

EconoFact Chats: Understanding Global Poverty Reduction

Lant Pritchett, University of Oxford

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Michael Klein:

I'm Michael Klein, executive editor of EconoFact, a non-partisan web-based publication of the Fletcher School at Tufts University. At EconoFact, we bring key facts and incisive analysis to the national debate on economic and social policies, publishing work from leading economists across the country. You can learn more about us and see our work at www.EconoFact.org.

Michael Klein:

The World Bank estimates that one person in 11 in the world lives in extreme poverty. While this is a troubling statistic, it's also worth noting that three decades ago, this number was more than one in three. Now, however, there are concerns that the economic contractions due to the effects of the COVID-19 pandemic will reverse this progress. The World Bank estimates that as many as an additional 115 million people will fall into extreme poverty because of slowing economic growth. The field of development economics focuses on improving the prospects of those in low income countries.

Michael Klein:

One of the most prominent economists focusing on this issue is Lant Pritchett, my guest today on EconoFact Chats. Lant is currently the research director for the program Research for Improving Systems of Education at the Blavatnik School of Government at the University of Oxford. Previously he taught at the Kennedy School of Government at Harvard University. Lant also worked at the World Bank for almost two decades before taking his position at Harvard. Lant, welcome to EconoFact Chats.

Lant Pritchett:

Glad to be here.

Michael Klein:

Lant, first off, how do we define extreme poverty?

Lant Pritchett:

Well, the important thing to understand about any poverty definition is it's fundamentally a social construct. You choose some level of wellbeing and say people below that level of wellbeing, we're going to say in poverty. How the World Bank created its estimate of extreme poverty was actually by looking at poverty rates around the world, and different countries have different poverty rates. So they chose for their definition of extreme poverty the poverty line used by the poorest countries in the world. They said, "Look, if you're poor by the standards of the poorest countries in the world, then that's a pretty good absolute threshold for what we'll call extreme poverty." At the time, that was about a dollar a day, and so it's often called the dollar a day standard, even though by inflation, it is now about a \$1.90 a day per person, as a threshold.

Michael Klein:

But in the United States, a dollar a day would not be the poverty level, right?

Lant Pritchett:

Exactly. One of the things is that countries as they get richer, they naturally raise their standard of living that people would have in order to be considered poor. In the United States, for instance, the official poverty standard is actually about \$18 a day. So someone poor in the United States actually has about 10 times the purchasing power as someone considered in extreme poverty by the World Bank statistics.

Michael Klein:

So this suggests there's a basic incomparability of poverty in rich and poor countries.

Lant Pritchett:

Very much so. The phenomena of high levels of poverty by thresholds like extreme poverty is fundamentally one of being in poor places. When you have very high levels of poverty, it isn't that you have poor people, it's that you have people trapped in low productivity and hence poor places. It's often more helpful for dealing with levels of extreme poverty in developing countries to think about what's keeping the productivity of this place low, rather than thinking about the individual.

Lant Pritchett:

For instance, in Vietnam, the poverty rate went from more than half of the country to only 2.5% in the span of just 20 years. That was because it wasn't that the people of Vietnam were intrinsically poor or had characteristics that didn't allow them to be more productivity, it was that Vietnam was a low productivity place and rapidly became, through economic growth, a high productivity place. So yes, when you think about poverty in the developing world, it's much more helpful to think of poor places than it is to think of poor people.

Michael Klein:

That's a really striking statistic you cite about Vietnam. In the introduction I cited some statistics on the reduction of world poverty over the past few decades. Was this unusual or has poverty in the world generally been falling over the past few centuries?

Lant Pritchett:

Well, over the past few centuries, poverty was slowly falling and then kind of accelerated in the 20th century. And then accelerated even more, perhaps not surprisingly when the countries became independent after decriminalization. So since 1950, there's been pretty rapid progress globally, but it's also quite differential. According to the World Bank, which are kind of the standard measurement, from 1981 to 2015, global extreme poverty fell from 42%, which means just sort of in the last 40 years, one in three people in the world has moved out of extreme poverty.

Lant Pritchett:

That said, it's a very regional phenomena because in East Asia, that's gone from 80% to 2%. So fundamentally extreme poverty was far and away the norm in East Asia, even as recently as 1980, and now is essentially eliminated. Whereas regions like Sub-Saharan Africa, during that same period, the extreme poverty rate's only gone from 54% to 41%, so much less progress.

Michael Klein:

Americans listening to this podcast may be thinking of all of the evidence on rising inequality in the United States, but inequality and poverty are distinct concepts. And also the statistics on world poverty that you're citing point in the opposite direction, poverty is falling. How do we reconcile this? Or how would you explain to an American audience what's going on in the world, more broadly?

Lant Pritchett:

Well, first of all, it's really important that we explain this to an American audience because American audiences just have the wrong facts in their head about global poverty. And surveys where you ask people, "Has poverty in the world gotten worse, stayed about the same, or gotten better?" Only about 15% of Americans actually get it right, that poverty has gone down. Hence 85% believe that poverty is roughly the same or worse, which just isn't true. I think a lot of this is, it's really easy to be pretty attuned to the reality right around you and then it's pretty easy to look in the mirror and pretend you're seeing out a window and extrapolate your own experience for the rest of the world.

Lant Pritchett:

So in the rest of the world over this recent period, the countries have had much less on average, I think, increase in inequality and much higher rates of growth. Which means even in the developing countries in which inequality has been increasing, the rate of growth of the economy has been sufficiently fast that even the bottom part of the population, in absolute terms, is very rapidly coming out of this absolute standard of extreme poverty. So some of the poorer countries like China for instance, did in fact have vast increases in inequality. But on the other hand, the overall economy was growing so fast that even if you differentially benefited less from the growth, you still had large absolute improvements, and hence poverty went down.

Michael Klein:

Another aspect that the United State citizens might think about in the questions whether or not it's applicable to the rest of the world, is that in the United States, if you're born poor, there's a very good chance that you'll be poor when you grow up. There's not much churning between being poor and being rich. Is this true in low income countries as well?

Lant Pritchett:

No, this is quite a bit different in low-income countries, and one of the things that's important to remember is when we create a category called poverty, poverty is an episodic experience of individuals. We shouldn't think of people who experiencing an episode of poverty as being poor people, as if that's a chronic condition or a lifetime condition. I did a study with some other authors where we looked over 10 year periods, and what we found was really important, which was that net improvement in poverty had a lot to do with how much churn there was.

Lant Pritchett:

We found in the region of India we studied that about 20% of the population came out of poverty in a 10 year period, and about 8% went back in. So there was a net 12% improvement from the churn back in. Whereas in Africa, also about 20% of the population moved out of poverty, but 18% of the population moved into poverty. So the net reduction in poverty was only 2%. In the countries that I've studied, because so many people are near the poverty line and because poverty includes so many people, there is a lot of churn of individuals and households above and below the poverty line over time.

Michael Klein:

Going back to, Lant, the discussion on the links or lack of links between inequality and poverty, you've told me about something called the elephant graph that illustrates what's going on with inequality, and this was a pretty striking thing. Can you describe that, please?

Lant Pritchett:

Yeah, sure. Branko Milanović has studied global inequality and what he looks at is, let's line everybody in the world up from the poorest to richest and then see how their particular incomes of these different percentiles of the world distribution, fared. What he found is there was a group at the very bottom that didn't fare very well. But then in the broad middle of the global income distribution, which is India and China, and many of the large countries in Asia, they actually had very rapid growth rates. So the absolute progress of the broad middle of the global income distribution went up very fast.

Lant Pritchett:

However, as you move to say, the 80th percentile, which is the lower end, say of the United States or Europe, or in particular, the ex Soviet Union, they had almost no progress over a 30 year period. So it was in fact the case that the poorer within the rich countries fared very badly over this period, even though the broad middle of the world's poor countries did well. But then at the very top... and this is why it's called an elephant graph, it's like the elephant's trunk shoots way up. At the very top, it is the case that the world's richest had in some sense, the best experience and had their income go up by the most. There's a very high non-linearity in how inequality affected absolute change in income to where the broad middle, people in India, people in China, people in Bangladesh actually did quite well. While at the same time, the poorer people, both within the developed world did very badly and the richest of the rich fared very well.

Michael Klein:

So that middle section, that's really remarkable. A remarkable change in a couple of generations in the level of human material wellbeing, especially considering human history up to that point where it was flat for a very long time. What's the source of poverty reduction?

Lant Pritchett:

The basic source of poverty reduction is economic growth. When you look either at the levels of poverty against the levels of income, or how income changes over time with respect to changes, if you compare the income of the typical individual in the economy or the median to the poverty rate, they're almost perfectly correlated. So if we look across time for the data that we have, more than 90% of the variation in whether poverty went up or down is associated with whether the median household in your country had their income grow or fall.

Lant Pritchett:

So as a proximate determinant of poverty, essentially all of the variation and all of the variation over time and space is accounted for by the broad based productivity of the economy as measured by the income of the median person. It just isn't the case that we've gotten particularly better at designing or implementing, or funding anti-poverty programs. Most of the reduction in poverty has come from economic growth.

Michael Klein:

You have that [crosstalk 00:13:21].

Lant Pritchett:

As I lay out in an EconoFact memo from last year, you just look at these graphs and it's just overwhelmingly striking. It's one of the most powerful correlations that I've ever seen in four decades of empirical research.

Michael Klein:

Yeah, that was a very striking graph in your memo about the level of poverty and the amount of economic growth. It struck me when you published that. Well, what about the causes of economic growth? That's still kind of a puzzle, right?

Lant Pritchett:

I think it's still very much a puzzle. I've been living and working for instance in India over the last 30 years, and over those last 30 years, India has demonstrably had very rapid accelerations and decelerations in growth, but there's no particular consensus on what caused those. I think this is why this is an important area of research and the answer, not surprisingly I think, is going to turn out to be very complex.

Lant Pritchett:

I think nearly everyone who studies economic growth has realized that there's not going to be any simple answer that applies in all times and all places. But I think we are making some progress towards understanding what accounts for both episodes of rapid growth and episodes of collapse as well. But we don't want to confuse the two issues. Factually we know broad-based economic growth is super powerful and basically explains whether poverty goes up or down. Now as for the underlying causes, that is still much more up in the air among economists as to what the real causes are.

Michael Klein:

Another related issue, Lant, is that some people have put forward this idea of gross national happiness rather than gross national product. Bhutan famously has its gross national happiness index, and by this index, maybe not surprisingly, it ranks itself as the happiest country on earth. In Bhutan, they're very good at archery, maybe archery really helps them to be happy, I don't know. Should development economists be more focused on overall wellbeing, happiness rather than material welfare?

Lant Pritchett:

I don't think so, and I don't think so for two reasons. One, it's a complete and total myth that development and development of economists have been overly focused on GDP as a metric. No economist has confused GDP in and of itself is a goal. And moreover, if you look at other indicators of human wellbeing, like education and like health, they were increased actually spectacularly as well. So it's not the case that we live in a world where GDP has been very high, but kids haven't been getting educated. The average child in Haiti, which has not had a particularly striking successful development experience, is still higher than it was for children in France or for adults in France, even as late as 1960.

Lant Pritchett:

So there's been massive progress in getting kids into school. There's been massive progress in infant mortality and improvements in life expectancy in these countries. So again, it's a complete and total myth that development and development economists have been exclusively focused on GDP and not focused on overall wellbeing. Most measures of overall wellbeing have actually gone up more than we would've expected from the rate of economic growth of a country. It's not less. So again, complete and total factual inaccuracy to think, oh well yes, these countries have had a high GDP, but not invested in education or not invested in health. That's just not true.

Michael Klein:

That's striking that the increase in these indicators of wellbeing were actually greater than the increase in GDP. You said there was a second aspect as well?

Lant Pritchett:

The second aspect is that, at different levels of income, even if we have the same underlying preferences, we have different priorities because we have more or less of something. If you look at the typical person in the typical country, they spend about 50% of their existing household budget on food. So most of their expenditures are actually going to necessities and hence most of their increase in expenditure is going towards necessities. In these circumstances, I think a continued focus on improving material wellbeing is in fact appropriate.

Lant Pritchett:

Once one gets to the levels of prosperity and productivity of the United States or Denmark or other countries, then sure, relatively more focused on other intangible aspects that lead to happiness is probably a high priority. But we shouldn't again, look in a mirror and tell other people what we see out the window. I think for the poorer countries, economic growth is going to remain a very high priority because so much of their income is really devoted to necessities.

Michael Klein:

So Lant, I'd like to conclude by asking you about international development agencies, like the World Bank, where you worked for almost 20 years. The World Bank and other agencies, what roles have they played in advancing the fortunes of the world's poorest countries?

Lant Pritchett:

I think again, I have a two-fold answer. First is that many people believe, for instance, in the United States, that poverty hasn't gone down and hence they believe that the development agencies haven't been effective in their goal. Well, the first thing is the last 60 years have been the best 60 years for the improvement in human wellbeing on nearly every metric, by an order of magnitude. So the last 60 years of what I call roughly the development area in which there have been development agencies focused on development, have happened to be the best 60 years for human mankind by a lot. The question is, there's been massive success in improving human wellbeing of exactly the type and in exactly the places that development agencies were promoting it, that still doesn't say there was cause and effect and they did anything right. It might've happened without them, but the question is attributing success, not accounting or allocating blame for failure and I think getting that fundamental fact right helps have a better discussion.

Lant Pritchett:

Secondly, I think a lot of the rhetoric around the development agencies was about transferring resources, that these countries were actually short of foreign exchange and hence needed investible resources. I think looking back, we understand that this was much more about ideas and the development agencies creating a space in which research and discourse could happen about what the ways were to promote development for the countries to adopt on their own. And much less about the fact that this transfer of this many billions or that many billions made all the difference. Because in the end countries that adopted the right set of policies and processes to promote their own development have done fantastically well, whether or not they had sources of foreign exchange, because they could generate their own productivity and their own exports.

Lant Pritchett:

Whereas countries that have remained dependent on foreign aid resources and not of their own initiative adopted development promoting policies, just fundamentally have struggled. So I don't think development aid by any stretch of the imagination, through its transfer of resources, can make the difference for a country. But overall, I think it helped by creating a forum and impetus to think through and help countries think through their own problems and say, "What is it that we can do on our own that would promote our own success?" I don't think it's been the most important thing in the world, but neither do I think that on average it's been particularly terrible. And keeping in mind, this is a question of who's responsible for the enormous success the world has had in reducing poverty and increasing education, and increasing life expectancy? So there's been massive progress in nearly everything and I think development agencies played some small role in that.

Michael Klein:

So it's knowledge and best practices that were really important. Even while growth is a very multifaceted, difficult process, there's stuff that people can learn that seems to help.

Lant Pritchett:

I very much think so. I balk a bit best practices, I think more of achievable practices and relevant practices.

Michael Klein:

Good enough practices, yeah.

Lant Pritchett:

Good enough practices, yeah.

Michael Klein:

Yeah. Well Lant, thank you very much for speaking with me today on this issue, which in many ways is the core issue for the world as a whole, how to bring people out of poverty. Thanks for your time.

Lant Pritchett:

Thanks for having me.

Michael Klein:

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