

WP 2006-05
January 2006



Working Paper

Department of Applied Economics and Management
Cornell University, Ithaca, New York 14853-7801 USA

WHAT'S SOCIAL POLICY GOT TO DO WITH ECONOMIC GROWTH?

Ravi Kanbur

It is the Policy of Cornell University actively to support equality of educational and employment opportunity. No person shall be denied admission to any educational program or activity or be denied employment on the basis of any legally prohibited discrimination involving, but not limited to, such factors as race, color, creed, religion, national or ethnic origin, sex, age or handicap. The University is committed to the maintenance of affirmative action programs which will assure the continuation of such equality of opportunity.

What's Social Policy Got To Do With Economic Growth?

By

Ravi Kanbur¹

www.people.cornell.edu/pages/sk145

First Draft: November, 2005

Second Draft: January, 2006

Contents

1. Introduction
 2. What's Social Policy, Anyway?
 3. Objectives and Instruments
 4. Growth Regressions
 5. Mechanisms and Disciplines
 6. What's It Mean for the World Bank?
 7. Conclusion
- References

Abstract

So what's social policy got to do with economic growth? Quite a lot, it would appear, if one takes the results of cross-country growth regressions at face value, as they are by many social policy analysts, even as they criticize the findings of the economic policy part of the very same regressions. I argue that these regressions are deeply problematic, and are antithetical to social policy analysts' normal instincts on the importance of country and community specificity. At the same time, attempts to distinguish social policy from economic policy in terms of policy objectives is not very successful, while classifying policy instruments into economic or social also leaves a significant grey area. But the economic and social policy analysis literatures can indeed be distinguished in their approaches to understanding the mechanisms of policy transmission. Despite the difficulties of defining social policy analysis, except in contradistinction to economic policy analysis, both types of analysis are needed to advance understanding of policy impact and design of policy. The Bank should (i) play a lead role in developing and assessing such multidisciplinary approaches, (ii) move to a much more outcomes based system of aid allocation in recognition of the country-specific complexities of linkage between (economic or social) policy and outcomes, and (iii) understand itself better as an institution, and its institutional footprint in countries where it is a big player.

¹ T.H. Lee Professor of World Affairs, International Professor of Applied Economics and Management, and Professor of Economics, Cornell University. Keynote address at World Bank conference, "New Frontiers of Social Policy," Arusha, Tanzania, December 12-15, 2005.

1. Introduction

There are two ways in which one might approach the topic of this paper. One is to take a relatively straightforward interpretation through cross-country econometric growth regressions, and to discuss the range of factors that are adduced as explanatory variables in such analyses. In fact, a section of this paper will indeed be devoted to this literature. However, as you will see when we come to that discussion, I believe this would limit the scope of the topic considerably. So I am going to take another approach, a broader approach, which uses the title of the paper as a way into a deeper discussion of the relationship between the social and the economic in the theory and practice of development.

2. What's Social Policy, Anyway?

To answer the question in the title of this paper, we need to define the key terms—economic growth and social policy. The first is relatively straightforward. Economic growth is the rate of increase of real per capita income. There may be some technical issues do with GDP versus GNP, or exchange rates versus purchasing power parity, but we all basically know what we mean when we use the term economic growth. What about economic development? There can be different degrees of broadening out from economic growth, adding changes in the structure of production to begin with. A recent undergraduate text (Lynn, 2003, p4) offers this definition:

“Economic development means sustained and sustainable growth in per capita income, accompanied by diversification of production, reduction of absolute poverty, and expanding economic opportunities for all citizens.”

In this view, environmental sustainability and poverty reduction are all part of the definition of economic development.

Let us consider, then, some definitions of social policy in the literature. The concept note for this conference (World Bank, 2005b) touches on a number of different aspects of social policy:

“A more holistic approach to social policy in development contexts, where markets are grossly imperfect and labor markets often incomplete, would seek to promote policies, institutions and programs that balance a concern for equity and justice with the concern for economic growth....[S]ocial policy is defined as a series of public policies designed to promote social development... We envision social development as a natural complement to economic development with both intrinsic and instrumental value... While there is lack of consensus on the definition of social development it is generally understood to comprise of a set of objectives including social inclusion, sustainable livelihoods, gender equity, increased voice and participation.”

The World Bank's Social Development Strategy (World Bank, 2005a) defines social development as “transforming institutions to empower people,” and goes on to specify three operational principles—Inclusion, Cohesion and Accountability. The concept note for the conference (World Bank 2005b) tries a related triple when it says:

“As a working definition, social development can be described as the process of increasing
-the assets and capabilities of individuals to improve their wellbeing,
-the capacity of social groups to exercise agency, transform their relationships with other groups, and participate in the development processes,
-the ability of society to reconcile the interests of its constituent elements, govern itself peacefully, and manage change.
Social Policies then are public policies aimed at promoting *equality of opportunity* to benefit individuals, *equality of agency* to benefit groups, and both *horizontal and vertical social integration*.”

In the glossary of the well known text by Hall and Midgley (2004, p xv), we find the following definitions:

“Social development: A process of planned social change designed to improve the welfare of the population as a whole in conjunction with economic development.
Social exclusion: The exclusion of certain groups from an acceptable standard of living or basic level of political participation.
Social policy: Measures that affect people’s well-being, whether through the provision of welfare services or by means of policies that impact upon livelihoods more generally.”

Finally, consider Mkandawire’s (2001) perspective:

“Social policy should be conceived of as involving overall and prior concerns with social development, and as a key instrument that works in tandem with economic policy to ensure equitable and socially sustainable development...I define social policy as collective interventions directly affecting transformation in social welfare, social institutions and social relations.”

The above quotations are, I believe, representative of the attempts to define social policy and social development. Two striking features stand out from these and other attempts in the literature. First, the definitions are almost always with reference to, or in relation to, or in opposition to, the “economic”. Thus we find that the hallmark of social policies is that they “balance a concern of equity and justice with the concern for economic growth”; that social development is “a natural complement”, or operates “in conjunction with” economic development; and that social policy “works in tandem with economic policy.”

Second, the definitions range over objectives, instruments and mechanisms, without necessarily making clear distinctions among them. Thus, as noted above, in these definitions, social policy is that which brings considerations of equity and justice to the table, in contrast to a focus on economic growth alone; it uses instruments like spending on education and health, in contrast to instruments like the exchange rates or trade liberalization; and it emphasizes mechanisms that work at the group level rather than at the level of the individual. For each of these orientations—objectives, instruments, and mechanisms—the “social” is once again characterized, more often than not, in relation to the “economic.” In the following sections I will argue that the distinctions between the economic and the social based on objectives are not very persuasive, while those based on instruments are only slightly more so. The real distinction comes at the level of mechanisms, which in turn takes us to the different disciplines that straddle the economic and the social.

3. Objectives and Instruments

Which objectives of development are economic, which are social? Does it even make sense to ask this question? Surely the normative objectives of a society that emerge from deep reflection are neither wholly economic nor social. The objective, for example, of improving the lot of the worst off individual in society is just that. It emerges from a contractarian theory of justice under certain specifications (like the “original position” or the “veil of ignorance” of Rawls, 1971). It does not make sense to class this as an economic or a social objective. Sen (1985, 1999) also attempts to derive objectives for a society, and for that society’s development, from first principles. His view on enhancing capabilities, for example, is just that—it is neither economic nor social.

Economic growth for its own sake cannot be a sensible final objective of society. At least, it seems difficult to derive it from fundamental normative principles. So if it nevertheless plays such an important part in discussion of policy and outcomes, it must be because of a strong belief that it is causally related to more sensible final objectives like enhancing capabilities or making the worst off person better off. In other words, at best it plays a role as an intermediate objective which may in turn lead to the achievement of the final objective if other things happen. But here we enter the realm of mechanisms, which will be taken up in the next two sections.

Given that there has been a tendency in policy circles to focus on economic growth, it is understandable that some of those writing on social policy should view themselves as balancing “a concern for equity and social justice with the concern for economic growth.” But this stance itself gives economic growth the status of a final objective, which is a mistake. The focus, rather, should be on what is the final objective of policy and what is an intermediate objective, and on the mechanisms that link the intermediate outcomes to the final ones, and policy to both.

As noted in the previous section, according to some definitions social development has a “set of objectives including social inclusion, sustainable livelihoods, gender equity, increased voice and participation” (World Bank, 2005b). But are all of these final objectives? What about social inclusion? Its opposite, social exclusion, is defined by Hall and Midgely (2004) as “the exclusion of certain groups from an acceptable standard of living or basic level of political participation.” Two issues arise. First, since voice and participation are already on the list of objectives, is one subsumed in the other, or is one an intermediate objective for the other? Second, is social exclusion part of the final objective because exclusion based on group membership is per se objectionable, or only instrumentally because it makes individuals in the group worse off, in which case it would be an intermediate objective? The issue of individuals versus groups will be revisited when we discuss mechanisms later in this paper. For now we note a lack of clarity in the literature on the final objectives of social development.

As another example, take the definition in the Concept Note (World Bank, 2005b), that “Social Policies then are public policies aimed at promoting *equality of opportunity* to benefit individuals, *equality of agency* to benefit groups, and both *horizontal and vertical*

social integration.” This seems to define as an objective the benefit of individuals, and equality of opportunity as a way of achieving that—an intermediate objective. It also defines as an objective the benefit of groups and equality of agency as a way of achieving that—an intermediate objective. But horizontal and vertical integration seems to be left as a final objective by itself. Moreover, it is not clear whether the benefit of groups has a value in and of itself or only instrumentally because it benefits individuals.

Of course the definition of economic development given in the previous section is no better, since it lumps together economic growth, sustainability and poverty reduction all as objectives, with no indication of which, if any, are final objectives and which are intermediate ones. In general, there is a lack of clarity in both economic and social writings about the hierarchy of objectives, and a lack of distinction between intermediate and final objectives, or rather, too easy an identification of intermediate objectives with final ones on the basis of an implicit mechanism linking the two (economic growth and poverty reduction, social inclusion and individual well being, etc.).

What, then, are the final objectives? Since these depend on values and on alternative conceptions of the good life, there is no uniform or unique answer. What we can say, however, is that for each stated objective it should be specified whether it is valued for its own sake or because it is supposed to enhance some other objective through some mechanism (which should itself be clarified), or both. And a key issue is whether the final objectives are ultimately reduceable to the wellbeing of individuals, as opposed to the wellbeing of a group to which they belong, or whether there are some final objectives which stand independently of individual (or group) wellbeing. Gender equity is an example. Is it an objective in its own right, or is it an intermediate objective which leads, ultimately, to higher wellbeing of women and of men? Clarity on such issues can illuminate policy debates considerably.

So much for objectives. What about instruments? Does social policy have a distinctively different set of instruments from economic policy? Hall and Midgely’s (2004) definition of social policy as “Measures that affect people’s well-being, whether through the provision of welfare services or by means of policies that impact upon livelihoods more generally,” broadens the scope of instruments that come under the purview of social policy to any set of measures that “impact upon livelihoods more generally.” Exchange rates and tariffs surely do this, so are they instruments of social policy? One senses that those who identify themselves as social policy analysts would not go quite so far. Mkandawire (2001) takes the middle ground when he says:

“...social policy may be embedded in economic policy, when the latter has intended welfare consequences or reflects implicit or explicit socioeconomic priorities, such as reducing politically unacceptable levels of unemployment. Nevertheless, some elements of social policy are more explicit, such as direct government provision of social welfare, in part through broad-based social services and subsidies.”

The World Bank’s (2005a) Social Development Strategy identifies the operational principles of inclusion, cohesion and accountability, and it is unlikely that exchange rates and tariffs will contribute directly to these channels. However, instruments such as reforming corporate law, circumscribing customary restrictions on the property rights of

women, or introducing multi-party democracy, can be argued to be closely related to these channels, and seem in the literature to fall naturally into the social policy category.

Social policy instruments tend to be defined in the literature with reference to economic policy instruments. Social policy instruments are those which are not, and which go beyond, what are considered conventionally to be economic policy instruments. What are these? Monetary policy, fiscal deficit, exchange rate, tariffs and quotas, and capital account controls—all these seem to fall fairly clearly into the economic policy category. As we disaggregate the fiscal deficit, problems of categorization may arise. Are tax instruments part of economic policy or social policy or both? What about expenditure policies? The level and composition of public expenditures on health and education? These are claimed, it would seem, by both economic policy and social policy. Social safety net policy is certainly claimed by social policy, but anything with budgetary implications is also claimed by economic policy. Then there is labor market policy—minimum wages, employment guarantees, health and safety standards at the workplace. And credit market policy, ranging from financial repression, through the regulation of banks, to microcredit. Is the regulation of banks economic policy, but the regulation of microcredit social policy? Finally, there are a whole set of legal and institutional interventions such as those discussed earlier. There is no consensus on what exactly these are and what their effects are, but there would seem to be agreement that they are not economic policy and, as is clear from the Social Development Strategy paper (World Bank, 2005a), they are certainly claimed for the social policy domain.

The above shows that there is a continuum of policy instruments, from those that are conventionally and clearly recognized as being economic policy, through a spectrum to which both economic and social policy literatures lay claim, to a set of instruments that are conventionally and clearly recognized as social policy instruments. It should be clear that any or all of these instruments can affect any or all of the objectives discussed earlier in this section, whether they are final or intermediate objectives. While a division of instruments into “economic” and “social” may have some utility despite being a not very clear cut division, the claim that instruments in one set necessarily relate more closely to some objectives rather than others is a claim that cannot be made without a detailed investigation of the mechanisms involved. And yet we do find this in the social policy literature. There is a certain tendency to associate social policy instruments, in contrast to economic policy instruments, with certain objectives such as equity or justice, in contrast to the presumed objective of economic policy (economic growth, for example). Such simplistic association may be necessary in the early stages of the development of a social policy constituency, the self definition in relation or in opposition to economic policy being a useful device at these early stages, but it ultimately leads to weak analysis and weak policy conclusions.

Thus a distinction between the economic and the social is not, in my view, very usefully made in the realm of objectives and instruments. However, this still leaves the area of mechanisms.

4. Growth Regressions

How can we know the impact of policy instruments on objectives? The central and dominant method for answering this question, certainly in agencies like the World Bank, has been the method of searching for statistical regularities in instruments and objectives across countries. The usual objective considered is an intermediate one—economic growth. Each country’s historical experience generates observations on the rate of growth, and on a range of either policy variables or variables that can be interpreted to be closely related to policy variables, as well as structural variables that a country cannot change (like its geography). Cross-country econometric regression analysis is then used to test various hypotheses about the causal links between policy instruments and economic growth. Although economic growth is most often used as the variable to be causally explained, the method can of course be used for any objective of interest (for example, changes in infant mortality rates).

Growth regressions are used and abused in the debate on economic and social policy. For example, they are the leading piece of evidence in the claim that trade liberalization is good for growth. This is then fed into another regression—that of changes in poverty on economic growth, to argue that since trade liberalization is good for growth, and growth is good for poverty reduction, trade liberalization is good for poverty reduction. These very same types of regressions, but this time with explanatory variables from the “social policy” set, are used to argue for the importance of social policy not only for “social” objectives but also for “economic” ones (like economic growth). This certainly applies to variables that measure institutional quality, or ethno-linguistic fragmentation, or “trust”, or gender equity, or land inequality, and so on. For example, the Social Development Strategy paper (World Bank, 2005a, p3), argues as follows:

“By transforming institutions to empower people, social development matters for growth and who benefits from it...Research shows that some social development indicators, particularly cohesion indicators, correlate positively with foreign direct investment. Conversely, from a cross-section of 98 countries, Robert Barro found that lower initial conditions of cohesion hampered growth...Finally, based on cross-country data of social development indicators, more accountable institutions in a given year correlate with higher growth in the following decade.”

The literature on cross-country growth regressions is huge and cannot possibly be surveyed here (for a more detailed development of my views on this literature, see Kanbur, 2005a). The cross-country regressions literature is useful in many ways, as a pattern description exercise or a method for suggesting initial hypotheses. And I have myself used the method on many occasions. But there are at least three types of problems with it: (i) data and econometrics; (ii) variations around the average regression; and (iii) interpretation of the results in terms of mechanisms.

Data shortcomings are endemic in the explanatory variables used in growth regressions. The problems apply equally well to “economic” as to “social” variables. For example, one way to measure trade openness is the level of tariffs. But tariffs are not necessarily implemented—indeed, the corruption of customs officials is a stock anecdote used to bolster up perception based measures of institutional quality (like Transparency

International's corruption rankings). So what is the real level of tariffs if the rates on paper are not the ones that apply in reality? One answer is to take tariff revenue as a measure. The problem here is that this measure is an amalgam of a policy instrument (tariffs) and the response to this policy instrument (imports). This introduces statistical problems in disentangling the true effects of the policy on growth. But data on the social side is not problem free either. For example, much of the corruption data that is used in cross-country regressions is based on the perceptions of a relatively small number of domestic and foreign observers in business. As such, it may only reflect phenomena in the large scale formal sector.

Even if the data were problem free, there remain basic problems in interpreting statistically significant regression coefficients as indicators of policy efficacy. Rodrik (2005) provides a litany of econometric problems with such regressions (parameter heterogeneity, outliers, omitted variables, model uncertainty, measurement error, endogeneity, etc.). He then highlights the central conceptual problem—for the regression to have causal cutting power, the basic assumption must be that variations in the policy are independent of variations in other variables in the regression, in other words, policy variation is exogenous. But if governments are choosing policy (whether the instrument is “economic”, or “social”, or in between) to advance certain objectives, variations in the policy variables cannot be exogenous. To quote Rodrik (2005, p4):

“Consider an illustration from trade policy. The estimated coefficient on import tariffs in growth regressions run for the contemporary period is typically negative (albeit insignificantly so) and rarely positive. One frequently hears the argument that we can at least draw the conclusion from this fact that import protection cannot be beneficial to growth. But once again this and similar inferences are invalid. A negative partial correlation between growth and import tariffs is not only consistent with protection being growth-enhancing, it is actually an equilibrium consequence of trade protection being used in a socially optimal fashion.”

It is important to emphasize that while the example is given from trade policy it applies to any policy, “economic” or “social.” This is a generic critique of cross-country regression analysis, and gives no comfort to those who highlight to the importance of social policy by pointing to significant coefficients on social variables in cross-country regressions.

All of the above is about the statistical relationship between policy and growth on average. But there is considerable variation around the estimated average in all cross-country regressions. What are we to make of the fact that some countries are well above the estimated relationship (in other words, they are doing much better with the policy than would be predicted from the average), or are well below it (doing much worse than predicted). The usual econometric answer is that these variations are caused by purely random factors and so have no information content whatsoever. But this is most implausible. What is quite likely is that variations around the estimates of average relationships are not simply pure random variations, but reflect country specific factors that are not captured in our model and in our data (Kanbur, 2005b). As a recent World Bank report on economic growth in the 1990s argues (World Bank, 2004, pp vi-vii):

“The Study concludes that valid general principles do not imply generic “best practice” policy or institutional solutions....

Regarding trade, the analysis highlights the fact that countries that have successfully integrated into the world economy have followed different approaches and also adopted a range of complementary policies, making it difficult to pin down the exact relationship between trade integration and growth....

Perhaps the lesson of the lessons of the 1990s is that we need to get away from formulae and realize that economic policies and institutional reforms need to address whatever is the binding constraint on growth, at the right time, in the right manner, in the right sequence, instead of addressing any constraint at any time....”

This leads then to the final problem, which is in fact highlighted by the first two problems. A statistical correlation between growth (or some other outcome) and a policy variable, even if it is not subject to the econometric critiques laid out above, tells us nothing about the underlying mechanisms through which the policy variable affects the (intermediate or final) objective. Ultimately it is confidence in these mechanisms that should guide our confidence in the impact of policy instruments. And building that confidence is not (just) about running cross-country regressions, or even some other technique. It is about using different methods of analysis, and different types of micro and macro level evidence, to aim for a coherent position on how and why a particular policy instrument, whether economic or social, or combinations of policy instruments, will have a particular effect on an objective of interest, in a given context. But such a perspective inevitably leads us to a discussion of different modes of analysis and different disciplinary approaches.

5. Mechanisms and Disciplines

An earlier section of this paper has already alluded to the fact that social policy analysts tend to define social policy in relation to, often in opposition to, “economic policy.” And it cannot of course escape notice that those who analyze “economic policy” are by and large are those whose training is in the discipline of economics, while those who analyze “social policy” are by and large those whose disciplinary training is not in economics. While the discipline of economics is unified (pretty much) by a single paradigm and method, “non-economics” is not. For a start, it is several disciplines—anthropology, political science and sociology being the most prominent. And, within each of these disciplines one does not find the paradigmatic unity that there is in economics. At least in the context of development policy studies, what seems to unite these disciplines, and their sub-branches, is viewing themselves as an alternative paradigm to the economic method, each in its own different way.

The tensions between economics and other disciplines, in academia and in development agencies, are palpable, and we have to confront them in any discussion of social and economic policy. As I have observed elsewhere (Kanbur 2002, p1):

“Development economics stands in beleaguered ascendancy, atop development studies and development policy. Economists and economic thinking dominate the leading development institutions. The prestige of development economists within academia, now that they have demonstrated themselves to be squarely in the mainstream of economics, has never been higher. And yet, something is clearly not right. Particularly in the policy domain, development economics is under scrutiny like never before—its prescriptions attacked, its analysis of development phenomena questioned. Often this criticism comes

from other social science disciplines and social scientists, who feel shut out from the commanding heights of development analysis and policy making, and who feel looked down upon by economists, as being “soft” and “unrigorous”. But increasingly, the criticism is coming from economists themselves, who are finding their tools and techniques, strong as they are, to be inadequate by themselves to address pressing policy and analytical problems.”

I argued earlier in the paper that characterization of economic policy in terms of pursuing a particular objective (economic growth), and social policy as pursuing a different objective (equity and justice) was not a very powerful or a useful classification device. Certainly if economic policy is what economists do, many of them would object to a definition of their role as not including the pursuit of equity (Kanbur, 2004b). Also, while the division of policy instruments into “economic” and “social” fares a little better in terms of conventional classification, there is a continuum, and many instruments can be claimed by either. Rather, I believe the real differences can be identified if we focus on the mechanisms through which a policy instrument is thought to have an effect on objectives. This in turn leads us to a discussion of different frameworks of analysis and different theoretical presumptions that underly different disciplines.

General characterizations are fraught with difficulties, but I believe they can be attempted for economics—at least, the critics of economic method seem to have no difficulties in offering such generalizations. One characterization is of course that the economic method focuses on mechanisms that work through the operation of markets. Thus, a classic piece of economic analysis goes as follows. Opening out an economy increases demand for the product which that economy produces most cheaply. This will be the product which uses the cheapest factors of production most intensively. And the cheapest factors of production will be those which are the most abundant. Since unskilled labor is abundant in a developing country, opening out that economy will increase total demand for products that use unskilled labor most intensively, and will therefore increase the demand for unskilled labor. This increase in labor demand will reduce unemployment and raise wages among unskilled workers. What I have just described, the Stolper-Samuelson theorem, is at the heart of arguments made by many economists that trade liberalization will be good for poverty, and it has to be said that this is the dominant instinct of the vast majority of economists. The role of markets in the above chain of mechanisms is very clear—product markets and labor markets interact to produce the above result. The problem, however, is not that the mechanism operates through markets. It would be difficult to imagine an economy engaged in international trade in which the chain of consequences following on a trade liberalization did not go through markets. Rather, the problem is to do with assumptions about the nature of these markets, in particular, that they are “competitive”, with no individual or group of individuals exercising market power because of various structural features (Kanbur 2001, 2002, 2004a). Again, the problem is not that economic analysis that is taught in graduate schools does not broach issues of monopoly or oligopoly—it is that in economic policy analysis the canonical model seems to dominate.

Not all economic analysis of mechanisms operates solely through markets. For example, the vast economic literature on intra-household inequality is about interaction between individuals within a household, with no prices or markets in the conventional

sense. But what this literature has in common with the general literature on individual interactions through markets is the specification of individual behavior as optimizing a specified and stable objective function. This is often criticized, and rightly so, when the individual level objective functions are too narrowly specified, for example as having only monetary and consumption determinants or not having concern for others. It is important to realize, however, that there is nothing inherent in the method that precludes a broadening of individual objectives, even including, for example, the characteristics of a group that the individual identifies with. Indeed, much work on the frontiers of economic theory is precisely of this type (see Akerlof and Kranton, 2000, Dasgupta and Kanbur, 2005, Kanbur, 2003a, and Banerjee et al., 2005). But it is yet to become embedded in basic graduate courses in economics. However, even the most advanced work, which views individuals in the context of groups, shares with the rest of economics a thoroughgoing methodological individualism—the behavior of groups cannot be discussed except as an aggregation of the (possibly complicated) behavior of individuals who form that group.

Another characterization of economic analysis of policy is that the analysis is supremely unconcerned about the processes, particularly the political processes that generate policy. This is related to the Rodrik (2005) critique of the tendency to view the explanatory policy variables in growth regressions as exogenous to the process, when they are in fact manipulable by policy makers and therefore endogenous. But these policies are the outcome of group and political interactions that take place according to rules whose origins lies in previous historical interactions, for example the legacy of colonialism. Once again, the frontiers of economic theory are alive to these possibilities (for recent examples, see Persson and Tabellini, 2000, 2003, Acemoglu and Robinson, 2005), but economic policy analysis is not, at least not to the same extent.

In my view, then, the core characterization of the economic method, as it is used in policy analysis, is three fold: (i) a focus on understanding outcomes through the behavior of and interaction between individuals qua individuals; (ii) a focus on market mechanisms, particularly competitive market mechanisms; and (iii) a tendency to treat policy variables as exogenous and manipulable independently of individual and group interactions. All of these features are being questioned at the theoretical frontiers of the discipline, but they define the centre of gravity of economic policy analysis.

One characterization that can be offered of other methods or disciplines in development studies is simply as the opposite of the three features mentioned above: (i) a focus on understanding outcomes through the behavior of interaction of groups qua groups; (ii) a focus on non-market mechanisms; and (iii) explicit attention to the processes that determine policy. One might identify the first primarily with sociology, the second with anthropology and the third with political science. Such a simplistic characterization will and should be resisted. But such resistance does raise the question—what comparable core features quintessentially characterize the anthropological, the sociological or the political science method? Part of the difficulty in answering this question is of course the lack of paradigmatic unity within each of these disciplines. But I believe that we do need to have such a characterization if we are to use different methods and techniques of analysis to help us understand the impact of policy instruments on objectives.

6. What's It Mean for The World Bank?

I have argued that the real difference between “economic policy” and “social policy” literatures and approaches lies not in objectives, and not entirely in instruments, but rather in the mechanisms and methods that the two approaches bring to the understanding of phenomena and to the understanding of causality from policy instruments to objectives. I have argued that the economic method, despite its considerable strengths, has significant shortcomings, and other approaches and methods are needed to provide an overall approach to policy analysis. However, it is not entirely clear how exactly different approaches are to be combined (for an example of general juxtapositions of economics and sociology see Grusky and Kanbur, 2004; for economics and anthropology see Kanbur and Riles, 2004; for combining qualitative and quantitative approaches to poverty analysis, see Kanbur, 2003a, Kanbur and Shaffer, 2005).

With this background, and given the Bank's interest in social policy, the question arises—what should the World Bank do? The World Bank's Social Development Strategy Paper (World Bank 2005a, pp v-vi) gives an answer to this question that is worth quoting at some length.

“To enhance impact and improve efficiency, the Bank proposes a new business model for how it will promote social development in its operations....

Under **Strategic Priority 1** the Bank will increase support for countries to bring social development processes, analysis and content into their overall poverty reduction or development strategies. This shift implies building government capacity for more effective and representative stakeholder participation while countries prepare and implement their country strategies...Finally, requiring no additional Bank-imposed conditionality, development policy lending will support government efforts to improve inclusion, cohesion and accountability using countries' own systems. For example, it will support policies that promote greater budget transparency or enable communities to manage public funds.

Under **Strategic Priority 2** the Bank will enhance the impact and reduce the cost of how it approaches social development processes, analysis and contents in each of its projects...Given the Bank's emphasis on more and better agriculture and infrastructure lending, it will increase support for community involvement, participation and understanding of social context in such projects.

Under **Strategic Priority 3** the Bank will strengthen the grounding for its social development work by enhancing research, capacity building and partnerships. Bank-supported research will build upon existing context-specific analysis to improve understanding of the complex relationship between social development and economic growth...The Bank will also strengthen evaluations of the social development impacts of its economic activities...”

Given that the Social Development Strategy Paper (World Bank 2005a) defines social development as “transforming institutions to empower people,” in other words a fairly instrument-oriented definition, it is not surprising that the above tends to think of social policy instruments as being distinct and in a separate domain from economic policy instruments. It is also not surprising given that this is the strategy developed by the Social Development Department, and institutional divisions are more naturally done along instrumental lines.

I have several observations on the above strategy, which makes a lot of sense in the institutional context in which it is developed. First, in my view it tends to fall into the trap of separating off economic policy analysis, and the economic method, from social policy analysis and the approaches of other disciplines, despite the difficulties in defining

precisely what these alternatives are. In my view no single approach, drawing on any single method, can give an entirely convincing explanation of outcomes, and thereby underpin a satisfactory policy analysis. The key is to combine these different approaches, and yet we do not have sufficient experience of doing so, and sufficient assessment of attempts at doing so. The Bank and its projects are fertile ground for purposive deployment of multidisciplinary teams. This already happens, of course. But it would be very useful to have an assessment of the issues raised by attempts to bring different perspectives on a single project. Such assessments, and then a meta-assessment, would provide guidance for design of future social policy work, indeed future policy work. Such an exercise could easily fall under Strategic Priority 3.

A related idea to bring together the power of different approaches, the “economic” and the “social”, is to start with a specific problem and task a multidisciplinary team to address it. This also happens, of course—I am suggesting a more systematic and purposive use of the device. For example, take the millennium development goal of achieving significant reductions in infant mortality rates. With that as the final objective, what policy package would be recommended by a team of economic and social policy analysts in, say, a group of three or five countries, each with very different circumstances? In keeping with the previous paragraph, one would at the same time assess how well this exercise worked and what could be done to improve it.

An altogether more radical idea follows from the critique of cross-country regression analysis, which I have argued is misused as much by the social policy camp as by the economic policy camp. This framework, which searches for an average relationship common to all countries, underlies the link between the Country Policy and Institutional Assessment (CPIA) of the Bank and the IDA allocation formula. As I have argued elsewhere (Kanbur, 2005b) the logic of this relationship is that when the CPIA score is high “aid performance” will be high. The formula is the same for every country, only the scores vary on different dimensions of the CPIA, which encompasses standard economic policy variables as well as a slew of institutional and social variables. The assumption is that when these standardized variables are better, aid will do more good. I argue in Kanbur (2005b) that even if we accept this as an average statement (which is subject to all the critiques discussed in an earlier section); it is deeply problematic to apply the average relationship to every country. Economists may (wrongly) slip into such habits of thought, but social policy analysts have no excuse, since one of their critiques of the economic method is its neglect of country specific institutional and social factors. If it is unacceptable to say that a lower level of tariffs will necessarily lead to a higher growth in a particular country, then surely it is equally unacceptable to say that a lower level of “corruption” (as measured for example in the CPIA guidelines) will necessarily lead to an improvement in infant mortality rates.

Once again, what is important is the detail of the specific mechanisms, which will vary from country to country. This is why pulling the same policy lever (whether economic or social) can and does have very different effects in different countries, and why taking the experience of one country (or the average experience of all countries) as “best practice” to be applied to each country is deeply problematic. The radical idea, then, is to use the rate of

change of a final objective (for example, infant mortality rate, or income poverty, or girls enrollment) itself as a measure of performance, it being recognized that we cannot set down general rules for the linkage of policy instruments to those outcomes, at least not rules that are the same for all countries. This line of argument, which is developed and defended in its conceptual and operational dimensions in Kanbur (2005b), leads to an output based allocation of aid, as opposed to an input based allocation of aid which is what the CPIA based method actually is, albeit that it takes into account instruments conventionally thought of as economic, social, and in between. My specific operational proposal is to introduce *one* such outcome based category in the CPIA to begin with, and to then assess the experience in three years' time (Kanbur, 2005b).

The final and most radical idea, or rather a radical set of questions, flows from a glaring dissonance in the Social Development Strategy Paper (World Bank, 2005a). It is striking, for an approach that emphasizes institutions and power, that there is no direct engagement with the Bank itself as an institution, and an important institution, a “big player”, in many countries, especially in Africa. And this despite a huge literature, some by the very social policy analysts whose work is used and quoted approvingly in other contexts, on the Bank and its institutional footprint. There are many layers to be peeled off here. At its most parochial, the Bank is an organization with a particular culture. What is this culture? What are its functionalities and dysfunctions if the objective is to help in the removal of poverty? Then in the countries, the Bank, and this applies equally well to big donors in each country, is not a passive player. Its every move and utterance is carefully watched and scrutinized. Particularly where it is a big player financially, even if it doesn't want to it becomes part of the domestic political discourse. Is this good, bad, or indifferent? Would the Bank be more effective if it were a smaller player? Relatedly, culturally Bank staff in developing countries are clearly part of the well heeled expatriate set. They exude wealth and privilege and power. And yet in one sense the power that they have is limited. As I have argued elsewhere (Kanbur, 2000):

“How can the strong be weak? It is of course true that representatives of the aid agencies in Africa, those who “parachute in” for missions of a few days and those who are resident locally, are the symbols of the power of the donor agencies. They stay in the big hotels (or big houses), are driven around, and demand to see policy makers at the drop of a hat. As they travel in convoys of four wheel drives to inspect projects funded by their agencies, and as they mingle on the diplomatic cocktail circuit, the resentment they evoke in the local population should not be underestimated. But, when it comes to it, these symbols of strength hide fundamental weaknesses that arise from the inner logic and dynamic of the aid process and donor agency imperatives.”

The “inner logic and dynamic of the aid process and donor agency imperatives” then takes us back to the beginning, to the Bank as an institution.

This is not the occasion for specifics on Bank reform. And I am not suggesting that the Bank spend vast amounts of resources analyzing itself as opposed to analyzing developing country institutions. I merely want to say to those who emphasize the institutional aspects of development: “institutionalist, understand thyself!”

7. Conclusion

So what's social policy got to do with economic growth? Quite a lot, it would appear, if one takes the results of cross-country growth regressions at face value, as they are by many social policy analysts, even as they criticize the findings of the economic policy part of the very same regressions. I have argued that these regressions are deeply problematic, and are antithetical to social policy analysts' normal instincts on the importance of country and community specificity. At the same time, attempts to distinguish social policy from economic policy in terms of policy objectives is not very successful, while classifying policy instruments into economic or social also leaves a significant grey area. But the economic and social policy analysis literatures can indeed be distinguished in their approaches to understanding the mechanisms of policy transmission. Despite the difficulties of defining social analysis, except in contradistinction to economic analysis, both types of analysis are needed to advance understanding of policy impact and design of policy. The Bank should (i) play a lead role in developing and assessing such multidisciplinary approaches, (ii) move to a much more outcomes based system of aid allocation in recognition of the country-specific complexities of linkage between (economic or social) policy and outcomes, and (iii) understand itself better as an institution, and its institutional footprint in countries where it is a big player.

References

- Acemoglu, Daron and James Robinson. 2005. *Economic Origins of Dictatorship and Democracy*. Cambridge University Press.
- Akerlof, George and Rachel Kranton. 2000. "Economics and Identity." *Quarterly Journal of Economics*. 115(3): pp. 715-53.
- Banerjee, Abhijit, Pranab Bardhan, Kaushik Basu, Ravi Kanbur and Dilip Mookherjee. 2005. "New Directions in Development Economics: Theory or Empirics?" *Economic and Political Weekly*, Vol. XL, No. 40, pp. 4328-4346.
<http://www.arts.cornell.edu/poverty/kanbur/NewDirectionsDevEcon.pdf>
- Dasgupta, Indraneel and Ravi Kanbur. 2005. "Bridging Communal Divides: Separation, Patronage, Integration". In Christopher B. Barrett (Editor), *The Social Economics of Poverty: Identities Groups, Communities and Networks*, Routledge.
<http://www.arts.cornell.edu/poverty/kanbur/DasKanBridge.pdf>
- Grusky, David and Ravi Kanbur. 2004. "Conceptual Ferment in Poverty and Inequality Measurement: The View from Economics and Sociology."
<http://www.arts.cornell.edu/poverty/kanbur/GruskyKanbur.pdf>
- Hall, Anthony and James Midgley. 2004. *Social Policy for Development*. Sage Publications.
- Persson, Torsten and Guido Tabellini. 2000. *Political Economics—Explaining Economic Policy*. MIT Press. Cambridge, MA.
- Persson, Torsten and Guido Tabellini. 2003. *The Economic Effects of Constitutions*. MIT Press. Cambridge, MA.
- Kanbur, Ravi. 2000. "Aid, Conditionality and Debt in Africa". In Finn Tarp (ed), *Foreign Aid and Development: Lessons Learnt and Directions for the Future*, Routledge, 2000.
<http://www.people.cornell.edu/pages/sk145/papers/africaid.pdf>
- Kanbur, Ravi. 2001. "Economic Policy, Distribution and Poverty: The Nature of Disagreements." *World Development*.
<http://www.people.cornell.edu/pages/sk145/papers/Disagreements.pdf>
- Kanbur, Ravi. 2002. "Economics, Social Science and Development." *World Development*.
<http://www.arts.cornell.edu/poverty/kanbur/Cross-Disciplinarity.pdf>
- Kanbur, Ravi. 2003a. "Behavioral Development Economics."
<http://www.arts.cornell.edu/poverty/kanbur/Stig-Kanbur.pdf>

Kanbur, Ravi (Editor). 2003b. *Q-Squared: Qualitative and Quantitative Methods of Poverty Appraisal*. Permanent Black. <http://www.arts.cornell.edu/poverty/kanbur/QQZ.pdf>

Kanbur, Ravi. 2004a. "On Obnoxious Markets." In Stephen Cullenberg and Prasanta Pattanaik (editors), *Globalization, Culture and the Limits of the Market: Essays in Economics and Philosophy*. Oxford University Press.
<http://www.arts.cornell.edu/poverty/kanbur/Obnoxious%20Markets.pdf>

Kanbur, Ravi. 2004b. "Pareto's Revenge." *Journal of Economic and Social Development*.
<http://www.arts.cornell.edu/poverty/kanbur/ParRev.pdf>

Kanbur, Ravi. 2005a. "Growth, Inequality and Poverty: Some Hard Questions." *Journal of International Affairs*. Spring. Pp. 223-232.
<http://www.arts.cornell.edu/poverty/kanbur/GroIneqPov.pdf>

Kanbur, Ravi. 2005b. "Reforming the Formula: A Modest Proposal for Introducing Development Outcomes into IDA Allocation Procedures."
<http://www.arts.cornell.edu/poverty/kanbur/IDAForm.pdf>

Kanbur, Ravi and Annelise Riles. 2004. "And Never the Twain Shall Meet? An Exchange on the Strengths and Weaknesses of Anthropology and Economics in Analyzing the Commons." <http://www.arts.cornell.edu/poverty/kanbur/KanburRiles.pdf>

Kanbur, Ravi and Paul Shaffer. 2005. "Epistemology, Normative Theory and Poverty Analysis: Implications for Q-Squared in Practice." Introduction to a forthcoming Special Issue of *World Development*.

Lynn, Stuart R. 2003. *Economic Development: Theory and Practice for a Divided World*. Prentice Hall. New Jersey.

Mkandawire, Thandika. "Social Policy in a Development Context." UNRISD.
[http://www.unrisd.org/80256B3C005BCCF9/httpNetITFramePDF?ReadForm&parentunid=C83739F8E9A9AA0980256B5E003C5225&parentdoctype=paper&netitpath=80256B3C005BCCF9/\(httpAuxPages\)/C83739F8E9A9AA0980256B5E003C5225/\\$file/mkandaw1.pdf](http://www.unrisd.org/80256B3C005BCCF9/httpNetITFramePDF?ReadForm&parentunid=C83739F8E9A9AA0980256B5E003C5225&parentdoctype=paper&netitpath=80256B3C005BCCF9/(httpAuxPages)/C83739F8E9A9AA0980256B5E003C5225/$file/mkandaw1.pdf)

Rawls, John. 1971. *A Theory of Justice*. Harvard University Press.

Rodrik, Dani. 2005. "Why we learn nothing from regressing economic growth on policies."
<http://ksghome.harvard.edu/~drodrik/policy%20regressions.pdf>

Sen, A.K. 1985. *Commodities and Capabilities*. Elsevier. Amsterdam.

Sen, A.K. 1999. *Development As Freedom*. Knopf. New York.

World Bank. 2004. *Economic Growth in the 1990s: Learning from a Decade of Economic Reform*.

World Bank. 2005a. *Empowering People By Transforming Institutions: Social Development in World Bank Operations*. Social Development Department.

World Bank. 2005b. "Concept Note: Rethinking Social Policy."
<http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTSOCIALDEVELOPMENT/0,,contentMDK:20692151~pagePK:210058~piPK:210062~theSitePK:244363,00.html>

OTHER A.E.M. WORKING PAPERS

WP No	Title	Fee (if applicable)	Author(s)
2006-04	Ghana's Economy at Half Century: An Overview of Stability, Growth and Poverty		Aryeetey, E. and R. Kanbur
2006-03	Poverty and Well-Being in a Post-Apartheid South Africa: An Overview of Data, Outcomes and Policy		Bhorat, H. and R. Kanbur
2006-02	Epistemology, Normative Theory and Poverty Analysis: Implications for Q-Squared in Practice		Kanbur R. and P. Shaffer
2006-01	Terrorism and Residential Preferences: Evidence from NYS Polling Data in New York State		Kay, D., Geisler, C. and N. Bills
2005-27	An Econometric Evaluation of a Geopolitical Theory of Oil Price Behavior		Slaibi, A., Chapman, D. and H. Daouk
2005-26	The Politics of Oil and the Aftermath of Civil War in Angola		Kyle, S.
2005-25	A Strategy For Agricultural Development in Angola		S. Kyle
2005-24	New Directions in Development Economics: Theory or Empirics? A Symposium in Economic and Political Weekly		Banerjee, A., Bardhan, P., Basu, K., Kanbur, R., Mookherjee
2005-23	Spatial Inequality and Development: Overview of UNU-WIDER Project		Kanbur, R. and Venables. A.
2005-22	Oil and Politics in Angola		Kyle, S.
2005-21	A Framework for Scaling Up Poverty Reduction, With Illustrations from South Asia		Devarajan, S. and R. Kanbur
2005-20	Membership Based Organizing of Poor Women: Reflections After an Exposure and Dialogue Program with SEWA in Gujarat, India, January 2005		Editors: Chen, M., Jhabvala, R., Kanbur, R., Mirani, N., Osner, K. and C. Richards
2005-19	Oil Revenue, the Real Exchange Rate and Sectoral Distortion in Angola		Kyle, S.
2005-18	Minimum Wages and Poverty		Fields, G. and R. Kanbur
2005-17	Characterizing Distributions of Class III Milk Prices; Implications for Risk Management		Wang, D. and W. Tomek
2005-16	The Development of Development Thinking		Kanbur, R.

Paper copies are being replaced by electronic Portable Document Files (PDFs). To request PDFs of AEM publications, write to (be sure to include your e-mail address): Publications, Department of Applied Economics and Management, Warren Hall, Cornell University, Ithaca, NY 14853-7801. If a fee is indicated, please include a check or money order made payable to Cornell University for the amount of your purchase. Visit our Web site (<http://aem.cornell.edu/research/wp.htm>) for a more complete list of recent bulletins.