

# Battle against World Poverty

## What Are Its Causes & What Can Be Done about It?

By Naoyuki HARAOKA

### Poorest Countries Hit Hardest by Economic Crisis

The economic crisis in wealthy countries affects the poorest countries through the channel of trade and investment. The rapid decline in wealthy countries' demand for primary goods produced by poor countries has brought a great loss in export revenues to the latter. The decline in wealthy countries' tax revenues resulting from the economic crisis has made it difficult for them to maintain their level of ODA, while the business sector's worsened balance sheet has caused a decline in capital investment in poor countries. In addition, seasonal workers from poor countries employed in rich countries can no longer earn much money due to the recession in these countries, and so cannot send money back to their home countries.

The severity of this economic crisis is shown in the latest IMF World Economic Outlook, issued in July. The growth in global output is predicted to shrink from 3.1% in 2008 to -1.4% in 2009; in particular, the

TABLE

### Overview of world economic growth projections

	Year over year			
	2007	2008	Projections	
			2009	2010
<b>World output</b>	<b>5.1</b>	<b>3.1</b>	<b>-1.4</b>	<b>2.5</b>
<b>Advanced economies</b>	2.7	0.8	-3.8	0.6
United States	2.0	1.1	-2.6	0.8
Euro Area	2.7	0.8	-4.8	-0.3
Germany	2.5	1.3	-6.2	-0.6
France	2.3	0.3	-3.0	0.4
Italy	1.6	-1.0	-5.1	-0.1
Spain	3.7	1.2	-4.0	-0.8
Japan	2.3	-0.7	-6.0	1.7
Britain	2.6	0.7	-4.2	0.2
Canada	2.5	0.4	-2.3	1.6
Other advanced economies	4.7	1.6	-3.9	1.0
Newly industrialized Asian economies	5.7	1.5	-5.2	1.4
<b>Emerging &amp; developing economies</b>	8.3	6.0	1.5	4.7
Africa	6.2	5.2	1.8	4.1
Sub-Sahara	6.9	5.5	1.5	4.1
Central & eastern Europe	5.4	3.0	-5.0	1.0
Commonwealth of Independent States	8.6	5.5	-5.8	2.0
Russia	8.1	5.6	-6.5	1.5
Excluding Russia	9.8	5.4	-3.9	3.2
Developing Asia	10.6	7.6	5.5	7.0
China	13.0	9.0	7.5	8.5
India	9.4	7.3	5.4	6.5
ASEAN-5	6.3	4.8	-0.3	3.7
Middle East	6.3	5.2	2.0	3.7
Western Hemisphere	5.7	4.2	-2.6	2.3
Brazil	5.7	5.1	-1.3	2.5
Mexico	3.3	1.3	-7.3	3.0

Source: World Economic Outlook, IMF

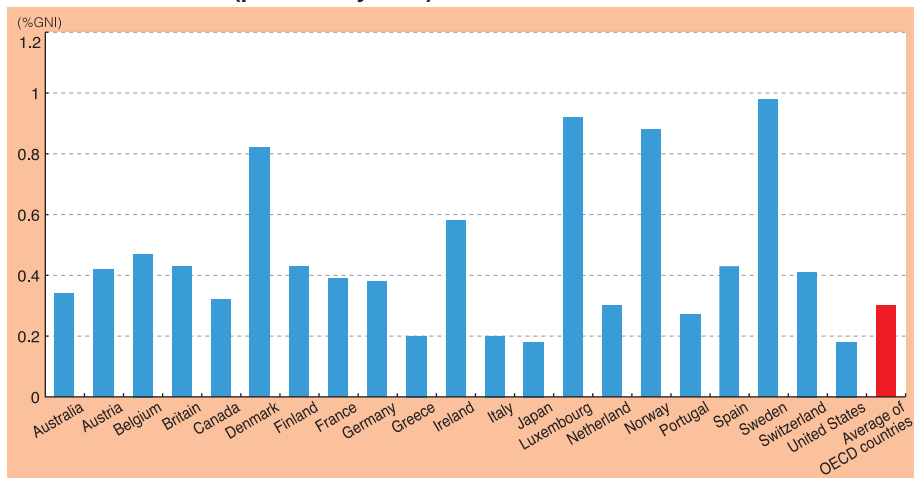
growth rate of advanced economies in 2009 is predicted to be -3.8%, showing a significant decline from the 2008 growth rate of 0.8% (Table). This drastic decline in the economic growth of wealthy countries naturally affects, through the above-mentioned process, poor countries' economic health. In the sub-Saharan group of poor countries, the growth rate is slowing significantly as well, to 1.5% in 2009 from 5.5% in 2008. Unless poor countries can achieve two-digit economic growth rates, it will be difficult for them to catch up with rich countries since their population growth is much higher than that of rich countries and it is probable that the GDP per capita difference between rich and poor will expand under low-growth economies. According to an estimate by the World Bank, by the end of this year, more than 53 million people will revert to extreme poverty, where they can earn no more than \$1.25 per day as a consequence of the economic crisis, and there is also concern that infant mortality could increase by 200,000-400,000 due to the economic slowdown. This means that the economic crisis could develop into an unprecedented social and human crisis.

### Rich Countries to Benefit from Continued Aid to Poorest Countries

How can we prevent this from happening?

First of all, advanced countries should continue to increase their percentage of ODA in relation to their GDP to help the poorest countries get out of a very difficult situation. As the chart shows, the reality does not meet the expectations and advanced nations' average percentage of ODA to GDP is far less than the 0.7% they committed themselves to in 2002. Most importantly, advanced countries are responsible for the current economic crisis and the poorest countries are not. It should not be forgotten that the poorest countries are suffering seriously from something they are not responsible for.

There are also three points to be considered as benefits that advanced countries can enjoy as a result of their continued efforts to aid the poorest countries. One is that they can win their war against political instability in these countries, which tends to breed civil war, violence and terrorism, by winning the war against poverty, one of the fundamental causes of political turmoil. World peace will then be successfully achieved without blood being shed. Second, rich countries can stimulate their economic recovery by promoting large infrastructure projects in poor countries. Development of transportation systems, hospitals, power stations, telecommunication systems, etc., which poor countries are clearly running short of, could stimulate the production and investment of advanced countries' suppliers of those systems. Lastly, the world could benefit greatly from the promotion of infrastructure projects to support possible alternative energy sources in poor countries. In particular, African countries are endowed with a wide range of new energy sources such as solar, geothermal and hydrogen. The development of such renewable sources of energy in

**ODA in 2008** (preliminary data)

Source: OECD

these countries would be highly instrumental in reducing the world's overall CO<sub>2</sub> emissions and thus would greatly contribute to the achievement of a non-carbon society against the background of global climate change. Advanced countries should strengthen their cooperation through the G-8, G-20 or other global governance mechanisms to maintain their efforts to support poor countries, bearing in mind these great potential benefits of such continued aid on their side as well.

### Structural Reform Slow in Poor Countries, Caught in 4 "Traps"

In pursuing economic assistance, advanced countries should remember that poor countries need structural reform as well as aid. Oxford University Professor Paul Collier suggests in his recently published book, *"The Bottom Billion: Why the Poorest Countries are Falling and What Can Be Done About It,"* that the poorest countries are caught in four traps that make it difficult for them to make progress. Structural reform for them means precisely the elimination of these traps.

The first is the trap of civil war. Low income, low growth and high dependency on the export of primary products are liable to provoke political conflict among different domestic interest groups, leading eventually to civil war or a coup d'état. Such conflicts could damage the economy and increase poverty.

The second trap relates to natural resources. According to Collier, countries endowed with rich natural resources tend to depend heavily on easily acquired natural assets and to ignore the potential of developing other economic activities for earnings. Therefore, their economic structure tends to be a "monoculture" and thus is very vulnerable to external shocks such as the current drastic world economic slowdown. This economic structure also tends to create a dictatorship since those in power try to monopolize the profits arising from natural resources, making it more difficult to create a democracy in these countries. A dictatorship is more likely to provoke civil war than a democracy is.

The third trap is geographical location. In most cases, in particular in the case of Africa, poor countries are located in inland areas and are surrounded by other poor countries. Since they are some distance from the sea, these countries' economic activities are heavily dependent on logistics infrastructure in neighboring countries. If these countries are also poor, the infrastructure they provide is insufficient and thus the poor countries cannot escape from poverty.

The fourth trap is bad governance. Bribery and corruption of government officials in these countries could deprive them of the opportunity to spread the benefits of economic development among their people.

The administration's incapacity to formulate a relevant policy is another reason that poor countries remain trapped in poverty.

We should think about possible countermeasures needed to solve each structural problem. However, before doing so, let me explain how these traps could end up marginalizing poor countries to exclusion from globalization of which wealthy nations are all enjoying its benefits.

High political risks of a coup d'état or civil war and bad governance discourage foreign direct investment (FDI) from wealthy countries. Lack of infrastructure due to the geographical location of poor countries is another factor making it difficult for companies to invest in such countries. The mono-

culture structure of trade also takes away stable earning opportunities from these countries since natural resources tend to be subject to significant price fluctuations such as the one we experienced last year. A more diversified export structure would naturally maximize the benefits of globalization. Thus, poor countries will be more and more marginalized from the trend of globalization as it goes on, and the income gap between wealthy nations and poor ones can only end up expanding.

How can we stop this vicious cycle and get poor countries onto the normal track of globalization, where they can enjoy the benefits of globalization as wealthy nations do?

Collier suggests the following. Firstly, to reduce the risk of civil war, international military intervention by wealthy nations is inevitable to restore peaceful order. Since poor countries' own militaries are often unable to maintain peace even after intervention, it is necessary for wealthy nations' militaries to stay for a while in these countries to keep the peace.

This may be somewhat unacceptable to people stressing the importance of observing international law, which obliges us to respect each country's sovereignty. However, in light of the enormous cost of civil war as described above, military intervention must be accepted.

To reduce this political risk as well, we have to pursue countermeasures to resolve the various problems arising from the other traps. High dependency on exports of natural resources should be corrected by industrial policy to diversify industrial structure and by trade policy through the WTO to ask for tariff concessions from wealthy nations for products manufactured in poor countries. Inadequate infrastructure in inland countries surrounded by poor neighboring countries is hard to resolve. However, wealthy nations could give aid to support large infrastructure projects such as highway or railway construction across borders. Then, all countries in the area would be the beneficiaries of such projects.

We should support the restructuring of legal institutions to overcome the problems caused by bad governance. The international treaty on bribery adopted by OECD countries about 10 years ago could work in favor of poor countries since under this treaty both the government officials who accept bribes and the businesspeople who bribe them are penalized.

The "opportunity cost" of these traps is enormous since the benefits that could have been gained without them are also enormous. I believe we should follow Collier's advice as closely as possible. **JS**

*Naoyuki Haraoka is Editor-in-Chief, Japan SPOTLIGHT, and Executive Managing Director, Japan Economic Foundation.*