

Opening Presentation
by
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**ENDING POVERTY IN A GENERATION:
THE CHALLENGE OF POLITICS AND INSTITUTIONS**

Ladies and Gentlemen, Colleagues, and Friends:

- It is a pleasure to be here today with all of you. Not only will I have the privilege to hear and learn from the important work you are doing on South Asia, I will finally have a chance to see a small corner of Australia.
- This is my first visit to this wonderful continent. But, I am familiar with Australia. Indeed, its experience with policy and institutional reforms is increasingly informing the policy debate in South Asia. How Australia has reformed its Competitions Policy, its impact on utility reform, the way the relations are managed between the Commonwealth, the States and local governments, and the ongoing discussions about the management of water resources – to name a few - are all influencing important policy discussions in South Asia.
- Before I talk more about the value of your experience of institutional change, let me first share with you my perspectives on South Asia.

The first theme of my message today is one that we in the World Bank are very excited about. And that is the real prospect of eliminating poverty in South Asia.

- There is no doubt that these are extra-ordinary times for South Asia.
- Who would have thought that the finals of the World Cup 20-20 would be an exclusively South Asian affair? I hope you'll forgive my emotional allegiances. As a Ugandan, I celebrated Zimbabwe's feat. And as an African of South Asian descent, a Pakistan-India final was a dream contest.
- But the reality of South Asia off the cricket field is even more extraordinary.

- During the past decade, every country in South Asia has either been growing rapidly or reducing poverty rapidly – or both.
 - o India is currently registering 9 percent growth and lifting 10 million people a year out of poverty. Long buried is Lal’s infamous “Hindu rate of growth” that depicted India as a slow giant.
 - o Bangladesh, Pakistan, and Sri Lanka are growing at nearly 7 percent a year. And Bangladesh’s rate of poverty reduction is twice that of India, putting to rest Henry Kissinger’s image of Bangladesh as a “basket case”.
 - o Even Nepal, which has had anemic growth, managed to reduce poverty by 11 percentage points in eight years.
- This raises the distinct possibility that South Asia – the region with the world’s largest concentration of poor people – will not just reduce poverty, but it may eliminate it in a generation. Knowing South Asia well, you may well be surprised by this assertion.
- Success will require that South Asia’s growth be sustained and made more inclusive. This in turn means closing the large infrastructure deficits and realizing much faster growth in lagging regions and states. It will also require that human development be accelerated; and deep problems of governance be overcome.
- Can this be done? My answer is: “Yes. But it won’t be easy.”
 - o “Yes”, because South Asia is in the grips of a “growth momentum” that is changing the dynamics of policy making..
 - o “Not easy” because most of the key obstacles stem from a policy or institutional failure whose reform is deeply political. And as you know, anything political is hard to reform. We should remember that these policies and institutions were often introduced with the best of intentions - and often to protect the poor. But in many cases, they have now become obstacles rather than enablers.

My next theme is challenge of institutional and structural reforms that are urgently needed for South Asia to eliminate poverty.

- Whether policy makers are able to resolve these challenges will make the difference between just advancing poverty reduction and achieving the dream of a sub-continent free of poverty within a generation. I see four key imperatives: the need plug the region's huge infrastructure deficit; the importance of ensuring growth benefits all; the central priority to invest in people; and the need for the right governance environment. Allow me to say a few words on each of these.

Infrastructure Deficit

- South Asia faces formidable infrastructure deficits. Power outages and load shedding are common. Not a single city in South Asia is able to deliver drinking water 24 hours, seven days a week even though in most cases there is plenty of water available. Traffic congestion is bringing many a city in South Asia to a standstill.
- Among the reasons for these deficits is the lack of investment in the past, under-spending on operations and maintenance, weak regulation. I think there was also possibly an optimistic view – for which donors must accept the lion's share of the blame – that the private sector will “take care” of infrastructure.
- But these are only proximate reasons for the deficits; at the heart of the problem is how infrastructure is managed.
- For example, most utilities in South Asia are run directly by political leaders. The Chairperson of Water Boards in India is, for example, in many cases, the Chief Ministers of the State. There is little distance between the policy maker and service provider – judge and jury are one and the same. Under these conditions, political considerations, not service delivery objectives, drive the provision of services.
- The pricing of infrastructure services reflects these political decisions. Prices of electricity and water have been kept deliberately low, so that poor people can afford them. But the outcome has been everything but: a decrepit electricity grid, intermittent service, and deficit-ridden utilities. The Ceylon Electricity Board, for example, loses 50 million rupees every day. That's the cost of one rural hospital. Worse, poor people, the very ones for whom the prices were kept low, are usually left out of the electricity or water networks. They end up buying it in the private market at about five to sixteen times the meter rate. Various estimates suggest that India needs

to invest about 8 percent of GDP in mainly water and power infrastructure to sustain growth. Our calculations show that about half of this investment can be financed by better pricing of infrastructure.

- This is no secret. So why haven't South-Asian governments been more pro-active in changing how infrastructure is managed? Simply put, this a deeply political act, not simply a question of applying technocratic solutions.
- Subsidized electricity is a good example. There are winners and losers. The winners can mobilize themselves to block the reform. One of the most distorting and inequitable policies is the practice in some Indian states of giving free power to farmers. Yet when Chandra Babu Naidu, the chief minister of Andhra Pradesh, reformed the policy, he lost the election. His opponent ran on the platform that, if elected, he would restore free power, which he did. I have to admit that the World Bank has not always helped. Given the enormous distortions and losses of the utilities, the Bank in the past took a rather absolutist position, saying that we would not lend for infrastructure unless there was reform. As a result, there was neither reform nor infrastructure investment. Over time, we have realized that this is not productive. In the past three years, we have been working with governments, using a mix of financial and knowledge assistance, to help them reform and crowd-in investments in infrastructure. For instance, we have been working with the new government in Andhra Pradesh in a series of policy reform operations to rationalize the energy sector and improve public expenditure management. While AP still has the "free-power" policy, it is much more finely targeted to small farmers; they have introduced metering of all power users; and the state now has the best-run power sector in India. We haven't solved all of AP's power problems. Much more investment and reform will be needed. But the state appears to be on a virtuous cycle of policy and institutional reforms, more investment, higher growth, more reforms, and so on.

Inclusive Growth

- Let me turn next to the problem of inclusive growth. Inequality is rising in South Asia partly because certain well-intentioned policies have backfired, making it harder for poor people to benefit from growth.
 - o In Sri Lanka, for example, agricultural policies have fueled inequality. Economic growth has been concentrated in the Western Province. The rest of the country has not grown because agriculture has hardly expanded, in large part due to policies that restrict farmers to growing rice rather than allowing them to diversify their crops. Recently a farmer was fined 35,000 rupees for growing bananas on his land. But, even though the evidence is clear that changing the rice policy would enhance growth and benefit the poor, political inertia makes this a difficult shift.
 - o Another source of rising inequality in South Asia is the lack of unskilled employment growth. In India, Pakistan and Sri Lanka especially, economic growth has not been accompanied by a commensurate increase in employment. A major reason for this is the set of restrictive labor regulations in most of these countries. The average severance pay in Sri Lanka is 175 weeks. Not surprisingly, firms stay out of the formal sector so they can avoid these regulations. In Sri Lanka, the number of employees per firm peaks at 14. Why? Because the employment regulations kick in at 15 workers. But informal sector firms cannot invest in large-scale equipment that will then give employment to significant numbers of workers. In short, due to some restrictive employment regulations, low-skilled manufacturing employment has not grown in South Asia. The solution is not to get rid of these restrictions, but to replace them with regulations that provide workers with adequate security and employers with flexibility to hire more workers. Needless to say, reforming labor laws can be political dynamite. The challenge to us is “how can we help in this process?”
- On the subject of inclusion, I want to make one quick point. The Bank has shifted its strategy from one where we supported reforming states to one that emphasizes lagging states.

- o In India, we are focusing on Bihar and Orissa (and possibly Uttar Pradesh), with development policy operations;
- o In Pakistan, we have programs in North West Frontier Province and Balochistan.
- The shift represents an increase in the riskiness of our investments. And the environment in these lagging regions is more difficult to work in. But we are convinced that this is the right path.

Human Development

- Human development is lagging behind economic growth in most South Asian countries. One symptom of institutional failure is the high rates of absenteeism among teachers in public schools and doctors in primary health clinics. In India, the average rates are 25 and 40 percent respectively. Even when providers are present, the quality of services provided is appallingly low. As a result, 80 percent of health spending is in the private sector. Poor people bypass the free, public clinic and pay the private doctor (who may be a quack) because at least he is present and treats them well.
- The problem is the failure of service providers to be accountable either to policymakers or to their clients. Public-school teachers are absent because no one is monitoring them; and they collect their paycheck even if they don't show up for work. Changing this situation is changing the politics of the sector – again a task beyond the traditional technocratic solutions.
- So what can be done? One path is to change the incentives is to make schools and health care providers more accountable for performance.
 - o In Bangladesh, they do this by giving students – in this case, female secondary school students – a choice. Girls can chose between public, private, NGO-run, or madrassa and the schools are compensated according to the number of girls they enroll. Not only is secondary school enrolment rising rapidly in Bangladesh – and twice as fast for girls as for boys – but many schools now have separate latrines for girls and boys. Schools are hiring female teachers to attract more girls to enroll there.

- o A second way to make schools accountable is to have parents and the local community participate in their management. Nepal has handed of the running of 5,000 public schools to management committees consisting of parents, teachers and respected members of the local community. Teacher and student absenteeism is down, and the program is likely to cover all schools in the country before long.
- o A third form of strengthening accountability is to allow schools to hire teachers from the local community, as is being done in Punjab, Pakistan. While they may be less qualified than the public sector teachers, these people are more reliable in attendance. Also, some studies show that the quality of teaching is not significantly different from that by more qualified (and more expensive) teachers from urban areas.
- o Finally, contracting out health services increases accountability and appears to improve outcomes. In Afghanistan, an independent evaluation of a program of contracting out health services showed, among other things, that about 40,000 babies a year were saved from dying before their first birthday, a tremendous turnaround in a country which had among the highest infant mortality rates in the world

Governance

- Let me turn to governance. There is no question that South Asia suffers from various problems of weak governance. One symptom is the high levels of corruption
- Bangladesh, for example, is at the bottom of the Transparency International index. Yet this same country has seen its GDP growth rate increase by one percentage point every decade. Poverty has fallen by about 1.8% per year for the last ten years. There are equal numbers of boys and girls in both primary and secondary school. And the country is on track to achieve the Millennium Development Goal in child mortality.
- This “Bangladesh paradox” as we call it shows that we need to un-bundle governance into its components and understand what works and what doesn’t. For instance Bangladesh has a thriving civil society. The government has traditionally made room for NGOs to deliver basic services and the microfinance revolution now reaches some

20 million households. Meanwhile, corruption has contributed to the fact that Bangladesh has not been able to attract a single independent power producer this decade – despite severe power shortages. And confrontational, sometimes violent politics has clearly dampened the climate for investment.

- In addressing Bangladesh’s governance problems, we need to build on its strengths. The presence of an active civil society has led to the demand for bringing the state closer to communities – in other words, there is an organic demand for decentralizing one of the most centralized systems of governance. The Bank with the support of the SDC, UNDP and the EU has stepped in to help strengthen the country’s local government system even as we support the funding of community organizations.
- Formation and strengthening of local governments is a political act; but done correctly, it can have deep impact on development and poverty eradication. For that reason we have chosen to engage in the policy dialogue on decentralization.

Conflict

- Finally, the persistent civil conflict in countries like Sri Lanka and Afghanistan undermines development. And conflicts are perhaps the thorniest of the political problems to address.
- In places of conflict, the Bank’s approach is not to walk away from these situations. Rather, we tailor our assistance to help reduce poverty within the context of the conflict.
 - o For instance, during the Maoist rebellion in Nepal, we continued to provide support to community-run health clinics. In Afghanistan, we support the National Solidarity Program which provides communities with funds to run schools, clinics and small infrastructure projects. In Sri Lanka, we are going a step further and using our assistance to address the causes and consequences of conflict. We have a program of housing to resettle internally displaced persons. And we are introducing common-language programs in our education projects to bring divided communities together.
- Equally important, in many of the conflict areas, we are investing in supporting the stakeholders to look at the issues of the restructuring of the state, the role of local

governments, and the design of the interface between the state and communities. Again these are all political changes, but changes that will impact on the accountability of the state to deliver development to its citizens.

The final theme of my presentation is to share some thoughts on possible solutions to some these challenges and mention suggestions for the next generation of donor support and research focus.

As I have said, policy and institutional changes will be necessary to address the key obstacles facing South Asia if eliminating poverty is a dream that can be realistically achieved within a generation. Strong growth will help, but it won't be enough.

- This can only be done if we recognize that policy and institutional changes are a highly political affair. They emerge from complex policy reform processes. And as donors our understanding of these processes is critical if we are to support the extraordinary changes that are happening in South Asia.
- None of this is easy, and we certainly don't have all the answers – which is why I have chosen to focus on these issues today. In this context, let me talk about our relationship with AusAid and priorities for donor and research focus.
- In the past we have focused on supporting fiscal stability, getting macro prices corrected, opening local economies up to global opportunities, funding bulk infrastructure, and investing in intelligent interventions at the household level. Now we need to focus on institutional change to improve accountability of the state to its citizens. This may be the best way to have impact on poverty reduction on a sustained basis and at scale.
- For IDA to have the necessary impact on poverty reduction, we need to leverage and build on reform processes that support institutional change.
- In recognition of this, AusAid and the World Bank have entered a partnership whereby an AusAid trust fund is funding teams to engage in policy processes in all countries in South Asia with the aim at supporting institutional change at the country level. In particular, the fund is focused on understanding and strengthening the

linkage between decentralization, local governance, and service delivery in South Asia.

- This is one of the most important bilateral relationships the South Asia Region of the Bank has with any one donor. The fund's focus on institutional change and its regional coverage places it at the cutting edge of the next generation of focus on development issues. It will significantly leverage the use of IDA resources in South Asia.

Research Implications

- There are also important implications for the research community as we focus more on institutional change. In particular we need to know more about:
 - o What the drivers are of policy and institutional change
 - o And when institutional change happens
- In this context, I would go back to where I started: Australia's reform process. To answer these questions, we need to better understand the history of institutional change in countries such as Australia. These are not questions that can be resolved from first principles, we need to know what has worked and has not worked in different environments – and why.
- Take for example the policy debate on the management of the Murray Darling Basin. It has been viewed by South Asia as one of the most successful institutional systems of river basin management. Indeed we recently brought a team from Pakistan to learn from this experience. Yet in Australia, it is now facing a serious review. Understanding the history of Murray Darling and the institutional changes in river basin management in Australia has a lot to offer regions such as South Asia.
- I look forward to your contribution as researchers to our understanding of institutional change.

Conclusion

- To conclude, I am optimistic that in South Asia we can end poverty in a generation. South Asia has already shown that it can accelerate growth and reduce poverty. The remaining obstacles to ending poverty – inequality, infrastructure, lagging human development, weak governance – are all man-made. If we erected them, surely we can also dismantle them.
- While removing these obstacles is deeply political, South Asia’s recent growth and some successful initiatives around the subcontinent are helping to build political support for reform. By providing knowledge and financial assistance to support reforms, by working with governments to overcome political obstacles rather than imposing strict conditionality, and by engaging with lagging states and countries in conflict, the World Bank’s recent strategy in South Asia, with support from AusAid, is producing results.
- As you enter the World Bank’s building in Washington, D.C., there is a sign that reads “Our dream is a world free of poverty.” For the 1.4 billion South Asians, together we have a chance to help make that dream a reality.
- I look forward to a lively discussion.