a steady migration of people to urban areas in search of work: the annual rate of net migration is likely to be about 4.6% by the year 2000.

Taking into account the number of people unemployed or underemployed, the total requirement for the next decade is around one billion new jobs. This would imply increasing total employment in developing countries by more than 4% a year in the 1990s, compared with less than 3% in the 1980s.

If present trends continue, it is extremely doubtful that countries will achieve such an increase in employment. The ILO estimates that the labour force for Sub-Saharan Africa will grow 3.3% a year in the 1990s, while productive employment will increase by only 2.4% a year. Even this employment growth assumes an acceleration of GDP growth from 3.7% to around 5%. The situation is unlikely to be any better in Latin America or South Asia (figure 3.3). And the capacity in industrial countries to absorb more economic migrants from developing countries may also be limited, given their own high unemployment.

### *Deteriorating job security*

The problem of labour today is not only the discrepancy between demand and supply in quantitative terms. The problem is that there is also a change in the quality of the work available: job security is deteriorating.

In both industrial and developing countries, the composition of the labour force has been changing significantly. Enterprises have been reducing their reliance on a permanent labour force, engaging instead a highly skilled core group of workers surrounded by a periphery of temporary workers.

Some of these peripheral workers will be engaged under short-term contracts or as part-time, temporary or casual workers. In the United Kingdom by the early 1990s, almost 40% of jobs did not involve regular full-time wages or employment. Others among these workers may be self-employed individuals working from home. But a large number will be engaged through subcontractors. Medium-size and large firms in South and South-East Asia—particularly in garments, footwear and woodworking—are subcontracting a growing proportion of their production to smaller firms.

This problem exists in industrial countries but it is even more pronounced in the developing countries. Here, many subcontractors are small entrepreneurs—either microenterprises or enterprises in the informal sector.

### *The East Asian path*

Maintaining competitive production and ensuring substantial increases in employment will be no easy task. But the experience of Japan and the East Asian industrializing countries indicates one potentially successful path.

One of the essential starting points was land reform. In the Republic of Korea between 1952 and 1954, the proportion of cultivators who were owners rather than tenants increased from about 50% to 94%. As a result, between 1954 and 1968, the labour used per hectare increased by 4.7% a year.

FIGURE 3.3  
Labour force and employment  
projection, 1990–2000  
(1990=100)





Land reform also had a very positive impact on employment in Taiwan (province of China). After the reform, the number of people involved in agriculture increased rapidly—from 400,000 to about two million between 1952 and 1968. There was a substantial increase in output, too, particularly from adding new crops. Using multiple-cropping techniques, accompanied by irrigation facilities and improved water management, the farmers were also able to grow fruits, pulses and vegetables. These opened up more job opportunities after harvesting since they required more processing—whether drying, pickling, canning, freezing or dehydrating. In Taiwan (province of China) in the 1960s, the number of workers in food processing rose

from 11,000 to 144,000. Such increases in employment led to enhanced income and purchasing power for the people. As a result, the domestic markets for goods and services also expanded, which in turn had positive effects on technology choices and on further increases in employment.

In addition to redistributing assets, these countries simultaneously invested in the health, education and skills of their people—so the workforce was ready and able to take advantage of the latest technologies and methods of production as they were introduced. These societies also established a comprehensive framework for the rapid growth of private enterprise and combined outward orientation of their economies and exposure to foreign competition with support for national economic capacity building.

Labour productivity in these countries has been increasing at an annual rate of 10% or more—half of which has been attributed to investment in education and technical skills. And during the 1980s, while unemployment was in double figures for most developing countries, and more than 6% in the OECD nations, it consistently stayed below 3% in Japan and East Asia.

In this connection, it may also be useful to look specifically at the Japanese experience. The Japanese entrepreneurial system has been based on three pillars, often referred to as the three sacred treasures—lifetime employment, seniority wage system and enterprise unions. It is primarily a community of people, rather than a piece of property belonging to the shareholders. It is made up of the people who work in it, not only for it. But according to recent reports, the system of lifetime employment is now coming under pressure and being abandoned, even for white-collar workers.

A participatory process in the workplace can also lead to significant productivity benefits. One investigation of a problem plant of the ASEA Brown Boveri Group in Sweden, for example, found women workers doing monotonous production-line work. Personnel turnover was about 40% annually, and productivity was low. The company decided to make a complete change in the production system—allowing

#### BOX 3.4

##### Education for life—addressing educated unemployment

Education and training are often put forward as the keys to employment, but in developing countries many remain unemployed despite, or because of, their high level of education. In Asian countries, the least educated often have the lowest recorded unemployment rates, because they are usually involved in informal subsistence activities. In India, while the unemployment rate in 1989 for people with no education was 2%, that for those with secondary education was 9% and for university graduates 12% (box table). In Bangladesh, about 40% of people with a master's degree are either unemployed or underemployed. In Thailand during 1973–83, unemployment rates among university graduates ranged from 20% to 35%.

In Africa, too, secondary school graduates are more likely to be unemployed

than those with less education. Graduate unemployment, not yet as high as in some Asian countries, is expected to rise in the years ahead with cuts in recruitment to government service, where many graduates would previously have expected automatic employment.

The fundamental problem is the mismatch between supply and demand. This can be tackled in the short term by offering the unemployed more vocationally oriented training—and perhaps by offering the private sector greater incentives to employ them. But in the longer term, the educational and training systems of societies must be such that people can acquire relevant skills—skills that help them master their lives. This change has to come at all levels of learning—from literacy courses to university training.

#### BOX TABLE

##### Unemployment in selected countries by educational level (percent)

Country	Year	No education	Primary	Secondary	Tertiary
Algeria	1989	9.2	24.2	28.9	5.8
Tunisia	1989	11.2	20.4	17.4	5.2
Ghana	1988	3.4	7.6	13.5	14.7
Kenya	1986	13.5	15.6	22.2	5.4
Zimbabwe	1987	1.6	6.8	11.6	..
Malaysia	1985	4.7	22.9	30.6	3.9
India	1989	2.0	3.0	9.0	12.0
Indonesia	1985	0.6	1.5	7.5	5.3
Sri Lanka	1981	4.5	14.5	15.1	4.2
Côte d'Ivoire	1985	1.0	5.2	21.7	13.7

workers to move among different tasks and take charge of many aspects of production, including material planning and quality control. This made a dramatic difference. Labour turnover was reduced virtually to zero, and while previously only about 10% of production was being delivered on time, afterwards the level rose to 98%.

Most developing countries, and many industrial countries, have been slow to pick up on this lesson. Many of their workers have skills that are out of date or inappropriate for the fast-changing environment of the 1990s. And in some cases, a striking mismatch between supply and demand leads to high unemployment even among the more educated (box 3.4).

It would be naive to assume that the experience of one group of countries can be easily replicated elsewhere. But if one message does emerge, it is that the solution is to focus not merely on capital or on production processes—but on people. Too often, human beings have had to fit into roles preordained by economic theorists, state planners and the developers of technology. A much more refreshing approach is to start with human beings, invest liberally in their education and technical skills, and see how their energy and creativity can best be released.

Working people need to be seen as creators of development rather than as one of its residuals. Employment should be seen as a deliberate process of empowerment, rather than as a mere by-product of production.

#### *Promoting entrepreneurship and small enterprises*

One of the surest ways of encouraging employment is to promote small businesses. The increasingly important role of small enterprises is evident from the extent of self-employment in industrial and developing countries (table 3.2). In the United States, for example, half of all private sector employees work for companies with fewer than 100 employees.

Developing countries also have increasing numbers of small enterprises. In Singapore in 1983, small and medium-size enterprises made up over 90% of all enter-

prises. In Kenya during the 1980s, more than 1,500 new private limited liability companies were registered each year.

Many productive enterprises are started on the initiative of one individual. A study in Malaysia found that 86% of a sample of firms were started by their owners, who were relatively young and well-educated—and often had experience in working in the same field with another company.

And an increasing proportion of new enterprises today are being started by women. In the United States, 22% of small businesses in 1982 were owned by women, while by 1987 the figure had risen to 30%. There seems to be a similar trend in developing countries. In Latin America as a whole, one-third of microentrepreneurs and their workers are women, and in some cases, as in rural Honduras, women entrepreneurs are now in the majority.

Of all the steps that governments can take to encourage entrepreneurs, probably

*It would be naive to assume that the East Asian development experience can be easily replicated elsewhere*

TABLE 3.2  
Share of self-employment  
in selected countries

Developing countries	Year	Self-employment in total labour force (%)
Ghana	1984	68
Pakistan	1984	56
Ecuador	1981	56
Nigeria	1983	56
Mexico	1981	48
Indonesia	1986	44
Bangladesh	1987	41
Philippines	1987	36
India	1981	31
Korea, Rep. of	1987	30
Thailand	1982	29
Colombia	1987	28
Malaysia	1981	28
Brazil	1981	27
Industrial countries	Year	Self-employment in non-agricultural sector (%)
Italy	1987	22
Spain	1987	20
United Kingdom	1987	14
Australia	1987	13
Ireland	1987	12
France	1987	11
Netherlands	1987	8
Germany	1987	8
USA	1987	8
Canada	1987	7

*Three groups find it difficult to get credit: small farmers, entrepreneurs in the informal sector in general and women in particular*

none is more important than ensuring ready access to capital. The capital market is generally very unfriendly to the small entrepreneur—particularly the poorest ones. Banks are generally unwilling to lend to poorer people, partly because they cannot offer acceptable collateral and partly because the sums they require are often too small to be profitable. So, banks often ignore the needs of small-scale operators in agriculture, industry and services—or between 30% and 70% of the labour force in developing countries. In the Philippines in 1991, small enterprises received only 8% of institutional credit.

Lack of credit can be a significant brake on progress. In Ghana, small enterprises report that up to 50% of their capacity is idle because of a shortage of working capital. A 1989 survey found that almost 90% of the enterprises perceived the lack of credit as a serious constraint to new investments. And if they get credit, smaller firms tend to pay interest rates around one-third higher than larger firms. A similar situation was found in Tunisia.

Three important groups find it difficult to get access to credit: small farmers, entrepreneurs in the informal sector in general and women in particular. In Bangladesh, large owners of land, who constitute 7% of rural households, received 37% of institutional credit in 1989. In Kenya, less than 5% of the institutional credit goes to informal activities.

Women, in both the formal and the informal sectors, also have great trouble getting bank loans. Women account for about 18% of the self-employed in developing countries. But in the Philippines, only 10% of formal credit goes to women, and in Pakistan, the Agricultural Development Bank makes less than 0.1% of its loans to women.

Without access to formal credit, many poor people are forced to turn to moneylenders who charge usurious rates (in Bangladesh, 70% of total rural credit comes from moneylenders). One common mechanism in many countries is a "five-six" arrangement, in which a borrower receives five pesos in the morning and repays six pesos in the evening—20% interest a day.

In Sierra Leone, the trade and tariff regime is such that smaller firms pay 25% more than larger firms for capital goods. In Pakistan, they pay 38% more. And in the Philippines, sectors dominated by large-scale enterprise enjoy effective rates of tariff protection of 25–500%, while sectors providing two-thirds of small-scale employment have negative rates of effective protection. Similarly, the protective tariffs in Malaysia tend to be higher the larger the plant size.

Clearly, smaller enterprises should not face this discrimination. Indeed, it can be argued that governments should give preference to smaller enterprises.

In addition to giving greater assistance to smaller enterprises through fairer macro-economic policies, such as protective tariffs and interest rates, governments can take specific measures to promote the development of small enterprises.

Experience shows that the best way to support small-scale enterprise is to combine improved availability of credit with measures aimed at enhancing competitiveness.

In western Guatemala, the weavers of Momostenango use almost 40% of the country's wool to weave ponchos, blankets and other products. But the quality of the wool had been low, and the weavers lacked credit to expand production. In 1986, a foundation with technical and financial support from the government and international donors was set up to help the farmers, the weavers and those marketing the finished products. A year later, 14 technical assistance centres were organized to help increase wool quantity and quality. Funds of up to \$20,000 were available to offer credit to weavers to increase production. As a result of these and other measures, export volumes have increased substantially—11 weaver groups with 160 members have been formed to fill export orders.

In rural Cameroon, the extension of credit has been used with new basic technologies to offer new opportunities for women. The staple crop there is maize, chiefly grown by women but mostly ground by mechanical plate mills in towns and cities. The farmers could not afford either

to buy the imported mills or to maintain them subsequently. But in the mid-1980s, some organizations came together to develop a cheaper locally made plate mill, and to help form rural groups that could buy and run them. By mid-1989, 28 such groups had received credit and gone into production. Each mill is owned on average by 50 women, serving 250 families and earning for the group the equivalent of \$70 a month.

People-friendly capital markets would address the needs of those groups, who find it difficult to get credit. First, on preconditions, a better distribution of assets (such as land) would increase their chances of offering collateral. Second, the corrective actions would give special access to weaker groups—either through government action or through informal credit schemes, such as cooperatives, savings groups and credit unions. These have played an important role in many industrial countries, and in the developing world as well: in Togo, loans from credit unions grew by 33% in the past decade.

One of the most important forms of assistance to small enterprises is training—not just vocational training but an introduction to management skills. One interesting example of a more comprehensive approach is the Malawian Enterprise Development Institute, targeted mainly at educated unemployed youths. In addition to vocational training, the programme offers training in business management and entrepreneurship. At the end of the course, the graduates are rewarded with a tool set and loans, but they are not given a trade certificate, which might encourage them to go simply into wage employment.

There is also a need for a working system of enterprises with medium-size and large firms feeding off the smaller ones. In Europe, large enterprises such as General Electric, Olivetti and Philips have all developed broad-based technological cooperation networks for manufacturing new technologies available to smaller companies.

People-friendly markets should encourage and nurture small enterprises, for the profit not only of the individual entrepre-

neurs, but for society as a whole, through steady increases in output and employment.

### *Informal sector support*

In the developing countries, the informal sector is growing almost everywhere. And small-scale enterprises are often part of this sector. In Latin America, 25% of all non-agricultural employment was in the informal sector at the beginning of the 1980s, 31% at the end.

In Sub-Saharan Africa, the informal sector increased by 6.7% a year between 1980 and 1989, substantially faster than the modern sector. Between 1980 and 1985, while the modern sector added only 500,000 jobs to the urban labour market, the informal sector created some six million new jobs. By 1990, the informal sector employed more than 60% of the urban workforce—more than twice the share employed by the modern sector.

In some Asian countries, including India, the Philippines and Sri Lanka, wage employment in the urban informal sector has been growing faster than in the formal sector. In India, twice as many jobs have been created in the unorganized manufacturing sector as in the organized.

Swollen by young people leaving school with nowhere else to go, the informal sector is also absorbing large numbers of workers who have lost their jobs in government or in the formal private sector. Some of those made redundant may have small sums they can invest in a new business, but most seek work from other people (the majority of people in the informal sector are wage-earners). Their reduced family income may mean that other members of the family have to work: when males lose jobs in the formal sector, it is often easier for women to replace some of the income with informal work. In Kenya, women's participation in the urban labour force rose from 39% in 1978 to 56% in 1986.

Support for small-scale enterprises should, therefore, not only focus on the formal sector. It must also extend to the informal sector without discouraging the courage and vibrancy of its enterprises. The objective must be to promote the transition from informal to formal.

*In Sub-Saharan Africa, the informal sector employs 60% of the urban workforce*

The technological breakthroughs of the past two decades—particularly in informatics—have transformed traditional services. Human skills are now the most important input in modern banking, finance, advertising and communications, as well as business management and public administration.

The notion that manufacturing is the foundation for all other economic activity is an old illusion. The distinction between industry and services is now largely meaningless. In industrial countries today, over half the workers in a typical manufacturing firm do service jobs—design, distribution, financial planning; only a minority make things on the factory floor. Second, the productivity in services, which is difficult to measure, does not lag behind that in manufacturing. There are many signs that a productivity revolution is sweeping services. Third, services are also the fastest-growing part of international trade, accounting for 20% of total world trade. Services account for 40% of the stock of foreign direct investment by the five big industrial economies.

Generating about 60% of the GDP and two-thirds of the employment opportunities in the industrial countries, services dominate the world economy (figure 3.4). Manufacturing's share will continue to dwindle as more low-technology factories move to countries where labour-intensive assembly or other operations can be performed more cheaply. The United States has by far the biggest service sector, accounting for about 70% of its GDP and nearly 80% of its labour force. But the developing countries still lag behind with only 47% of their GDP and 25% of their labour force coming from services. So, there is increasing scope for these countries to generate employment in their service sectors.

Between 1980 and 1990, the trade in services increased by an average of 7.7% annually, reaching some \$990 billion in 1990. By 2000, the trade in services could approach \$2 trillion.

Most developing countries are still net

importers of services. Their net deficit in services increased from \$4 billion in 1970 to more than \$17 billion in 1990.

This new global services economy shifts comparative advantage more in favour of people than natural resources. Developing countries have a majority of the world's people, but still only a small share of the global trade in services. The rapid expansion of trade in skill-intensive services thus offers a tremendous opportunity to developing countries—if they can impart new knowledge and skills to their people.

#### *Employment safety nets*

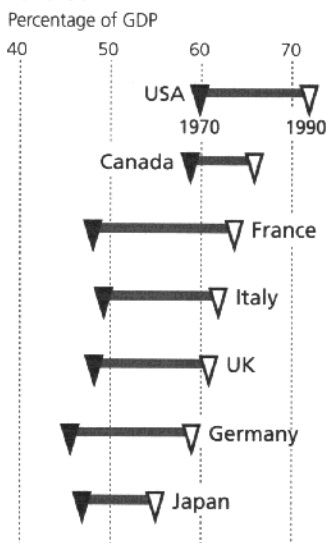
Even with all the positive measures just proposed, the employment situation might be so serious, and the role of employment in a human development strategy so important, that a structural reform in the form of a guaranteed employment scheme should be considered. The point of departure of such a scheme is the recognition of the right of everyone to work.

Thus, for those who cannot find work, some developing countries have designed employment guarantee schemes, generally offering work, however poorly paid, through public works programmes. These schemes serve a function similar to unemployment benefits in industrial countries but are much less expensive, since they are narrowly focused on those prepared to do hard manual work for very low pay or for small amounts of food. In Bangladesh during the 1980s, 90% of the participants in the Food for Work programme were below the poverty line. In Botswana and Cape Verde, public works programmes in the 1980s are estimated to have saved the lives of 60,000 to 90,000 people in each country. In Chile and Peru, such programmes helped soften the impact of recession during the 1980s, and in Egypt, the Productive Families Programme is benefiting one million people.

Public works programmes also have the advantage that they build assets, such as roads or irrigation schemes.

One of the largest public works programmes in the developing world is the Employment Guarantee Scheme of Maha-

FIGURE 3.4  
**Services' growing share in GDP, 1970-90**





rashtra, in India. This was started in 1972 to provide employment on request at a stipulated wage, within 15 days, no more than five kilometres away from the participant's village home. During 1990–91, the scheme provided more than 90 million person-days of work, with nearly two-thirds of the workers from households below the poverty line. As well as providing work, the scheme has helped mobilize the rural poor as a political force and acted as a check on the power of local officials. The programme pays the official minimum wage, which is somewhat higher than the market wage (around \$1 a day), and in 1991 cost Rs 2.4 billion (\$103 million). It is one of the most cost-effective schemes anywhere for helping the poor.

The Maharashtra programme and other such schemes show that programmes need to be very carefully designed to ensure that they contribute useful assets and that they do not distort the local labour market. Above all, such schemes should enhance production, not just welfare.

In the future, it would also be desirable to consider whether employment guarantee schemes could not be expanded beyond their traditional, primarily public-works-oriented fields. Certainly, they could cover many environmental tasks that need to be done. They could also focus more on provision of social services, which would be critical to improved human development. They could include proposals for national service in exchange for a guaranteed education, as currently proposed by the new US administration. Too many societal activities remain undone while too many people remain unemployed. It does not take real genius to match unmet human needs with unemployed human resources.

### Trade unions

When trade unions are closely in tune with their members and also with national needs, they can make the whole industrial process work more smoothly. Like many other institutions of a democratic society, trade unions help fuse the interests of different people so they form a coherent group. This can avoid disruptions and help increase productivity.

Germany has had powerful labour unions and its tripartite system of consultation and decision-making—involving employers, workers' representatives and government—has given the country almost the highest wages and the shortest working time of the OECD countries. Similarly, the Scandinavian countries have combined high standards of living with the highest “density levels” in the OECD (the density level is trade union members as a proportion of the total workforce). The five countries with the highest density levels are Sweden (85%), Iceland (78%), Denmark (73%), Finland (71%) and Norway (55%).

Trade union membership has been falling in most industrial countries in recent years. In the Netherlands, membership in unions fell from 39% in 1978 to 24% in 1991. And the United States has seen a three-decade slide in union membership from 30% to about 15%.

Trade unions in industrial countries have been undermined from different directions. Unemployment has reduced the number of workers and strengthened the hand of employers. And unions have also faced much tougher legislation from governments. Furthermore, enterprises and capital have moved from countries with powerful trade unions to low-wage, non-unionized countries. But a more fundamental problem is the fragmenting of the labour force, which is now much more resistant to mass organization. The shift to services and the growing numbers of part-time workers, or those adopting flexible working patterns, puts them beyond the reach of traditional methods of organization.

In the developing countries, a smaller proportion of the workforce tends to be unionized because there are fewer workers in the formal sector. In Latin America, around 20% of the workforce is unionized (rates are higher for Argentina, Brazil, Mexico and Venezuela). Singapore and Sri Lanka have some of the highest rates in Asia—up to 40%—while Malaysia and the Philippines have membership levels between 20% and 40%. In Africa, where only around 10% of the workforce is in the formal sector, union members are probably

*Too many societal activities remain undone while too many people remain unemployed*



*Trade unions must  
reinvent themselves  
to represent a  
new generation  
of workers*

only 1% or 2% of the total workforce. But unions are weakest of all in many Arab states. In most of these countries, governments restrict their activities—and in Bahrain, Oman, Qatar, Saudi Arabia and the United Arab Emirates, trade unions are banned.

Democratization may now offer the trade unions more freedom, but the accompanying process of economic liberalization is much more problematic. Trade unions often oppose privatizations since they frequently lead to job losses. Colombia, for example, was paralysed for a week in 1992 by a strike of telecommunications workers protesting privatization. Elsewhere, the process has been smoother: in Mexico, telecommunications workers were given credits of \$325 million to help them purchase shares in the privatized company.

But a more basic problem for unions all over the world is a shift in the nature of the workforce, away from ranks of production-line workers towards the more fragmented workers in the service industries—as well as those on the precarious periphery, as discussed earlier in this chapter. As the ILO's *World Labour Report* points out in its 1993 survey of trade unions: "Working life today is very different from that in the old smoke-stack industries where trade union solidarity was originally forged. Today's workers in manufacturing are more likely to be operating complex equipment, often using computers and robots and developing skills which blur the traditional dividing lines between blue-collar and white."

Workers doing different jobs feel much less solidarity. And as they move out of manufacturing, their aspirations change and they tend to be even more individually oriented. Employers are capitalizing on this by adopting strategies of "human resource management" that deal with workers as individuals or small groups. This may or may not allow for greater participation by individual workers, but it certainly weakens the unions.

Unions also suffer from their relative neglect of women workers. Trade unions in many countries are very much a male preserve. In many sectors, women are now

more than half the workforce, yet in the largest international trade union organization, the International Confederation of Free Trade Unions, only 34% of members are women. In Latin America, only 3% of trade union officials are women. Many of the newer women entrants to the workforce are working part-time or in complex shift patterns, which makes them especially difficult to organize (box 3.5).

If trade unions are to be in the forefront of participation in the workplace in the years ahead, they clearly have to reinvent themselves to represent a new generation of workers.

**Liberating private enterprise**

About 80 countries are in the process of economic liberalization and privatization. Many industrial market economies have also made some movement in this direction, involving privatization not just of industrial production but also of some public services. There have been similar changes in developing countries, where programmes of economic adjustment have involved the state's withdrawing from some productive activities, as well as liberalizing the economy and opening to international trade.

Facing the most radical shifts are the countries of Eastern and Central Europe and the former Soviet Union as they move from command economies to more open markets. The country studies at the end of this chapter illustrate the diversity in the nature and pace of reforms, with details of the recent experiences of Argentina, Brazil, China, Ghana, Egypt, India, Kenya, Malaysia, Poland, Russia and Viet Nam.

*Developing countries*

Most developing countries moved towards more market-oriented policies in the 1980s and early 1990s—bringing domestic prices more into line with international market prices and offering greater encouragement to the private sector. A study of 47 developing countries by the International Finance Corporation shows that since the mid-1980s, private investment has been playing an increasingly important role. It

compensated for the slight decrease in public investment, increasing as a proportion of GDP from about 12% in 1985 to 15% in 1990 and 16% in 1991.

The trend is not universal, however. Even in some countries with liberalization measures, private sector investment actually declined as a proportion of GDP during the 1980s—as in Argentina, Bolivia, Colombia, Kenya, Peru and Trinidad and Tobago.

The changes have been greatest in developing countries, such as China and Viet Nam, that started from centrally planned economies. There, the basic reform was the legalization of private ownership and entrepreneurship, and—particularly significant for China—the breakup of agricultural communes. The new private sector has responded quickly and vigorously and helped increase output dramatically. Although the transition process has not been without social costs, millions in China have benefited from the new economic opportunities, and poverty reduction has progressed at an unprecedented pace. In Viet Nam, too, a large proportion of the population has already benefited from the reforms.

For other developing countries that already had a larger private sector, the shift has been less drastic. For them, the transition is usually referred to as “adjustment”. The changes have usually included liberalizing trade and finance, reforming taxation systems, deregulating the labour market and reforming or privatizing public enterprises. These reforms have usually been preceded or accompanied by economic stabilization measures, such as sharp cuts in public spending.

In many countries, these reforms have yet to bear fruit in terms of human development. True, it is difficult to say whether their performance would have been worse without the reforms, but the fact is that three-quarters of adjusting countries in Sub-Saharan Africa have suffered declining per capita incomes, and in Latin America the declines were at least as bad.

It will be some years before any real balance sheet can be drawn up for the human development effects of liberalization and adjustment in developing countries. In

## Affirmative action for women

BOX 3.5

By 1990, women's share of the total economically active population in the industrial countries increased dramatically to 42%. In East Asia, it had risen to 43%, in Latin America and the Caribbean to 32%, and in North Africa and the Arab States to 13%.

But women are generally employed in a restricted range of jobs—in low-paid, low-productivity work, where they are subject to discrimination and sometimes to sexual harassment. Added to this are the long hours of household work that frequently go unrecognized. According to a 1990 UN survey, if unpaid house and family care work were counted as productive output in national income accounts, global output would increase by 20–30%.

In developing countries, one of women's greatest contributions outside the home is to agriculture. In Africa, about 78% of economically active women work in agriculture (compared with 64% of men). And in Asia, 80% of post-harvest work is carried out by women.

Women also make up a significant proportion of the informal sector—often forced to combine work and child-care responsibilities. In Latin America, women make up 25–40% of informal sector employment.

Women in almost every country tend to be concentrated in lower-status jobs. In manufacturing, women often do much of the routine production-line work. In the export-processing zones of South-East Asia, in industries such as

electronics, food processing, textiles and footwear, women provide up to 80% of the workforce.

Low status is reflected in low productivity and low pay, with women's earnings frequently only 50–80% those of men (box table). Women are also more likely to be unemployed. In Colombia, men's unemployment in larger cities was 8.1% in 1990, women's 13.2%.

Many forms of discrimination against women arise because of the family responsibilities they have to shoulder. So, it is important that enterprises offer adequate parental leave and access to child-care facilities. But there may also be a need for specific legislation to ensure that discrimination in the workplace is illegal and for policies of affirmative action to redress persistent biases against women.

Affirmative action programmes are more common in industrial countries. A Department of Labor study in the United States has shown that women's employment increased by 15% in companies subject to affirmative action goals, compared with only 2% in other establishments.

There have been few affirmative action measures for women in developing countries, but there are some. In Bangladesh, 10–15% of government jobs are reserved for women. As a result, women's share of all government jobs increased from less than 3% in the early 1970s to 8% in 1990.

BOX TABLE

### Disadvantageous position of women at work, 1990

Country	Unemployment rate (%)		Female earnings in non-agriculture (male pay=100)	Hours worked per week, including housework	
	Male	Female		Male	Female
<i>Industrial countries</i>					
Australia	9.8	9.1	88.0	48.3	46.9
Denmark	9.3	12.1	82.1	40.3	45.1
Germany	4.0	4.8	73.6	46.9	51.2
United Kingdom	11.8	5.1	67.4	47.2	51.9
Japan	2.0	2.2	50.7	50.6	45.4
<i>Developing countries</i>					
Kenya	15.6	18.6	80.5	40.1	47.2
Sri Lanka	10.8	24.3	78.5	52.4	56.7
Costa Rica	4.2	5.9	65.9	45.7	48.3
Korea, Rep. of	2.9	1.8	53.5	48.2	53.3

most countries, the reforms have yet to lead to improved economic performance. And social statistics usually lag far behind economic ones—particularly in the poorest countries.

#### *Formerly socialist countries*

The countries of Eastern and Central Europe and the former Soviet Union have been transformed in recent years—and not just in the economic, social and political spheres. They are also undergoing a democratic transition from autocratic rule to greater political freedom and participation, a sociocultural transition from a life without free movement and travel to one of open borders, and a psychological transition from a life of being provided for by the state to having individual and household living standards depend very much on private initiative and effort.

The economic reforms in these countries envisage a complete restructuring from a command economy to a market economy. This transition—much delayed—is likely to be traumatic. The economic mess has been accumulated over a long period: it cannot be sorted out very quickly or without pain. But the transition is necessary and inevitable. The only question is how skilfully it is carried out by various countries.

Many of the economic reforms are common throughout the region, but there are significant differences for individual countries. Some already had more of the elements of a market-based economy (such as private agriculture) or had started their reforms earlier than others—distinguishing such “early starters” as the Czech Republic, Hungary, Poland and the Slovak Republic from such “late starters” as Albania, Bulgaria, Romania and the newly independent states of the former Soviet Union. There have also been differences in the speed of reform—the “shock therapy” of Poland, compared with the more “institutional reformist” approach of Hungary.

All these countries started with distorted economic structures. Typically, they had a high proportion of the workforce working in large enterprises with obsolete technology. And many regions had a very narrow economic base, making them very vulnerable to the play of market forces. The service sectors were generally very small—and inadequate for the functioning of a modern economy. Agriculture was often very inefficient, particularly in the former Soviet Union.

**THE REFORM PROCESS.** Reforms throughout the region aim to change the balance between the private and public sectors—by allowing many new private enterprises to be created and by privatizing the state sector. Privatization will be an enormous undertaking. State-owned enterprises produced 60–90% of the GDP of these countries. Poland had more than 8,000 large industrial state enterprises, and the Soviet Union 47,000.

Private enterprise has, indeed, been growing on a significant scale in some of the early starting countries—generally through self-employment or the creation of small enterprises.

But the process of privatization has yet to get fully under way (box 3.6). One of the most important problems concerns the method of asset distribution. First, since few people owned much property, they now lack the money to purchase any new assets on offer. Second, there is the question of equity. Those who do have the money are often the “nomenklatura”, who legally or il-

#### **BOX 3.6**

#### **Unequal transitions—a tale of two cities**

The transition to market-based economies in Eastern Europe will be long and difficult—and involve much more than just a shift from public to private sector industries. Its impact will be very different from one region or city to another—and require different policies.

This is illustrated by the varied experiences of two Polish cities, Krakow and Lodz. In both cities during the central planning period, large state-owned enterprises provided up to 80% of all industrial employment.

Today, unemployment in Lodz is around 18%, while in Krakow it is less than half this. Lodz is a textile city, hard hit by the collapse in trade with the former Soviet Union and by cheap imports from Asia. Krakow, a centre of metallur-

gy and metalworking, has managed to find new markets in Germany for its relatively cheap components.

This has a knock-on effect in the private sector. In Lodz, the private sector is largely in the retail and wholesale trade, leaving the city trapped in a downward spiral of low-paying jobs. In Krakow, a significant proportion of the growing private sector is based on subcontracting industrial services—a virtuous circle in which the growth in one firm feeds into that of another.

These two cities are a stark demonstration that the transition will have a different impact in different places—increasing inequalities and requiring special measures for those regions and cities that seem destined to lose out.

legally accumulated wealth under the old system and stand to make considerable further gains.

This problem is being tackled in different ways. One is through the distribution of property rights to all citizens in the form of vouchers that can either be traded or exchanged for stakes in one or more companies (as in Russia and the Czech Republic). Another way is through buyouts by management and employees (the common method in Hungary).

In Russia, when managers or workers are interested in buying a state enterprise, they are given financial assistance. They are allowed to use the net profits of the enterprise to establish funds for buying it. And if their bid for the company succeeds (through auction or competitive tender), they are entitled to a 30% discount off the sale price, with payment deferred for one year. In April 1992, more than 40% of the shops sold at a pilot auction in Nizhny Novgorod were purchased by workers taking advantage of such concessions. In Lviv, Ukraine, in the first pilot auction of shops in February 1993, nine of the 17 properties on offer were sold to the workers.

**HUMAN COSTS OF REFORM.** The long-term objectives of privatization may be to increase economic growth and promote human development, but the immediate effects have been traumatic. During 1990–92, the economies of all countries in the region were plunged into ever-deepening crises. Between 1988 and the first half of 1992, industrial production fell more than 40%. And in 1992 alone, output in Eastern Europe fell an estimated 10%, with much of the fall in defence industries (consumption did not fall as much). Also figuring heavily in the decline was the collapse of trade between the formerly socialist economies, which were also hit by the recession in the other industrial countries.

The human impact has been dramatic. In every country for which data are available, the proportion of the population living in poverty has increased. In Bulgaria, the Czech Republic, Poland, Romania and the Slovak Republic, the number of households living below the poverty line has risen

sharply—and the available figures are probably considerable underestimates.

Millions of people all over the region have joined the “new working poor”, whether through cuts in real wages, losses of social benefits or shorter working hours. Managers in Bulgaria, Romania and Russia are obliging many workers to take long periods of unpaid leave.

Millions more are unemployed. Current figures for unemployment are alarming enough, but even these are likely to be considerable underestimates. In Poland in 1992, when the official rate was 12%, the Polish Minister of Labour and Social Policy gave statistics for induced early retirements, and those with jobs but no work, suggesting the real figure to be nearer 20%. Eastern and Central Europe is entering an era of mass unemployment, at rates well above 15%, that could last for years.

Affecting almost the entire populations of these countries, the current crises hit some groups particularly hard: women, youths, older workers and ethnic minorities.

Women used to be reasonably well-integrated into the workforce. They had very high participation rates, even if they did not get the jobs they deserved. Now, however, it seems that they are treated more as “secondary workers”, being displaced from enterprises more quickly than men, or seeing their wages and benefits fall more rapidly.

The youngest and oldest workers are also very vulnerable. Few companies are taking on new workers, so youth unemployment is becoming serious: in Poland in early 1992, one-third of all the unemployed were under 24. At the other end of the scale, the drive for efficiency is also eliminating the practice of keeping on workers beyond official retirement age to compensate them for miserable state pensions. In Czechoslovakia in the late 1980s, where the official retirement age for men was 60 years, more than 30% of men between 65 and 69 were still working.

Unemployment is also rising alarmingly among minority groups. In Slovakia in 1992, the official unemployment rate for gypsies was 30%—more than four times the rate for the rest of the population. And in Bulgaria, there are reports of unemploy-

*Eastern and Central Europe is entering an era of unemployment that could last for years*



ment of 50% for the Turkish minority and more than 80% for gypsies. These minorities tend either to be overrepresented in jobs that are eliminated, or to suffer direct discrimination in new recruitment.

In the face of rising unemployment and poverty, social security systems are finding it increasingly difficult to cope. State-owned enterprises used to distribute most social benefits, from child care to health care to pensions. But over the past three years, these widespread automatic benefits have been dramatically curtailed and are being replaced by "social safety nets" whose services are targeted much more narrowly—and thus risk missing millions of people in desperate need.

#### *Experiences with privatization*

Between 1980 and 1991, nearly 7,000 state enterprises were privatized, most in eastern states of Germany (4,500) and other countries with formerly centrally planned economies. Only around 1,400 were in de-

veloping countries, of which 59% were in Latin America, 27% in Africa, 9% in Asia and 4% in the Arab States (table 3.3). Because most privatizations in the developing world have been recent, they do not appear fully in the 1991 data.

Public enterprises are being privatized mainly because of the belief that, in manufacturing and other productive sectors, private enterprise can deliver better results. But the final nail in the coffin of most public enterprises has been their demonstrable inefficiency, and above all, their enormous financial losses, which have drained the public purse of funds that could have been put to better use elsewhere.

Not all public enterprises lose money, and not all are always more inefficient than private sector firms. A recent study in Kenya found a number of public enterprise manufacturing companies performing better on a number of indicators than private sector firms. And the state-owned steel industry in the Republic of Korea is among the most efficient in the world. But in some countries, a high proportion of state enterprises do make losses. In China in 1991, despite substantial reforms, about a third of state enterprises were still operating at a loss. In Tanzania during the 1980s, about half the state-owned enterprises persistently made losses.

Such losses—equal to more than 3% of GDP in Bangladesh and Mexico in the 1980s, 4% in Turkey, 5% in Sub-Saharan Africa and 9% in Argentina and Poland—had to be covered by government subsidies. In Sri Lanka, those subsidies have accounted for 20% of government expenditure and 60% of the budget deficit. In Cameroon, the losses of state enterprises often exceeded the government's total revenue from oil.

The social opportunity cost has been staggering. If governments did not have to finance such losses, total expenditure on health and education in Bangladesh and Poland could have been doubled, and in Argentina almost tripled (table 3.4). According to the finance minister of Mexico, a small fraction of the \$10 billion in losses of the state-owned steel complex could have brought drinking water, sewerage, hospitals

TABLE 3.3  
**Privatization of state-owned enterprises, 1980-91**

Region	Enterprises privatized	Share of total privatizations (%)
Eastern Europe	5,305	78
Of which, former GDR	4,500	66
OECD countries	170	2
Latin America and the Caribbean	804	12
Sub-Saharan Africa	373	5
Asia	122	2
Arab States	58	1

TABLE 3.4  
**Social opportunity cost of public enterprise losses, 1988-90**

Country or region	Estimated losses of public enterprises as % of GNP	Public education and health spending as % of GNP	Potential increase in education and health spending if public enterprise losses are eliminated (%)
Argentina	9	5.5	164
Poland	9	7.6	118
Bangladesh	3	3.1	97
Turkey	4	4.6	87
Egypt	3	11.0	27
Philippines	2	8.3	24
Sub-Saharan Africa	5	6.5	77



and education facilities to an entire region of his country.

Privatization is no panacea, however. Hastily conceived or executed, it might achieve very little. Privatization should thus be seen not as an end, but as a means to higher levels of human development.

The first task must be to ensure that companies are being privatized in an environment conducive to business. Newly privatized companies need to operate in an "enterprise culture" for there to be any real progress. Indeed, changing this culture—by providing adequate training for new entrepreneurs, for example, or ensuring a competitive environment—is probably more significant than changing ownership. And if the enterprise is still a monopoly after privatization, as is often the case with utilities, it must be subject to suitable controls—otherwise inefficiencies and monopoly power will merely be transferred to the private sector, with the costs being borne by consumers. Or monopolistic exploitation by efficient private owners replaces the inefficiencies of public ownership.

Clearly, the poorer countries, and those that have only recently adopted the principles of a mixed economy, will find it difficult to create such environments. They may also have limited capacity to manage the privatization process, and trouble finding suitable buyers for enterprises and ensuring that resources are distributed in an equitable way. Malawi and Papua New Guinea have struggled to achieve their privatization objectives because of the difficulty of mobilizing savings for equity investment.

The speed of privatization must also be a concern. Building a suitable framework of institutions and regulations takes time, so privatizations should not be rushed—even when there is pressure from financial institutions during structural adjustment programmes. And it may be better to gain experience by starting with smaller enterprises—as Chile, Jamaica, Mexico, Poland and Togo did—before moving on to larger ones.

Governments should also be realistic about the revenues that privatization can generate. In Malaysia, Papua New Guinea and Sri Lanka, privatizations in an average

year produced less than 1% of GDP. Indeed, the taxes paid by the newly privatized enterprises have often generated more revenue than the original sale of the assets.

One of the most important issues—and the one usually given least attention—is what the impact of privatization will be on people. It is usually taken for granted that privatization has to be accompanied by unemployment, but this need not be so. With a better sequence of policy measures, much unemployment could be avoided. Restructuring many of the enterprises before they are privatized and making prior efforts to develop alternative employment in the private sector would be much more rational. And if layoffs are inevitable, governments should carry them out before the privatization. This would help ensure that workers get suitable compensation, with possible retraining or access to credit if they want to start their own enterprises.

Bear in mind that privatization may not be the only—or even the best—way to reduce losses from public enterprises. In Trinidad and Tobago between 1982 and 1988, reforms in state-owned enterprises reduced cumulative transfers to the state-owned sector over the period by more than 10% of GDP, compared with cumulative privatization receipts of only 2.3%. Similarly, in Sri Lanka between 1982 and 1988, reforms of state-owned enterprises reduced transfers by more than 6% of GDP, compared with privatization receipts of 0.2%. There can be competition among public enterprises as well as between public and private ones which keeps the public enterprise on its toes.

#### *Seven sins of privatization*

Privatization, conceived as one element of a total package, can stimulate private enterprise. Unfortunately, the process in many countries has been very different from this—more a "garage sale" of public enterprises to favoured individuals and groups than an integral part of a coherent strategy to encourage private investment.

Privatization in developing countries has therefore had very mixed results. In

*If governments did not have to finance public enterprise losses, their social spending could increase manyfold*

some cases, as in Mexico, it has been part of a process of fundamentally altering the organization of production—with benefits for consumers and the economy as a whole. In too many cases, however, privatization has taken place for the wrong reasons, under the wrong conditions and in the wrong way. Many countries seem to have been committing one or more of the seven deadly sins of privatization (box 3.7):

1. *For the wrong reason*—Many privatization strategies have aimed at maximizing short-term revenue rather than building competitive markets for the long term. For example, the sale of a telecommunications company as a monopoly would probably get a better price from a buyer who thought the company's activities would not be closely regulated: short-term revenue for the government but long-term losses for consumers and the efficiency of the economy as a whole. As the World Bank cautioned in its latest review of privatization experience: maximizing short-term revenues should not be the primary consideration. So, it could be better to create a competitive environment than to maximize revenue from sales into protected markets.
2. *In the wrong environment*—Privatization makes sense only if enterprises are released in an environment that allows them to become competitive and efficient. Where the market functions poorly and enterprises are still vulnerable to arbitrary government

edicts, transferring ownership to the private sector is unlikely to achieve much. It may merely transfer the ownership of rents from the public to the private sector. Similarly, creating private monopolies without an effective system of monitoring and control opens up the danger of exploitation of consumers.

3. *With non-transparent procedures*—Privatization has sometimes been accompanied by allegations of corruption, and claims that the process has enriched a few privileged cronies of the government. The disposal of assets should be so open and public that such allegations cannot arise. It should start with a publicity campaign explaining the rationale for the privatization and the method of selling and then proceed through competitive bidding, preferably through the stock exchange. The entire process of transferring ownership should be kept open to outside scrutiny—and should clearly state the national objectives that privatization hopes to accomplish. There should also be a detailed report on the sale to document if, and how, the objectives have been achieved.

4. *Only to finance budget deficits*—Harassed finance ministers are often tempted to sell state assets to cover their current budget deficits. The sale of public assets should be seen instead as a way of reducing the national debt—since these debts were often incurred in the first place for the establishment of such enterprises. Selling assets to meet current liabilities is mortgaging the options of future generations.

5. *With a poor financial strategy*—The best way to dispose of assets is through the capital markets selling shares to the public, difficult in many developing countries where capital markets are underdeveloped. Rather than take into account that stock exchanges are narrow and monopolized by a privileged minority, the financial strategies of many governments often make matters worse. A surprising number of governments have actually tried to privatize while at the same time issuing high-yield, low-risk, tax-free government bonds. Many governments have further narrowed their options by restricting sales of shares to foreigners. The aim instead should be a widespread distrib-

#### BOX 3.7

#### Privatization's seven sins

- Don't only maximize revenue—create a competitive environment
- Don't replace public monopolies with private monopolies
- Don't sell through discretionary, non-transparent procedures, which invite allegations of corruption and nepotism
- Don't use sales proceeds to finance budget deficits—retire national debt
- Don't "crowd" financial markets with public borrowing at a time of public disinvestment
- Don't make false promises to labour—retrain them for new industries
- Don't rely merely on executive orders—create a political consensus

ution of shares to nationals and foreigners alike—with a timing and a distribution of shares that both maximize revenue and protect national interests.

6. *With unrealistic labour strategies*—Some governments have been so nervous about labour agitation in privatized industries that they have demanded guarantees from prospective buyers that no workers will subsequently be laid off. Others have “bought” labour cooperation by offering handshakes so golden that they exceed the asset’s sale value. Employment is one of the most difficult and sensitive areas of privatization. But experience shows that it is better to have an open and free dialogue in advance. This should cover the possibilities of worker ownership and retraining schemes, as well as the inevitable job losses. False promises in the initial stages will create worse problems later.

7. *With no political consensus*—Privatization is not merely a technocratic exercise. It is also a political process. A hasty privatization forced through executive orders risks immediate conflict—and reversal after a change in government. There are many contending schools of thought on privatization, and unanimity is unlikely. But governments should still attempt to build as broad a consensus as possible and to use democratic parliamentary procedures to minimize violent lurches in policy.

The enumeration of these sins is a caution not against privatization, but against privatizing within the wrong framework and without a human development purpose in mind. Policy-makers can learn much from free and frank exchanges of experience—and from using information from the 80 countries that embarked on privatization strategies in the 1980s and early 1990s.

The enormous changes that have swept the world in recent years can be seen as a threat to the security and livelihoods of millions of people—or as a unique opportunity for people to shape new and different forms of social and economic participation. People-friendly markets have a vital role to play here—allowing people much broader opportunities to participate, and releasing some of the enormous human potential that remains untapped.

## Markets and the state

The concept of people-friendly markets clearly envisages state and markets working in tandem. For this to happen, there must be a realistic assessment of the strengths and weaknesses of each.

Past discussions of the role of the state have generated more heat than light. Some believe in the benevolence of the state and the need for it constantly to correct the ill effects of the market. Others glorify the virtues of the market-place and argue that the economy should be liberated from the dead hand of state bureaucracy.

Changes in ideology have produced swings in policy backwards and forwards. Policy-makers in developing countries have highlighted the imperfections in markets. And they have been tempted to supplant them with state action, often in the mistaken belief that the public sector would necessarily do better.

Today, markets are much more popular. Indeed, some people claim that recent events prove the triumph of capitalism and the demise of socialism. This is too simplistic a view. If there is a triumph of capitalism, it need not be the triumph of personal greed. If there is a demise of socialism, it need not be the demise of all social objectives. Indeed, such labels inhibit creative thinking and risk repeating the mistakes of the past.

The issues are further clouded by three persistent myths about the roles of the public and private sectors in developing countries.

*Myth 1: The public sector is too large in developing countries*—As a proportion of GNP, public spending in developing countries is lower than that in industrial countries. In fact, to ensure that everyone has the basic education and health to benefit from people-friendly markets, and to maintain adequate and efficient social safety nets for their vulnerable groups, many countries will need to increase public spending.

*Myth 2: After privatization, the balance between private and public investment will change dramatically*—In fact, privatization will have very little effect on this balance. First, the number of enterprises that can be

*Privatization is not merely a technocratic exercise. It is also a political process*

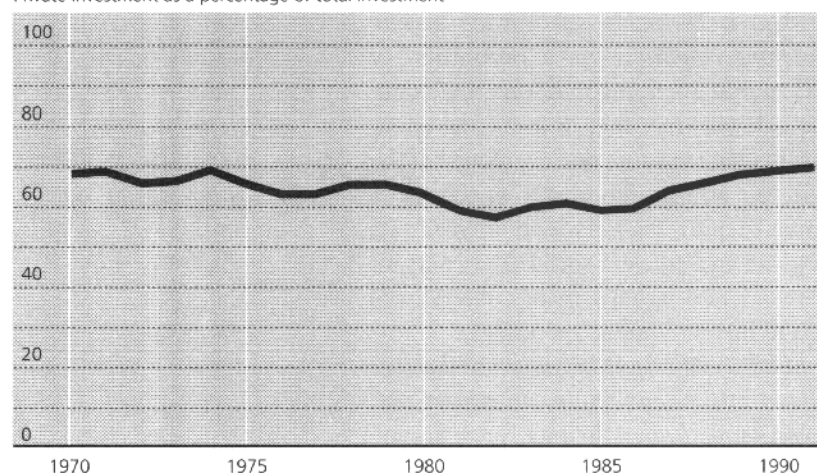
privatized is not that great in most countries. And second, the state will simultaneously have to increase its investment in physical and social infrastructure since it had to be curtailed significantly in the 1980s. For the developing countries having data, the share of private investment in total investment fell from around 68% in 1970 to 57% in 1982 and then rose to 69% in 1991 (figure 3.5 and table 3.5). The share of private investment rebounded in the past few years but is still only a little higher than in the early 1970s. And a large part of the recent increase is a consequence not of privatization—but of governments decreasing their investment in infrastructure and of private sector growth from removed controls and regulations.

*Myth 3: The activities of the state should be minimal*—The real problem with the public sector in developing countries is not so much its size as its activities. Public enterprises have been overeager to engage in productive activities in industry and trade, which the private sector could have undertaken, often more efficiently. Consequently, governments have neither the time nor the resources for the job they should be doing. To quote Keynes: “The important thing for Governments is not to do things which individuals are doing already, and to do them a little better or a little worse; but to do those things which at present are not done at all.”

FIGURE 3.5

### Trends in private investment in developing countries, 1970–91

Private investment as a percentage of total investment



Based on a sample of 47 developing countries.

Japan and the industrializing “tigers” of East Asia are powerful evidence of the value of such an approach. There, the state has played an enabling role for people-friendly markets—building the infrastructure, educating and training workers and providing a stable climate that enables enterprises to grow and flourish.

Entrepreneurs in developing countries have certainly been concerned about the role of government in economic activity. But they have been less bothered about government spending than about government control. Many forms of private investment demand numerous licences and permits before being allowed to go ahead—consuming valuable time and creating enormous uncertainty.

The central fallacy in the old ideological debate was that the state and the market are necessarily separate and even antagonistic—and that one is benevolent, and the

TABLE 3.5

### Trends in private investment for selected developing countries

Country	Private share in total investment (average annual %)		Change in share (percentage points)
	1970–74	1987–91	
Mexico	65.2	77.1	+11.9
El Salvador	72.4	78.3	+5.9
Costa Rica	73.1	78.5	+5.4
Pakistan	46.6	51.3	+4.7
Tunisia	46.6	51.0	+4.4
Thailand	76.0	78.8	+2.8
Guatemala	78.2	80.6	+2.4
Ecuador	60.8	63.1	+2.3
Paraguay	78.1	80.2	+2.1
Korea, Rep. of	77.3	78.5	+1.2
Singapore	79.2	77.9	–1.3
Sri Lanka	60.7	58.4	–2.3
Kenya	60.4	57.2	–3.2
Turkey	58.2	54.2	–4.0
Malaysia	69.1	64.7	–4.4
India	58.7	53.7	–5.0
Belize	61.0	55.7	–5.3
Argentina	62.7	54.2	–8.5
Uruguay	75.7	65.6	–10.1
Zimbabwe	62.5	50.5	–12.0
Dominican Rep.	67.8	52.5	–15.3
Colombia	69.6	52.5	–17.1
Fiji	62.5	44.8	–17.7
Unweighted average	66.2	63.4	–2.8
Weighted average	63.2	65.0	+1.8

other not. In practice, both state and markets are often dominated by the same power structures.

This suggests a more pragmatic third option: both state and market should be guided by the people. The two should work in tandem, and people should be sufficient-

ly empowered to exert effective control over both. They may do so through participation in governance, as producers or consumers, or in many cases, through people's organizations or non-governmental organizations—an issue addressed in subsequent chapters.



# Argentina

*Argentina's liberalization programme seems to have stabilized the economy, and the government is pressing ahead with a massive privatization programme. Although this has yet to show demonstrable human development benefits, the long-term picture should be brighter.*

Argentina's economic position deteriorated sharply in the 1980s. GNP per capita fell by an annual average of 1.8%. Investment, which in the 1970s was above 20% of GDP, dropped in 1990 to only 9%. And the economy was disrupted by hyperinflation. The government introduced shock programmes in both 1985 and 1987, including devaluations and wage and price controls, but neither stabilized the economy.

In 1989, the current government launched another stabilization programme. Since then, it has:

- Cut the government budget sharply
- Reformed the tax system and increased taxes
- Pegged the national currency to the US dollar
- Established large foreign currency reserves in the central bank and set a legal limit to printing money not backed by foreign currency
- Simplified government regulations
- Lowered tariff barriers
- Privatized many industries.

This time it seems the government has managed to stabilize the economy—and set it on the path to fundamental recovery. GDP grew by 6.5% in 1991, and at a similar rate for the first half of 1992. Investment also has risen signifi-

cantly, and the tax base is increasing.

Argentina's privatization programme is massive: the plan is to divest almost the entire public sector. In the three years through 1992, the government privatized 51 companies, raising about \$5.6 billion. Major privatizations included one of the telephone companies and an iron and steel company.

The process has not been entirely smooth, and in several cases the privatizations were in uncompetitive markets.

But the privatizations and the greater economic stability have attracted a large inflow of foreign investment—much of it the return of capital that fled in the 1980s. These capital inflows have financed the balance of payments deficit on the current account and helped build up international reserves.

Argentina's liberalization programme is relatively recent, but it does seem to be having a positive impact on the economy, with growth driven largely by an increased demand for private sector goods and services. In the long term, this should help increase levels of human development. But liberalization has yet to improve urban employment: in early 1992, unemployment in greater Buenos Aires was still more than 6.5%, and in other cities it was more than 10%.

HUMAN DEVELOPMENT RANK	46
GNP PER CAPITA RANK	62
GNP PER CAPITA ANNUAL GROWTH RATE (1980-90)	-1.8%
INFLATION RATE (1991)	128%
DEBT SERVICE RATIO (1990)	34%
CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	16%
TOTAL INVESTMENT AS % OF GDP (1990)	9%
PRIVATE SHARE OF TOTAL INVESTMENT (1970-74)	63%
PRIVATE SHARE OF TOTAL INVESTMENT (1990)	60%
FOREIGN DIRECT INVESTMENT INFLOWS AS % OF GROSS CAPITAL FORMATION (1986-89)	6.5%
LOSSES OF PUBLIC ENTERPRISES AS % OF GDP (1989-91)	9%
NUMBER OF PUBLIC ENTERPRISES SOLD (1990-92)	51
REVENUE FROM PUBLIC ENTERPRISE SALES AS % OF GNP (1989-91)	7%

# Brazil

*Brazil's liberalization programme started in earnest in the 1990s. Many measures have already been taken to liberalize trade and reform the financial system. Some public enterprises have already been privatized, but the process still has a long way to go, since privatization policy is only now being defined.*

Brazil seems to have been riding an economic roller-coaster, switching between periods of fast and slow growth, occasionally dipping into contraction. The period between 1968 and 1974 was the "Brazilian miracle", with an average annual growth rate of 11%. The 1980s saw the country sink into recession, with widespread economic instability, high external debt, and rocketing inflation, which in 1989 and 1990 was over 1,500%.

Successive Brazilian governments have, since the mid-1980s, tried shock tactics to stabilize the economy, including attempts to freeze wages and prices. But they had little success—budget deficits and inflation continued to soar.

In 1990, the government introduced a major new set of reforms, which combined stabilization measures with trade liberalization and deregulation. Among other things, it:

- Reduced tariffs on imports, abolished non-tariff barriers and sped up import licencing, repealing part of Brazil's protectionist legislation
- Relaxed the conditions for foreign investment and technology transfer: since June 1991, direct foreign investment has been permitted on equal terms with domestic investment
- Let the currency float on the international exchanges
- Simplified some of the bureaucratic procedures
- Eliminated the single-retail-price structure, and removed the monopoly on domestic wheat distribution
- Launched a large-scale privatization programme.

The government had increased its direct participation in the economy from the 1940s onwards, launching some new industries and assuming control, or becoming a large investor, in others. Its involvement today includes banking, petroleum, mining, road and rail networks, ports and power generation, as well as distribution and storage.

Brazil has 159 public enterprises, some of them well-run and efficient. But on average they are less efficient than those in the private sector and often make losses. The operating deficit of public sector enterprises between 1986 and 1988 was about 3% of GDP, more than half the budget deficit. The state-owned enterprises hold about half of Brazil's total external debt. Broad support for privatization has developed.

Although privatization started in the 1980s, the current programme is the first to show any real results. Between 1990 and 1992, the government privatized 17 enterprises, with smaller shareholders, including employees, buying most of the shares (foreigners have so far bought very few). The revenue from future sales is unlikely to be significant in national terms—in 1990, the

total market value of public enterprises was \$25 billion, about 6% of annual GDP.

The government has yet to make much progress in dismantling monopolies. In telecommunications, it still monopolizes both local and long-distance services.

Liberalization, like privatization, is slow. Entrepreneurial activity remains stifled by numerous rules and regulations, and companies are uncertain about the direction of future government policies.

So far, there are few signs of a positive impact on human development. Poverty is widespread, and there are enormous income disparities, which the taxation system does little to reduce. Most revenues come from highly regressive payroll taxes, and neither personal income tax nor corporation tax is very progressive either.

High inflation continues to be a problem—particularly for those on fixed incomes and for the poor, who hold a large proportion of their assets in cash.

HUMAN DEVELOPMENT RANK	70
GNP PER CAPITA RANK	53
GNP PER CAPITA ANNUAL GROWTH RATE (1980-90)	0.6%
INFLATION RATE (1991)	429%
DEBT SERVICE RATIO (1990)	21%
CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	36%
TOTAL INVESTMENT AS % OF GDP (1990)	22%
FOREIGN DIRECT INVESTMENT INFLOWS AS % OF GROSS CAPITAL FORMATION (1986-89)	2.4%
OPERATING DEFICIT OF PUBLIC ENTERPRISES AS % OF GDP (1986-88)	3%
NUMBER OF PUBLIC ENTERPRISES SOLD (UNTIL NOVEMBER 1992)	17
REVENUE FROM PUBLIC ENTERPRISE SALES AS % OF GNP	1%



# China

*China's reforms have taken place gradually over 15 years. The most significant steps have been in agriculture, with the breakup of agricultural communes. Widespread deregulation also boosted industrial output and trade, and encouraged a new private sector to emerge. Although some major problems persist, the reduction of poverty has been unprecedented.*

China's reforms have been carried out in two major stages. Between 1979 and 1984, they were concentrated in the rural areas, focusing on agriculture and rural industry, and from 1984 to the present, the emphasis has been on the urban sector and enterprise reform. Since 1979, the government has:

- Broken up the communes and turned the land over to household farming units
- Encouraged the growth of township- and village-owned enterprises, as well as non-public enterprises
- Introduced price reforms
- Decentralized state enterprise management and development planning.

The agricultural reforms between 1979 and 1984 broke up about 50,000 agricultural communes, distributing the land on the basis of a "household contract

responsibility system". This meant that farmers had to produce agreed quotas of certain products for the state but were otherwise free to diversify to meet market demand. At the same time, most agricultural prices were freed to reach market clearing levels. By 1984, following these reforms, agricultural output almost doubled in value, and per capita consumption among the agricultural population increased by 68%.

As the agricultural reforms took place, the surplus rural labour and capital were encouraged to move into township-owned and village-owned enterprises. By 1991, these enterprises, which operate outside the influence of central planning, were the most rapidly expanding segment of the industrial sector—producing 31% of industrial output value and employing more than 22% of the labour force.

After 1984, the government encouraged the growth of non-public industrial enterprises. These included petty urban services, private enterprises, urban cooperatives and corporate enterprises, as well as foreign private investment in joint and wholly owned ventures—either in urban areas or in specially designated economic zones. By 1991, this sector accounted for 47% of total industrial output value.

To introduce greater competitiveness in the market-

place, the government also reduced the number of products manufactured or distributed on the basis of state planning. Between 1982 and 1991, the number of these items had been reduced from 837 to 20. Most consumer products had been deregulated and were trading at market prices.

The state enterprises also underwent extensive reforms. Under the "contract responsibility system", managers were given shared responsibility for production planning, marketing, income distribution and investment decisions. The con-

tracts specify production quotas and the amount of taxes and profits to be remitted to government. If the quotas are met, the enterprises can retain additional earnings. In 1992, further measures were introduced to separate state enterprise operations from government controls and fi-

HUMAN DEVELOPMENT RANK	101
GNP PER CAPITA RANK	142
GNP PER CAPITA ANNUAL GROWTH RATE (1980-90)	7.9%
INFLATION RATE (1991)	3.5%
DEBT SERVICE RATIO (1990)	10.3%
TOTAL INVESTMENT AS % OF GDP (1990)	39%

financial subsidies. But labour productivity in these enterprises is still low, and around one-third are unprofitable.

Along with the economic reforms, there have been administrative ones—with a steady decentralization of responsibility for infrastructure and social services to lower levels of government.

China's reforms have been remarkably successful in many ways, but not without problems. The management of monetary and fiscal policy has been inadequate, and there have been economic fluctuations due to weakened planning and administrative controls. Some people are clearly benefiting more than others, with inequality increasing in favour of those employed in industry, trade and commercial agriculture. And there has been some deterioration in social services, especially in the poorer counties, since the services now rely more on local funding.

Pollution remains serious, both by state enterprises and by township- and village-owned enterprises unable or unwilling to comply with environmental regulations.

Most people in China are better off, with the number of rural people living in absolute poverty having fallen dramatically over the past two decades.

# Egypt

*Egypt's economy faces some structural problems. High reliance on oil income and overseas remittances have made it vulnerable to external shocks. The government has a new reform programme. To protect human development in the short term, it is also establishing a substantial social safety net.*

Egypt made considerable progress in human development in the 1970s and early 1980s. Between 1974 and 1981, GDP was growing 9% a year, spurred by rising oil production and prices as well as remittances from overseas workers. Since 1986, however, oil prices have fallen, Suez Canal revenues have declined and remittances have levelled off. As a result, annual GDP growth has been less than 5%, falling to about 2.5% in 1992.

The government, under pressure in the mid-1980s to repay the external debt, responded in 1987 with a reform package that included a liberalization of trade and domestic prices. But this did little to solve the underlying problems. And in the early 1990s, the economy was hard hit by the Gulf crisis—both by the fall in remittances from overseas workers and by the need to find jobs for returning workers when unemployment was already over 10%.

In 1991, the government adopted its Economic Reform and Structural Adjustment Programme—to move away from a reliance on the public sector, develop a stronger market economy and create more opportunities for the private sector. The programme:

- Freed interest rates
- Floated the currency
- Reduced subsidies on a wide range of items
- Curbed the growth in the money supply
- Overhauled the public enterprises and made plans for privatization.

These measures proved quite successful in restoring macroeconomic balances. Inflation fell below 10% in 1992. The balance of payments deficit was reduced, and the deficit in 1991/92 was brought down to its target figure of 7% of GDP. It is too early, however, to judge the long-term economic impact.

The public sector has dominated Egypt's economy since the 1960s, with large holding companies for textiles, food

processing, electronics, chemicals, metals and engineering. In addition, the four public sector banks hold around 80% of all deposits and are major shareholders in companies run as joint ventures with the private sector. Public enterprises currently employ about 1.3 million people and account for 70% of the industrial sector and 80% of exports—but many operate at a loss.

The government is now seeking to privatize more than 70 state enterprises. Pilot programmes in the tourist industry have auctioned off two hotels, and another hotel company is to be

floated on the stock market for about \$300 million. In addition, a stake in one of the highly profitable joint-venture banks has been sold to employees. The first major privatizations were scheduled for early 1993, with one batch of ten companies for sale in January, and another ten in March.

One major problem for privatization is the small Cairo

stock market, dormant since the 1960s. In 1990, it listed 500 companies, with shares traded in only around 20 companies a day. It is being revamped to make share-trading easier and more responsive to market fluctuations. The privatization programme is expected to increase Egypt's already high unemployment. It is estimated that 80,000 to 100,000 workers may have to move from the public sector to the private.

Egypt's reforms are a very promising step towards sustained economic growth and employment creation in the medium and long term. In the short term, however, they are likely to create several pressures for its people. The price of food and other basic goods is rising, and social services are deteriorating. Unemployment is still rising, particularly among youths and women. In response, the government has, with the assistance of such external donors as the World Bank and UNDP, established a Social Fund for Development to protect the most vulnerable groups, including displaced public enterprise workers, unemployed youth, Gulf crisis returnees and women-headed households.

HUMAN DEVELOPMENT RANK	124
GNP PER CAPITA RANK	120
GNP PER CAPITA ANNUAL GROWTH RATE (1980-90)	2.1%
INFLATION RATE (1991)	22%
DEBT SERVICE RATIO (1990)	26%
CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	40%
TOTAL INVESTMENT AS % OF GDP (1990)	23%
PRIVATE SHARE OF TOTAL INVESTMENT (1991)	42%
FOREIGN DIRECT INVESTMENT INFLOWS AS % OF GROSS CAPITAL FORMATION (1986-89)	8.1%



# Ghana

*Ghana's liberalization started in 1983, and in 1987 the government began to divest itself of some enterprises. But so far, private entrepreneurs have been hesitant to take advantage of the new environment. Economic growth has picked up, but people's living conditions have yet to improve.*

The Ghanaian economy declined in the 1970s and early 1980s, and real incomes and living standards fell. In the rural areas, cocoa farmers were hit particularly hard, with their real incomes falling sharply.

In 1983, the government adopted an Economic Recovery Programme. Since then it has:

- Liberalized consumer prices
- Reduced and rationalized import duties and trade taxes
- Devalued the currency several times
- Improved the banking system
- Established a stock exchange, which started trading in November 1990
- Liberalized the foreign exchange market
- Eliminated several subsidies
- Reformed the tax structure and increased revenue.

Investment, though increasing since the mid-1980s, is still low. By 1990, it had risen to 15% of GDP. But that is still very low considering that about 13% of GDP merely replaces depreciating capital.

The private sector is gradually responding to the improved economic environment. Between 1984 and 1990, private investment increased from 4% of GDP to 8%, and in 1991 it accounted for 50% of total investment. But most of the increase was in gold mining.

Entrepreneurs do not yet have much confidence in the government's economic management. Much of investment is seeking short-term profits, and many people are holding their savings in foreign currencies or outside the banking system. A 1989 survey of enterprises found that 38% considered economic uncertainty a problem, and most (particularly the larger ones) considered the regulatory framework still overly restrictive and cumbersome.

As formal sector employment and incomes declined,

microenterprises and self-employment proliferated, driven mainly by excess labour.

For entrepreneurs without sufficient capital, credit is a major problem. About 90% of enterprises perceived the lack of credit as a serious constraint on new investment—even though the private sector's share of total credit rose from 30% in 1984 to 65% in 1989.

Public enterprises in Ghana have had low productivity and suffered substantial losses. In 1984, they had 28% of formal sector employment. In 1989, they commanded 12% of government expenditure—net of revenues.

As part of the structural adjustment programme, the government is aiming to improve the efficiency of many state enterprises and divest itself of others. From 1987 to late 1992, it disposed of 80 enterprises, through partial or total privatization or liquidation (26 cases). In the initial stages, almost all these enterprises were small (fewer than 60 employees), but larger enterprises have been privatized

more recently. Delays in the implementation of the programme were partially due to technical matters in preparing for the sales. In 1992, the government still owned around 200 enterprises.

The divestiture programme has not yet been a financial success, and privatization has not yet adequately stimulated the local capital market or attracted the interest of domestic and foreign investors to the extent expected.

Economic growth in Ghana has picked up since 1984—averaging 5% annually. But considering the decline of the economy in the 1970s and early 1980s and the growth of the population, the recovery is only modest. And the recovery has not yet been translated into improved living conditions for the majority of people.

HUMAN DEVELOPMENT RANK	131
GNP PER CAPITA RANK	140
GNP PER CAPITA ANNUAL GROWTH RATE (1980-90)	-0.6%
INFLATION RATE (1991)	18.1%
DEBT SERVICE RATIO (1990)	35%
CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	14%
TOTAL INVESTMENT AS % OF GDP (1990)	15%
PRIVATE SHARE OF TOTAL INVESTMENT (1991)	50%
FOREIGN DIRECT INVESTMENT INFLOWS AS % OF GROSS CAPITAL FORMATION (1986-89)	0.9%
NUMBER OF PUBLIC ENTERPRISES DIVESTED (1987-92)	80



# India

*India's reforms have encouraged some capital to return and stimulated foreign investment and imports of technology. There also are extensive privatization plans. But the benefits in efficiency have yet to appear—and meanwhile, output growth in 1992 was only about 1%.*

India's recent efforts at economic reform started in 1985, when the government eliminated some licence regulations and other controls that had inhibited competition. But after this initial attempt, the process slowed.

In 1991, the new government, in response to a balance of payments crisis, initiated a fresh wave of reforms. Since June 1991, it has:

- Devalued the currency, and made it partially convertible
- Reduced quantitative restrictions on imports
- Reduced import duties on capital goods
- Cut a number of subsidies, including that on fertilizers
- Progressively liberalized interest rates
- Abolished production licences for most industries
- Eased restrictions on repatriating dividends and royalties
- Established a partial tax exemption on profits from export sales
- Allowed a partial sale of shares in selected public enterprises
- Reduced restrictions on foreign trading companies
- Revised the system of personal income tax.

Public enterprises account for about one-fifth of India's non-agricultural GDP and supply crucial inputs for the rest of the economy. They dominate the energy and financial sectors as well as the steel and fertilizer industries.

The privatization process in India is likely to be spread over about ten years. The first phase started in 1991, when the government sold shares in 31 state enterprises to mutual funds. In the second phase, in 1992, it started selling company shares through open auctions. Although the government intended to dispose of loss-making enterprises first, the pressure to earn revenues has caused it also to start selling some of the more profitable companies. Since the privatization process is still in its early stages, it is too soon to assess its impact.

The same is true for many other aspects of economic reform, but there are some early indications. On the positive side, capital has started to return to India. After the budget was announced in February 1992, the flow of private funds into India in the following weeks was estimated at \$50 million a day. There also are signs of improved industrial efficiency, as liberalization has encouraged foreign investment and permitted the import of higher levels of technology. The electronics industry, for example, has received a major boost from the liberalization of technology and component imports, as well as from delicensing and cuts in excise duties. And a

wider range of foreign goods—often of better quality than local goods—is now competing on the domestic market.

On the negative side, the reforms initially fuelled inflation, and the Bombay stock-market scam destabilized financial markets. In the year to July 1992, consumer prices for agricultural workers increased 20%, and those for industrial workers were up by 13%. At the same time, industrial

output stagnated. The cold wind of foreign competition in a previously protected market has forced some companies out of business. The government established a fund to help soften the blow to workers affected by restructuring and to assist social sectors, especially primary education and basic health care, but this has not yet become operational.

The rural poor, more than a third of India's people, are paying a price for the reforms but not yet seeing many of the benefits: agricultural production fell more than 2% in 1992. It will therefore—at least during the period of reform—be important to improve the efficiency and coverage of social programmes.

It is too early to judge the course of India's economic reforms. What is apparent is that they are proceeding along the right lines but will need to cushion the adverse impact on the poor people, lest there be a major political backlash.

HUMAN DEVELOPMENT RANK	134
GNP PER CAPITA RANK	146
GNP PER CAPITA ANNUAL GROWTH RATE (1980-90)	3.2%
INFLATION RATE (1991)	12.8%
DEBT SERVICE RATIO (1990)	29%
CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	18.2%
TOTAL INVESTMENT AS % OF GDP (1990)	23%
PRIVATE SHARE OF TOTAL INVESTMENT (1970-74)	59%
PRIVATE SHARE OF TOTAL INVESTMENT (1990)	56%
FOREIGN DIRECT INVESTMENT INFLOWS AS % OF GROSS CAPITAL FORMATION (1986-89)	0.2%
LOSSES OF PUBLIC ENTERPRISES AS % OF GDP	0.4%

# Kenya

*Kenya's liberalization programme has been slow. The government has concentrated more on stabilization measures than on adjustment. Privatization has been held back by political considerations. But the privatization programme has recently been revived.*

Kenya experienced considerable economic growth in the 1960s and 1970s. During 1965–80, its average GDP growth was 6.8% a year. The 1980s were different, with economic growth only slightly higher than population growth (4% a year)—due in part to the effects of the second oil shock and the breakup of the East African Community. Kenya has a fairly open economy (exports and imports make up over 40% of GDP), and it has been hurt by sharply deteriorating terms of trade.

The government made several attempts in the 1980s to adjust the economy to changes in the external environment, focusing mainly on stabilization—devaluing the currency several times and exerting more control over public spending. But little was done to liberalize trade or stimulate production.

Some of the adjustment policies succeeded—particularly agricultural diversification. Horticultural exports doubled in the 1980s to become one of the top four export earners, along with coffee, tea and tourism.

The government has frequently expressed its intention to increase the private sector's role in the economy. But private investment has declined as a proportion of GDP—from 14% in 1970 to 10% in 1991, as total investment stayed at around 20% of GDP (except for a few years around 1980, when it was 25%).

Kenya's public enterprises are in a broad range of economic activities, including agriculture, finance, transport and trade. They produce about 11% of GDP and employ about 9% of the workforce. There is no clear evidence that public

enterprises need be less efficient than private ones; the quality of management seems to be a more significant factor than ownership. But it has recently been calculated that the productivity of public enterprises declined by 2% annually during 1986–90, while that of the private sector rose 5% annually.

Kenya is thought to be the African country likely to benefit most from privatization. It has a relatively well-developed capital market, with a level of savings about twice as high as the average for Sub-Saharan Africa. And some of the markets in which public enterprises operate are quite competi-

tive. But progress so far has been very limited. Indeed, between 1980 and 1990, only one enterprise was privatized. The problems seem to have been mainly political, with concerns that the assets, like much of Kenya's other commercial, financial and managerial capital, would be taken up by foreigners, and particularly privileged or enterprising ethnic groups. But the privatization programme has recently been revived, with the announcement in mid-1992 of

the full or partial sale of 207 companies.

Even if privatization has been slow, the reforms in public enterprises and the threat of privatization have prevented the creation of more state enterprises.

If privatization does proceed, it is likely to lead to layoffs, which could cause considerable hardship, given Kenya's already high unemployment and underemployment. The government has already pledged to introduce redeployment programmes and social safety nets.

HUMAN DEVELOPMENT RANK	127
GNP PER CAPITA RANK	144
GNP PER CAPITA ANNUAL GROWTH RATE (1980–90)	0.3%
INFLATION RATE (1991)	8.9%
DEBT SERVICE RATIO (1990)	34%
CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	31%
TOTAL INVESTMENT AS % OF GDP (1990)	24%
PRIVATE SHARE OF TOTAL INVESTMENT (1970–74)	60%
PRIVATE SHARE OF TOTAL INVESTMENT (1991)	55%
FOREIGN DIRECT INVESTMENT INFLOWS AS % OF GROSS CAPITAL FORMATION (1986–89)	1.4%
NET OUTFLOW OF CENTRAL GOVERNMENT BUDGET TO PUBLIC ENTERPRISES AS % OF GDP (FISCAL 1991)	1%
NUMBER OF PUBLIC ENTERPRISES SOLD (1980–90)	1



# Malaysia

*Malaysia has a dynamic private sector and a large public sector. Fast economic growth has enabled substantial reductions in poverty. Privatization, so far not extensive, is likely to become more significant.*

The exposure of Malaysia's dynamic private sector to a relatively liberal trade regime has ensured that it remains internationally competitive. The country has combined this with a relatively large public sector.

The government's major concern has been less the balance between private and public sectors than that between the levels of economic power of different ethnic groups. So, its New Economic Policy (NEP), adopted in 1971, was to promote economic growth while encouraging greater economic participation by the Bumiputras (Malays)—rather than by other Malaysians, mainly of Chinese and Indian origin. The Bumiputras are the indigenous people, forming the largest ethnic group and the largest number of poor. This effort included, for example, giving the Bumiputras preferential access to credit.

The policy appears to have been fairly successful at redistributing corporate assets. In 1980, foreigners owned 62%, other Malaysians 34% and Bumiputras 4%. By 1985, the figures had changed to foreigners 25%, other Malaysians 57% and Bumiputras 18%. Since 1990, the National Development Policy, successor to the NEP, has relaxed the quotas in favour of the Bumiputras but still aims at redistributing resources in their direction.

The government has also introduced more general economic liberalization measures. Since the early 1980s, it has:

- Liberalized investment licencing and foreign investment criteria
- Reformed the tax and tariff systems, increasing their simplicity and transparency
- Privatized state enterprises.

This has encouraged greater investment by the private sector—from 13% of GDP in 1970 to 24% in 1991. More than two-thirds of total investment is now private, though a

significant proportion of this is foreign (one-third of paid-up capital in the industrial sector).

Even so, the state sector is still substantial—about 25% of GDP, among the highest proportions outside the world's (once) centrally planned economies. From 1970 onwards, the number of public enterprises grew rapidly as the state involved itself more in commerce and industry. In 1983, however, the government began to privatize these enterprises, starting with large enterprises in transport, infrastructure and telecommunications, such as the national airline and the container terminal. The privatization has also been managed to distribute ownership to Bumiputras and Bumiputra institutions, specifically reserving a part of all public share issues for them.

So far, the impact on the economy has been limited. Some enterprises have become more efficient, and privatization has helped develop the local capital market. But the volume remains small—between 1984 and 1989, total asset sales were less than 0.1% of GDP. And it is doubtful that the government has real-

ly decreased government control, since the assets merely passed to organizations of the ruling party. There is also the problem that government monopolies have in some cases, as with the container terminal, become private monopolies.

The process is nevertheless continuing. In 1991, 15 enterprises were privatized, including a cement factory and a shipyard. And some of the privatizations currently planned look much more significant—as with water and telecommunications, whose proceeds could be around 15% of GDP.

Malaysia is one of the world's fastest growing economies and has considerably reduced poverty—a demonstration that a sensible balance between private and public sectors can lead to rapid economic growth and good progress in human development.

HUMAN DEVELOPMENT RANK	57
GNP PER CAPITA RANK	66
GNP PER CAPITA ANNUAL GROWTH RATE (1980-90)	2.5%
INFLATION RATE (1991)	3.2%
DEBT SERVICE RATIO (1990)	11.7%
CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	31%
TOTAL INVESTMENT AS % OF GDP (1990)	34%
PRIVATE SHARE OF TOTAL INVESTMENT (1970-74)	69%
PRIVATE SHARE OF TOTAL INVESTMENT (1991)	68%
FOREIGN DIRECT INVESTMENT INFLOWS AS % OF GROSS CAPITAL FORMATION (1986-89)	9.6%
NUMBER OF PUBLIC ENTERPRISES SOLD (1980-90)	36

# Poland

*Poland's three-year economic reform has in many ways been a remarkable success. The economy has stabilized, and the private sector has enjoyed sustained growth. But the benefits have not been shared equally: many people in smaller towns and rural areas suffer from high unemployment.*

In the autumn of 1989, the Solidarity government inherited a catastrophic situation: declining output, widespread shortages and price increases close to hyperinflation. The new government acted quickly to stabilize the economy. At the beginning of 1990, it:

- Made drastic cuts in the budget, including reductions in consumer subsidies
- Increased interest rates to restrict credit growth
- Fixed the exchange rate to the US dollar
- Fully liberalized foreign trade.

External donors supported this package with a \$1 billion stabilization loan and later wrote off a substantial part of Poland's external debt.

This "shock therapy" was the beginning of the transition towards a market economy. It brought a number of immediate benefits—significantly reducing inflation, eliminating shortages and stimulating an increase in exports to Western Europe and North America (which partly offset the collapse in trade with formerly socialist countries).

But the shock therapy also produced a sharp decline in economic activity. GDP fell by 12% in 1990 and by 7% in 1991. And during 1990–91, industrial output fell by 36% and employment by 14%.

More recently, the economy appears to be recovering. Inflation declined to about 43% in 1992. Economic growth in 1992 is estimated at about 1%, and growth in industrial production at 4%. Efficiency is on the increase in both the public and the private sectors, and industrial firms operate largely without subsidies. As an OECD study pointed out: "Except in the energy sector, the few subsidies that remain may be lower than those received on average by private firms in most OECD countries."

The Polish government has managed to build the infrastructure and legal framework for a market economy remarkably quickly. It has introduced laws to govern private

property rights (in areas ranging from agricultural land transfer to urban land taxation) and developed bankruptcy legislation. But much still needs to be done to improve the financial system and the telecommunications infrastructure. And environmental standards are still low; for example, Polish industry is extremely inefficient in energy use.

Most of the privatization was initially concentrated on wholesale and retail trade. Lately, however, privatization has been carried out in broader areas, including manufacturing. By the end of 1992, around 97% of all shops were in private hands. And the availability of goods and the quality of service have increased dramatically.

The privatization process has generally been slower than expected. Most privatizations so far have been through liquidation methods, generally involving small and medium-size enterprises. About 50 enterprises have been privatized through capitalization methods (public offerings, trade sales and management and

employee buyouts). The basic scheme for the Mass Privatization Programme has also been developed, but it has run into political obstacles.

Meanwhile, the urban private sector is growing rapidly under its own steam—particularly in services. By mid-1991, there were around 1.3 million individual private businesses in Poland (96% of which had fewer than five employees). During 1991–92, the number of domestic private companies rose by more than 20%. And about 58% of the employed workforce was in the private sector, including family farming.

In human development terms, most people are better off today than in the disastrous final days of central planning. But the gains have not been equally distributed. Most of the private sector growth has been in the big cities, where the younger and better-educated people have benefited most. Smaller towns have done less well, and in many agricultural regions unemployment is more than 20%.

HUMAN DEVELOPMENT RANK	48
GNP PER CAPITA RANK	80
GNP PER CAPITA ANNUAL GROWTH RATE (1980–90)	1.2%
INFLATION RATE (1991)	65%
DEBT SERVICE RATIO (1992)	11.1%
CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	40%
TOTAL INVESTMENT AS % OF GDP (1990)	31%
GOVERNMENT TRANSFERS AND SUBSIDIES TO PUBLIC ENTERPRISES AS % OF GDP (1989)	9%
NUMBER OF PUBLIC ENTERPRISES PRIVATIZED (1990–92)	766



# Russia

*Russia is undergoing a radical shift from a planned to a market economy in the midst of a deepening economic crisis. The government is going ahead with its privatization programme, distributing vouchers free to all citizens—though with unemployment widespread and increasing, most people are preoccupied with the struggle to survive.*

The first serious attempt to open Russia's centrally planned economy to market forces was in 1987, when the former Soviet Union gave state-owned enterprises greater independence and more incentives to improve efficiency.

After Russia emerged as an independent nation, the government introduced "shock therapy" to stabilize the economy. At the beginning of 1992, it:

- Liberalized trade within the economy, removing price controls on almost all goods
- Sharply reduced government spending
- Introduced a value added tax
- Made the currency partly convertible.

Political considerations limited the extent of reform, which included almost no liberalization of foreign trade and continuing restrictions on access to hard currency. The government did cut the budget, but it failed to reach its deficit targets. At the same time, the central bank was making loans to industry at negative real interest rates, fuelling inflation and jeopardizing the stabilization programme.

Russia's economic situation deteriorated dramatically in 1992. Industrial output fell by at least 20% and inflation accelerated—by early 1993 it threatened to become hyperinflation.

The government is having to make radical changes to its economy at a time of economic crisis. It will, for example, have to find alternatives for much of the military industry, which accounts for 20% of employment and output. It will also have to use its resources more efficiently. At the end of 1992, oil was still being sold at only 20% of the world market price, encouraging inefficient use and adding to pollution. But raising the price sharply would be very painful for industries still inflexible in their use of technology.

In short, the government faces the stark choice between hyperinflation and mass unemployment. The external environment offers little help. Trade with the other newly independent states of the former Soviet Union has sharply

declined, and trade with Eastern Europe has virtually disappeared. Unlike most of Eastern Europe, Russia has been unable to reorient its economy to western markets, and exports have fallen dramatically. Foreign donors have promised some assistance, but of the \$24 billion pledged, less than half had been paid in 1992.

Despite the crisis, the government is still pursuing an ambitious privatization programme. This started with smaller enterprises, such as municipally owned shops. In the first half of 1992, nearly half the shops in Moscow and St. Petersburg were privatized. Now, it is moving on to larger undertakings. In 1993, the government plans to sell 5,000 large enterprises.

To achieve this, it is distributing vouchers free to all citizens, who can sell them if they prefer cash in their hands today, or use them to buy privatized assets.

Agriculture is still dominated by state farms and large

cooperatives—though management decisions and incentives for workers are increasingly being guided by market forces. And from the middle of 1992, it was planned that these farms would become joint-stock companies owned by the workers. As in the former Soviet Union, workers are also allowed their own small plots and can sell their produce on the open market. Private farming is increasing, but it still accounts for only about 3% of agricultural production.

Markets are developing very rapidly in Russia, but they are not proving very people-friendly. Studies by the ILO reveal massive poverty and deprivation. Real wages in 1992 fell by more than 40%—at the beginning of 1993 they were as low as \$10 per month. Unemployment is expected to increase further because of the demobilization of much of the armed forces.

The Russian people now have great difficulty making ends meet. In late 1992, about 75% of family expenditure was going for food, and an estimated 80% of the population was below the poverty line.

HUMAN DEVELOPMENT RANK	37
GNP PER CAPITA RANK	47
INFLATION RATE (1991)	105%
CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	47%
TOTAL INVESTMENT AS % OF GDP (1990)	33%



# Viet Nam

*Viet Nam is undergoing a rapid transition, and many new enterprises have sprung up following its economic liberalization. Public enterprises are becoming more efficient, and some will be privatized. Most of the population has benefited from these changes, but unemployment has now become serious.*

Viet Nam is changing rapidly. Since 1987, through its *doi moi* (renovation) policy, the government has started to transform the country into a socialist market economy. It introduced some agricultural reforms in 1988—giving farmers greater incentives to work land privately, lifting price controls and removing the requirement to deliver a quota of rice production to the government. Farmers were given long-term rights to land, but landownership is still vested in the state. Since 1989, the government has:

- Legalized private enterprise
- Liberalized prices
- Lifted controls on domestic trade
- Reorganized the tax system
- Introduced a managed float for the currency
- Given public enterprises greater autonomy and decreased their subsidies.

Viet Nam has recently faced a very hostile economic environment. Its major aid donor and trading partner, the Soviet Union, has disappeared (between 1988 and 1990, Soviet assistance amounted to 6% of GDP), and the United States sustains a trade and investment embargo. Nevertheless, Viet Nam's output grew about 4% in 1991 and growth in 1992 is estimated at 8%.

The non-state sector produces about 75% of GDP—in industry about 45%, and in agriculture (about half of GDP) 97%. Non-state industrial output comes from "households", cooperatives, private enterprises and "manufacturing groups".

Since private enterprise was legalized, family-based enterprises have restored many crafts, such as shoe making, tailoring and furniture making. And such cottage industries as silk weaving and ceramics have also revived. For some products, such as leather shoes for the domestic market, the non-state sector now dominates. All this has helped increase the supply of consumer products. The non-state sector has also increased its share of employment and now accounts for 88% of total employment. Most of these jobs (80%) are in agriculture, largely in cooperatives.

Enterprises still find it difficult to get credit, however. Banks are relatively underdeveloped, and most of the loans go to state enterprises. Some foreign capital is arriving, particularly from other East Asian countries, and beginning to have a significant impact, particularly in urban areas.

State organizations still play an important role in wholesale trade, but the share of the state in domestic trade fell from 41% in 1987 to about 25% in 1991. Market prices prevail for more than 80% of state enterprises' output and for nearly all agricultural produce.

Although Viet Nam is a socialist country, its 12,000 state enterprises account for only one-quarter of GDP. Few of

these are large: even in industry, the median size is 225 employees. About one-third of state enterprises were making losses in the late 1980s.

The government is increasing the efficiency of state enterprises

by cutting their workforces. Between 1988 and 1990, their share of the total labour force fell from 14.2% to 11.9%.

Ownership of these enterprises may follow one of several paths. The state will retain ones related to state security, such as electricity and railways. It might also retain some of the more profitable ones, such as cigarette manufacturing and breweries (though there may also be joint ventures for these). Others will probably be converted into joint-stock companies in which the state retains some equity interest. Still others are likely to be liquidated when a new bankruptcy law comes into force.

Unemployment and underemployment have become very serious. People have been laid off from state enterprises, and half a million soldiers were demobilized after the withdrawal of forces from Cambodia. It will take some time for them to be absorbed into the economy.

Most of the population is, however, already gaining from the reforms. Over the past five years, income has increased about 6% a year, and the majority of the population has benefited from the liberalizations in agriculture.

HUMAN DEVELOPMENT RANK	115
GNP PER CAPITA RANK	156
INFLATION RATE (1991)	83%
LOSSES OF PUBLIC ENTERPRISES AS % OF GDP (1987)	5%



## People and governance

The 1980s saw a move away from authoritarian rule towards greater political freedom and democracy. A positive trend, but there is still some way to go before people in developing countries are truly in command of their lives. Even where citizens can elect their leaders in regular, free and fair elections, they seldom have achieved full political participation. If people in developing countries are to influence development, the trend towards democracy will have to widen and deepen.

### Participation in shaping governance

The movement towards democracy in the 1980s was partly a result of internal weaknesses in authoritarian regimes. Their claims to rule had been based on the promise of firm government that could establish order and promote economic growth. When growth faltered, particularly in Africa and Latin America, their legitimacy was undermined. In Brazil, the economic slowdown of the 1980s made it difficult for the military to justify what already was an unpopular rule. Internal disagreements on political and economic strategy further undermined the regime, and this enabled popular pressure to force a transition to democracy, as in other Latin American countries. Elsewhere, popular movements were the most significant element in forcing changes—most notably in Eastern Europe, Africa and the Philippines, where a broad coalition of popular organizations united against a corrupt regime.

These democratic movements are spreading. International media make people in the remotest areas aware of political unrest on the other side of the globe and inspire them to make similar demands—as

many governments in Africa and the Arab States are now discovering. The reason in many cases is that governments are failing economically. But even where governments have been alleviating poverty, as in China and the Republic of Korea, people sooner or later want greater democracy.

There have also been attempts by outsiders to promote or encourage democracy—say, by making aid conditional on democratic reforms. While often an expression of shared concern for universal human rights, it can be counter-productive. It can antagonize people unnecessarily and undermine those pressing for democratic change—and it might not produce enduring change. Democracy is not a matter of one decision or of hastily organized elections. Democracy requires a long process of political development. And given the immense diversity of possible political forms, it is unlikely that the demands of outsiders will match another country's real needs.

People everywhere want to determine their own destiny. The kind of democracy they choose need not follow the models of Western Europe or North America—it usually has to be adapted to local circumstances. But the formal structure a country opts for, whatever it is, is only the starting point in a long process of facilitating effective forms of popular participation.

Democracy brings its own problems. One immediate difficulty is managing competing claims of different classes, ethnic groups and political actors. Developing countries are especially vulnerable because the state often controls a big part of the country's economic resources. When these resources are allocated by government decision, the rewards for influence can be very

*Democracy is not a matter of one decision or of hastily organized elections*

*Decentralizing  
governance is  
one of the best  
means of  
promoting  
participation  
and efficiency*

high. And if everyone makes claims at once, the outcome can be chaos.

The central problem for many developing countries is that they lack strong democratic institutions. Democracies, to work, need much more than voting booths. They also need stable political parties that can themselves draw together many diverse interests and weave them into a cohesive organization. And they need independent groups—farmers' organizations, trade unions, consumer groups, chambers of commerce, cultural and religious groups—and all the other elements of a civil society that systematically facilitate and regulate the process of articulating people's demands.

Building these institutions takes time—and constant renewal, if they are not to become instruments for a small elite to manipulate the levers of power.

Whether the leaders of new democracies always recognize the need for strong and democratic civil institutions is far from clear. In many countries, the prognosis is not good. Even in India, where political institutions were once strong and taken for granted, populist leaders pursuing their narrow goals have been weakening the instruments of democratic rule. Secularism, enshrined in the Indian constitution as the very foundation of the state, is now gravely threatened by the rising tide of communalism and fundamentalism.

There are also dangers from the other direction—from the creation of new forms of central control. Many countries are going through two difficult processes simultaneously—democratization and economic liberalization—straining the political capacities of many a newly elected leader. In Brazil and Russia, there is the risk of "two-track" democracy. Once elected, the government might want to be as free as possible from popular control in order to carry out unpopular reforms—negating the major goal of broadening political participation.

In many countries, it has therefore been found necessary to complement democratization with efforts aimed at enhanced transparency and accountability of government. Because it is one thing for people to be able

to elect their representatives and another for them to be able to know and influence what policies the representatives pursue once they are elected.

In recent years, there has in many countries been a marked improvement in people's opportunities to take part in selecting governments. Yet governments still are quite removed and distant from people, especially in the case of their implementing arm—governmental bureaucracy and governmental programmes and projects. Many developing countries have, after gaining independence, initially emphasized efforts to build a nation-state. This has often had a highly centralizing effect. And external assistance, which in many countries forms a large part of the national budget, has only helped to reinforce these trends.

The following sections examine how governments reach out to people—and, in particular, how decentralization helps improve human development.

**Decentralizing governance to increase local decision-making**

Decentralizing governance—from capital cities to regions, towns and villages—can be one of the best means of promoting participation and efficiency. Local officials and politicians can be much more open to public scrutiny than national governments—and more accountable to the communities and individuals they are supposed to serve. And public projects—be they dams, roads, schools or health programmes—all become much more relevant and effective if the communities concerned have a real say in their planning and implementation.

Decentralization can take several forms: it might, for example, be horizontal or vertical. *Horizontal* decentralization disperses power among institutions at the same level—a government's spending decisions, rather than being concentrated in an all-powerful finance ministry, might be spread across different ministries. *Vertical* decentralization, which is more important, allows some of the powers of central government to be delegated downwards to lower tiers of authority—to states in federal countries, for example, and then further

down to regional and local governments, or even to village associations.

Vertical decentralization of government can itself take three forms:

- *Deconcentration*—This is limited to passing down only administrative discretion—to local offices of central government ministries, for example. Although it does result in some dispersal of power, few decisions can be taken without reference to the centre.
- *Delegation*—This involves passing some authority and decision-making powers to local officials. But central government retains the right to overturn local decisions and can, at any time, take these powers back.
- *Devolution*—The strongest form of decentralization: granting decision-making powers to local authorities and allowing them to take full responsibility without reference back to central government. This includes financial power as well as the authority to design and execute local development projects and programmes.

### **Why governance is not decentralized**

In most developing countries, decentralization has generally been limited to deconcentration. Even Chile, Indonesia, Morocco and Zimbabwe have dispersed relatively little real power. All four have ostensibly autonomous levels of local government—the municipalities in Chile, the villages in Indonesia, the communes in Morocco and the district councils in Zimbabwe. But the resources they control are small, their decision-making powers narrow and many local appointments are imposed from above. (The country studies at the end of this chapter highlight the decentralization experience in these four countries. They are based on field studies and sample surveys, and their data do not always correspond to the tables in this chapter.)

In industrial countries, much social spending tends to be centralized—especially that for social security benefits. France, for example, spends nearly 20% of its GDP on social security. And other forms of social spending (such as education) may also be controlled centrally when there is a nation-

al consensus on the minimum standards that should prevail throughout the country. Nevertheless, local governments in many industrial countries do have considerable powers to raise revenue, and many spend substantial sums on social concerns.

The position is very different in developing countries. Social security systems are relatively weak, or non-existent, and so do not have the same centralizing influence. The explanations for concentration lie elsewhere.

#### *1. Centralization for nation-building—*

Many countries lack democratic institutions and traditions—partly a legacy from colonial times. The colonial powers tried wherever possible to concentrate finance and decision-making in the capital. And the newly independent countries continued this practice, partly to enhance their political and economic control, but also because they were convinced that the state should assume the major responsibility for economic development and “nation building”. This resulted in an overwhelming concentration of national power in the hands of central governments, as well as a massive accumulation of rules and regulations. Some countries have started to liberalize these controls, but there is still a long way to go.

#### *2. Weak democracy—*

Many governments have been ruled in a non-democratic way with authoritarian structures. This perpetuates strong centralizing tendencies as central governments seek to maintain complete control. In the absence of democratic structures, local governments lack an effective political power base from which to generate local control over decision-making.

#### *3. Low social spending—*

Many governments devote a high proportion of their budgets to centrally controlled military expenditure. Social spending, which has a greater potential for decentralization, tends to take up a smaller proportion of public allocations.

#### *4. Urban bias—*

Most countries have a bias in social spending towards urban areas and more “prestigious” forms of service delivery: the city hospital rather than the rural health clinic, the elite university rather than

*In the absence of democratic structures, local governments lack an effective power base*



*Most foreign aid  
has a centralizing  
effect*

the provision of basic education for the mass of the people. These large and expensive items are usually the prerogative of central rather than local government.

5. *Foreign aid*—Also tending to have a centralizing influence, most forms of international assistance are negotiated by central governments which, when required, must also take responsibility for repayment of loans. This does not mean, however, that the aid need necessarily be spent centrally. Some countries do manage to delegate the implementation of development projects to local government. Indeed, some donors, particularly the Nordic countries, insist that management of projects, wherever appropriate, be executed by local governments or NGOs. But in practice, aid expenditure is still quite centralized. It would be useful if donors published annual estimates of the percentage of aid they channel through local governments.

The composition of aid also has a centralizing effect. Most aid is directed to large infrastructure projects, and only 15% goes to the social sectors—and less than half of this (6.5% of total official development assistance) is earmarked for human priority concerns that could normally be implemented locally. In addition, a large amount of assistance is for military purposes.

## Measuring the decentralization of expenditure

It would be useful to compare the extent of decentralization between one country and another. This is difficult, however, primarily because there are no statistical measures for many aspects of decentralization. There could, for example, be substantial local autonomy in the way the judicial system works, or in the police force or in social and cultural affairs—all difficult to quantify. But the discussion here concentrates on financial flows between central and local government and on the distribution of government employees—which are more open to objective analysis. For many countries, even these data are unavailable or incomplete. The central government might appear to decentralize expenditure, but if it retains tight control over standards and priorities, such financial delegation may be meaningless.

Local spending should also take into account the contributions local people make to self-help projects “in kind”—through time and materials. Because this is often difficult to quantify, local spending is generally underestimated.

Cross-national comparisons of decentralization should, in addition, allow for the size of countries (table 4.1), with decentral-

TABLE 4.1  
Governance structure in selected developing countries

Country	Total 1991 population (millions)	Largest state or province			Largest local body		
		Name	Population (millions)	Percentage of total	Name	Population (thousands)	Percentage of total
India	863	Uttar Pradesh	138.8	16.1	Midnapur	8,350	1.0
China	1,171	Sichuan	107.2	9.2	Ghazal Yang	1,999	0.2
Pakistan	122	Punjab	62.3	51.3	Faisalabad	5,962	4.9
Indonesia	188	Jawa Barat	35.4	18.9	Lampung Tengah Regency	1,900	1.0
Bangladesh	116	Dhaka	32.3	27.7	Dhaka	5,775	5.0
Brazil	152	Sao Paulo	26.9	17.7	Sao Paulo	10,063	6.6
Mexico	86	Mexico	9.8	11.4	Guadalajara	1,629	1.9
Egypt	54	Cairo Governorate	6.5	12.1	..	..	..
Nigeria	112	Kano	5.6	5.0	Ojo	1,012	0.9
Zaire	39	Kivu	5.4	14.0	Word Kivu	2,434	6.3
Kenya	24	Eastern	4.4	18.0	..	..	..
Colombia	33	Antioquia	3.9	11.9	Medillin	1,468	4.5
Ecuador	11	Guayas	2.0	18.5	Guayaquil	1,328	12.3
Algeria	26	Algiers	1.7	6.6	Oran	610	2.4
Cameroon	12	Extreme-Nord	1.7	14.3	Douala III	399	3.4
Panama	3	Panama	1.1	44.0	Panama	585	23.4
Congo	2	Brazzaville	0.6	26.1	Pool	184	8.0



ization a higher priority for large countries than for small ones: the degree of decentralization acceptable for India would not be suitable for Jamaica. The population of one state in India, Uttar Pradesh, exceeds the populations of 168 member states of the United Nations. Larger countries need more layers of government than smaller ones—just to ensure that the smallest units are a manageable size.

All quantitative estimates of decentralization should thus be treated with caution, always to be complemented by a broader knowledge and understanding of the countries concerned.

With these qualifications, tables 4.2 to 4.4 express the financial decentralization using several statistical ratios.

1. *The expenditure decentralization ratio*—the percentage of total government expenditure spent by local governments.
2. *The modified expenditure decentralization ratio*—takes into account the fact that some government expenditure cannot be decentralized (specifically defence and debt servicing). Subtracting such expenditures gives a modified expenditure ratio that expresses the degree of decentralization of responsibilities that can, in practice, be decentralized.
3. *The revenue decentralization ratio*—assesses the significance of local taxation. It is the percentage of local government revenue in total government revenue.
4. *The financial autonomy ratio*—gives an indication of local government's independence from central government funding. It is the percentage of locally raised revenue in total local expenditure.

The ratios reveal some interesting contrasts between industrial and developing countries (tables 4.2 and 4.3). In industrial countries, local governments normally account for 20–35% of total government expenditure, and in some countries the expenditure decentralization ratios are even higher—45% in Denmark and 41% in Finland. In developing countries, however, the ratio is usually below 15%. Even modifying the ratio to exclude defence and debt servicing does not significantly improve the

position. Except for the Republic of Korea and Zimbabwe, the decentralization of public expenditure in developing countries is extremely limited.

A similar picture emerges from a comparison of revenue decentralization ratios. In industrial countries, local governments exert considerable taxation authority, and account for about 25% of total government revenue. In most developing countries,

TABLE 4.2  
Financial decentralization in local government in selected countries

Country	Year	Expenditure decentralization ratio		Revenue decentralization ratio <sup>c</sup>	Financial autonomy ratio <sup>d</sup>
		Total <sup>a</sup>	Modified <sup>b</sup>		
<i>Developing countries</i>					
Korea, Rep. of	1987	33	..	31	99
Zimbabwe	1986	22	29	17	58
Nigeria	1988	17	..	..	..
Algeria	1986	14	..	16	101
Bangladesh	1987/88	12	..	8	39
South Africa	1988	10	11	10	79
Chile	1988	8	10	6	61
Brazil	1989	7	14	1	33
Thailand	1990	7	10	4	75
Philippines	1988	6	..	7	119
Morocco	1987	6	..	8	108
Paraguay	1989	4	5	3	88
Kenya	1989	4	5	7	134
Pakistan	1987/88	4	..	6	100
Costa Rica	1988	3	..	3	123
Ghana	1988	2	..	2	71
Côte d'Ivoire	1985	2	..	2	115
<i>Industrial countries</i>					
Denmark	1988	45	51	31	58
Finland	1989	41	43	29	63
Sweden	1989	37	42	30	78
Norway	1990	31	35	21	59
Poland	1988	27	27	23	78
United Kingdom	1989	26	31	16	55
Czechoslovakia	1990	26	27	19	61
Ireland	1989	23	28	10	33
Netherlands	1990	23	26	5	16
Iceland	1986	23	25	26	99
Switzerland	1984	22	24	22	87
USA	1989	21	26	16	65
Hungary	1990	19	21	11	53
France	1988	18	19	12	63
Germany	1988	17	18	14	73
Austria	1990	16	18	17	89
Canada	1989	16	18	11	53
Luxembourg	1988	15	16	7	42
Spain	1988	13	14	10	62
Belgium	1987	12	15	6	41
Romania	1989	9	10	8	103
Australia	1990	5	6	5	83

a. Local government expenditure as a percentage of total government expenditure.

b. Local government expenditure as a percentage of total government expenditure less defence expenditure less debt servicing.

c. Local government revenue as a percentage of total government revenue.

d. Local government revenue as a percentage of local government expenditure.

however, local authorities raise only around 6% (the Republic of Korea and Zimbabwe are again exceptions). Industrial countries have a wide range of local taxation options: property taxes, sales taxes, income taxes and user charges. Developing countries, by contrast, tend even at the national level to rely less on taxes on individuals and more on centralized sources like corporation tax or import duties, and the taxation options are fewer still at the local level.

International comparisons produce a curious result when it comes to financial autonomy ratios. The ratios for industrial and developing countries turn out to be much the same—in both cases, local governments control about 60% of local spending. But this covers two very different realities. In industrial countries, local governments have 60% control over a significant proportion of public spending. In developing countries, where local spending is smaller in the first place, local authorities control 60% of very little.

To discover the proportion of total expenditure controlled by local governments,

multiply the financial autonomy ratio by the decentralization ratio. For industrial countries, this produces a figure of about 25%, compared with 5% for developing countries. The available data do suggest, therefore, the limited decentralization in developing countries. Although several countries have, in recent years, attempted decentralization, few have made significant progress.

Industrial countries are also more decentralized than developing countries in the distribution of government employees. This can be expressed through the employment decentralization ratio: local government employees as a percentage of all government employees. A sample of 16 industrial and 31 developing countries for the late 1970s showed that in the industrial countries the ratio was 42%—compared with 21% in Asia, 19% in Latin America and only 10% in Africa.

Another key indicator of decentralization is control of social spending. It is generally presumed that when local governments are responsible for education or health, for example, they use the resources more efficiently and effectively, distribute the benefits more equitably and generally respond more sensitively than central governments to the needs of the local community (the validity of this presumption is discussed later).

The distribution of social spending can also be analysed through a series of ratios:

1. *The central government social allocation ratio*—the percentage of the central government budget devoted to social spending.
2. *The local government social allocation ratio*—the percentage of local government budgets devoted to social spending.
3. *The social expenditure decentralization ratio*—local government social spending as a proportion of total government social spending. This indicates the extent to which social spending is decentralized.
4. *The human priority ratios*—for both central and local governments, the percentage of their social spending devoted to social items that deserve first priority in most developing countries—basic education, primary health care, safe drinking water,

TABLE 4.3  
Financial decentralization in provincial government in selected countries

Country	Year	Expenditure decentralization ratio		Revenue decentralization ratio <sup>c</sup>	Financial autonomy ratio <sup>d</sup>
		Total <sup>a</sup>	Modified <sup>b</sup>		
<i>Developing countries</i>					
Nigeria	1988	68	..	..	..
China	1991	60	..	61	96
Costa Rica	1988	48	..	40	96
India	1988	44	56	32	48
Argentina	1987	39	43	21	38
Pakistan	1987/88	24	..	18	50
Brazil	1989	21	42	8	80
Malaysia	1990	15	18	11	67
Bolivia	1990	13	15	10	65
South Africa	1988	11	12	2	17
Indonesia	1989	10	13	3	21
Mexico	1987	7	17	12	99
Algeria	1986	3	..	3	105
<i>Industrial countries</i>					
Canada	1989	41	47	41	79
Australia	1990	37	41	23	53
Switzerland	1984	30	32	25	74
Germany	1988	24	26	22	80
USA	1989	23	30	24	86
Austria	1990	13	15	10	67
Spain	1988	11	13	4	30

a. Provincial government expenditure as a percentage of total government expenditure.

b. Provincial government expenditure as a percentage of total government expenditure less defence expenditure less debt servicing.

c. Provincial government revenue as a percentage of total government revenue.

d. Provincial government revenue as a percentage of provincial government expenditure.

family planning services and nutrition programmes.

Social provision ultimately appears almost entirely at the local level in terms of clinics or schools or welfare services. So control over this could, in theory, be highly decentralized. In practice, this does not happen—in either industrial or developing countries (table 4.4). *Equity* considerations may well point to a critical role for the centre in social expenditure, especially in reallocating resources from better-off to worse-off regions—and in ensuring a *minimum* degree of participation.

For 15 industrial countries for which data are available, the social expenditure decentralization ratios are generally around 25%—significantly lower, in fact, than the 40% average for their decentralization ratio for total expenditure. Social spending is most highly centralized in Australia, France, Luxembourg and Romania. Denmark delegates more than half its budget to the local level.

The situation is worse in developing countries. In most, the social decentralization ratio is only around 5–6%, with central governments responsible for over 90% of total social spending.

The available statistical evidence is sketchy and inadequate because governments of developing countries do not make a concerted effort to collect and publish data on expenditure patterns at all significant levels: central, state, provincial and local. The World Bank and the International Monetary Fund (IMF) do little better—collecting and publishing only central government budgets, even though much of the social spending in large federal states such as Brazil or India is at the state or local level. Even their information on central budgets contains little useful detail on social spending priorities.

The lack of statistical evidence on decentralization means that this important issue is often subject to sweeping generalizations and unsustained assertions. A coherent reporting system is needed, with contributions from:

- *National governments*—which could publish all their central, provincial and local

budgets, with details of social and human priority expenditure.

- *Donors*—which could give similar details on aid, indicating its distribution at the various levels of government as well as through NGOs.

- *The World Bank and the IMF*—which could collect and publish consolidated social expenditure budgets, subdivided into human priority expenditures, for each different level of government, in cooperation with other international agencies.

Such information would illuminate the links between decentralization and human development and permit a more thorough analysis than is currently possible.

### Resources for decentralization

A shift to decentralization not only affects the way resources are spent—it affects the way money can be collected. It could, for example, allow more taxes to be raised locally if people are confident that their money will be used for the benefit of their own

TABLE 4.4  
Social expenditure decentralization ratio in selected countries

Country	Year	Social allocation ratio <sup>a</sup>			Social decentralization ratio <sup>b</sup>	
		Central	Provincial	Local	Provincial	Local
<i>Developing countries</i>						
Chile	1988	46	..	31	..	6
Argentina	1987	41	35	..	36	..
Nigeria	1988	39	24	9	69	7
Zimbabwe	1986	32	..	34	..	23
Kenya	1989	25	..	22	..	3
Malawi	1984	21	..	22	..	6
Indonesia	1989	10	50	..	35	..
India	1988	5	35	..	85	..
Colombia	1984	..	67	35	85	15
<i>Industrial countries</i>						
Germany	1988	68	48	47	20	13
Austria	1990	67	62	..	15	..
France	1988	67	..	39	..	11
Switzerland	1984	66	55	46	28	18
Luxembourg	1988	59	..	24	..	7
United Kingdom	1989	49	..	43	..	23
Denmark	1988	48	..	81	..	58
Iceland	1986	48	..	49	..	24
Australia	1990	48	50	6	40	1
Canada	1989	44	62	50	49	15
USA	1989	41	68	59	31	24
Hungary	1990	40	..	55	..	25
Romania	1989	34	..	18	..	5
Czechoslovakia	1990	25	..	49	..	40

a. Central/provincial/local government social expenditure as a percentage of total central/provincial/local government expenditure.

b. Provincial/local government social expenditure as a percentage of total social sector expenditure.

*More efficient  
collection and  
enforcement can  
also boost revenue*

communities. The main ways of increasing local revenue are through taxation, cost recovery, voluntary contributions and borrowing.

*Taxation*

Central governments tend to leave local governments relatively little flexibility when it comes to taxation—partly because central governments want to reserve for themselves the most buoyant and lucrative revenues, but also because they generally like to keep tight control over local government finances.

These controls determine, first of all, what kind of taxes can be raised. In Nigeria, local councils must get central approval before including any levy in their revenue estimates. Then there are controls over taxation rates. In Bangladesh, the rates of taxes levied by the *zila parishad* (district council) have to be approved by the district commissioner—a central government appointee.

Urban local authorities tend to be somewhat better off in this respect than rural ones. They generally have more political influence with the centre—as well as wealthier and more diverse communities to tax. In Zimbabwe, the urban councils usually manage to finance all their recurrent expenditure from their own revenue, while the rural district councils manage to finance only about 15%.

The most common form of local tax in both urban and rural areas is on property. In the Philippines, the property tax accounts for more than two-thirds of local tax revenues, and it is the mainstay of many other local taxation systems in Asia, including China, India, Pakistan and the Republic of Korea. It is such a significant source of revenue that in some cases, including Chile and Indonesia, the revenue is shared between central and local governments.

A World Bank survey of 14 major Third World cities in the mid-1970s showed that, for four of them, property taxes represented more than half of local revenue, and for five more, more than a third.

In the rural areas, the most significant property taxes are applied to land—and

produce substantial revenues. But they are often difficult to collect from rural elites and from other farmers who may resist payment when agricultural prices are low. Some countries have tried to index land taxes to crop prices, but since such indexation does not take productivity increases into account, revenue tends to lag behind agricultural incomes.

The next most common taxes are those based on motor vehicles and entertainment. And some of the poorer authorities also derive significant income from minor charges on local businesses, particularly through trading licences. Individual countries also produce many specific local taxes: in Indonesia, local taxes have been levied on cash-crop exports.

Even when local governments in developing countries are allowed to levy taxes, they often have great difficulty in collecting them, probably because of strong resistance from potential payers. In Zimbabwe between 1985 and 1988, local governments managed to collect only 16% of the “development levy”, a type of poll tax that was widely resented.

A more common problem is that local governments lack the administrative capability. Property taxes, for example, require fairly regular surveys. In Baranquilla, Colombia, only three of the city’s ten districts have had recent surveys—so the city collects revenues from less than half the taxable properties. And in Monrovia, Liberia, the land adjudication teams lack the necessary logistical support and have never been able to collect property taxes. Similar problems can arise in rural areas.

Local political influence can also reduce potential revenue. In Nigeria, local taxation has allegedly been used as a political weapon—supporters of the governing party are exempt, while members of opposition parties are overassessed. In Iloilo City, Philippines, the city’s revenue has been undermined by the strong representation of property owners on the city’s decision-making bodies—contributing to a gross underassessment of property values and the granting of numerous exemptions.

As administration systems improve, however, there have in places been consid-



erable improvements in local tax collection. In Accra, Ghana, the city council computerized its budgeting and accounting procedures and restructured its Land Valuation Board—and so increased its revenue considerably in the second half of the 1980s.

More efficient forms of collection and enforcement can also boost revenue. New Delhi, India, with an improved management information system, can now offer rebates for those who pay on time and penalize those who pay late. Taxpayers also now have to pay their assessments before being allowed to appeal in court. These and other reforms produced significant increases in revenue, 16% in 1986 and 96% in 1987.

Revenue also rises as the opportunities for taxation increase. Car taxes are likely to prove a more important source of revenue in many developing countries. In Seoul, Republic of Korea, while total local tax revenue increased by 64% between 1982 and 1986, the automobile tax revenue more than doubled.

#### *User charges*

Local authorities can also raise revenue by charging users for services. In 25 countries surveyed by the World Bank, user charges accounted for nearly a third of all locally raised revenue.

Although businesses can reasonably be charged for many services, such as garbage collection, great care needs to be taken in charges for individuals, particularly for such social services as education or health care. Charges can deter many of the poorest users and cause considerable hardship—while raising relatively little money.

*Human Development Report 1991* examined this issue at some length, concluding that some services should always be free: specifically primary health care (though there could in some cases be charges for drugs and hospital care) and basic education. The case is also strong for free secondary education. And for water and sanitation, the Report concluded that governments should bear the capital costs but that users might contribute to recurrent costs.

A slightly different kind of user charge can be levied on businesses that benefit from local authorities' investment in infrastructure. These "betterment levies" have been used extensively in Colombia, India and Indonesia as a way of recovering costs from landowners who benefit from public improvements on or near their property. In New Delhi, such charges have been used to recover 50% of the costs of public works. Sometimes these payments can be made in kind—often by giving some private land to the local authority—a system used successfully in the Republic of Korea, Taiwan (province of China) and Thailand.

#### *Voluntary contributions*

One advantage that local government has over central government is the ability to tap local voluntary contributions, in cash or in kind. This has proved valuable in the *harambee* movement in Kenya and the Tesito movement in the Gambia.

But such contributions are not always very effective, possibly because of poor co-ordination between voluntary groups and local authorities.

A common problem is that local people may be enthusiastic about building a school or a health centre, but the question of who is to finance the subsequent running costs is left open. In some countries, schools have been built with local labour on the understanding that they would then be supported by central government, and when this has not materialized they have stood empty for want of teachers.

There can also be questions about just how voluntary this labour is. In India, Indonesia and Nepal, university students are required to "volunteer" to help supervise and implement small-scale rural development projects. In some African countries, including Tanzania, local people can also be obliged to work on "self-help" development projects or suffer a fine or confiscation of property. Voluntary contributions should, however, be kept in proper perspective. One can never hope to finance projects having collective benefits entirely from individual voluntary contributions. Some element of social mobilization may be necessary and

*Some services should always be free: specifically primary health care and basic education*

*Many local power structures are dominated by elites little interested in human development*

acceptable, as long as it consists of encouragement and persuasion.

### *Borrowing*

National governments are increasingly allowing local authorities to borrow to finance improvements in infrastructure, especially when local governments can subsequently be charged fees to recover costs.

An inherent danger here is that the central government could lose control over the national creation of credit—and macroeconomic management. So, the centre might have to either exert some kind of control over local government borrowing or adjust its fiscal and monetary policies to compensate.

An alternative way of financing local government investment is through special funds. In Jordan, the central government has an autonomous Cities and Villages Development Bank to provide investment finance and technical assistance to municipal and village councils. This has helped finance improvements throughout the country, bringing roads, schools, clinics and water supplies to even the smallest and most remote communities.

The same kind of arrangement can be made between lower levels of government. In Brazil, the state governments of Santa Catarina and Paraná have set up funds from which creditworthy municipalities can borrow for capital investment. There are some conditions, however. The municipalities have to be prepared to accept technical assistance to help them increase their capacity to raise revenue locally. And the federal government sets limits on the amount of debt and debt service that the municipalities can incur.

These types of funds have often been established with international aid. The Regional Development Fund in Chile is partly financed by the Inter-American Development Bank. This enables money to go straight to local authorities rather than passing through the central government—though generally, the central government still has to approve projects.

The fact that local authorities can raise their own funds could, in theory, expand to-

tal government expenditure. On the other hand, decentralizing public services might reduce costs and total expenditure. The fact is, however, that there is little conclusive evidence on the effect of decentralization on total public expenditure.

### **Decentralization in practice**

One presumed benefit of decentralization is that local governments, being closer to the people and more responsive to local needs, make better use of resources—and that they will direct them at such human priority concerns as basic education and primary health care. But there's not enough data to test this hypothesis thoroughly. The discussion in this Report is based partly on four detailed case studies—Chile, Indonesia, Morocco and Zimbabwe—as well as a less systematic body of evidence. So, the conclusions reached can only be suggestive.

One issue the case studies highlight is that of choice. It was possible to investigate whether local governments that raised more of their own funds locally tended to use these more for social needs—that is, whether local bodies with greater financial autonomy ratios tended to have higher social allocation ratios. In Indonesia, this pattern appeared to be true at the provincial level, but the opposite was observed at the village level. In Zimbabwe, for a small sample of district councils, the results were also contrary to expectations: the higher the financial autonomy ratio, the lower the social allocation ratio. But this was largely due to the fact that central government transfers for basic education both reduced local financial autonomy and raised priority ratios.

The case studies suggest that decentralization would favour expenditure on human development. But this may not be true elsewhere. Many countries have local power structures dominated by elites little interested in human development. In Pakistan in 1985, members of parliament were each allocated a sum of money from the national budget to be devoted to development projects that met the needs of their constituencies. Most chose infrastructure priorities or more prestigious colleges and hospitals. Few chose primary schools or ba-

sic village health units. If the central government had not specified that at least 50% be devoted to basic education and primary health care, these concerns would have been neglected.

Since participation has thus far been quite limited, it is difficult to make a systematic assessment of its impact. This section therefore draws together some of the available information to help illustrate the major issues—showing what has happened in practice, what has worked and what has failed—summarized under efficiency, equity, economic participation and political participation.

### *Efficiency*

In theory, decentralization should improve efficiency. At the outset, projects would be better able to match local needs. And with projects monitored locally, lines of communication should be shorter, with fewer delays due to conflicts between project staff and the beneficiaries.

One of the most important benefits of decentralization is the opportunity to cut costs, in several ways. First, if local people feel that it is their money being spent, they are likely to keep a tighter lid on expenditure and to use resources more efficiently. In the Philippines, schools that rely more heavily on local funding are more efficient, and operate with lower unit costs, than comparable schools financed centrally. Similarly, in the Indian state of Karnataka, the involvement of local people through the *gram sabhas* (village meetings) led to a notable improvement in the attendance of teachers when they became more accountable to the local community.

Involving local people can also result in a more appropriate structure of services, particularly in health care. In Tamil Nadu in India, local community health workers have proved superior to junior doctors and nurses on health projects. Not only are they more effective—they cost up to 75% less.

Local involvement also opens up the opportunity for people to add voluntary contributions to amplify a programme or project's impact. In Kenya, high levels of local participation in the Rural Access Roads

Programme encouraged people to donate land to the project—and permitted the construction of 150 extra kilometres of roads, which would otherwise not have been built.

Some of the most effective contributions as a result of decentralization come from local labour and materials. In the Baglung district of Nepal, local committees working under the auspices of village councils built 62 bridges with little outside help, covering the whole district in five years. They used local materials and artisans, and no one was paid. Each bridge cost only a quarter of what the central government would have spent, and was built three to four times faster.

A final and lasting benefit of greater participation in the provision of local services is that they can be more efficiently run and maintained. In Guatemala, local involvement in the operation of 34 village water projects—villagers were trained in operation and maintenance—significantly increased their success rate. There, as in many other countries, the locally built systems have suffered fewer breakdowns, and the villages have had far fewer days without clean water.

Decentralization does not automatically produce gains in efficiency. If poorly planned and executed, decentralization can add to costs rather than reduce them. One common danger is duplicating layers of administration at national, regional and local levels. In Mexico and Venezuela, decentralizing the education systems increased costs because of the proliferation of different agencies.

Another risk is that the benefits of decentralization can be offset by losses in economy of scale. Some energy production, such as that through windmills, can be locally generated very efficiently. But the same may not be true of more conventional powerplants. In China in the 1980s, the construction of small local powerplants provided rural areas with much-needed energy. But the small plants proved much less efficient: for each unit of electricity, capital costs were about 30% higher and operating costs about 50% higher than those for centrally generated power—and they created more pollution.

*One of the most important benefits of decentralization is the opportunity to cut costs*

*Devolving power to regions, although promoting equity within them, can increase disparities among them*

And while decentralization may in some cases help raise standards of service, there is also the danger of letting standards slip. In Kenya, the *harambee* schools built through local initiative are generally inferior to the central government schools. The teachers tend to be poorly qualified, and levels of pupil achievement are low—only 13% of the pupils reach the minimum standards, compared with 80% for government schools.

Above all, decentralization should not mean that higher levels of government completely withdraw support from, or neglect, social services. In Ecuador, decentralization of the rural public health programme meant that there was no effective supervision or logistical support, resulting in severe delays and supply shortages.

For decentralization to increase efficiency, a lot depends on the technical and financial support offered to local governments—and on how much it attracts local leadership and captures local enthusiasm.

#### *Equity*

Most countries, particularly those in the developing world, have very uneven levels of development, with marked disparities between different regions, between urban and rural areas or between different income and ethnic groups. Decentralization certainly alters some of these balances—though it can either improve equity or reduce it. In general, devolving greater power to regions, although promoting equity *within* individual regions, can increase disparities *among* them.

Within the region covered by a local authority, the effect can be positive. If decentralization produces more effective government services, the effect will be redistributive—since poor people generally make more use of local public services than rich ones. But unless the central government takes compensatory action, decentralization can increase the disparities between various regions and districts. Passing more responsibility for taxation and expenditure to local governments can benefit richer areas.

One reason for this is that richer areas have more political influence and can lobby

more effectively for resources. In the Mexican state of Guerrero, decentralizing the health system allowed the wealthier areas to negotiate higher budgets. As a result, people living in the tourist areas and in the most important cities were better off, while the Indians and peasants living in small dispersed settlements suffered a significant decline in services.

Decentralization can also heighten inequalities if more of the services are funded locally—poorer areas can afford less. In Zambia, transferring some recurrent costs for primary education from the central government to the district level and to parents tended to increase interregional inequality. Parental spending on books and other materials in the six poorer regions was only half that in the three richer ones.

In general, decentralization causes interregional disparities to worsen unless the central government takes strong action. Some have done this through their systems of grants to local governments. Rather than just allocating funds on a per capita basis, they also take relative poverty levels into account. Brazil redistributes its tax revenue preferentially to the poorest states. In 1976, for every 100 cruzeiros it collected in taxes set aside by law for transfer to the states, the federal government returned only 25 cruzeiros to the richer states in the South and South-East while giving 75 cruzeiros to those in the poorer North.

The same principle can also be applied at lower levels of government, particularly for states in federal systems. In Uttar Pradesh, India, grants are distributed to districts on a criterion of “backwardness”—as indicated by the condition of their infrastructure and the proportion of their population in “scheduled castes”. This arrangement, introduced in the process of decentralization, has helped reduce disparities between districts.

Another approach is to redistribute locally raised revenue. In Chile, the *Fondo Común Municipal* follows a set formula to pass revenue from the property and business taxes of the richer municipalities to spend in the poorer ones. In the metropolitan region of Santiago, this effectively reduces the per capita revenue of the three



richest municipalities by 7–14%, while increasing that of the poorer ones by 35–50%.

Another way of containing interregional disparities is to set minimum national standards in various social services that the central government undertakes to finance and maintain—irrespective of local resources.

### *Economic participation*

Decentralization can increase economic participation by facilitating local entrepreneurial activity, and thus increasing employment, in several ways.

- *Increased public expenditure*—The construction and maintenance of local infrastructure, such as roads, water supply and electricity, will directly employ local contractors and workers.
- *Higher-quality services*—Local facilities are likely to be more appropriate and better maintained if the local community influences their construction. They will thus be of more use to local entrepreneurs and help increase their profitability.
- *Better support for entrepreneurs*—Local governments might be able to offer better support to local business. They can offer management assistance and market information tailored to local needs. They are also in a much better position to cater to the needs of scattered rural enterprises.

In rural areas, one of the most important routes to increased economic participation is through land reform. In Taiwan (province of China), land reform in the 1950s and 1960s had a significant impact, not just on economic growth but on its spatial distribution—creating some 200,000 new owner-farmers as well as many new job opportunities in the rural areas. This, together with the decentralization of infrastructural improvements across the island, seems to have encouraged balanced growth of agriculture and industry and avoided overconcentration of population and economic activities in the metropolitan areas.

The distribution of government grants is another way of increasing economic opportunities in poorer regions. In Indonesia, the transfer of resources through block grants has probably promoted better

growth rates in relatively poor regions, especially in the eastern islands.

Economic participation can also be increased by decentralized investment strategies that promote small-scale industries and make better use of local resources, raw materials and skills. In Tanzania, this has promoted local production of goods and services that would otherwise have had to be imported, using up scarce reserves of foreign exchange.

Nevertheless, there are many cases where decentralization does not seem to have produced tangible economic benefits—often because it has not been carried through with sufficient resources or conviction. In Zimbabwe, the government tried to promote regional industrialization through a “growth point” strategy. But the results, with a few exceptions, have been disappointing—perhaps because of the limited financial devolution, or the continuing centralizing tendency of government controls.

Similarly in the Philippines, the Regional Cities Development Project was designed to reduce some of the grave economic imbalances between regions—by developing urban infrastructure, and strengthening the management capabilities of the city governments. A 1988 study of the impact in Iloilo City concluded that the project had not yet induced economic growth. Some infrastructure had improved, particularly the port and the road system. But the city still lacked the adequate supplies of water and reasonably priced electricity that heavy industry needed.

Identifying a local economic effect specifically linked to decentralization is not easy. Economic development is, of course, subject to numerous other influences, from the government’s macroeconomic policy and development strategy to its choices on investment in both infrastructure and human resources. But in general, there is little systematic hard evidence.

### *Political participation*

If participation takes the form of deconcentration and delegation, the centre will retain effective control, and an increase in political participation is unlikely to result.

## *Decentralized investment strategies can increase economic participation*

*Democratic regimes are the most likely to encourage genuine decentralization and popular participation*

Devolution, by contrast, should lead to fuller political participation. But not necessarily, since power may merely be devolved to non-democratic and non-participatory local institutions. Indeed, devolution in some cases could require a strong central government to ensure that local administrations respect national standards on such matters as women's rights and civil liberties.

Three country case studies show the diversity of decentralization's possible outcomes.

*Indonesia's* central government, despite commendable decentralization, retains strong political control. Even where power is delegated to provinces or *kabupaten* (regions), it passes only into the hands of people appointed from above: the governors of provinces and the heads of *kabupaten*, who often come from the military. Both provinces and *kabupaten* also have legislative bodies, but their powers are largely advisory.

*Chile's* system of local government has passed through different stages in its recent turbulent history. The military government from 1973 onwards removed the elected local mayors and councils and replaced them with appointed mayors. The re-establishment of national democracy in the 1990s saw the return of local democracy: elections were reinstated for mayors, local councils and neighbourhood groups—and indirectly for regional councils.

*Zimbabwe*, since independence, has offered local people the opportunity to participate in the planning process through elected village and ward development committees, but this participation varies considerably. Some committees are dominated by traditional leaders, and there is relatively little participation. A 1985 survey discovered that many people did not know the name of their councillor or even that the committees existed. In some places, however, there is wide local participation and a high level of debate, particularly where there are substantive financial decisions to be made—on the revenue raised from wildlife, for example. But Zimbabwe also has separate rural councils in the white farming areas, which retain their pre-independence structure in that only tax-

payers and their spouses have the right to vote.

Other developing countries show a diversity of experience. Decentralization has often merely taken the form of deconcentration and permitted the centre to retain strong political control. *Zambia*, for example, has had a policy of "deconcentration in centralism". Some political power has been passed to the district level but is exercised by party officials and political appointees. Whether the opening up to a multiparty system and the election of a new president have caused significant changes remains to be seen.

*Peru*, like *Chile*, has seen significant changes in the status of local government as central government regimes have changed. The authoritarian military regimes in the 1970s were determined to retain strong political control. But more recent democratic governments have emphasized political devolution. Indeed, before the recent setback to democracy, the previous government was attempting an extensive programme of devolution to regional and local levels.

The authoritarian regime in the *Philippines* up to 1985 also made a point of strengthening central power over local government. It created the new *barangays* as the main administrative unit of the country. While purportedly aimed at broadening local democracy, in practice these were led by people loyal to the regime and they primarily served to extend central control and political mobilization. More recently, the Philippines has adopted a promising local government code, which transfers responsibility for public works, agriculture, health and social welfare to the *municipios*, a level above the *barangays*. And for this purpose, the *municipios* will, over the next three years, be allocated 40% of all taxes. But exactly how this will be implemented has yet to be resolved.

Experience in many developing countries suggests that democratic regimes are the most likely to encourage genuine decentralization and popular participation. Authoritarian or single-party regimes, whether from the "right" or the "left", generally limit decentralization to deconcentration and aim to retain strong central control.

The shift towards multiparty democracy throughout the developing world is therefore a very promising sign.

### **The reality of decentralization**

Decentralization of local government has the potential to improve government decisions with increasing democratic participation. As decisions are brought closer to the people they affect, expenditure on priorities often increases and efficiency of resource use improves. But this potential is realized only where there is genuine decentralization to democratic structures. We have found that:

1. *There is not much evidence of full devolution in many developing countries.* On average they are merely delegating less than 10% of total government expenditure to local governments, and less than 6% of total social expenditure. The taxation powers of most local authorities remain fairly limited.
2. *Where there has been some form of decentralization, it has generally increased efficiency.* This can be a result of lower costs, better maintenance, closer monitoring and supervision and the use of voluntary local labour. Decentralization also enables local people to insist that human priority concerns move to the top of the local development agenda.
3. *Where decentralization occurs, it often leads to better priority ratios.* This is partly the

result of government rules allocating basic expenditure to the local level. But it also occurs as a result of choices made by democratic local governments. Care must be taken in non-democratic states, especially where local governments are dominated by elites who may neglect social priorities.

4. *Decentralization needs to be accompanied by central government action to reduce existing disparities among regions and districts.* Central governments need to devise innovative formulae to redistribute tax revenue from richer regions and districts to poorer ones. They can fund the implementation of minimum standards to be maintained throughout the country.

5. *Effective decentralization is not possible without the reform of existing power structures.* If power remains concentrated in the hands of elites—as is still the case in many developing countries—decentralization might further empower the elites rather than the people.

Many of the most effective forms of decentralization are not, however, based on the institutions of local government. Some of the most important local bodies, which can serve as a countervailing power to the influence of central government, are voluntary associations—including people's organizations and non-governmental organizations, the subject of the chapter that follows.

*If power remains concentrated in the hands of elites, decentralization might further empower the elites rather than the people*

# Chile

CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	33%
EXPENDITURE DECENTRALIZATION RATIO (1990)	8%
REVENUE DECENTRALIZATION RATIO (1990)	5%
FINANCIAL AUTONOMY RATIO (1990)	62%

Chile's decentralization experience can be divided into three periods. First, the governments of Frei and Allende continued Chile's long democratic tradition of broadly based but centralized services. Next, the Pinochet dictatorship drew all political power to the centre but decentralized services. Then, the government of Aylwin restored local democracy, continuing with the decentralized services.

During the earlier democratic periods, there were elected municipal councils and various neighbourhood groups, which General Pinochet abolished, replacing them with a military hierarchy that included centrally appointed governors and mayors. He also gave municipal governments greater responsibilities for the delivery of services, particularly education and health. Municipal leaders thus became "service delivery agents" without local governing power.

Decentralization was initially accompanied by an increase in resources for local authorities. First, more of the locally raised property taxes could be spent locally. Before 1979, municipalities received only a fraction of the revenue—after, they got all of it. They could retain some 40% of the property tax and receive the rest through a redistribution among municipalities through a *Fondo Común Municipal*. This took 60% of the property tax, 50% of the vehicle tax and a proportion of the receipts from a tax on business in three high-income municipalities.

The second major new source of income took the form of flat subsidies to allow municipalities to provide basic education and primary health care. This payment system, intended to give municipalities an incentive to control costs, resulted in their subsidizing these services from elsewhere in their budgets—and running deficits.

For primary and secondary education, the central government has given a flat subsidy per pupil. This could go either to municipal schools or to new private (non-fee-charging) schools. But its real value fell through the 1980s, and municipal schools suffered because, while they lost pupils to the private sector, they could not readily cut their costs proportionately. In the health services, the flat payments to municipalities were in line with specific services provided. But these, too, failed to keep pace with costs and inflation.

The decentralization programme also dispersed some investment. A new Regional Development Fund was established in 1975 to finance projects in health and education, as well as minor infrastructure projects such as rural roads. These funds are distributed in response to project submissions by municipalities and regions, supposedly weighted towards the poorer communities.

This fund currently amounts to about 15% of the public sector investment budget, and there is a proposal to increase it by 25%. There is also an additional mechanism for sectoral ministries to allocate a small part of their funds (around 5%) to regional governments, which are free to select their own projects.

As a result of these reforms, Chile's revenue and expenditure decentralization ratios rose sharply during the 1980s. Municipal revenue rose to 6% of total government revenue, and the expenditure ratio to 8.3%. But since health and education are financed by transfers from the central government, the financial autonomy ratio fell sharply. Even so, municipalities in 1990 financed 60% of their activities from their own resources. There was nevertheless some decline in the decentralization ratios between 1988 and 1990. For investment, however, the municipalities depend more heavily on outside money. They finance only 16% of investment in their area (another 16% comes from the various regional funds, 68% from central ministries).

A major objective of Pinochet's policies was to increase the professional level of local government employees, and he seems to have succeeded. Professional and technical staff as a proportion of municipal employees rose from 8% to 33% between 1975 and 1988—a result of, among other things, increased staff training but also contracting out more of the unskilled work.

In the quality of services, the outcome of decentralization was mixed. The standards in municipal schools fell, and the differences between social groups widened. Private schools (which by 1986 had 31% of the school population) did rather better, though the differences were not so marked when controlled for socioeconomic status (the lower socioeconomic groups tended to do better in the municipal schools). The secondary enrolment ratio increased, and the number of years required for pupils to pass through the system fell.

In health, the resource picture is similar. Decentralization was accompanied by a cut in real resources and the introduction of some user charges. Public expenditure on health fell from 3.3% of GDP to 2.4% in 1988 (due to the privatization of contributions and services among the upper-income groups). But the outcome for health standards was generally positive with continuing (and marked) reductions in infant mortality rates and maternal mortality. In both health and education, the larger and richer municipalities did better than the others.

On balance, the outcome of decentralization in Chile seems to have been positive—and the situation should improve further as the present government combines it with more local democracy.



# Indonesia

CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	20%
EXPENDITURE DECENTRALIZATION RATIO (1989)	19%
REVENUE DECENTRALIZATION RATIO (1989)	8%
FINANCIAL AUTONOMY RATIO (1989)	25%

Indonesia's widely dispersed territory argues both for a unifying central state to hold the country together—and for extensive decentralization to match government to local needs. The country's 188 million people live on more than 13,000 islands covering more than two million square kilometres—60% of the people live on the island of Java, with 7% of the land area. The government, in power since 1965, initially placed its emphasis on national unity and economic stabilization. But since the mid-1970s, it has paid increasing attention to economic growth, regional development and decentralization.

Indonesia is formally a parliamentary democracy, but authority for decisions is concentrated in the presidency. The elected assemblies at central, provincial and district levels can debate and advise, but the president and his ministers make most decisions. And though governors of the 27 provinces are elected by the provincial assemblies, the president has to confirm their appointment. In addition, the central government has officials dispersed throughout the country to assist with decisions. This has made Indonesia's planning system good at transferring commands from above, but not very sensitive to local priorities.

Local governments raise 25% of their financing from their own taxes and fees, with the rest coming from central government transfers and grants. Their largest source is the property tax, collected by the central government but given to districts. Local governments are responsible for the delivery of most health and education services, for which they receive direct transfers from the central government. These transfers come through the INPRES programme, Indonesia's principal means of decentralization. In the 1991 budget, these transfers accounted for 12% of total development expenditure and 51% of local government development expenditure.

INPRES funds, as block grants to each province or locality, come in two forms. First, there are the "general" funds intended to promote regional autonomy and improve local infrastructure. These are not centrally controlled, but they are subject to "general guidelines", strict for provinces though less so for districts. Another INPRES grant provides lump sums directly to each of Indonesia's nearly 67,000 villages. These grants are small but can be used for almost any purpose. Second, "specific" grants go only to the district level and are earmarked for specific purposes by the central government—say, for the construction of schools or their running costs. Districts have limited discretion on how to use these grants.

Indonesia's national budget, and the INPRES grants, are strongly influenced by the flow of oil revenue. Between 1975 and the mid-1980s, oil income rose to more than 50% of central government revenue—but then dropped to 41% in 1988–89, and INPRES grants also fell.

Provincial authorities do not, on average, have much financial auto-

my, though the position varies considerably. At the provincial level, "own" funds as a percentage of the total range from 8% to 70%. At the district level, own funds controlled by local governments range from 4% to 56% of the total. Jakarta, with its diversified service and industrial economy, has plenty of scope for generating local revenues.

At both provincial and district levels, the proportion of total funds spent on development tends to rise as the financial autonomy ratio rises. And provincial governments spend a higher proportion of their funds on social investment than does the central government. In 1988–89, the local social allocation ratio was more than four times that of the central government, though the ratios are about the same when it comes to infrastructure investment. Again, however, there is considerable variation in the spending patterns. At the provincial level in 1983, social expenditure as a percentage of development expenditure varied between 8% and 43%, while infrastructure investment varied between 20% and 66% of development expenditure.

The system of decentralizing expenditure seems to have produced substantial improvements in basic services in health and education. In education, the government was generous with funding for investment in the 1970s, and although this dropped as oil revenues fell in the 1980s, education standards continued to improve. Government investment in education is also becoming more redistributive, as provinces with lower literacy rates receive a higher share of investment funds.

The picture is similarly positive for health. Resources declined in the 1980s, but standards continued to rise, probably reflecting increased investment in health by local governments. The number of health centres rose significantly, infant mortality fell by nearly 50% and life expectancy rose by eight years. The central government grants favour to areas with below-average health levels, and the variation in health standards between the regions decreased between 1976 and 1987.

A major problem is that many local authorities have proved ill-equipped to implement development projects. So far, the strengthening of local capacity has mostly entailed improving the professional standards of central officials stationed at lower levels of government, not those of local people. And since local government officials are paid out of central government allocations and their promotion and pay depend on central government decisions, any real devolution of decision-making is difficult.

By international standards, the real degree of decentralization in Indonesia is not high, but it is substantial for a large country with a unitary form of government. As the economy becomes more complex and regionally specialized, Indonesia will inevitably have to move towards greater decentralization and to improve the efficiency of local tax collection to provide local governments with additional revenue and autonomy.

# Morocco

CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	30%
EXPENDITURE DECENTRALIZATION RATIO (1986)	6%
REVENUE DECENTRALIZATION RATIO (1988)	8%
FINANCIAL AUTONOMY RATIO (1988)	108%

Morocco has undergone a steady process of decentralization in recent decades. Until 1960, the country was organized through traditional assemblies—*jmaa*—based on ethnic groups. These have been largely replaced by a system based on territory: seven regions, 60 *préfectures* or provinces, and 1,544 *communes* (1,297 rural and 247 urban).

Each commune has an elected president and assembly. The commune *councillors* in turn elect councillors for the *préfectures*.

The activities of the communes were greatly enlarged in 1976 to include responsibility for the management of a large number of local services, including water, sanitation, electricity and transport, as well as primary schools, health centres and vocational training. And the president of the commune was given considerable legal powers for local administration.

Alongside this increased responsibility went an increased flow of resources. In 1977, the revenue of the communes represented 5% of total public revenue, but by 1991 it had reached nearly 11%.

In 1988, the communes were given financial autonomy. Previously, the government made grants to help local authorities balance their budgets, but it has since decided to give them 30% of the proceeds of the value added tax (VAT). The local authorities do not consider this sufficient to meet the obligations placed on them. For capital expenditure, many have had to take loans from the *Fonds d'Équipement Communal*. They have therefore been pressing for an additional share of the VAT—to be distributed more on the basis of local needs and levels of development.

Decentralization has certainly changed the character of spending by local authorities. Between 1977 and 1987, the proportion of their budgets devoted to capital expenditure rose from 26% to 53%. And while the communes made 3.5% of total public capital expenditure in 1987, their share reached 17% by 1991.

The staff of local authorities has also increased—by 210% between 1977 and 1991. And to ensure an adequate supply of qualified personnel,

several vocational and administrative training centres have been established. In 1991–92 alone, 1,571 people were being trained, 12.5% of those trained over the past 35 years. The rural communes were given special attention, being allocated university graduates such as doctors, veterinary surgeons and agronomists. Even so, there is a marked disparity in personnel between urban and rural areas. The urban areas have more than three times as many staff per 1,000 people as the rural ones.

The educational levels of the local councillors have also been a matter of concern. In 1983, a survey of the presidents of local councils found that 16% had no schooling, and of the rest, 39% had no more than primary education—let alone the experience in administration and finance that would allow them to work efficiently. Several political parties have organized training sessions for their members.

As far as the ordinary people are concerned, many features of the recent decentralization have offered considerable improvements. Administrative procedures have been speeded up—it now takes much less time to get many of the official certificates and licences. And people have plenty of opportunities to bring their complaints to the communal assemblies.

For services, it is too early to say whether education standards have been affected, but the health services have improved. One indicator is the substantial reduction in the time taken to walk to the nearest health centre. In 1979–80, 51% of households could reach a centre in less than an hour, and in 1990–91, 78%. And while more than half the patients previously had to wait more than an hour for a consultation, ten years later that proportion had dropped to less than a quarter.

The process of decentralization in Morocco is under constant review. So far, there have been five national conferences to bring together elected councillors, government officials, academics and representatives from the private sector. These allow for a critical assessment of the successes and failures of decentralization as well as a sharing of experience.



# Zimbabwe

CENTRAL GOVERNMENT EXPENDITURE AS % OF GNP (1990)	41%
EXPENDITURE DECENTRALIZATION RATIO (1986)	20%
REVENUE DECENTRALIZATION RATIO (1986)	6%
FINANCIAL AUTONOMY RATIO (1986)	27%

The first democratic government inherited a highly centralized system in 1980 and has since established laws and procedures to devolve responsibility to lower levels of government—with limited impact. Although a government that grew out of a war of liberation with strong local roots might have had a headstart in establishing a decentralized state, Zimbabwe's restructuring of local government has essentially been a top-down initiative, partly due to the disarray of traditional structures in the wake of independence.

Before 1980, local government was divided on the basis of race. The whites elected their own urban and rural councils, while the black communal lands had African councils. After 1980, the government retained the white councils but consolidated the previously fragmented African councils into 55 district councils. Above both white and black councils, the eight provinces have appointed governors and provincial administrators.

The white rural councils and the black district councils were the subject of amalgamation legislation in 1988. But compromises undermined this effort to end the colonial legacy of separate development. The district councils are elected bodies, though they have some chiefs and headmen as ex-officio members, with a district administrator responsible for overall planning, development and coordination.

The district councils raise only 15% of their total revenue—through taxes, fees and other charges. Secondary school fees are the most important component—and in 1984–85, they made up 60% of local revenue, with substantial variations among districts. Districts also apply a “development levy”, a form of poll tax on all adults. Very unpopular, this has proved difficult to collect. Although the district councils have generally been raising an increasing proportion of their revenues, they still depend heavily on the central government. The urban councils do rather better. They receive a significant proportion of revenue from taxes on property, as well as a levy on beer, and manage to raise between 80% and 90% of recurrent revenue.

Local authorities raised only 6% of total government revenue in 1986, and they have almost no financial autonomy. In education, the ministry administers grants under the heading “tuition” and interprets this very narrowly to encompass only spending directly related to classroom learning, such as textbooks or chalkboards.

In 1984, the government established a hierarchy of representative bodies—development committees—at village, ward, district and provincial levels. The idea was to mesh bottom-up and top-down planning. These bodies were to draw up development plans and projects for central funding, but the links between national and local bodies have proved weak. The national plan, for example, is finalized before the regional ones, and in practice the key decisions for the operation of sector ministries have continued to emanate from Harare, where local efforts are often (literally) shelved.

In 1990, the social allocation ratio for central government expenditure was 36%. One possible indicator of local priorities is the preference expressed through requests for funding in the local plans—though these, too, may be influenced by central government, as districts might request funds for projects they believe the centre will fund. Analysis of a sample of development plans of district councils revealed that social development made up 39% of total bids, with agriculture next in importance at 30%. On the whole, the evidence suggests that more devolution of decision-making would focus public attention on infrastructure and priority social services.

Decentralization can also affect equity. The most striking inequalities in Zimbabwe are between the white minority and the black majority, but there are also wide divisions within the black communal areas. A 1991 sample survey indicated that the top 10% of households controlled 42% of measured income, the lower 50% only 15% and the bottom 25% less than 5%.

The clearest change in equity has been to focus attention on the communal lands. Since 1980, the school construction programme has increased the number of primary schools in communal lands by 86% and that of secondary schools by more than 700%. The number of village health workers increased 26-fold, and the share of the population with access to safe water has increased from 33% to 55%.

The distribution among the provinces has been less progressive. In fact, more public resources are directed at provinces with the highest per capita incomes. In health, Harare and Bulawayo, the two provinces with the four central hospitals, receive 1.4 to 2.7 times more per capita expenditure than the other provinces, even after adjusting for out-of-province patients. And the expenditure on water supplies is greater for those provinces that already have better facilities. Similarly, at the district level, a sample of 16 districts for 1982 and 1985 revealed that both central government grants and local government revenues were lowest in the neediest areas.

In principle, people can be involved at all levels of decision-making in Zimbabwe, from the village through wards and districts to the province. In practice, participation is much more constrained. Local decision-making is often dominated by central government employees: the village community workers, for example, often “tell” the community what its needs are, rather than allow for the people's participation. And local interests are often represented by a small elite: ward submissions to district councils are often prepared by the ward chairmen without consulting the local community. Overlaid on all this is the role of the ZANU (PF) party, which generally carries more weight than local government.

Zimbabwe has taken many significant steps towards decentralization in the short period since independence, but this has been constrained by the historical context of race and class.



## People in community organizations

*People are more likely to be excluded than included in civil and political life*

People's understanding of the world is formed and nurtured in face-to-face interactions in small social groups—first in the family, then the street, perhaps, or the neighbourhood or village. Such groups also serve a political purpose, for people generally gain greater benefits in groups than as individuals.

As people move outside such groups, however, they find the wider world organized on very different principles, and they are more likely to receive decisions handed down from on high. Whether in social services, in markets or in civil and political life, they are more likely to be excluded than included.

The problem is partly practical. Many facets of modern life cannot be confined to the home, village or street. The complexity and the sheer numbers of people involved reduce the possibilities for face-to-face interaction. The intrusion of market values also plays a part, with many more goods and services now obtained with hard cash than through mutual exchange within the community.

In time, countries develop the institutions of civil society—a fair judiciary, a responsive executive, a free press and traditions of transparency, accountability and fair play. Group action is often necessary for the evolution of such institutions and for ensuring that they continue to respond to people's aspirations for genuine participation.

But governments in developing countries often discourage such participation. Starting from a "top-down" development philosophy, they have generally concentrated on providing food, services or assets—rather than enabling people to do more for themselves. Governments have seen devel-

opment as something to be done for, rather than by, people—stifling many grass-roots initiatives, holding them in check, rather than nurturing and extending them.

Things are changing. Many community groups now command the attention and respect of governments in many developing countries. The energy of the people who form them, and the creative solutions they demonstrate, have helped persuade governments of the value of involving participatory community groups. Donors, too—disillusioned with the performance of much official aid—are passing more of their money through non-governmental channels. As a result, there has been an explosion of participatory movements in most developing countries.

The community organizations driving those movements are by their nature difficult to classify and analyse. This Report refers to two broad types: people's organizations and non-governmental organizations (NGOs).

*People's organizations* can be defined as democratic organizations that represent the interests of their members and are accountable to them. They are formed by people who know each other, or who share a common experience, and their continued existence does not depend upon outside initiative or funding. In developing countries, many of them are small, locally based and loosely established. But they need not be confined to the grass roots—they can spread upwards and outwards from the local to the regional and national level, representing networks of community groups, or professional groups or trade unions.

*Non-governmental organizations (NGOs)* can be defined as voluntary organizations that work with and very often on behalf of



others. Their work and their activities are focused on issues and people beyond their own staff and membership. NGOs often have close links with people's organizations, channelling technical advice or financial support as intermediate service organizations. But organizationally NGOs can be quite different from people's organizations, often having bureaucratic hierarchies without the democratic characteristics or accountability of most people's groups.

The distinction between the two is not rigid—many groups could reasonably fall into either category.

### People's organizations in developing countries

The idea to form a people's organization can come from the people themselves—as with those traditional self-help groups in Asia and Sub-Saharan Africa in which people come together to pool their labour, to obtain credit, to buy goods in bulk or to promote and develop more sustainable forms of agriculture (boxes 5.1 and 5.2). Or the impetus can come from outside the group, perhaps from a dynamic individual who recognizes a community's needs and suggests ways they could meet them (box 5.3).

Sometimes, the groups are formed in response to a failure by government to provide infrastructure or services. The Cairo Public Housing Project was set up in the late 1970s as a result of prolonged government neglect of poor neighbourhoods. The aim was not just to provide some of their own housing, water and sewerage but also to induce the government to provide such services (box 5.4).

In other cases, it is what the government does that prompts groups to form. Police brutality, political oppression or the infringement of civil liberties has shown the need in most countries for groups that protect human rights, as with *Action Sociale et d'Organisation Paysanne* in Zaire.

People's organizations can also arise because the market fails to offer them the goods or services they need. The Self-Employed Women's Association in India is a striking example of how poor and disadvantaged people can enhance their bargain-

ing strength through cooperation (box 5.5).

How many people's organizations are there? It is impossible even to come up with a reliable estimate, for a phenomenon so flexible and dynamic can never be captured in statistics. But here are some illustrative figures:

- *Kenya* has 23,000 women's groups alone.
- *Tamil Nadu* state in India has 25,000 registered grass-roots organizations.
- *Bangladesh* has at least 12,000 local groups that receive local and central government financial support (and many more that do not).

BOX 5.1

#### Self-help farming groups

Farmers all over the world have traditionally come together in self-help groups, particularly to share their labour. Neighbours might, for example, arrive on an appointed day to help work one farmer's land. Not paid, but fed, any of them can ask for similar help from the others.

In a more formal arrangement, farmers might, on a rotating basis, help each other prepare land for the cultivation of various crops. Widespread in Africa, this form of cooperation goes under the names *nhimbe* and *janganjo* in Zimbab-

we, *owe* and *are* in western Nigeria and *mbobea* in south-eastern Ghana.

Self-help groups have also been formed to provide credit, normally among people with similar incomes, though individuals might join several groups if they meet the requirements. These groups also have a variety of names: *esusu* among the Yoruba people of western Nigeria, *susu* in Ghana, *ibim-ina* in the Kivuye commune in northern Rwanda, *tonlines* or *njangis* in Cameroon, *cheetu* in Sri Lanka and *samabaya* in Bangladesh.

BOX 5.2

#### Mexico—Union de Ejidos Julio Sabines

In the 1970s, poor rural farmers migrated to the rainforest region of Marques de Comillas, near Mexico's border with Guatemala. Their shifting cultivation practices, combined with cattle ranching by more powerful groups, deforested some 40% of the area. In 1988, the Mexican government responded with a ban on the cutting of trees.

The ban drew a strong reaction from the farmers represented by the *Union de Ejidos Julio Sabines*. They held meetings with government agencies—discussing soil erosion, river flooding and changes in rainfall as a result of deforestation. They also discussed global warming—with some farmers pointing out that the international community should, if it wanted them to stop cutting trees, offer some compensation.

The majority, however, agreed to work with government agencies to develop sustainable forms of agriculture and look for alternative sources of income.

For the past four years, they have successfully developed farming techniques for both food and commercial crops, using natural fertilizers without using more land. They are also cultivating forest products for sale, as well as breeding some of the forest animals.

The government has provided medical and educational services and support for Indian communities—and created a special task force for community development.

As a result, the rainforest is being used and preserved—and the local community is flourishing.

- *The Philippines* has 18,000 registered NGOs, of which at least two-thirds might be considered people's organizations, such as community associations or cooperatives.

- The OECD suggests that there were up to 20,000 NGOs in developing countries in the 1980s, a considerable underestimate—the number is probably closer to 50,000 and could well be higher.

- The OECD's Directory of NGOs had information on more than 2,500 NGOs in the 25 OECD countries in 1990, up from 1,600 in 1980.

Among the largest people's organizations in both industrial and developing countries are the trade unions, which have offered the most significant form of group

participation in the workplace. There might have been little that individual workers could do to influence the employer, but when individuals cooperated with the rest of the workforce—and with the ultimate threat of a mass strike—employers had no option but to listen and reach a compromise.

The wave of democratization of the 1980s received much of its impetus from trade unions. In Latin America, the unions in Argentina, Bolivia, Brazil, Ecuador and Uruguay—and most recently in Chile—were often the major source of opposition to dictatorships. In Asia, the unions have also been instrumental in democratization: in the Republic of Korea, it was a wave of strikes in 1986–87 that led to many democratic reforms.

In Africa, too, the trade union movement, though small in numbers, played a disproportionately large role in the moves towards multiparty democracy. In Mali, the National Union of Malian Workers organized nationwide strikes to bring down the government in 1981, and its secretary-general became vice-president of the transitional government that helped bring in a civilian administration in 1992. In Zambia, the Congress of Trade Unions was in the forefront of the opposition to the previous one-party state, and in the subsequent multiparty elections its leader was voted in as the new president.

In Eastern Europe and the Soviet Union, the new workers' organizations—Solidarity in Poland, Podkrepa in Bulgaria, Fratia in Romania, the miners' strike committees in the Soviet Union—propelled the moves towards democracy.

### Non-governmental organizations in developing countries

NGOs cover a very wide spectrum, from small loose-knit local organizations to nationwide federations and international networks. And the issues they tackle might be anything from the human rights of one ethnic group to the entire mosaic of development concerns.

NGOs sometimes grow out of one people's organization, extending its principles

#### BOX 5.3

##### Pakistan—the Orangi Pilot Project

Orangi, a suburb of Karachi, Pakistan's largest city, has grown rapidly and now has more than 700,000 people crowded into it.

Akhtar Hameed Khan came to Orangi in 1980, a charismatic leader with considerable experience in organizing community self-help from his previous work in the Comilla project in Bangladesh. He found that housing was poor, sanitation and drainage facilities inadequate, health problems on the increase and epidemics frequent.

Khan was convinced that the best way to deal with Orangi's problems was to shun outside help and strengthen the capacity of local people to help them-

selves. The Orangi Pilot Project concentrated on five areas:

- Low-cost sanitation
- Low-cost housing
- Women's work centres
- Women's welfare programmes
- School education.

The results have been spectacular. The sanitation programme involves 28,000 families that have constructed some 430,000 feet of underground sewerage and built more than 28,000 latrines. They financed this with 30 million rupees (\$1.2 million) of their own savings, at a cost of \$66 per house—about one-quarter of what it would have cost local government.

#### BOX 5.4

##### Egypt—Cairo public housing project

Khalafaway, like many Cairo neighbourhoods, deteriorated greatly in the 1960s as a result of prolonged neglect by the government. Blocked sewage systems and piles of garbage in open areas were contaminating the drinking water and producing other serious health threats.

Disgusted by the deteriorating conditions, the Khalafaway neighbourhood started a self-help project in 1978 to improve its environment. Using their own money and volunteer labour, the people in the neighbourhood replaced broken water pipes, unblocked the sewage sys-

tems, cleared the garbage and organized regular collections. They also created a children's garden.

Three years later, these self-help efforts found a strong ally in Wafaa Ahmed Abdalla, a senior expert with the Institute for National Planning in Cairo. She developed a more scientific approach for community improvement and started training programmes for local people. As a result, five more self-help projects emerged in public housing neighbourhoods, enabling 5,000 residents to improve their environment.

and ideas to other places. Or they can be an amalgam of people's organizations coming together.

Or they can be offshoots of larger organizations, often churches that set up NGOs or task forces to tackle particular problems. In Chile, the Catholic Church established the *Vicaría de la Solidaridad* to expose atrocities and provide support to victims during the Pinochet regime. The Justice and Peace Commission in Rhodesia played a similar role under the Smith regime.

On other occasions, a group of like-minded people might set up a new NGO in response to a national problem. They might focus attention on women's issues, as in the Dominican Republic, where the *Centro de Investigación para la Acción Feminina* is committed to changing the status of women in the country (box 5.6). And in recent years, many new groups have been established around environmental concerns—as in the Philippines, where the Green Forum aims to raise the consciousness of local communities and the government on environmental protection.

Many NGOs have placed much of their emphasis on empowerment. The formal purpose of a programme might be improvements in health or literacy or agriculture, but NGOs have also been concerned with how much each project enhances people's power. And they have been particularly determined to empower the poor and marginalized—many say that their prime constituency is the "poorest of the poor".

Most NGOs work with, and through, people's organizations, offering financial and other support. The links can be established in different ways. In much of Africa, NGOs usually provide assistance to existing people's organizations. In Bangladesh and India, the NGOs often take the initiative to form new people's organizations. In Latin America, both approaches are common.

Other NGOs confine themselves to advocacy—mobilizing the public to put pressure on the government to act on a particular issue. Human rights is a common focus, as with the *Foro Nacional por Colombia* and the Shuar Federation in Ecuador.

Many others take on both roles—material help and advocacy—and their links with people's organizations give them unique sources of information and authority. The *Comissão Pastoral da Terra* in Brazil offers support to landless groups and argues for their rights at both national and international levels.

At a final level of cooperation, NGOs also link up with other NGOs in networks to enable them to present a common front to regional or national governments and to international agencies like the UN. In India, individual states have networks of NGOs—such as the Federation of Voluntary Organizations for Rural Development in Karnataka, and the Association of Volun-

BOX 5.5

#### India—Self-Employed Women's Association

The Self-Employed Women's Association (SEWA) is a trade union of poor women in Ahmedabad, India (in Hindi, *sewa* means service).

SEWA draws its membership from three types of workers: petty vendors and hawkers, home-based producers and those who provide casual labour and other services. Although it started in response to the needs of urban women, SEWA now also covers rural women in agriculture and other sectors.

SEWA's aim is to enhance women's income-earning opportunities as well as their working environment. It does this in several ways:

- Savings and credit cooperatives provide working capital to hawkers, vendors

and home-based workers.

- Producer cooperatives help women get better prices for their goods.
- Training courses impart such skills as bamboo work, block printing, plumbing, carpentry, radio repair and accounting and management.
- Legal services enable women to obtain the benefits of national labour legislation. Until SEWA was formed in 1972, the women in the informal sector were not recognized as workers, either in law or by society.

SEWA has also developed a welfare component. It now gives assistance to its members through a maternal protection scheme, widows' benefits, child care and the training of midwives.

BOX 5.6

#### Dominican Republic—Centro de Investigación para la Acción Feminina

The *Centro de Investigación para la Acción Feminina* (CIPAF), a women's NGO in the Dominican Republic, is promoting lasting social change in the status of women. It tries to engineer basic changes in attitude through programmes of research, education, training and public information. By mobilizing the energies of middle-class women, it has organized over 200 workshops, trained thousands of workers and issued 31 publications.

One of CIPAF's major studies has

been *Mujeres Rurales*—a report on the condition of peasant women. It followed this up with a nationwide information campaign to highlight the findings of the report and seek concrete changes in government policy. It is now completing a sequel on the problems of urban women.

CIPAF publishes a monthly newsletter that is reproduced in a nationwide daily newspaper, and it has conducted graduate seminars in the Dominican Republic, Honduras and Panama.



tary Agencies in Tamil Nadu. And at the national level, NGOs come together in the Voluntary Action Network India.

Some NGOs are not as non-governmental as they seem. Although formally independent, they might have links to government. In Zimbabwe, three NGOs are intimately linked with the ruling party: the President's Fund, Child Survival (under the patronage of the president's late wife) and the Zimbabwe Development Trust (under the tutelage of one of the country's vice-presidents). The Philippines similarly has government-inspired NGOs, known as GRINGOs, some of which were set up to further the aims of national and local politicians, and others to serve as recipients for foreign donors that required that a certain portion of their aid be channelled through NGOs. And while the vast majority of NGOs have a voluntary non-profit ethos, some are really commercial companies in disguise. For example, several NGOs in India have set themselves up as consultancies working (for a fee) with the voluntary sector.

In some cases, the most effective way for NGOs to operate is at the international level—as the remarkable success of Amnesty International and Greenpeace has demonstrated (box 5.7).

#### BOX 5.7

##### International advocacy by NGOs

Many of the issues that concern NGOs are truly global—and can often be best addressed by truly international NGOs. One of the best-known and respected of these is Amnesty International. By tirelessly recording and publicizing human rights violations, it has amply demonstrated the power of information to protect the rights of individuals and groups.

Amnesty has more than 6,000 groups of volunteers in more than 70 countries. Through their reports and letter-writing campaigns in 1990, these groups publicized the cases of 4,500 prisoners and contributed to the release of 1,296 of them.

A new organization—Transparency International—also plans to operate through international investigation and

publicity by identifying and exposing corruption in international business transactions and documenting its political, social and economic effects. The globalization of world trade increases the potential for large-scale corruption—as the Bofors arms sales scandal has shown only too vividly. Transparency International is unlikely to be short of work.

Another new international advocacy agency—in this case on environmental issues—is the Earth Council. It draws the lesson from the Rio environmental summit that people's continuing international participation is vital to the solution of environmental problems. It will provide a continuing global non-governmental forum for debate and action on sustainable development.

## Northern NGOs in the South

All the industrial countries have a wide range of NGOs working on development issues, and their numbers are growing. These northern NGOs send large sums to developing countries. As with the various national Save the Children organizations, they do this in addition to helping in their home countries. Or as with the Oxfams, they spend their funds almost exclusively in developing countries.

On average, two-thirds of the funds northern NGOs raise for spending in the South come from private contributions. The highest per capita private contributions to NGOs were in Sweden, followed by Switzerland, Norway and Germany (above \$13 per capita in all cases). Between 1970 and 1990, grants by northern NGOs to projects and programmes in developing countries increased from just over \$1 billion to \$5 billion. The country raising the most, however, is the United States—\$2.7 billion, almost half the total in 1991.

Northern NGOs also serve as channels for government funds. On average, a third of their funds comes from governments, though the proportions vary widely—from 10% in Austria, Ireland and the United Kingdom to more than 80% in Belgium and Italy. Between 1970 and 1990, such funds increased from less than \$200 million to \$2.2 billion (table 5.1).

Taking private and government contributions together, the total transferred by and through northern NGOs increased from \$1.0 billion in 1970 to \$7.2 billion in 1990—in real terms twice the rate of increase for international development assistance. Indeed, government funding of northern NGOs has grown faster over the past ten years than support from the general public.

Many northern NGOs still execute their own programmes in the South—as with CARE, Plan International and World Vision in the United States, and ActionAid, Save the Children and Oxfam in the United Kingdom. But the trend is away from hands-on involvement and towards working in partnership with NGOs and people's organizations in developing countries. In



the United Kingdom, this is common for some of the largest NGOs, like Christian Aid and CAFOD—similarly with NOVIB in the Netherlands, and the church agencies in Germany and Scandinavia.

Most large NGOs in the South depend heavily on those in the North for finance. The northern NGOs typically refer to this as “partnership”. But seen from the South, this relationship is often far removed from the equality the term implies.

The partnership clearly works best if donor and recipient agencies share a common perspective on development. And relations are smoother if the northern agencies provide a steady flow of funds and the southern agencies are willing and able to meet the reporting, management and accounting standards that the northern donors require.

In practice, these conditions do not always obtain. A central question that often remains unanswered is who defines the development agenda at the grass roots. The northern agencies can rarely guarantee long-term funding—and those in the South often resent the administrative demands on them. Agencies that receive money from child sponsorship organizations, for example, have to spend much of their time collecting copious quantities of personal information about the sponsored children—and employ large teams of “social workers” for this.

The donor agencies are thus in a position to set the conditions of the relationship. These may or may not be onerous, but they do restrict the freedom of the agencies they are placed on.

An additional complication in recent years has been that northern governments have been channelling aid through northern NGOs to NGOs in the South. While governments may find this attractive, they often ignore some fundamental incompatibilities. First, on the type of project: governments prefer programmes that produce tangible results, so they place a major emphasis on economic projects. NGOs, by contrast, prefer projects with stronger social or political elements that empower the poor.

Second are conflicts in time. Governments like their funds disbursed quickly, so

they are not too keen on long preproject assessments. NGOs, however, know only too well that participatory projects can be implemented only gradually—and after painstaking assessment and consultation with the people concerned.

The effect: northern NGOs have to persuade those in the South to generate economic projects with quick results—adding to the tensions between donor and recipient agencies. In response, there has been, as in the Philippines and Thailand with Canadian NGOs, the emergence of a collective dialogue between groups of NGOs, and the creation of consortia, as with the Bangladesh Rural Advancement Committee.

### NGOs and people

Participation is a central tenet for almost all NGOs. Do they promote participation in practice? Mostly, it seems they do. Many studies have shown participation to be a dominant feature of their operations. And governments of developing countries, as well as donor agencies, concur that participation is the feature that distinguishes NGOs most sharply from the “top-down” approach of many official programmes.

NGOs’ support for people’s organizations, where face-to-face contact is the normal style of working, opens an ongoing debate on the form that interventions should take—sometimes with disconcerting results. In Bangladesh in the 1970s, Save the Children Fund (SCF) began working with the poorest women and children in the city slums. SCF wanted to concentrate on immunization and family planning, but the Slum Committees rejected this approach, insisting that the most urgent need was for curative health programmes. So that was the project’s initial emphasis, and it was two years before SCF’s preventive aspects were introduced.

But it should not be assumed that NGO contacts with people’s organizations necessarily enhance participation. Sometimes, external assistance can discourage participation—or even repress it. This can happen when the NGOs feel under pressure to demonstrate concrete achievements quickly—to spend money fast. In the Philippines,

TABLE 5.1  
**ODA flows through  
NGOs, 1983–86**  
(% of total)

Switzerland	19.4
USA	11.1
Canada	10.8
Netherlands	7.0
Belgium	6.6
West Germany	6.5
Sweden	4.6
Italy	1.9
Japan	1.6
United Kingdom	1.3
France	0.3

*Efforts to promote participation and empowerment cannot be divorced from concrete economic achievements*

the Ecosystems Research and Development Bureau, a quasi-autonomous agency, is working with local people's organizations to help improve livestock production in upland areas. Where people's organizations do not exist, the agency encourages people to form them, merely to take delivery of predetermined technologies.

Indeed, potential recipients might be tempted to form temporary or superficial groups if they sense that this is an easy way to obtain more goods or services. They tell the NGO "what it wants to hear" to gain access to the inputs they require. There is also the danger that people's organizations, after successfully attracting funds, are taken over by local elites who want to steer the inputs their way.

How far NGOs really enhance participation is impossible to say. But one recent Dutch study—with evidence from Brazil, Burkina Faso, Chile, India, Indonesia and Zimbabwe—concluded that NGOs had broadly increased empowerment, even if it could not offer quantitative evidence. It reported that people in the target groups now "... act more often as partners in discussions with organizations outside the village, have the courage to lodge complaints with civil servants of the local government, move freer and travel more. These are seemingly small changes but of essential importance for the people themselves."

A lesson many NGOs have learned is that efforts to promote participation and empowerment cannot be divorced from concrete economic achievements. If they are not simultaneously offering such improvements, efforts to promote empowerment come under strain.

An example: The Development Education and Leadership Training programme, initiated in Kenya in the early 1970s, has been adapted in Ghana, Nigeria, Sierra Leone, South Africa and Zimbabwe. The approach is to encourage communities to reflect on their place in society and their power to bring about change. But unless this awareness raising is matched by efforts to meet the immediate tangible needs of the groups involved, the result can be frustration and the group's disintegration.

The need for tangible outcomes is also an issue in Latin America now. For many years, NGO support of popular movements offered an outlet for people's democratic aspirations. Now that these have in many cases been fulfilled, people are focusing more on other matters. The poor and marginalized in people's organizations are demanding that empowerment efforts be complemented by activities that also address their pressing social and economic needs.

NGOs, like people's organizations, tend to be "value-driven" rather than profit-oriented or bureaucratically propelled. But this does not necessarily mean that they themselves work in a participatory fashion. While certainly open to a broad range of internal debate and discussion, many large organizations develop conventional bureaucratic characteristics.

Who exactly should be allowed to participate in the running of NGOs? Their trustees, their staff, their donors or the people they help? The order of priority today is probably staff, trustees, donors and, finally, beneficiaries. Many organizations refer not to "beneficiaries" but to "partners", though the equality of this partnership is sometimes open to doubt.

With such concerns so widespread, a statement at the end of a colloquy between NGOs and people's organizations in Sri Lanka in 1992 concluded that "NGOs must, as an objective, strive to increase the capability of people's organizations to articulate their concerns directly at the highest levels."

### **NGOs and government**

NGOs have complex relations with governments, sometimes cooperating, sometimes in conflict—and often both simultaneously over different issues.

The NGOs' ability to promote participatory development is strongly influenced by the nature of the government. Where governments have been strong and authoritarian, one of the major contributions of NGOs has been to keep participatory democracy alive. In many countries in Latin America, and in the Philippines under

Marcos, NGOs nurtured and supported a range of popular movements to oppose the excesses of national security states and to address poverty issues at the local level.

Where governments are hostile but weaker, there are many opportunities for NGOs to promote participatory development through social and economic projects. If the central government does not exert strong control, regional and district governments might be more able and willing to work with NGOs, especially where their interventions are successful and have the support of the people. Zaire in recent years falls into this category.

Strong governments that welcome NGOs may sound ideal, but not necessarily. Strong governments have strong views on what NGOs should be doing, and they commonly see NGOs as "gap-fillers" for inadequate social services rather than as champions of a different kind of development. But NGOs that have demonstrated successes with people's organizations may still be able to influence government approaches to development—as in Thailand and Zambia.

In recent years, the question of how NGOs and governments should work together has been sharpened by the widespread adoption of structural adjustment programmes. NGOs around the globe have been called upon to help mitigate the worst effects of these programmes, as well as take over some of the social services that governments can no longer finance. In most cases—such as the Gambia, Ghana, Guatemala and Uganda—NGOs have agreed to cooperate, often because this qualified them for government and external funds. In others—Bolivia is a striking example—NGOs have responded with greater reluctance. But in both cases, NGOs have been forced to reflect on how their approach meshes, or conflicts, with national policy. And governments for their part are realizing that NGOs and the participatory methods they promote have a role in national development.

The key issue now is how best to promote the strengths and interests of both governments and NGOs. Governments, seeing NGOs as widening their activities,

will want to monitor, or probably control, them more closely. But they will have to find ways of doing this without nullifying the benefits they bring—introducing cumbersome procedures, for example, which inhibit NGOs or delay the speedy implementation of their programmes. And NGOs increasingly recognize that if they are not to be marginalized in national debates on the participatory approach to development, they have to engage more constructively with governments.

Governments and NGOs have to interact at three levels: line ministries, local government and national forums.

- *Central line ministries*—Government ministries need to know what NGOs are doing and devise mechanisms for using the insights that emerge from NGO interventions, and, where appropriate, include the activities of NGOs in future planning. They also need to encourage greater NGO involvement where the government is not involved.

The NGOs, for their part, need to carry out more rigorous assessment of their projects, cooperate and coordinate more closely among themselves and provide governments with more information on their activities and provide critiques and proposals on policy and legislation.

In many instances, it will be useful to have some form of government-NGO liaison body. These already exist in some countries, such as in the Philippines for agricultural research, and in Tanzania for health issues.

- *Local government*—NGO activities often challenge the local power structure. Indeed, that is often the intention. If the local power structure is elitist and oppresses the poor, this is something that NGOs will seek to change. But this attitude can spill over into arrogance and antagonism towards local politicians and administrators. NGOs need to be more sympathetic to the real problems facing local politicians and administrators.

And local governments for their part need to look beyond merely eliminating or controlling NGOs—to see them more as an opportunity for local gain than as a threat to local alliances. It ought to be possible in

*The key issue is how best to promote the strengths and interests of both governments and NGOs*

*The indirect impact of NGOs is often much wider than their direct contribution*

each district to establish a forum that provides for some interchange of ideas between the administration and NGOs, covering local development problems and the best ways of tackling them.

- *National forums*—In the past, NGOs have often had only a minimal impact on national debates about the form and content of development strategies. This is partly because most NGOs have concentrated on grass-roots activities and pursued only informal contacts with government officials. And in part it is also because governments have chosen not to discuss overall policy issues with NGOs. A major exception has been Latin America, where both NGOs and people's organizations have had a major role in the democratic movement, and in the Philippines, where NGOs constitute one-third of the membership of the Philippine Council for Sustainable Development, established in September 1992 to guide national followup to the Earth Summit.

But NGOs now recognize more the limits on what can be achieved at the grass-roots level and aim at having greater influence on national debates. This will require them to present a more united front and to devote more resources to having a much greater voice at the national level. If NGOs achieve that, the contribution they already make to participatory development at the grass-roots level could well be seen as only a relatively small part of their larger struggle to widen the opportunities for participatory development at the national level. In other words, the indirect impact of NGOs is often much wider than their direct contribution. Some specific country experiences are discussed below.

- *Bangladesh*—has one of the largest and most diversified NGO sectors in the world. No one knows the precise number, but at the start of the 1990s at least 12,000 groups were receiving financial and technical support. More than 550 local NGOs were registered with the Association for Development Agencies, and more than 300 national and foreign NGOs were getting funds from abroad. Around \$100 million is channelled to NGOs from external sources (about 5% of total aid flows). Most are lo-

cal and small, but some employ thousands of people.

Thought to reach 10–20% of the poor, NGOs in Bangladesh generally focus on the rural poor through a wide range of activities, which include both emergency assistance and long-term development. Credit has been one of their most important activities, and they have also been concentrating on income generation.

Most NGOs aim at empowering the poor, and particularly women, and they have had significant success. In some cases, however, groups have fallen apart, and there have been violent clashes when NGO programmes have encouraged people to confront local power blocs.

NGO relations with the government are complex and contradictory. On the one hand, they are welcomed to “supplement and complement government's development programmes”. But the government has also at times seen them as a threat, undermining its legitimacy, and as a growing competitor for development finance, and has responded by placing obstacles in their way, including a restrictive process of registration and approval.

NGOs in Bangladesh do have an influence on government development policy, and the government has given some leading NGO figures important advisory positions. This could be seen as an endorsement of the value of NGOs—or as a way of co-opting potential opposition.

- *Chile*—showed a more rapid proliferation of NGOs in the 1970s than any other country in Latin America, a direct response to repression by the military regime. Large numbers of middle- and senior-level personnel were forced to leave government. Some were killed, and some fled abroad. But a high proportion moved to the voluntary sector, joining or creating NGOs sustained both by the church and by a massive injection of funds from overseas, governmental and non-governmental supporters.

The NGO movement worked in two ways. It was the focus of political opposition to the government, giving rise to an array of popular movements. But it was also working to mitigate the worst effects of pover-



ty—though here, too, popular education was always an important part of the process. NGOs were thus able to keep democratic ideals alive.

When a democratic government was elected in 1990, the participatory approach that NGOs had fostered became an important aspect of government policy—indeed, many people who spent time in NGOs now hold key government positions. In addition, the government has accepted that NGOs have an important role.

But this leaves the NGOs in something of a dilemma. Previously, their role was clear: they were united in opposition to General Pinochet. Now they have to develop a new role, which could take one of roughly three forms. Some groups are likely to draw back from popular education and participatory development to focus more on the delivery of services. Others, less certain of the durability of democracy, will maintain their distance from government. And a third group will probably combine its promotion of grass-roots participation with attempts to work with, and influence, the government.

Chile in the years ahead should be an interesting demonstration of participatory development being promoted simultaneously by the government from the top down, and by the NGOs from the bottom up.

- *Uganda*—is one of the poorest countries in Africa, and for most of its post-colonial history has been ravaged by war and civil unrest. Since 1986, the government has been attempting to create working state institutions. And alongside them are at least 250 local NGOs and 24 foreign-based ones with an emphasis thus far on emergency assistance and health programmes. More than \$25 million in foreign funds went to local NGOs in 1990.

The government has been broadly supportive of NGOs, and the controls it applies to them are usually only administrative. This gives NGOs considerable freedom, but it has also meant that their services often run in parallel with those of the government and sometimes overlap. It means too that, with the possible exception of health care, NGOs have had little impact on public policy.

One significant area of NGO overlap with the government is in personnel. Since government salaries are inadequate, some NGOs, particularly the foreign ones, have been poaching government staff. Others have been “supplementing” the salaries of government workers and thus drawing them away from government projects and programmes. Either way, the effect has been to substitute NGO programmes for government ones.

Most Ugandan NGOs espouse participation, but this is not always evident in practice. Perhaps understandably, there is very little participation in emergency relief programmes. But even in long-term development programmes, the beneficiaries may have little involvement in planning. And when it comes to evaluation, the NGOs (like official aid organizations and developing country governments) often consider themselves more accountable to their donors than to the beneficiaries.

### Effectiveness of NGOs

NGOs have certainly increased their outreach in recent years. Both the funds they spend and the numbers of people they deal with have been rising dramatically. In the early 1980s, one rough estimate suggested that NGO activity “touched” 100 million people in developing countries—60 million in Asia, 25 million in Latin America and some 12 million in Africa. Today, the total is probably nearer 250 million—and will rise considerably in the years ahead.

But NGO activity needs to be placed in perspective. The flows from northern NGOs and northern governments to NGOs in the South have been increasing. But the \$7.2 billion in 1990 was still a small proportion of overall flows from North to South, equivalent to 13% of net disbursements of official aid, and only 2.5% of total resource flows to developing countries. Even if NGOs were to treble their spending by the year 2000, they would still account for less than 20% of official aid flows. But if ODA flows stagnate or shrink in real terms, the percentage will be higher.

It is difficult to judge how effective NGOs have been, whether in increasing ef-

*NGO activities today touch the lives of about 250 million people in developing countries*

iciency, relieving poverty or promoting participation. There has been very little systematic analysis by the NGOs themselves or by independent organizations. Any general assessment of the impact of NGOs can thus be based only on partial evidence. This chapter considers:

1. Tackling poverty
2. Providing credit to the poor
3. Reaching the poorest
4. Empowering marginal groups
5. Challenging gender discrimination
6. Delivering emergency relief.

TABLE 5.2  
Shares of NGO credit in  
total credit advanced  
(percent)

Country	Year	NGO credit share
Kenya	1990	1.6
Bangladesh	1990	0.6
Costa Rica	1992	0.2
Philippines	1990	0.1

### *Tackling poverty*

Many people judge NGOs primarily by their success in improving the living standards of the poor, and there are plenty of individual success stories. The landless have obtained land. Farmers are growing more food. Wells and boreholes have been sunk. Children have been inoculated against killer diseases. In these and countless other ways, NGOs have transformed the lives of millions of people all over the world.

The results have often been outstanding. In Zimbabwe, the agricultural groups supported by Silveira House increased crop yields sevenfold to tenfold, enabling farmers to break out of subsistence agriculture and move into the cash economy. In Burkina Faso, the *Groupements Naam* are helping 160,000 people to improve their communities and protect the environment (box 5.8). In south India, the Kanyakumari District Fisherman Sangam have signifi-

cantly improved the lives of fishing communities by increasing the fish catches and by cutting out the merchants, giving the communities a fairer reward for their efforts.

But there have also been failures. An evaluation of income-generating activities supported by the Ford Foundation in Africa in the late 1980s concluded that there were "very few successes to talk about, especially in terms of post-intervention sustainability". Likewise, a mid-1980s study of projects supported by the European Community found that even projects selected for analysis because they had been "successful" failed to satisfy the evaluation criteria in a surprisingly large number of cases. Of the seven microprojects visited, six had quite serious problems.

More successes than failures? Nobody really knows.

What seems clear is that even people helped by successful projects still remain poor. NGO interventions do not generally help people escape from structural poverty, but they do reduce some of the worst forms of poverty. This might seem a modest achievement, but for the people helped, it can be very significant. If they are less preoccupied with the daily drudgery of making ends meet, or have a little cash to spend on items other than the barest necessities, they are in a much better position to focus on the next stage of the struggle to improve their lives.

Any assessment of NGOs' results should also take into account their operating circumstances. Compared with official aid donors (whose success rate is also unknown), NGOs take on much tougher tasks in very inhospitable environments. In Africa, where per capita incomes are falling almost everywhere, if NGOs can help people hold their incomes steady, this is a considerable accomplishment. And NGOs do this with very little money—less than 60 cents per person assisted, according to one Dutch study.

In addition, the benefits of NGO activity can often be indirect. Successful NGO interventions can induce other agencies to follow suit and replicate their experience elsewhere. In Zimbabwe, the experience of

#### BOX 5.8

#### **Burkina Faso—Groupements Naam**

The *Naam* groups started in 1967, in the Yatenga province of Burkina Faso, as a revival of traditional work groups. The basic idea is for the community to accumulate a production surplus and invest it in community development.

During the rainy season, group activities include cultivating market-garden plots and planting millet, cotton, sesame and groundnuts in communal fields. In the dry season, the focus shifts to soap making, textile production, animal husbandry and building fuel-efficient ovens. After provision is made for depreciation

and the capital needed for new investments, the proceeds are shared among group members.

The *Naam* groups also undertake various community works, digging ditches, building rainwater storage tanks and small dams and tending community forests. The groups also promote sports and cultural activities and run literacy programmes.

In 1989, there were some 2,800 groups with more than 160,000 members. Their motto is "development without damage".

the Silveira House groups has been used by the government as the model for a major rural development initiative across the country. NGO successes can also induce other groups to form—and produce a ripple effect across communities or beyond, as has happened in Bangladesh and Sri Lanka (box 5.9).

#### *Providing credit to the poor*

One of the most important ways NGOs have made up for failures of the market is by providing credit. Poor people are often regarded as bad credit risks, and banks seldom are prepared to deal in the small sums that the poor need.

Many NGO credit schemes have taken over and adapted traditional self-help initiatives—known as *susu* in Ghana and *cheetu* in Sri Lanka. In Bangladesh, the traditional *samabaya* scheme was upgraded to the Swanirvar Movement. One of the best-known larger credit initiatives is also in Bangladesh—the Grameen Bank—which has an international reputation as an efficient rural credit scheme (box 5.10).

These schemes have often been highly successful—reaching the poorest people and giving them small amounts of low-cost credit. They have also had very high repayment rates—frequently in excess of 90%. They have shown that the poor are bankable—that their problem is lack of access to credit.

In some cases, however, administrative costs have been high, so that what had been intended as “revolving funds” have remained dependent on top-ups from donors. And on occasion, too many loans have been granted for consumption rather than investment.

A major concern for NGOs must be that their schemes—though generally useful, efficient and effective—are unlikely ever to be a major source of funds for poor people. In Costa Rica, where the *Fundación Costarricense de Desarrollo* is a significant source of credit for the poor, the NGOs provide only 0.2% of total credit. And in Bangladesh, even the impressive activities of the Grameen Bank account for only 0.1% of national credit. And all the NGOs

in Bangladesh combined provide only 0.6% of total credit (table 5.2).

This is not a criticism of the performance of NGOs, but a candid commentary on the situation. NGOs are in no position

BOX 5.9

#### **Sri Lanka—Sarvodaya Shramadana Movement**

The Sarvodaya Shramadana Movement (SSM) was founded in the late 1950s under the charismatic leadership of A. T. Ariyaratne to integrate low-caste families into the mainstream of national life. Now, it has more than 7,700 staff and covers 8,000 villages (more than a third of the total in Sri Lanka) in both Sinhalese and Tamil parts of the country.

SSM takes its inspiration from Buddhist and Gandhian sources. It aims to help people mobilize their own resources, especially their labour, through forms of participation and self-sufficiency in tune with the country's cultural traditions.

It runs a variety of income-generating programmes, including batik and sewing shops, workshops for mechanical repairs and carpentry, printing presses and activities for farmers. On the welfare side, it has programmes for the deaf and dis-

abled, relief and rehabilitation programmes (particularly for the victims of ethnic conflict), and nutrition programmes aimed especially at preschool children.

A recent survey of SSM and non-SSM villages in the same region found that people in SSM villages were much more likely to have overcome apathy and mutual suspicion. SSM's participatory approach has encouraged a new leadership, enabling people to bypass the egalitarian structures associated with the temples, mutual aid committees and political parties.

SSM has also begun to work at the national level. Through seminars and discussion groups with lawyers, the police, the judiciary and various action groups, it is challenging the idea of development as a purely economic issue—and arguing that it should give greater priority to human concerns.

BOX 5.10

#### **Bangladesh—the Grameen Bank**

The Grameen Bank in Bangladesh is one of the most successful experiments in extending credit to the landless poor.

It started in 1976 in the village of Jobra. Professor Muhammad Yunus saw that it was impossible for landless people to get loans from commercial banks since they could offer no collateral. He decided personally to guarantee bank loans to the poor. This proved very successful: repayment rates were above 99%. The poor were bankable.

In 1983, the project became a full-fledged bank. The Bangladesh government contributed 60% of the initial paid-up capital, and the rest came from the savings of the borrowers themselves. International support has been considerable, but dependence on foreign funding has declined from 83% to 60%.

The bank's most significant innovation is to organize people into groups of five, and ask each person to guarantee

the repayment of a loan to any of the other four members. The chair of each group has a weekly review meeting with a staff member of the bank. This combination of collective collateral, close supervision and peer group pressure has resulted in very high repayment rates (currently around 95%).

By 1991, the bank had extended its services to more than 23,000 villages through its nearly 900 branches. Around one million households have received credit. The average loan is \$60, and the interest rate (16%) contains no subsidy. Primarily for working capital, the loans have generated a great deal of employment, especially for rural women.

Borrowers are also required to add one taka per week to their savings account. By 1991 this compulsory savings fund had accumulated Tk. 962 million—62% of outstanding loans.

*Until the early  
1980s, most NGO  
interventions were  
gender-blind*

to replace governments or commercial markets in the provision of credit. So, one of the most important roles of NGOs in this area must be to put pressure on governments to change their policies and priorities.

*Reaching the poorest*

NGOs often manage to reach groups that governments find most difficult to help, tending to work with people in rural areas, where government services are usually weak or non-existent. But many are now also focusing on urban areas, as in Bangladesh, Chile, South Africa and Zambia.

Whether they reach the *very* poorest, however, is another matter. If government and official aid programmes usually fail to reach the poorest 20% of income groups, most NGO interventions probably miss the poorest 5–10%. This would include, for example, the sick and the elderly as well as those with few assets and little or no education—as well as the high proportion of households headed by women. Such people are often dispersed and difficult to form into groups. And because they often live in remote and inaccessible regions, reaching them can be very expensive. On the whole, it is easier for NGOs to reach the not-so-poor than the very poorest.

When helping in rural areas, it is usually easier to assist those who have some productive land. In the Gambia, NGOs participating in the Farmer Innovation and Technology Testing Programme focus on the middle-income farmers. And in Kenya, a local NGO has an Agroforestry Plots for Rural Kenya Project, funded by the Ford Foundation, which has rarely contained representatives from the poorest households.

Many interventions do, however, reach such people. NGOs in Latin America and South Asia in particular have often worked with landless labourers. One way even the poorest can be reached is to have the activity embrace everybody in a given area, as with the various Campfire projects run by the Zimbabwe Trust and the Worldwide Fund for Nature in the Zambezi Valley—projects that generate income through the hunting and care of wildlife.

*Empowering marginal groups*

In most developing countries, poverty is often caused less by an absolute shortage of resources than by their skewed distribution. The NGOs' emphasis on empowerment is partly a reflection of this, and their interventions do indeed occasionally enable poor people to resist local elites and claim their rights. In such cases, they are likely to come up against official opposition—as well as opposition from powerful local interests.

Some of the sharpest conflicts have been over land rights. In many countries, especially in Asia and Latin America, NGOs have been defending the land rights of minorities, pressuring governments to provide land for the landless and to embark on agrarian reform. In Ecuador, Indian federations have been formed to help the indigenous people gain secure title to their land. This has not only helped them materially, it has also strengthened their communities and helped challenge myths about Indian social and intellectual inferiority.

In several countries, NGOs have helped empower people in rural areas by organizing them into groups. For instance, in Zimbabwe, networking among groups has increased their effectiveness (box 5.11).

*Challenging gender discrimination*

Until the early 1980s, most NGO interventions were gender-blind, like those of other development agencies. Although there was always a small number of projects and programmes assisting grass-roots women's groups, the specific needs of women in general antipoverty programmes were often ignored. Today, NGOs are much more sensitive to such issues and often attempt to include gender- and women-focused elements in many of their initiatives. In part, this has been in response to pressures from the growing women's movement in many developing countries. And some NGOs have been established specifically to enhance the power of women in the family and in society.

In Cameroon, the Women's Networking Association brings together 50 women's



groups. It carries out literacy campaigns and gives women other practical help—such as establishing a cooperative to purchase the produce that village women bring to market but are unable to sell at the end of the day. The association also organizes seminars and conferences to raise women's concerns at the national level.

In Kenya, the Green Belt Movement, tackling the intertwined problems of environmental degradation and poverty, is encouraging women to use soil rehabilitation measures and natural fertilizers. With the involvement of 50,000 women, it has planted ten million trees in Kenya. Also responsive to the needs of the women in the poorest families, the movement has established training centres to increase women's employment opportunities.

NGOs in many countries concentrate on advocacy on behalf of women. The Alliance of Costa Rican Women provides legal and health services to more than 4,000 low-income women. But it also campaigns to improve the status of poor women and publishes information on legal and health issues, and on violence against women.

Even so, too many NGO projects still fail to challenge prevailing patterns of gender discrimination. Too often, the attempts to incorporate gender issues into projects have been only superficial, resulting in little empowerment of women. In other cases, project successes have been eclipsed by the more powerful forces in society.

### *Delivering emergency relief*

One great strength of NGOs is their ability to respond quickly and effectively to emergencies. Indeed, a high proportion of NGOs were founded in response to emergencies from famines, wars or earthquakes—and only later did they extend their activities to long-term development. NGOs can bring five main strengths to emergency and relief work:

1. *Warning of disaster*—With an extended network of contacts on the ground, NGOs are in a good position to draw the attention of the international community to existing or impending emergencies, particularly vi-

tal when the government chooses to downplay the emergency or exclude bilateral or multilateral agencies. NGOs often make powerful use of the news media for this purpose—as with the Bangladesh cyclone in 1970, the Maharashtra drought in 1974 in India, the Ethiopian famine in the early 1970s and the Sub-Saharan crisis of 1984–85. Their dramatic efforts can also attract international attention—as Oxfam did in 1979, when it chartered a boat, filled it with food and medical supplies and sailed it from Hong Kong to Kompong Som in Cambodia.

2. *Advocacy for international action*—Following their warnings, the NGOs can lobby governments and international organizations to increase their resources for emergencies, sometimes through international consortia. Agencies in the European Community, for example, lobbied the EC to raise food aid to Africa from 1.5 million tons in 1990 to 2.1 million tons in 1991.

3. *Speedy response*—Untrammelled by bureaucratic and political constraints, NGOs can usually act much faster than official agencies. And since they are less susceptible to political pressures, they sometimes work where governments forbid interventions from government or multilateral agencies—as in Cambodia in the late 1970s and in Eritrea and Tigray in the early 1980s. In Somalia in the most recent

*Attempts to incorporate gender issues into projects have too often been superficial*

### **Zimbabwe—Organization of Rural Associations for Progress**

BOX 5.11

The Organization of Rural Associations for Progress (ORAP), an indigenous NGO in Zimbabwe, acts as an umbrella organization for local groups, each with five to 30 rural families. These are often traditional work groups that managed to survive the paternalist and racist practices of the colonial period. ORAP provides funds and technical assistance, but the groups and their regional associations make the key decisions.

Most group members are farmers, so ORAP focused initially on generating income in agriculture. Lately, it has also been engaged in education, sanitation and extension services—and in food security and drought relief. Current projects include grinding mills, gardens,

irrigation schemes, sewing and savings clubs, animal husbandry and horticulture.

Now operating in three provinces, ORAP employed 60 people directly in 1990, had an annual budget of around \$1 million and covered more than 1,000 groups (80,000 families), which were also organized into 16 higher associations.

Also operating in the same areas as ORAP, the government is essentially delivering services, while ORAP puts the emphasis on participation and social mobilization. ORAP's approach is being studied by other groups in Zimbabwe, since it seems successfully to have blended an efficient service organization with a popular grass-roots movement.

*Advocacy clearly is  
the NGOs' greatest  
strength*

emergency, such organizations as the Red Cross, Save the Children, CARE, Concern and *Médecins Sans Frontières* stayed on after the international agencies had left, even during periods of intense fighting. Today, they are responsible for much of the food distribution and, along with the International Committee of the Red Cross, are bringing in nearly 20,000 tons of food a month and running 800 kitchens for more than a million people.

4. *Cooperation with indigenous organizations*—Emergency aid is generally better administered by local organizations more sensitive to local needs. NGOs have been able to use their existing contacts to good effect and to help boost the capacity of local groups where needed. In the Sudan recently, the only NGO permitted by the government to visit the urban slums around Khartoum has been the Sudan Council of Churches, through which northern NGOs have been able to channel funds.

5. *Disaster preparedness*—Most disasters hit the poor hardest, the people living on marginal land liable to flooding or in mud houses that collapse in earthquakes. Local NGOs can try to ensure that the poor are better able to anticipate problems. In Bangladesh, the Ganges-Kobadak cooperatives monitor embankment breaches to warn of danger. And the NGO emphasis on participation and empowerment puts local communities in a stronger position to pick themselves up again more quickly after a disaster strikes.

It would be wrong, however, to assume that NGO responses to disaster are always beneficial. They can also create problems by poorly coordinating many agencies and by bringing in inexperienced workers—as with the Karamoja drought in Uganda in the late 1970s. And there have also been occasions when foreign NGOs have moved in and undermined local agencies and government efforts—as in Mozambique in the late 1980s.

Another common NGO failing in emergencies is that there is little evaluation of their work, so that mistakes are repeated in one emergency after another.

## The future of NGOs

Many northern NGOs, but increasingly also southern NGOs, have joined in debates of such issues as the debt crisis, international trade, structural adjustment, the environment, women in development and peace. They now often employ or commission economists and other specialists to monitor such matters and produce detailed reports as well as campaigning materials.

NGOs have become accepted by people, governments and business as a legitimate voice, lobbying not just their own governments or enterprises, but also many international gatherings. And it seems clear that the voices of NGOs have prompted many actors to reassess their policies, as with the impact of structural adjustment on the poor. They have also enforced changes in the behaviour of multinational corporations, as in the marketing of infant formula and the use of fertilizers and pharmaceutical drugs in developing countries. And at the time of the Earth Summit in Rio de Janeiro in June 1992, NGOs kept up constant pressure on their governments for real changes in policy. Advocacy clearly is—and probably will continue to be—the NGOs' greatest strength.

NGOs affect relatively small (but growing) numbers of people: 250 million is less than 20% of the 1.3 billion people living in absolute poverty in developing countries. And by the end of the 1990s, optimistic assumptions suggest that they will reach nearly 30%.

In eradicating poverty and providing social services, NGOs are unlikely ever to play more than a complementary role. Much more significant is their ability to demonstrate participatory models that governments might follow—and to keep pressure on governments, in both the North and the South, encouraging them to focus more on the human development of the world's poorest people. Again, their importance lies more in making the point that poverty can be tackled rather than tackling it to any large extent. This, too, will continue to be a critical role for NGOs.

Encouraging participation means responding sensitively to the felt needs of people and communities—and responding in ways that meet those needs without “taking over”. There is always the risk of placing too much emphasis on effective delivery and too little on nurturing and strengthening participation. This tendency is likely to be heightened as NGOs open themselves up as channels for government funds. Government aid departments are used to demanding regular quantitative results and reports, and many have yet to accept fully that NGO projects need to be treated (somewhat) differently.

There is also the possibility that NGOs could “crowd out” governments. In some cases, they can offer local people better salaries and draw experienced people out of government service. Already happening in Mozambique and Uganda, this is likely to increase.

None of these concerns is new to the NGO community. Their “growing pains”, evident for some years now, have been the subject of considerable internal debate. As their responsibilities and activities increase further, they will no doubt respond to this new challenge with their usual energy, creativity and commitment.

The increasing numbers of people’s organizations and NGOs is a clear demon-

stration of how people all over the world are demanding greater participation in civil society.

These demands are likely to gather strength in the years ahead. Once set in motion, democratic movements are difficult to stop—they develop a rhythm and momentum of their own. People who know more, earn more and can do more will be raising their voices ever more loudly for greater participation in every process that affects their lives. And they will be requiring that governments, markets and all the institutions of a civil society respond to their real needs.

Authoritarian regimes might still stifle and repress. And new forms of intolerance, such as fundamentalism, might suddenly capture attention and power. But history is not on their side. The steady trend towards the dispersal of power, information and ideas cannot be reversed.

If states are to survive, they will have to establish new relationships with their people. Governments that have been able to respond sensitively and flexibly have so far been able to keep their countries intact. Others have not, and their states have come under increasing pressure.

Greater people’s participation is no longer a vague ideology based on the wishful thinking of a few idealists. It has become an imperative—a condition of survival.

*Greater people’s participation has become an imperative—a condition of survival*

# Technical notes

## 1. The human development index

### Construction of the human development index (HDI)

The HDI includes three key components—longevity, knowledge and income, which are combined to arrive at an average deprivation index (for a full technical description, see *Human Development Report 1991*, technical note 1, pp. 88–89). Longevity is measured by life expectancy at birth as the sole unadjusted indicator. Knowledge is measured by two educational stock variables: adult literacy and mean years of schooling. The measure of educational achievement is adjusted by assigning a weight of two-thirds to literacy and one-third to mean years of schooling:

$$E = a_1 \text{ LITERACY} + a_2 \text{ YEARS OF SCHOOLING}$$

$$a_1 = \frac{2}{3} \text{ and } a_2 = \frac{1}{3}$$

For income, the HDI is based on the premise of diminishing returns from income for human development using an explicit formulation for the diminishing return. A well-known and frequently used form is the Atkinson formulation for the utility of income:

$$W(y) = \frac{1}{1-\epsilon} \times y^{1-\epsilon}$$

Here,  $W(y)$  is the utility or well-being derived from income, and the parameter measures the extent of diminishing returns. It is the elasticity of the marginal utility of income with respect to income. If  $\epsilon = 0$  there are no diminishing returns. As  $\epsilon$  approaches 1, the equation becomes:

$$W(y) = \log y$$

The value of  $\epsilon$  rises slowly in the HDI as income rises. For this purpose, the full range of income is divided into multiples of the poverty line  $y^*$ . Thus, most countries are between 0 and  $y^*$ , some between  $y^*$  and  $2y^*$ , even fewer between  $2y^*$  and  $3y^*$  and so on. For all countries for which  $y < y^*$ —that is, the poor countries— $\epsilon$  is set equal to 0. There are no diminishing returns here. For income between  $y^*$  and  $2y^*$ ,  $\epsilon$  is set equal to 1/2. For income between  $2y^*$  and  $3y^*$ ,  $\epsilon$  is set at 2/3. In general, if  $ay^* \leq y \leq (a+1)y^*$ , then  $\epsilon = a/(a+1)$ . This gives:

$$W(y) = y \text{ for } 0 < y \leq y^*$$

$$= y^* + 2(y - y^*)^{\frac{1}{2}} \text{ for } y^* \leq y \leq 2y^*$$

$$= y^* + 2(y^*)^{\frac{1}{2}} + 3(y - 2y^*)^{\frac{1}{3}} \text{ for } 2y^* \leq y \leq 3y^*$$

So, the higher the income relative to the poverty level, the more sharply the diminishing returns affect the contribution of income to human development. Income above the poverty line thus has a marginal effect, but not a full dollar-for-dollar effect. This marginal effect is enough, however, to differentiate significantly among industrial countries. This method does not take  $\epsilon = 1$ , but allows it to vary between 0 and 1.

For example, Singapore has a real GDP per capita of \$15,880. With the poverty line set at \$4,829, there are four terms in the equation to determine the well-being of Singapore:

$$\begin{aligned} W(y) &= y^* + 2(y^*)^{\frac{1}{2}} + 3(y^*)^{\frac{1}{3}} + 4(y - 3y^*)^{\frac{1}{4}} \\ &= 4,829 + 2(4,829)^{\frac{1}{2}} \\ &\quad + 3(4,829)^{\frac{1}{3}} \\ &\quad + 4(15,880 - 14,487)^{\frac{1}{4}} \\ &= 4,829 + 139 + 51 + 24 = \$5,043 \end{aligned}$$

In calculating the HDI of Singapore using the improved variables and applying the methods described here, the following steps are taken:

Maximum country life expectancy	= 78.6
Minimum country life expectancy	= 42.0
Maximum country educational attainment	= 3.00
Minimum country educational attainment	= 0.00
Maximum country adjusted real GDP per capita	= 5,075
Minimum country adjusted real GDP per capita	= 367
Singapore life expectancy	= 74.0
Singapore educational attainment	= 2.04
Singapore adjusted GDP per capita	= 5,043
Singapore life expectancy deprivation	= (78.6 - 74.0)/(78.6 - 42.0)
	= 0.126



Singapore educational attainment deprivation  
 $= (3.00 - 2.04)/(3.00 - 0.00) = 0.320$   
 Singapore GDP deprivation  
 $= (5,075 - 5,043)/(5,075 - 367) = 0.007$   
 Singapore average deprivation  
 $= (0.126 + 0.320 + 0.007)/3 = 0.151$   
 Singapore human development index  
 $= 1 - 0.151 = 0.849$

### Making the HDI gender-sensitive

For 33 countries we have comparable data on the relative wages and the relative rates of labour force participation for men and women (technical note table 1.1). These data reveal a remarkable pattern of discrimination. The female-male wage ratio for these 33 countries ranges from a low of 51% (Japan) to a high of 89% (Sweden). In labour force participation, the lowest female-male ratio is 40% (Costa Rica) and the highest is 92% (Sweden). Multiplying these two ratios gives the female-male wage-income ratio.

This wage-income ratio combines two identifiable correlates of gender discrimination. There is a gap between male and female wages, and an even greater gap in labour force participation rates. When this is translated into absolute income levels, we see the profound consequences. To do this, a basic assumption has to be made that is clearly gender-biased: that the ratio of non-wage income to wage income is the same for men and women. This ratio therefore understates the inequality.

In adjusted real GDP per capita, female incomes as a percentage of male incomes range from a low of 26% (Costa Rica) to a high of 82% (Sweden). But of the 33 countries for which we have comparable data, only nine have a ratio of 60% or above, while ten have a ratio below 40%. So, even in a statistic that understates the inequality, the differences are stark.

The female HDI gains from the near-equal or better ratio in life expectancy but loses from women's unequal access to education, particularly in the developing countries. In education, the industrial countries show very little gender difference: though the value for female achievement as a proportion of male achievement never goes above 104%, in seven countries it goes below 96%. In poorer countries the differences become substantial.

The overall HDI calculated separately for men and women reflects this pattern. Of the 33 countries for which the data are available, 22 are industrial countries. So, technical note table 1.1 does not capture the full extent of gender inequality.

How should this inequality be reflected in the overall HDI for any country? A simple approach is to multiply the overall HDI for any country by the ratio of the female HDI to the male HDI.

### Adjusting the HDI for income distribution

The HDI is a national average, just like real income per capita, one of its components. The HDI therefore needs to be made sensitive to these distributions. It has the advantage that two of its three basic variables—life expectancy and educational attainment—are naturally distributed much less unequally than is income, the third

variable. A rich person cannot live a thousand times longer than a poor person, though their incomes may be in that ratio. Across countries, the range of life expectancy is 42 to 79, less than 2:1. Similarly, the percentage of adults who are literate ranges from 18% to 99%, a ratio of under 6:1. Mean years of schooling range from 0.1 to 12.3, revealing greater differences than in life expectancy.

All the variables used in the HDI have an obvious maximum, except for per capita income, which has no upper bound. For GNP per capita, the range among countries is \$80 to \$32,250, a ratio of 403:1. For real GDP per capita, the range is \$367 (PPP) to \$21,449 (PPP), or 58:1. Such inequalities in income are reproduced just as sharply within countries.

The ranking of countries by per capita income could be adjusted if per capita income were multiplied by a factor indicating distributional inequality—1 minus the Gini coefficient. For 41 countries data are available on the ra-

TECHNICAL NOTE TABLE 1.1  
**Gender-disparity-adjusted HDI**

Country	Female as % of male				Average female-male ratio for the three HDI components (percent)	Gender-disparity-adjusted HDI	Percentage difference between HDI and gender-disparity-adjusted HDI	Difference between HDI and gender-disparity-adjusted ranks <sup>b</sup>
	HDI value	Life expectancy <sup>a</sup>	Educational attainment	Adjusted real GDP				
Sweden	0.977	101.1	100.0	81.9	94.3	0.921	-5.7	4
Norway	0.978	102.1	98.3	69.5	90.0	0.881	-10.0	1
France	0.971	104.2	101.7	61.0	88.9	0.864	-11.1	5
Denmark	0.955	101.2	98.4	70.6	90.1	0.860	-9.9	8
Finland	0.954	103.8	97.9	68.3	90.0	0.859	-10.0	8
Australia	0.972	102.3	98.5	62.3	87.7	0.852	-12.3	1
New Zealand	0.947	101.5	103.9	61.7	89.0	0.844	-11.0	9
Netherlands	0.970	102.1	103.8	49.7	85.2	0.826	-14.8	1
USA	0.976	103.0	101.6	48.7	84.4	0.824	-15.6	-3
United Kingdom	0.964	101.0	101.8	51.6	84.8	0.818	-15.2	0
Canada	0.982	102.5	96.7	50.1	83.1	0.816	-16.9	-9
Belgium	0.952	102.3	100.0	52.5	84.9	0.808	-15.1	3
Austria	0.952	103.1	89.7	53.6	82.1	0.782	-17.9	1
Switzerland	0.978	102.1	93.0	40.7	78.6	0.768	-21.4	-10
Germany	0.957	102.1	90.4	48.4	80.3	0.768	-19.7	-4
Italy	0.924	102.2	98.6	47.3	82.7	0.764	-17.3	3
Japan	0.983	100.8	98.1	33.9	77.6	0.763	-22.4	-16
Czechoslovakia	0.892	103.8	88.4	61.4	84.5	0.754	-15.5	4
Ireland	0.925	100.9	102.3	30.4	77.9	0.720	-22.1	-1
Luxembourg	0.943	102.5	95.1	29.2	75.6	0.713	-24.4	-3
Greece	0.902	102.7	89.0	38.2	76.6	0.691	-23.4	0
Portugal	0.853	102.7	75.8	57.7	78.7	0.672	-21.3	3
Cyprus	0.890	100.1	85.5	35.5	73.7	0.656	-26.3	0
Costa Rica	0.852	99.8	96.6	26.3	74.2	0.632	-25.8	2
Hong Kong	0.913	100.6	62.8	39.8	67.7	0.618	-32.3	-5
Singapore	0.849	101.1	66.1	39.5	68.9	0.585	-31.1	1
Korea, Rep. of	0.872	102.4	60.9	27.5	63.6	0.555	-36.4	-3
Paraguay	0.641	100.0	88.1	67.4	85.2	0.546	-14.8	1
Sri Lanka	0.663	99.6	79.7	46.5	75.3	0.499	-24.7	-1
Philippines	0.603	99.5	89.3	35.4	74.7	0.451	-25.3	0
Swaziland	0.458	100.7	81.8	43.2	75.2	0.344	-24.8	0
Myanmar	0.390	99.3	71.8	57.7	76.3	0.297	-23.7	0
Kenya	0.369	100.2	41.8	54.0	65.3	0.241	-34.7	0

a. Adjusted for natural biological life expectancy advantage for females.

b. A positive figure shows that the gender-disparity-adjusted HDI rank is higher than the unadjusted HDI rank, a negative the opposite.

tio of the income share of the highest 20% to the lowest 20%. Of these, 17 have data on the Gini coefficient as well, and there was found to be a very strong association between the two—the logarithm of the ratio being a good predictor of the Gini coefficient. This regression result was used to interpolate the Gini coefficient for another 11 countries, for a total of 52 countries (technical note table 1.2).

TECHNICAL NOTE TABLE 1.2  
Income-distribution-adjusted HDI

Country	HDI value	Income-distribution-adjusted HDI value	Percentage difference between HDI and income-distribution-adjusted HDI	Difference between HDI and income-distribution-adjusted ranks <sup>a</sup>
Japan	0.983	0.981	-0.20	0
Netherlands	0.970	0.966	-0.41	7
Switzerland	0.978	0.958	-2.05	1
Sweden	0.977	0.958	-1.95	1
Norway	0.978	0.956	-2.25	-2
Canada	0.982	0.947	-3.56	-4
Belgium	0.952	0.946	-0.63	6
United Kingdom	0.964	0.945	-1.98	1
USA	0.976	0.943	-3.38	-3
France	0.971	0.938	-3.41	-2
Australia	0.972	0.934	-3.91	-4
Finland	0.954	0.932	-2.31	0
Denmark	0.955	0.925	-3.15	-2
Israel	0.938	0.912	-2.77	1
New Zealand	0.947	0.909	-4.01	-1
Ireland	0.925	0.908	-1.85	0
Spain	0.923	0.898	-2.71	1
Italy	0.924	0.892	-3.47	-1
Korea, Rep. of	0.872	0.885	1.49	2
Hungary	0.887	0.873	-1.68	0
Hong Kong	0.913	0.871	-4.60	-2
Singapore	0.849	0.836	-1.53	3
Costa Rica	0.852	0.829	-2.61	1
Chile	0.864	0.818	-5.33	-2
Portugal	0.853	0.802	-6.00	-2
Argentina	0.832	0.791	-4.92	0
Venezuela	0.824	0.771	-6.43	0
Mauritius	0.794	0.745	-6.18	1
Mexico	0.805	0.737	-8.46	-1
Colombia	0.770	0.734	-4.75	1
Malaysia	0.790	0.732	-7.35	-1
Thailand	0.715	0.672	-5.99	4
Panama	0.738	0.654	-11.35	-1
Turkey	0.717	0.650	-9.39	1
Syrian Arab Rep.	0.694	0.644	-7.22	2
Jamaica	0.736	0.643	-12.60	-3
Sri Lanka	0.663	0.634	-4.30	1
Brazil	0.730	0.627	-14.07	-4
Tunisia	0.600	0.583	-2.75	1
Philippines	0.603	0.575	-4.67	-1
Iran, Islamic Rep. of	0.557	0.519	-6.76	0
Indonesia	0.515	0.519	0.81	0
El Salvador	0.503	0.488	-3.01	0
Honduras	0.472	0.419	-11.21	0
Egypt	0.389	0.377	-3.12	0
Kenya	0.369	0.344	-6.83	0
Pakistan	0.311	0.303	-2.62	1
Zambia	0.314	0.291	-7.30	-1
India	0.309	0.289	-6.40	0
Côte d'Ivoire	0.286	0.246	-13.84	0
Bangladesh	0.189	0.172	-9.19	0
Nepal	0.170	0.138	-19.05	0

a. A positive figure shows that the income-distribution-adjusted HDI rank is higher than the unadjusted HDI rank, a negative the opposite.

Adjusted income was multiplied by  $(1 - G)$ , with  $G$  being the Gini coefficient, to modify income even further. Because this was done for the adjusted income,  $W(y)$ , rather than for the actual income, the diminishing return effect could be incorporated before the distributional adjustment modifies incomes further. This modified income  $W(y)[1 - G]$  is then used as the third variable in addition to life expectancy and educational attainment to compute a distribution-adjusted HDI.

#### Measuring progress in human development over time

The human development index ranks countries relative to each other for a particular year. The maximum and minimum values that define the maximum distance to be travelled for each variable are specific to that year. Over time, the actual achieved values of life expectancy, literacy and income change, as will the maximum and minimum values of these variables across all countries.

So, improvements in the components of human development in any country over time may be reflected as a decline in its HDI value, if in the meantime its relative position has deteriorated. To combine a measure of progress over time with comparisons among countries at one point of time, the HDI has to be modified.

The way to tackle this problem, without changing the logic of the HDI, is to say that the minimum and maximum should be defined, not for each point of time, but over a period of time, using fixed goalposts. Thus, if we are measuring progress between 1970 and 1990, the minimum would be the minimum of all values of, say, life expectancy for all countries over the 20 years. Similarly for the maximum. The distance to be travelled is thus stretched out as the maximum over the 20-year period.

With this adaptation, the human development index becomes comparable over time as well as across countries. The difference in the value of the human development index over time can be shown to be a weighted sum of the growth rates in the three variables: the weights are given by the ratio of the initial value of a variable to the maximum range.

To express this algebraically—with  $X_1$  as life expectancy,  $X_2$  as literacy and  $X_3$  as income—the contribution of each variable to the HDI can be written as  $Z_{jt}$ , where:

$$Z_{jt} = \frac{[X_{jt} - \min_{j,t} X_{jt}]}{[\max_{j,t} X_{jt} - \min_{j,t} X_{jt}]}$$

In the formula,  $j$  denotes the country,  $t$  the time period. Note now that the denominator will remain unchanged for all time periods and for all countries.

$$MHDI_{jt} = \frac{1}{3} \sum Z_{jt}$$

$MHDI$  stands for the modified HDI since we have a new definition of the maximum and minimum. Countries are ranked by the size of the difference between the 1970 and 1990 values for the  $MHDI$ . These differences range from 0.302 for Saudi Arabia to -0.089 for Romania. For Romania, however, the HDI in 1970 was already quite high (0.798), and the lack of change does not necessarily reflect absolute deterioration (technical note table 1.3).

### Disaggregating the HDI within a country

Within each country, there are very significant disparities: among ethnic groups, among subregions, between urban and rural areas and between the sexes. Unfortunately, there are not sufficient readily available data to present these disaggregations for most countries. They are illustrated in chapter 1 for five countries, one industrial country, the United States, and one from each of the developing regions, Mexico, India, Turkey and Swaziland. These countries have been used for illustrative purposes because reliable disaggregated data are available for them, and it is to their credit that such internal human development analyses are possible. The same disparities occur to a greater or lesser degree in other countries for which reliable disaggregated data are not available.

Disaggregated HDIs are arrived at by using the data for the HDI components pertaining to each of the groups into which the HDI is disaggregated, treating each group as if it were a separate country. The methodology is exactly the same as for the national HDIs. A country HDI using the same data components as the subnational HDIs is also calculated, and the country figure is adjusted to equal the figure for the national HDI found in indicator table 1 on the human development index. All group calculations are then adjusted proportionately so that the disaggregated HDIs are comparable to the national HDIs of this *Human Development Report*. In this way, it is possible to say where disaggregated groups of a particular country would rank among the other countries in indicator table 1 on the human development index.

TECHNICAL NOTE TABLE 1.3  
Changing HDI over time

Country	HDI 1970	HDI 1990	Difference 1970-90	Country	HDI 1970	HDI 1990	Difference 1970-90	Country	HDI 1970	HDI 1990	Difference 1970-90
Saudi Arabia	0.386	0.688	0.302	Norway	0.870	0.978	0.108	Nepal	0.126	0.170	0.044
Korea, Rep. of	0.589	0.872	0.283	Belgium	0.846	0.952	0.106	Bulgaria	0.815	0.854	0.039
Mauritius	0.525	0.794	0.269	Ecuador	0.542	0.646	0.104	Panama	0.703	0.738	0.035
Tunisia	0.335	0.600	0.265	Sweden	0.873	0.977	0.104	Madagascar	0.292	0.327	0.035
Syrian Arab Rep.	0.432	0.694	0.262	Netherlands	0.866	0.970	0.104	Paraguay	0.607	0.641	0.034
Malaysia	0.538	0.790	0.252	Egypt	0.286	0.389	0.103	Zimbabwe	0.365	0.398	0.033
Botswana	0.319	0.552	0.233	Luxembourg	0.841	0.943	0.102	Burundi	0.135	0.167	0.032
Turkey	0.492	0.717	0.225	Spain	0.821	0.923	0.102	Zaire	0.232	0.262	0.030
Indonesia	0.316	0.515	0.199	Iraq	0.489	0.589	0.100	Mali	0.054	0.082	0.028
Thailand	0.535	0.715	0.180	New Zealand	0.848	0.947	0.099	Liberia	0.194	0.222	0.028
Algeria	0.358	0.528	0.170	Congo	0.278	0.372	0.094	Somalia	0.061	0.087	0.026
Morocco	0.268	0.433	0.165	Italy	0.830	0.924	0.094	Niger	0.054	0.080	0.026
Brazil	0.569	0.730	0.161	Trinidad and Tobago	0.784	0.877	0.093	Central African Rep.	0.138	0.159	0.021
Jordan	0.428	0.582	0.154	Iceland	0.867	0.960	0.093	El Salvador	0.483	0.503	0.020
Colombia	0.617	0.770	0.153	Iran, Islamic Rep. of	0.464	0.557	0.093	Malawi	0.149	0.168	0.019
Hong Kong	0.762	0.913	0.151	Costa Rica	0.759	0.852	0.093	Bolivia	0.383	0.398	0.015
Portugal	0.710	0.853	0.143	Denmark	0.864	0.955	0.091	Bangladesh	0.174	0.189	0.015
Yemen Arab Rep.	0.093	0.233	0.140	Sri Lanka	0.574	0.663	0.089	Myanmar	0.384	0.390	0.006
Gabon	0.370	0.503	0.133	Honduras	0.385	0.472	0.087	Chad	0.083	0.088	0.005
Israel	0.806	0.938	0.132	Ireland	0.840	0.925	0.085	Sierra Leone	0.060	0.065	0.005
Mexico	0.675	0.805	0.130	Pakistan	0.226	0.311	0.085	Poland	0.829	0.831	0.002
Japan	0.853	0.983	0.130	Cameroon	0.228	0.310	0.082	Burkina Faso	0.073	0.074	0.001
Chile	0.736	0.864	0.128	Uruguay	0.799	0.881	0.082	Rwanda	0.185	0.186	0.001
USA	0.848	0.976	0.128	Haiti	0.200	0.275	0.075	Peru	0.595	0.592	-0.003
Australia	0.849	0.972	0.123	Côte d'Ivoire	0.212	0.286	0.074	Sudan	0.155	0.152	-0.003
Canada	0.860	0.982	0.122	Dominican Rep.	0.513	0.586	0.073	Angola	0.147	0.143	-0.004
Singapore	0.730	0.849	0.119	Guatemala	0.416	0.489	0.073	Benin	0.117	0.113	-0.004
France	0.854	0.971	0.117	Ghana	0.246	0.311	0.065	Zambia	0.320	0.314	-0.006
Kenya	0.253	0.369	0.116	Philippines	0.542	0.603	0.061	Afghanistan	0.083	0.066	-0.017
Finland	0.838	0.954	0.116	Senegal	0.124	0.182	0.058	Papua New Guinea	0.342	0.318	-0.024
Switzerland	0.863	0.978	0.115	Hungary	0.830	0.887	0.057	Guinea	0.074	0.045	-0.029
Austria	0.838	0.952	0.114	Nigeria	0.189	0.246	0.057	Uganda	0.241	0.194	-0.047
United Kingdom	0.850	0.964	0.114	Czechoslovakia	0.836	0.892	0.056	Nicaragua	0.549	0.500	-0.049
Lesotho	0.317	0.431	0.114	India	0.258	0.309	0.051	Mozambique	0.205	0.154	-0.051
Venezuela	0.714	0.824	0.110	Argentina	0.784	0.832	0.048	Jamaica	0.797	0.736	-0.061
Greece	0.793	0.902	0.109	Togo	0.170	0.218	0.048	Romania	0.798	0.709	-0.089



## 2. Human development index: a survey of recent reviews

The human development index (HDI) was first published in *Human Development Report 1990*. It immediately attracted a lot of attention in the print and visual media. It has also received academic scrutiny. Although the process of critical review has been slow, sufficient material now exists to enable us to review these criticisms and assess their usefulness for future work. That is the purpose of this note.

Even before these reviews began to appear, the process of revising and improving the HDI was already under way, and the 1991 Report included a survey of improvements made. Some of the criticisms were thus already allowed for in the second version of the HDI, sometimes even before the reviews of the 1990 Report appeared. Nevertheless, the task of responding to and incorporating the criticisms remains as necessary as ever. The HDI should be seen as evolving and improving rather than as something cast in stone. It is also an exercise in which as many of its users as possible should actively participate.

The HDI is an unweighted average of the relative distances measured in longevity, education and resources. The proximate variables that measure these dimensions are life expectancy, literacy and (since the 1991 Report) mean years of schooling, and some modified measure of income per capita purporting to measure the "utility" or the welfare-generating capacity of income. The measure of distance is the difference between the actual value of the variable in a country (or a region or a subgroup—for example, women) and a minimum value divided by the range of the variable—that is, the difference between the maximum and the minimum.

It should be made clear at the outset that the *concept* of human development is broader than the *measure* of human development. Thus, although the HDI is a constantly evolving measure, it will never perfectly capture human development.

### What does the HDI measure?

A question that immediately arises is: What does the HDI measure? Is it a normative measure of a desirable *standard of living* or a measure of the *level of living*? Does it measure *quality of life* or, as the British newspaper *The Daily Mail* said in its editorial on the 1992 Report, is it a *happiness index*?

A distinction needs to be made between the conceptual basis of the HDI and the measurement. Because for each dimension—longevity, educational attainment, access to resources—a relative distance is calculated that has a value between 0 and 1, it would seem that the HDI represents a normative measure. An overall value of 1 should represent a summit—bliss—if this were true.

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*This survey is a response to the many comments on the HDI during the last three years. The survey draws heavily on a special analysis prepared by Sudbir Anand and Amartya K. Sen (1992) for the Human Development Report Office, which will appear separately as an Occasional Paper of UNDP, and major contributions by Meghnad Desai.*

But if human development is a process of expanding choice, there can be no limit, no bliss point. The index is best seen as a measure of people's ability to live a long and healthy life, to communicate and to participate in the life of the community and to have sufficient resources to obtain a decent living. It is a *minimal* measure. For a country that has achieved a high value of the HDI, the question then arises about other dimensions in which people can grow.

It is good to be in a country or group that enjoys high life expectancy, or to be literate and to have attended school for a certain number of years, but that is not the sum-total of human development. Similarly for income. Income is a means to a better life, and a higher income indicates less binding material constraints than a lower income. Income indicates the possibilities open to a person—but not the use the person makes of those possibilities: "It is the lives that [human beings] lead that is of intrinsic importance, not the commodities or income that they possess" (Anand and Sen 1992).

The *Human Development Report* made this aspect clear in its original definition of human development:

*Human development is a process of enlarging people's choices. In principle, these choices can be infinite and change over time. But at all levels of development, the three essential ones are for people to lead a long and healthy life, to acquire knowledge and to have access to resources needed for a decent standard of living. If these choices are not available, many other opportunities remain inaccessible.*

Thus, human development goes beyond the essential choices that the HDI captures. As noted earlier, the concept of human development is larger than the measure contained in the index.

Much of the criticism and discussion of the index has overlooked this crucial distinction. Thus, the HDI has often been compared with the neoclassical concept of consumer utility. In standard welfare economics, the lifetime utility of consumption for an individual consumer is the measure of that consumer's welfare (Ferroni and Kanbur 1991). Under some simplifying assumptions, this can be reduced to life expectancy times the logarithm of income. Because this captures at least two of the three dimensions, it is superficially similar to the HDI. But the neoclassical exercise makes sense only on the assumptions that an individual knows at birth the (constant) level of lifetime income to expect and that, far from representing the minimum, essential choice, the welfare measure captures the entire sum of human satisfaction. Income (or consumption) is an essential ingredient in human development, but it is not the sole end or even a principal measure of that process.

Human development and the HDI have also been compared with other measures. Principal among these is the basic needs approach proposed by the ILO as a measure of the adequacy of a development process (ILO 1976, referred to by Pyatt 1991b and Smith 1992). These basic needs are health, education, food, water supply, sanitation and housing (Hicks and Streeten 1979). Again,



there is overlap with the HDI. The HDI moves away from a commodities-based approach though at the same time it constructs a scalar measure. What is more, human development goes beyond basic needs, as the 1990 Report made clear when it said the basic needs approach "focuses on the provision of goods and services rather than the issue of human choices."

The extensive literature on social indicators of development has attempted similar exercises to capture development. Three approaches frequently contrasted are (1) the use of a monetary measure—income, (2) objective social indicators and (3) subjective social indicators (Baster 1985 and Smith 1992). There is overlap between the HDI and the first two of the three approaches. A problem with the objective social indicators approach has always been how to weight them. This has also been frequently the issue in the debate about the HDI.

The questions to address here are:

1. Why only three dimensions? Are these too many or too few?
2. Are the variables (indicators) chosen to measure the dimensions adequate? And for each dimension, are the associated variables too many or too few?
3. Are the measures subject to measurement errors, and, if so, do such errors invalidate the results? A subsidiary question is how up to date are the data used to construct the index.
4. Is the choice of the minimum and the maximum justifiable, or is it arbitrary? In any case, how robust is the measure to alternative maximum and minimum values?
5. Why choose equal weights? How sensitive is the measure to other weighting schemes?

### The choice of dimensions

The three dimensions of the HDI relate to one or many capabilities that they are expected to capture. Thus, *longevity* captures the capability of leading a long and healthy life. *Educational attainment* captures the capability of acquiring knowledge, communicating and participating in the life of the community. *Access to resources* needed for a decent standard of living captures the capability of leading a healthy life, guaranteeing physical and social mobility, communicating and participating in the life of the community (including consumption).

An important omission frequently pointed out by critics is the dimension of freedom. Dasgupta has criticized the HDI for neglecting human rights: "As a measure of human development, it is quite incomplete; it is oblivious of what is commonplace to call human rights" (Dasgupta 1990; also Pyatt 1991b).

The 1991 Report made an effort to remedy this omission by constructing a human freedom index (HFI) based on the work of Charles Humana (1986). But a decision was made to keep the HDI separate from the HFI. As the 1991 Report argued, in addition to the lack of data on political freedom, there was another difficulty:

*A second difficulty is political volatility. The human development index is based on relatively stable indicators, which don't change dramatically from year to year. Political freedom, by contrast, can appear or vanish abruptly. A military coup, for example, would cause a sudden drop in the index, even though many aspects of life might remain unchanged.*

*Human Development Report 1992* continued to consider political freedom separately, emphasizing an adequate methodology for constructing an index of political freedom or of human rights performance. This task is clearly essential but incomplete even at this stage. It would be premature to rush to include inadequate measures of political freedom in a development index. Further work is needed, preferably by academics who can look at this question in an environment free from international political pressures.

A different line of criticism has been that there are too many dimensions, that there is redundancy in the HDI. But this criticism relates to the variables used to measure the dimensions and the empirical correlations among them. This has to be considered next.

### The choice of indicators

For longevity, life expectancy at birth has been chosen as the variable. This measure has been widely accepted as an indicator of development. But it has been suggested that infant mortality, life expectancy at one year, or under-five mortality would be desirable alternatives or complements to life expectancy. Pyatt (1991a) has argued that life expectancy is explained by income and infant mortality. If income is included in the HDI, infant mortality gives the extra information.

But although infant mortality and associated measures of mortality at a young age are good indicators of the quality of public health in developing countries, these variables fail to discriminate among the industrial countries. And the variable for life expectancy shows less difference between the group of industrial countries and the rest than the variable for infant mortality or under-five mortality. As a *universal* index, the HDI needs variables that discriminate among countries. Among the industrial countries as a group, maternal mortality is a better measure for this purpose.

Life expectancy at birth is an average for an entire group (nation, region, ethnic group), however, not the characteristic property of an individual, as income can be. In principle, for each person of a specific age, depending on the person's other characteristics (class, region of residence, race), a conditional expectation of remaining lifetime can be calculated. Such a variable potential lifetime (PLT) has been proposed as an alternative to life expectancy (Desai 1989). Although the PLT is a useful disaggregation, it is not suitable for comparisons between countries, however. The PLT computed for entire populations favours countries with growing populations and moderate life expectancy over those with static populations and high life expectancy. In a sense, the PLT as a measure for comparisons among countries has a "natalist" bias.

Life expectancy at birth has the further advantage that its true variance across individuals within a country is likely to be much smaller than that of income. Thus, as an indicator of the level of development, a group average for life expectancy is less misleading than one for income. A problem that remains, however, is that life expectancy is a quantitative measure. The quality of life is an issue that invites more attention than it has yet received.

For educational achievement, there are two indicators—the adult literacy rate and the mean years of school-

ing for individuals over 25 years of age. The 1990 Report used only the adult literacy rate, but this variable failed to discriminate among industrial countries, which often fail to report this statistic to UNESCO. It was for this reason that mean years of schooling was added to adult literacy.

There have been two strands of criticism of this choice. First, it has been argued that literacy is difficult to measure and that it takes different amounts of effort to achieve in different languages. Thus, a Chinese or a Japanese person has to put in much more effort to acquire literacy than a person whose language script is not ideographic (Lind 1991). But the definition of literacy is country-specific, and each culture appreciates the effort expended to acquire literacy. The relative difficulty of achieving literacy in different cultures would matter only if a universal definition were applied. Second, functional literacy is often much lower than recorded literacy, especially in industrial countries, which often claim an impossibly high 99% rate. As literacy is no longer the sole indicator of educational achievement, there is some correction to these biases, but a better definition of literacy would clearly be helpful. This is once again a question of the quality of the variable we are measuring, which is not captured by a simple quantitative measure.

One critic has urged that vocational education, on-the-job training and non-traditional modes of acquiring education be incorporated into the HDI (Nübler 1992a and 1992b). But it would be difficult to acquire reliable data across countries, and some of these variables relate more to human capital formation—and thus to income generation—than to the essential choices captured by the HDI.

Both life expectancy and educational attainment are *stock* variables; they change slowly. One strand of criticism says that school enrolment or university enrolment figures would capture recent educational advance better than the variables now used. In many developing countries, a substantial portion of the growing population is under 18, and often the majority is under 25. Measures that relate to adults or those over 25 cannot capture the *flow* of educational attainment being achieved (Smith 1992). This again is an argument for using a different indicator for the developing economies than that used for the industrial countries. This would make sense if the HDI were to be further developed for specific subgroups, but it is less plausible for a universal HDI (see below).

It is the third variable—*income*—that invites the most discussion. It is also the variable that has been subjected to revised treatment over the three Reports. The indicator used is real per capita GDP in purchasing power parity (PPP) dollars. Thus, there is already an adjustment for such factors as the degree of openness of an economy, the relative sizes of tradable and non-tradable sectors, and possible overvaluation of exchange rates. For income, the maximum difference is between per capita income as a group average and individual or household income as an indicator of access to resources. Income is notoriously unequally distributed but is nevertheless a misleading indicator of differences in well-being between people and households.

The many reservations concerning income as a measure of well-being have been trenchantly expressed by Anand and Sen (1992):

*Income, commodities ("basic" or otherwise), and wealth do of course have instrumental importance but they do not constitute a direct measure of the living standard itself. A person's income level, for example, does not reveal what expectation of life the person has, whether he or she is presently healthy (or suffering from a disease), is disabled and incapable of moving about freely, etc. Even for those features of the living standard where the instrumental significance of private income is likely to be greater, such as adequate nutrition, there is enormous variation in converting income into achieved well-being. People's metabolic rates vary, as do their activity levels and the climatic conditions in which they live. People living in mountainous areas need more energy from food and fuel because they lose more energy in the colder ambient temperature. A handicapped person with a physical disability needs more income to achieve the same degree of mobility than a normal person does. The same is true of elderly and infirm people.*

*To some extent, one can adjust private household incomes for differences in certain very specific and limited needs. For example, a child needs less food to achieve the same level of nutrition as an adult. A large household needs more income than a small household to achieve the same level of consumption of goods and services, though not quite in proportion to the number of its members because of "economies of scale" in such consumption. A household living in a high-price region needs more income to purchase the same food and other commodities than one living in a low-price area. For these differences in needs, and only these, we can adjust household income to take them into account. We do this through so-called "equivalence scales" which correct household income for the size and age-sex composition of its members. And we use price indices to correct for regional and temporal price differences. But it is simply not possible, through income, to account for individual differences in morbidity, mortality or disability—and these features would seem to deserve priority in any assessment of the living standard. There are also other, non-private, economic goods and services which cannot be captured adequately through household incomes. These are the standard public or publicly-provided goods—the environment, infrastructure (such as roads), electricity, transport and communication facilities, epidemiological protection, etc. Thus private incomes fail to capture even some very basic instrumental features of the standard of living in developing countries.*

In incorporating income in the HDI, two major variants were tried. First, in the 1990 Report, the logarithm of income was used rather than the actual value. Second, the poverty level of 17 industrial countries was averaged and converted to real PPP dollars. The logarithm of this poverty-level income was taken as a cut-off point. If a country had per capita income above this level, it was given no extra weight. The first of these two adjustments incorporated the principle of diminishing marginal utility, and the second was designed to emphasize the interest of the *Human Development Report* in poverty alleviation.

In general, the logarithmic transformation, though admitted as "analytically appropriate", was still thought to be "necessarily arbitrary". When combined with a poverty "cap", it was thought that "this implicitly provides greater weight to literacy and longevity than to" income. The treating of income differently than the other two vari-

ables was questioned also on the ground that "there is plausibly diminishing marginal utility to health and educational expenditure as well" (Kelley 1991).

The poverty cap by itself makes little difference, however, and removing it can be shown to have little effect on relative ranking among the rich countries. Kelley took a much higher value (\$12,952, the average real per capita GDP of industrial countries) than the poverty level used in the 1990 Report (\$4,861). He concluded that "the HDI does not appear to be particularly sensitive to the poverty line cut-off, a disquieting finding. It is difficult to believe that such a large increase in income per capita...would have only a small impact on 'enlarging people's choices'" (Kelley 1991).

This conclusion was reached independently in the 1991 Report, which explored a number of alternative treatments. The crucial transformation was to use the logarithm of income rather than the poverty cap. This transformation, though somewhat arbitrary, commands much support (McGillivray 1991 and McGillivray and White 1992a and 1992b).

In the 1991 and 1992 Reports, a different approach was tried. First, the logarithmic transformation was dropped. A modified way of allowing for diminishing marginal utility was introduced. Income up to the poverty level was not discounted at all; dollar for dollar, it was assumed to enhance well-being and to extend choice. Above the poverty level, a progressively severe correction for diminishing marginal utility was introduced through the use of a modified version of Atkinson's formula. Thus, for per capita income between the poverty level and twice the poverty level, the Atkinson parameter (the elasticity of marginal utility of income with respect to income) was taken to be one-half; for per capita income between two and three times the poverty level, the elasticity was taken to be two-thirds, and so on.

The logarithmic transformation over the entire range of income incorporates an elasticity of 1. A poverty cap imposes an infinite elasticity. The formula used in the 1991 Report and subsequently starts with zero elasticity below the poverty level and then gradually increases it. Thus, the capacity of income to produce diminishing marginal utility is taken to be progressive.

This modification has come in for some criticism. It is more complicated than a simple logarithmic transformation because it is a variable elasticity function rather than a constant elasticity one. But its functional form generates an anomaly at the boundary points. An extra dollar has a much higher marginal utility just above a multiple of the poverty level than just below it. Thus, above twice the poverty level, a dollar has a marginal utility of two. This "spike" is hardly visible in the final result but it is an anomaly (Trabold-Nübler 1991).

The main criticism has been that the transformation reduces the weight of extra income above poverty just as severely as the logarithmic transformation. Thus, between the United States and Brazil, the absolute difference in income was \$15,230, but after adjustment the difference was \$450 (Trabold-Nübler 1991).

Treating income above and below the poverty level differently is defensible. Our measure is per capita income, which is a group average rather than personal income. If we consider the poverty level the minimal cost

of providing for the essential choices, it is difficult to argue that extra income within that range is somehow less effective in increasing well-being. Indeed, it can be argued that, until a minimum level of income is reached, it is inappropriate to speak of *utility* in the sense of positive satisfaction derived from income or consumption. In economic theory, the Linear Expenditure System provides us with an example of a utility function that has exactly this property. There is no utility calculable until a minimum level of consumption is achieved with respect to each good in a set of goods. It is only extra consumption—above subsistence—that yields *utility* (Desai 1990).

That said, the issue is still under scrutiny, and later in this technical note alternatives are offered. A logarithmic transformation of income remains a strong challenge to the current approach.

On income, the suggestion has been not that it be replaced (except perhaps by consumption) or supplemented, but that it be retained as the sole variable. It has been argued that, conceptually, income covers the other two variables and that, empirically, these variables are so highly correlated that the other two variables are *redundant*.

With regard to the conceptual issue—whether income captures or encompasses the other two variables—the *Human Development Report's* approach is unambiguously and strongly in disagreement. The important question concerns the lives that people lead—what they succeed in being or doing rather than the goods they consume. The questions of interest are succinctly put by Anand and Sen (1992):

*Do they have the capability to live long? Can they avoid mortality during infancy and childhood? Can they escape preventable morbidity? Do they avoid illiteracy? Are they free from hunger and undernourishment? Do they enjoy personal liberty and freedom?*

*These are the basic features of well-being which derive from looking at people as the center of all development activity. Enhancing their capabilities to function in these elementary ways is what lies at the core of human development. The achievements of people—be it in terms of long life or functional literacy—are valued as ends in themselves. This should be contrasted with more mainstream economic approaches which discuss human resource development. Here the focus is on human beings as a resource—an input into production activities. The development of human resources is seen in terms of their contribution to income generation—as an investment, like any other, in enhancing the productive potential.*

*Whereas the human development approach values capabilities related to, say, health, nutrition, and basic education as ends in themselves—and income as only a means to achieve these—human resource development (like "human capital" investment) is based on precisely the opposite valuation. This approach assesses investment in human capital—including health, nutrition, and education—entirely in terms of the extra income or output the investment generates, judging it to be worthwhile if the rate of return exceeds the capital cost. By contrast, proponents of the human development approach would argue for the enhancement of people's ability to read and write, or to be well-nourished and healthy, even if the conventionally measured economic return to investment in*

literacy, or improved food intake and health care, were zero (though, of course, they are typically quite high anyway).

The empirical issue of redundancy is best tackled in terms of the weights assigned to the different variables, because redundancy implies that the weights should be unequal—one for income, zero for the other two.

### Measurement errors

A major problem with economic statistics at national and international levels is their accuracy. Very often, official statistics are estimates or projections based on past data. They frequently contain conceptual definitions that are inappropriate or not comparable with other countries' data, and errors due to faulty or inadequate sampling and to errors in recording and transmission. And the data are often not up to date. (Srinivasan 1992 offers a comprehensive overview of these problems.)

It has been pointed out that life expectancy data convey a spurious accuracy. These data should ideally be based on decennial censuses and then revised in the light of annual birth and death registrations. But seven of 180 developing countries have still not conducted a popular census, and for 22 others the most recent census dates to before 1975. For as many as 57 of 117 developing countries, reliable data on life expectancy are not yet available (Srinivasan 1992, citing Chamie 1992).

Data on literacy also depend on decennial censuses and are reported by countries to UNESCO. There may also be at least three widely accepted alternative definitions of literacy that UNESCO must try to reconcile in producing measures of literacy.

The measurement of income has a well-documented history of conceptual and statistical problems. For countries with substantial subsistence farming, there are formidable problems in estimating income. In many countries, industrial and developing, there is the problem of estimating informal sector and "black" income. In the transitional economies of Eastern Europe, the prices of many commodities have stabilized at levels that could be considered as reflecting relative scarcities, and pretransition prices have been exposed as misleading signals. This has led to drastic revisions in the estimated levels of income in pretransition years as well as to problems in gauging the challenges in maintaining incomes and living standards during the transition.

These problems are not easily overcome, but they need to be acknowledged more comprehensively. Ideally, all values should be interval estimates rather than point estimates. But while this remains a distant prospect, there is clearly a need for caution in taking HDI values (or any similar estimates) as firm guides in decision-making. At the same time, more resources can profitably be used in improving statistics.

On the issue of the robustness of HDI to measurement errors, McGillivray and White have tested the sensitivity of the HDI rankings to measurement errors in the underlying data. They considered two possibilities: first, that each variable was measured with an error of between -5% and +5%, and, second, that the errors lay between -10% and +10%. They generated random errors within this range and then added them to variables for different countries and calculated simulated HDIs. They found that

for the vast majority of countries, changes in ranking are relatively minor... If we calculate rank correlation coefficients between the HDI and its observed counterpart based on a measurement error within the range of -5 and +5 percent, we find coefficients of 0.996 and 0.995 in 1990 and 1991 respectively. Given the closeness of these coefficients to 1, we draw the conclusion that the HDI is extremely robust to measurement error within this range.

When they tried errors between -10% and +10%, the resulting correlation between the "true" and the simulated HDI was 0.993 for 1990 and 0.990 for 1991. Even when they tried a different range of errors for the poor and the rich countries, the conclusions were not altered. But none of this should detract from the need to improve the quality of the statistics.

### Choice of minimum and maximum values

Each dimension of the HDI is measured by one or more variables and then reduced to a measure of relative distance. This distance measure is taken as the actual value minus the minimum value relative to the range—that is, maximum less minimum. Thus, for a dimension  $i$  for a country  $j$

$$H_{ij} = \frac{X_{ij} - \min_k X_{ik}}{\max_k X_{ik} - \min_k X_{ik}}$$

where  $j$  and  $k$  are indexes for country. Then the overall index is

$$H_j = \frac{1}{3} \sum H_{ij}$$

In every *Human Development Report*, the maximum and the minimum for life expectancy have been defined by the sample. Thus, the actual maximum and minimum for all countries in any year enter the calculation of  $H_{ij}$ , labelling life expectancy as  $i$ .

If the maximum and minimum values were to change over time, this might lead to an anomaly in which a country's actual life expectancy could go up while its score goes down. This may happen because the minimum has gone up or the range has widened over time, or both. Thus, "moving the goalposts" makes comparing the HDI over time more difficult.

The 1991 Report considered trends in human development for the first time. For this purpose a modified HDI was introduced in which the maximum and minimum were defined not separately for each year but for the entire period 1960-90. Although this was good for each period, it fails to deal with the problem over time, because in the future—say, for 1960-95—the maximum and minimum values could move again.

TECHNICAL NOTE TABLE 2.1  
Maximum and minimum values

	1990		1991		1992	
	Max	Min	Max	Min	Max	Min
Life expectancy	78	42	78.6	42	78.6	42
Literacy	99	12	99	13.3	99	18.2
Mean years of schooling			12.2	0.1	12.3	0.1



Before considering the alternative of normatively fixed maximum and minimum values, it may be of interest to examine the extent of the shift over time. As technical note table 2.1 shows, the movements in life expectancy are very slight. Indeed, the improvement from 78 to 78.6 can be thought of as the correction of a rounding error. Only the minimum value for literacy shows a sudden jump, from 12 to 13.3 to 18.2. This continues the earlier discussion about the difficulty of measuring literacy. One cannot of course discount the possibility that once it is known that literacy rates enter the HDI, their measurement may become subject to policy manipulation (a problem known in macroeconomics as "Goodhart's law"). The problem of fixing normative constant maximum and minimum values has been discussed by Anand and Sen (1992):

*Granted that the "goalposts" need to be fixed if the HDI is to be comparable over time, we need to ask how the goalposts should be determined. It will not be enough to fix the range of values for each X by simply looking at the minimum and maximum levels achieved retrospectively, say in the period from 1960 to 1990. We also need to look prospectively at the projections for each X and ensure that individual country levels will remain inside the range forecast in the future, in other words, over the entire period—backward and forward—during which intertemporal comparisons are required to be undertaken.*

*In the main this affects the range for the longevity variable. Looking back in time to a point when sufficient data were available for intercountry comparisons (e.g. the year 1960), the minimum level of life expectancy at birth achieved was about 35 years. For comparisons in the future going as far as 2050, national life expectancy at birth has been projected to reach 85 years for some countries. Thus keeping to the basis definition of HDI, we could choose as our fixed endpoints for X a minimum value of 35 years and a maximum value of 85 years. This range encompasses the lower and upper bound of life expectancy estimates over which both cross-country and intertemporal comparisons of HDI are envisaged.*

*As far as the literacy variable is concerned we may choose the natural range of 0 to 100 percent. Although the lower end of the range is at the present time unlikely to be experienced at a national level, there are disaggregations we are proposing for which literacy rates even today fall below 10 percent (e.g. the female adult literacy rate in Burkina Faso or Somalia). Moreover, if intertemporal comparisons were to start back from 1960, we would indeed be approaching the lower end of the 0 to 100 percent range in some cases. Hence, we take 0 to 100 percent as the min-max interval for adult literacy.*

*The final component of HDI is the logarithm of per capita GDP in 1987 PPP dollars truncated at the average official poverty line income in nine developed countries. The logarithmic transform of income is taken in order to reflect diminishing returns to transforming income into human capabilities. The ceiling on income at the poverty line is imposed because of the particular relevance of poverty removal in human development (Desai 1991:355). The upper bound of the max-min range for the income variable is kept constant over time at the logarithm of PPP\$4,861 in 1987 prices. The lower bound for the variable again poses a slight difficulty: we choose a value of 0 to reflect negligible human develop-*

*ment beyond the minimal levels of life expectancy and literacy achieved in the past in some countries.*

## Weights

The equal weighting afforded to the three variables has led to much debate. In an ideal world, the "meta production function" of human development would be specified, and the contribution of each variable to human development would be its weight. Objecting to equal weights, Allen Kelley (1991) wrote:

*The greatest problem occurs with the relatively low weight accorded to GDP/N (per capita real income) in moderate to high income countries since the variable measured by this particular indicator (income) can be used to acquire and/or produce either of the other two indicators (improved health or education). Possibly a weight roughly reflecting the acquisition/production-transformation would have been appropriate under the premise that in some countries individuals may well have elected to use their income to expand choices in ways that do not result in, say, improved education or health. Indeed, it might be argued that the capacity to choose among many dimensions of human development accorded by increased income in particular merits giving a relatively higher weight to this indicator.*

Of course, in the long run, causality can run from education and health to income as well as the other way around. Because higher per capita real income can lead to better provision of public goods as well as higher consumption, it is misleading to think of income simply in terms of personal choice.

Lacking a meta production function, investigators have explored the pattern of correlation among variables. One approach has been to carry out a principal component analysis (PCA) on the data (Tatlidil 1992). There is, of course, a high degree of simple correlation among the variables. For the three variables—life expectancy, educational attainment and (adjusted) income—and the data from the 1992 Report, the pattern of correlation was as in technical note table 2.2. But the PCA shows that the principal eigenvalue explains 88% of total variance in the data, obviously a very high measure of commonality in the data (technical note table 2.3).

TECHNICAL NOTE TABLE 2.2  
Correlation matrix of variables

	Life expectancy	Adjusted GDP	Educational attainment
Life expectancy	1.000		
Adjusted income	0.848	1.000	
Educational attainment	0.871	0.729	1.000

TECHNICAL NOTE TABLE 2.3  
Principal component analysis results

	2.633	0.272	0.095
Eigenvalues			
Explained variance	87.769	9.080	3.151
Component loadings			
Life expectancy	0.969	0.030	-0.246
Adjusted income	0.916	-0.386	0.113
Educational attainment	0.925	0.350	0.146

But it is interesting to see that the eigenvector corresponding to the leading eigenvalue puts virtually equal weight on the three variables—life expectancy (0.969), adjusted income (0.916) and educational attainment (0.925). The second and third eigenvalues, which explain relatively less (9% and 3%), have radically different eigenvectors, including some negative ones. Thus, although an HDI based on the eigenvalues of the principal eigenvector would give results identical to those of the present HDI, one based on the second eigenvalue would give a negative weight to income (−0.386) roughly equal to the positive weight attached to life expectancy. An HDI based on these weights would yield a very different interpretation. Because of the low explanatory power of such an HDI, it would be unwise to put more faith in it.

Thus, the PCA confirms the equal weights but also points to the high degree of correlation. There is no presumption about causality in the PCA. Thus, it does not advocate omitting or downgrading a variable. In another exercise, McGillivray and White correlated a combination of two of the three variables with the third. But rather than the actual values of the variables, they used the ranks. This weakens their point, but they did find high correlations for both the 1990 and the 1991 HDI for all countries as well as for developing countries and industrial countries. When they carried out the same exercise for high, medium and low levels of human development, they found a much lower correlation. Such a change in correlation would not occur if the actual values of the original variables had been used, but it does with the ranks because the ranks are shuffled differently in classifying countries by levels of HDI.

Because of the symmetry of the three variables and the lack of causality ordering, it is difficult to decide which of the three variables dominates; McGillivray and White prefer income over the others. The results of the PCA, which advocates equal weight on the same database, seem persuasive.

But the equal weights are partly misleading. Because each variable is relative to its range and the ranges are very different, the actual effective weights are also very different. This can be seen by asking the following question:

How much does a country's HDI change for a unit change in an indicator?

The ranges—that is, the difference between the maximum and minimum—were 36.6 (=78.6 – 42) years for life expectancy, 80.8 (=99 – 18.2) percentage points for literacy, 12.2 (=12.3 – 0.1) years for mean years of schooling and \$5,074 dollars for adjusted income for 1992. Thus, a one-year improvement in life expectancy, a one-percentage-point increase in adult literacy, a one-year improvement in mean years of schooling and a \$1 increase in per capita income would represent the following changes in the HDI:

One unit change in	Change in HDI
Life expectancy	1/108
Literacy	1/365
Mean years of schooling	1/108
Income	1/15,222

It would be tempting to interpret the relative coefficients as trade-offs, but a note of caution should be introduced. Superficially, it would be easy to say that one extra year of life expectancy is "worth" \$150 of income, but these are not choices open to an optimizing economic agent. Take a poor country with per capita income as high as \$1,500 (only 17 of the 65 countries with low human development in 1992 had income this high). An extra year of life expectancy (above a median value of about 50 years) would be the same as 10% growth in real per capita income. Neither of these two outcomes is likely in the short run, nor are they independent of each other in the real world. Thus, it would be wrong to interpret the coefficients as reflecting a "menu of policy choices".

The real importance of the calculations is to show that what are frequently seen as equal weights (and were even reflected in the principal component analysis) miss the unequal ranges of the variables. In the 1990 Report, the actual effective weight of income, after the log transformation and the capping at the poverty level, was variable at different levels of income. Thus, an increase in income from \$400 to \$450 improved the logarithmic value by 0.06 relative to the range of 3.68—by 1/60—and hence the actual effective weight was 1/180. At \$2,000, an increase of \$250 would be required to get the same effect. Above the poverty cap no amount of improvement was sufficient. Even in the context of the present transformation of income, an extra dollar of per capita income is not the same above as below the poverty line. The higher the income, the steeper the trade-off is in actual dollars.

There is another reason to be cautious in treating the ratios of actual effective weights as trade-offs: the HDI is not a cardinal index to be maximized, but an ordinal measure for relative ranking among countries. This is well expressed by Anand and Sen (1992):

*Some commentators on the Human Development Report 1990 have been disconcerted by this normalization of each component  $H_i$  of the aggregate index  $H_j$ . They point out, for example, that an improvement in the achievement of the lowest-achieving country in the sample would decrease the HDI for country  $j$ , and this is not the sort of externalities that one wants in an index. But the human development index in the 1990 (and subsequent) Reports was constructed expressly as a measure of relative performance across countries at a point in time. No special significance is attached to the absolute value of the index, the entire analysis being conducted in terms of the ranking of countries relative to one another. Thus although a higher value of  $\min \{X_{ik}\}$  or of  $\max \{X_{ik}\}$  would indeed decrease for  $H_{ij}$  for country  $j$ , it would also do so for all other countries  $l$  too, and in proportion to the gap  $(H_i - H_j)$  between countries  $j$  and  $l$ . This, of course, has the effect—given the basic information—of leaving the relative ranking of countries unchanged.*

*As defined, the human development index  $H$  for country  $j$  is invariant to positive affine transformations of the underlying variables  $X_i$ ,  $i = 1, 2, 3$ . Thus if one were to substitute for each  $i = 1, 2, 3$ ,  $Z_i = a_i X_i + b_i$  where  $a_i > 0$ , the absolute value of each  $H_{ij}$ , and therefore also of  $H_j$ , would remain the same. In particular, if one changed the units of*

measurement of  $X_i$  by either scale changes ( $a_i > 0$ ) or level changes ( $b_i \neq 0$ ), the indices  $H_{ij}$  and  $H_j$  would have the same numerical values as before.

### Disaggregation of the HDI

In previous *Human Development Reports*, there has been an attempt to disaggregate the HDI for women and men. In a way, this disaggregation preserves the universality of the HDI while allowing for disaggregation. Gender is, after all, a universal classifier. But other such classifiers can also be used. Thus, disaggregation by urban versus rural residence, by ethnicity, or by region or continent is possible. In *Human Development Report 1993*, a disaggregation by ethnic groups has been carried out for a small number of countries.

Disaggregation by gender raises some interesting issues. Anand and Sen (1992) discuss this in detail, and their analysis bears quoting in full:

*...there is considerable evidence of anti-female bias in some countries in the world. This takes the form of unequal treatment in access to food, health care, education, employment and income-earning opportunities—and is reflected in different achievements of women relative to men. Gender bias exists both within the household and outside the household, for example, in the labour market or the provision of public health services. We should like to use the HDI to illuminate gender disparities that result from such unequal treatment.*

*Unlike conventional measures of development, such as those based on income or the possession of commodities, the HDI is particularly well-suited to examining gender inequalities. The reason is that the informational requirements of resource-use measures such as income—especially when estimation of their allocation within the household is involved—make them very problematic in shedding light on inter-individual differences. By contrast, the consequences of female disadvantage and gender bias, both intra- and extra-household, will be reflected in the achievements of the individuals concerned in terms of their life expectancy, literacy, survival chances, and so on. Data on these achievements are collected not at the household level through household income and expenditure surveys, but at the individual level through demographic surveys and population censuses. There is, thus, a strong practical reason—in addition to concern for what is intrinsically important—in adopting the HDI to examine gender and other inter-individual disparities.*

*In considering the disaggregation of HDI by gender, we must take note...of the higher potential life expectancy of females vis-à-vis males. The separate goalposts of life expectancy for females and males are taken to be 37.5 and 87.5 years for women, and 32.5 and 82.5 years for men. Thus the life expectancy range is 50 years for both women and men; this implies that a unit increase in longevity for either sex (over time) will contribute the same increment to the overall HDI...*

*The range for adult literacy is the same for females and males, as is that for the logarithm of per capita GDP truncated at the poverty line income. While separate adult literacy figures are in general available by gender, sex-specific estimates of income-use are difficult, if not impossible, to establish with any accuracy even for the advanced industrial*

*countries (for the reasons mentioned earlier). Thus if F and M refer to females and males, respectively, the female and male HDIs for country j are given by*

$$H_j(F) = \frac{1}{3} \left[ \frac{X_{ij}(F) - 37.5}{50} + \frac{X_{2j}(F)}{100} + \frac{X_{3j}(F)}{3.687} \right]$$

and

$$H_j(M) = \frac{1}{3} \left[ \frac{X_{ij}(M) - 32.5}{50} + \frac{X_{2j}(M)}{100} + \frac{X_{3j}(M)}{3.687} \right]$$

### HDI: universal or specialized

A constant concern in constructing the HDI has been to preserve its universality—to retain a single index for both the rich and the poor countries. This makes clear that human development is not a concern solely for poor countries. In the 1990 Report, the deformations caused in rich societies by a number of adverse developments—drug addiction, crime, family breakup—were remarked upon.

There has also been a search for variables that will help discriminate among rich countries that might otherwise all cluster near the top of the HDI ranking. Thus, mean years of schooling was introduced to allow fine distinction at the top. A similar motivation was behind the decision to remove the zero weight to income above the poverty line in the 1991 Report.

But if the HDI is taken to be a measure of the minimum necessary—of the essential choices—there is obviously scope for human development beyond the top value for the HDI. And at lower levels of human development, there may be a need to emphasize indicators that can be ignored at higher levels. The universality of the HDI would then be an obstacle to constructing subindices for special groups of countries.

One set of suggestions in this respect has been made by Anand and Sen. They propose using the distinction currently made among high, medium and low levels of development. Then, for each group they propose a specific group of indicators. Thus, for the low level, they would drop mean years of schooling and revert to the 1990 Report's definition of the HDI. For the medium level, they propose adding under-five mortality to life expectancy, secondary school enrolment to literacy and incidence of poverty to log of per capita income. For the high level, they propose further adding maternal mortality, tertiary enrolment and Gini-corrected mean national income; these suggestions are summarized in technical note table 2.4. Anand and Sen do not discuss the question of the weights to be assigned to these indices in each use, however.

### Suggestions for future improvements

This survey of the many critical papers written on the HDI shows that in many instances the criticisms have been implemented, and in some cases (for example, the treatment of income) there is scope for further change. No change has been incorporated in the 1993 Report, in part to avoid inconvenience caused to the users of the HDI by frequent revisions. But it is also the intention of

the *Human Development Report* team to invite suggestions from readers about the future course of the HDI.

Following are possible improvements that have been discussed:

- Keeping the maximum and minimum normatively fixed rather than variable. Thus, for longevity, the maximum would be 85 years and the minimum 35 years. With an adjustment for gender to construct separate indices for women and men, the maximum would be 87.5 years for women and 82.5 for men; the minimum would be similarly adjusted. For literacy, the limits would be 100 and 0 and for mean years of schooling, 15 and 0. For income, the upper limit can be taken to be \$35,000 in real income

TECHNICAL NOTE TABLE 2.4

**Suggestions for special human development indices for specific groups of countries**

Human development level	Low	Medium	High
Human development indicators	1.1 Life expectancy	1.1 Life expectancy	1.1 Life expectancy
		1.2 Under-five mortality	1.2 Under-five mortality
			1.3 Maternal mortality
	2.1 Adult literacy	2.1 Adult literacy	2.1 Adult literacy
		2.2 Secondary school enrolment	2.2 Secondary school enrolment
			2.3 Tertiary enrolment
	3.1 Log per capita GDP (up to international poverty line)	3.1 Log per capita GDP (up to international poverty line)	3.1 Log per capita GDP (up to international poverty line)
		3.2 Incidence of poverty	3.2 Incidence of poverty
			3.3 Gini-corrected mean national income

Source: Anand and Sen 1992.

per capita (PPP), which would require 2% growth for 50 years for the richest country to reach.

- Taking the logarithm of income over the entire range rather than the present variable elasticity approach. This would also mean removing the poverty cap.
  - Constructing supplementary indices for specific groups of countries with low, medium and high human development. The suggestions by Anand and Sen were described above, but there is clearly scope for other suggestions here.
  - Disaggregating the HDI within each country. The HDI is already disaggregated by gender, though only for a limited number of countries. Disaggregation by region and by ethnic group has been introduced in this Report. There is no doubt scope for further disaggregation—for example, by immigrants within a country, the elderly and the disabled.
  - Adding dimensions. The possibility of adding new dimensions has not been explored beyond refining the number of variables used for each of the three dimensions. The small number of dimensions has been helpful in preserving the simplicity of the HDI, which has been a strong factor in its transparency and the ease of communicating its meaning to a wide audience. Any additional dimension will have to have strong grounds for inclusion.
- It is hoped that some of the suggestions will be commented upon by our readers and by those who use the HDI—whether in academia, in policy-making circles or in the private sector. The participatory mode is desirable not only for the process of human development but for its measurement as well.

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