

# Leveling the economic and political playing fields

## PART III

WHAT CAN BE DONE TO INCREASE EQUITY IN THE WORLD? Can this be done in ways that also spur long-term prosperity? We read in part I that there are large inequalities of opportunity between people within countries and—even more—between people in different countries. These inequalities are perpetuated through interlocking economic, political, and sociocultural mechanisms, creating inequality traps. Individuals from different groups and countries face a highly uneven playing field, both in their capacities to acquire endowments and aspire to a better life, and in their opportunities to reap returns from those endowments through market and nonmarket processes. Because differences between countries often exceed within-country differences, it is of particular importance that national policies support, or are at least consistent with, the narrowing of international differences, notably through the growth process.

We argued in part II that many inequalities not only violate people's concern for fairness, but actually have costs for the development process. The effects on development depend on specific forms of inequality and their interactions with market imperfections and institutions. Unequal opportunities are associated with inefficiencies and wasted economic potential. Pronounced inequalities in the distribution of power are often associated with weak economic institutions, undermining the investment and innovation that is central to long-run growth. Greater equity is thus not only intrinsically desirable but also is complementary to long-run growth and prosperity. For poorer and excluded groups, a focus on equity can bring a double benefit—a bigger pie and a greater share.

But the scope for such a complementary relationship between equity and aggregate development is often not exploited. When examining this, we suggest there are two kinds of pathology in policy



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design. First, there is the pathology associated with oligarchic dominance—institutions and policies that further the interest of elites but not those of the whole society. This may take the form of extreme predation and high-level corruption, as in Mobutu's Zaire or Haiti under the Duvaliers. Or it may take the form of enmeshed alliances between economic and political elites that favor rent-seeking, as in the Philippines under Marcos, in much of Latin America in past decades, and in more subtle forms in many countries of the world.

Second, there is a more complex pathology of policies pursued with the intent, or in the name, of equity that have high efficiency costs or perverse effects. Communist economic policy was disastrous for efficiency, even while many communist societies did much in social provisioning. Directed credit—in India, for example—was intended for the poor (and reached some of the poor), but proved a high-cost strategy. Populist macropolicy is always bad for growth, and almost always bad for equity sooner or later—witness Argentina during much of the second half of the twentieth century. Perverse or growth-sapping effects of policies under this pathology can be caused by adverse consequences for incentives, unaffordable fiscal burdens, or the capture of the benefits, often by middle groups, which “hoard opportunities” at a cost for other groups and the overall growth process.

What can be done? At a fundamental level, the analysis underscores the centrality of shifting to a state that is more accountable, has checks on predatory behavior of political and economic elites, is responsive to all citizens—especially from middle and poorer groups—and has effective conflict management mechanisms. In part II, we sketched cases of transitions in this direction from history and contemporary experiences, and at the local level. The emphasis in the development community on issues of governance and empowerment is entirely consistent with this perspective.

While such overall shifts are central to development, the World Bank has neither the mandate nor the comparative advantage to discuss specifics of the design of political

institutions (even though action to support empowerment of the poor is now emphasized in the design of specific policies—see Narayan 2002). In part III, we focus on a set of areas that do lie squarely in the arena of development analysis and practice—in policies affecting the sectors, markets, and in the global arena. This recognizes the influence of the political and sociocultural context, but focuses rather on what an equity prism, based on the analysis of parts I and II, has to say about the policy design to break inequality traps and support aggregate growth. The lesson from part II is that this implies paying attention to *specific* inequalities and their interactions with markets, social structure, and power. This involves both issues of technical design and mechanisms that provide the political underpinnings for change, notably through broader accountability, coalitions for change, or compensation of losers. And while an overarching message is of the potential complementarity between greater equity and long-run prosperity, there will often be tradeoffs in specific areas and context. One cross-cutting area concerns the need to raise taxes to finance desirable public spending. The design of tax instruments is of great importance to minimize adverse efficiency effects, while also promoting equity where feasible.

We organize the discussion of domestic action into three areas. First is building and protecting people's human capacities—from the start of people's lives and through adulthood and old age. Here we focus on equalizing from the bottom up—equalizing up the opportunities of the least advantaged in terms of skills, health, and risk management. There are certainly issues of equity among more advantaged groups, but we give priority to the disadvantaged (in part for reasons of space). As seen in part II, there are major market imperfections in human capital formation and insurance that affect poor or lower-status groups most, yet political action has also often been biased against these groups.

Second is ensuring equitable access to justice and complementary assets. A fair and accessible justice system is crucial for constraining the power of the political and eco-



economic elite, avoiding discrimination, and protecting property rights and personal safety for all—with important implications for the willingness to invest and innovate. Inequitable access to land and infrastructure—by wealth, location, or social group—is typical of developing societies and often enmeshed with political structures. Policy design can help shifts to more equitable and often more efficient patterns (chapter 8).

Third is the domain of markets—financial, labor, and product—that have a powerful influence on the returns to people's endowments. As chapters 5 and 6 argued, markets are typically far from ideal, working in noncompetitive and discriminatory ways, whether because of intrinsic market imperfections, or because power structures have shaped them to serve the purposes of those in power. In these areas, and notably in the case of finance, a primary concern is equalizing down, by reducing protecting privileges of incumbents. Closely related is the conduct of macroeconomic policy (chapter 9).

In the global arena, concern remains with individuals—and the enormous, unjustified differences in opportunity that people face through the morally irrelevant fact of country of birth. The global playing field between

nation-states is uneven—and has uneven effects on different groups within countries. There is substantial scope for making the playing field more even. But as in the domestic arena, policy design involves both technical questions (such as the details of migration arrangements and the application and design of patent legislation) and the political underpinnings of rules and institutions for global governance. We examine the potential for change both in the key global markets—for labor, products, ideas, and capital—and in the potential scope for designing aid in ways that support (rather than undercut) domestic development, and through more effective and equitable management of the global commons (chapter 10).

The epilogue links the report's perspective on equity to the thinking and agreements that have evolved in the development community in the past decade—captured, for example, in the Millennium Declaration (2000) and the Monterrey Consensus (2002)—as well as the World Bank's own strategic pillars of an enabling investment climate and promoting empowerment. We argue that an approach to development that is deeply informed by equity is fundamental to the full integration of these frameworks into an effective development strategy.