

Introduction

chapter 1

Nthabiseng and Pieter—the hypothetical South African children who opened the report’s overview—are not unusual examples of people who face highly disparate initial opportunities. A girl born to a lower-caste family of nine in the slums of Dhaka has vastly different opportunities from a boy born to well-educated and affluent parents in the well-heeled neighborhoods. An AIDS orphan in rural Zimbabwe is almost certain to have fewer chances and choices in life than a compatriot born to healthy and well-educated parents in Harare. Those differences are even greater across borders: an average Swiss, American, or Japanese child born at the same instant as Nthabiseng will have incomparably superior life chances.

Such staggering inequalities in opportunity are intrinsically objectionable, and almost every culture, religion, and philosophical tradition has developed arguments and beliefs that place great value on equity for its own sake. In addition, Part II of this report will argue that we now have considerable evidence that equity is also instrumental to the pursuit of long-term prosperity in aggregate terms for society as a whole. But before one can describe inequity, or assess its impact on growth and development, a clear definition of the term is needed.

This introductory chapter presents our working definition of equity and briefly discusses its main component—equality of opportunity. It then turns from our central normative concepts to one of the report’s key positive concepts: inequality traps. An inequality trap encapsulates the mutually reinforcing nature of various inequalities, which leads to their persistence and to an inferior development trajectory.

Equity and inequality of opportunity: the basic concepts

What is equity? As with any normative concept, the word “equity” means different things to different people. It is a difficult concept, with a history of different interpretations, varying by country and academic discipline. Economists link equity to questions of distribution. Lawyers tend to think of principles meant to correct the strict application of the law, which may lead to an outcome judged to be unfair in specific circumstances. Philosophers have produced the most headway in the thinking about equity. Indeed, the attributes that would characterize a just and fair society lie at the foundation of Western political philosophy, from Plato’s *Republic* and Aristotle’s *Politics* onward. Equity is also central to most of the world’s great religions, including Buddhism, Christianity, Hinduism, Islam, and Judaism, as well as to most other faith traditions. More recently, social choice theory, and the closely related domain of welfare economics, have been concerned with the aggregation of preferences into some form of “social optimum.”

Summarizing such long-standing and nuanced characterizations is perilous, but the common denominator of these many different views is that equity relates to fairness, whether locally in families and communities, or globally across nations. We do not dwell on the different approaches to equity here, but we do elaborate on them in chapter 4, which reviews various categories of evidence in support of the intrinsic importance of equity. For this report, we think of equity as being defined in terms of two basic principles:

- *Equal opportunity.* The outcome of a person’s life, in its many dimensions,

should reflect mostly his or her efforts and talents, not his or her background. Predetermined circumstances—gender, race, place of birth, family origins—and the social groups a person is born into should not help determine whether people succeed economically, socially, and politically.¹

- *Avoidance of absolute deprivation.* An aversion to extreme poverty, or indeed a Rawlsian² form of inequality aversion in the space of outcomes, suggests that societies may decide to intervene to protect the livelihoods of its neediest members (below some absolute threshold of need) even if the equal opportunity principle has been upheld. The road from opportunities to outcomes can be tortuous. Outcomes may be low because of bad luck, or even because of a person's own failings. Societies may decide, for insurance or for compassion, that its members will not be allowed to starve, even if they enjoyed their fair share of the opportunity pie, but things somehow turned out badly for them.

The equal opportunity principle is conceptually simple: circumstances at birth should not matter for a person's chances in life. But to measure inequality of opportunities is much harder. Chapter 2 briefly discusses one approach, which decomposes observed income inequality into one part that can be attributed, in a statistical sense, to predetermined circumstances—such as race, place of birth, and parental background—and one part that cannot. The first component captures a lower bound value for the opportunity share of income or earnings inequality. But it is generally very difficult to measure things like family background precisely: years of schooling and broad occupational categories are imperfect proxies for a family's endowments of human, physical, and social capital.

A superior approach would be to capture the inherently multidimensional and group-based nature of inequality of opportunity. How do the factors that determine a person's chances in life—the access to health and educational opportunities, the ability to

connect to the rest of the world, the quality of the services available, the way institutions treat them—relate to one another? And how do these factors vary across groups? Such an approach would require a focus not only on the dispersion of univariate distributions (such as income inequality or life expectancy) but also on the correlations among them (how do health outcomes vary across socioeconomic groups?). This is the approach taken in most of chapter 2, which summarizes information on inequalities (with emphasis on the plural) in the various building blocks of opportunity and on their interrelationships.

In taking this route, the report recognizes that predetermined circumstances, or membership in prespecified groups, affect opportunities in two ways:

- The circumstances of one's birth affect the endowments one starts with, including all kinds of private assets, such as physical wealth (including land and financial assets), family background (the human, social, and cultural capital of one's parents), and access to public services and infrastructure (sometimes referred to as geographic capital).
- Group membership and initial circumstances also affect how one is treated by the institutions with which one must interact. Two individuals may both live in areas where formal labor markets exist, where courts are agile, and where a police force is present. But if these two (otherwise identical) people, because of their gender, race, religion, sexual orientation, political beliefs, residential address, or any other morally irrelevant reason, are differently rewarded for the same work in the labor market, are discriminated against by the court of law, or are treated with bias by the police force, then the rules are not being applied fairly. Therefore, these two people do not have the same opportunity sets. Equity also requires fairness in processes.

Endowments that are less unequal, processes that are fair, and protection from deprivation are not always mutually consistent. At the policy level, there may be

tradeoffs among them. Indeed, some policies or institutions developed to further one of the principles may compromise the other.

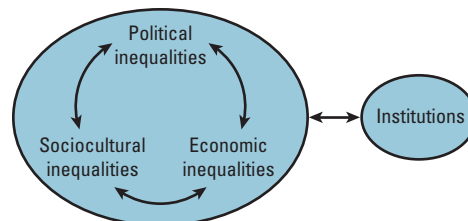
For example, a policy of affirmative action that seeks to correct past inequities in the access to educational opportunities for one group—to equalize endowments—may imply that individuals of greater merit (but from another group) are excluded, creating unfair processes. For another example, the taxes needed to raise government revenues to make transfers to poor individuals (desirable to avoid deprivation) expropriate some fruits of the efforts of hard-working men and women. This might be seen as violating property rights or the rights to appropriate the fruits of one's own labor, again creating unfair processes.

Whenever such tradeoffs exist—which is most of the time—no textbook policy prescription can be provided. Each society must decide the relative weights it ascribes to each of the principles of equity and to the efficient expansion of total production (or other aggregate). This report will not prescribe what is equitable for any society. That is a prerogative of its members to be undertaken through decision-making processes they regard as fair.

Inequality traps

If people care about equity, and if political systems aggregate people's views into social preferences, why don't the distributions we observe represent optimal choices? Why do inequalities of opportunity persist, if they are both unfair and inimical to long-term prosperity? And how do these inequalities reproduce themselves? The short answer is that political systems do not always assign equal weights to everyone's preferences. Policies and institutions do not arise from a benign social planner who aims to maximize the present value of social welfare. They are the outcomes of political economy processes in which different groups seek to protect their own interests. Some groups have more power than others, and their views prevail. When the interests of dominant groups are aligned with broader collective goals, these decisions are for the common good. When they are not, the outcomes need be neither fair nor efficient.

Figure 1.1 The interaction of political, economic, and sociocultural inequalities



The interaction of political, economic, and sociocultural inequalities shapes the institutions and rules in all societies. The way these institutions function affects people's opportunities and their ability to invest and prosper. Unequal economic opportunities lead to unequal outcomes and reinforce unequal political power. Unequal power shapes institutions and policies that tend to foster the persistence of the initial conditions (figure 1.1).

Consider the status of women in patriarchal societies. Women are often denied property and inheritance rights. They also have their freedom of movement restricted by social norms that create separate "inside" and "outside" spheres of activity for women and men. These social inequalities have economic consequences: girls are less likely to be sent to school; women are less likely to work outside the home; women generally earn less than men. This reduces the options for women outside marriage and increases their economic dependence on men. The inequalities also have political consequences: women are less likely to participate in important decisions within and outside the home.

These unequal social and economic structures tend to be readily reproduced. If a woman has not been educated and has grown up to believe that "good, decent" women abide by existing social norms, she is likely to transmit this belief to her daughters and to enforce such behavior among her daughters-in-law. An inequality trap may thus prevent generations of women from getting educated, restrict their participation in the labor market, and reduce their ability to make free, informed choices and to realize their potential as individuals. This

reinforces gender differences in power that tend to persist over time.

Similarly, the unequal distribution of power between the rich and the poor—between dominant and subordinate groups—helps the rich maintain control over resources. Consider an agricultural laborer working for a powerful landlord. Illiteracy and malnourishment may prevent him from breaking out of the cycle of poverty. But he is also likely to be heavily indebted to his employer, which puts him under the landlord's control. Even if laws were in place that would allow him to challenge his landlord's dictates, being illiterate, he would find it difficult to navigate the political and judicial institutions that might help him assert his rights. In many parts of the world, this distance between landlords and laborers is compounded by entrenched social structures: landlords typically belong to a dominant group defined by race or caste, tenants and laborers to a subordinate group. Because members of these groups often face severe constraints from social norms against intermarrying, group-based inequalities are perpetuated across generations.

Poor individuals in geographically isolated regions and racial and ethnic minorities also have less political power and less voice in many countries. This affects their ability to propose and implement policies that would reduce their disadvantage, even if such policies might be growth-enhancing for the country.³ The correlations between the unequal distribution of assets, opportunities, and political power give rise to a circular flow of mutually reinforcing patterns of inequality. Such a flow, and its associated feedback loops, help inequalities persist over long periods—even if they are inefficient and deemed unfair by a majority of the population.⁴

Economic and political inequalities are themselves embedded in unequal social and cultural institutions.⁵ The social networks that the poor have access to are substantially different from those the rich can tap into. For instance, a poor person's social network may be geared primarily toward survival, with limited access to networks that would link him or her to better jobs and opportunities. The rich, by contrast, are bequeathed with much more economically productive social

networks that maintain economic rank. Rich parents can use their social connections to ensure that their child gets into a good school, or they can call a few good friends to make sure that their son gets a good job. Conversely, poor parents are more subject to chance. Connections open doors and reduce constraints.

Social networks are closely allied with culture. (By "culture" we mean aspects of life that deal with relationships among individuals within groups, among groups, and between ideas and perspectives). Subordinate groups may face adverse "terms of recognition," the framework within which they negotiate their interactions with other social groups.⁶ One obvious expression is explicit discrimination that can lead to an explicit denial of opportunities and to a rational choice to invest less at the margin.

But the process may also be less overt. A person born into a low social class or a socially excluded group may adopt the dominant group's value system.⁷ Religious beliefs may propel this: women may take on gendered beliefs about their economic and social role, and low castes may absorb the upper castes' view of their "inferior" status. In schools, a stigmatized group may face a "stereotype threat," adopting the dominant group's view of their ability to perform in cognitive tests or in occupations historically controlled by dominant groups.⁸ This can affect a discriminated group's "capacity to aspire."⁹ It also implies that "voice," the capacity of individuals to influence the decisions that shape their lives, is also unequally distributed and that "effort" and "ability" are not necessarily exogenous (predetermined).¹⁰

The existence of these inequality traps—with mutually reinforcing inequalities in the economic, political, social, and cultural domains—has two main implications for this analysis. The first implication is that, because of market failures and of the ways in which institutions evolve, inequality traps can affect not only the distribution but also the aggregate dynamics of growth and development. This in turn means that, in the long run, equity and efficiency may be complements, not substitutes.¹¹

Capital, land, and labor markets in developing countries are imperfect. Informational

asymmetries and contract enforcement problems imply that some people with good project ideas (and thus a potentially high marginal product of capital) end up constrained in their access to capital. This, even as other people earn a lower return on their (more abundant) capital. In agriculture, land market failures mean that some farmers exert too little effort on some plots (where they are sharecropping), and too much effort on other plots (which they own).¹² Investment in human capital can also be allocated inefficiently, because of intrahousehold disputes, because credit-constrained households lack the resources to keep their children healthy and in school, or because discrimination in the labor market reduces the expected returns to schooling for some groups. What do such diverse market failures have in common? They cause differences in initial endowments—such as family wealth, race, or gender—to make investment less efficient.

There also are political and institutional reasons why equity and efficiency are long-term complements. Markets are not the only institutions in society. The functioning of states, legal systems, and regulatory agencies—indeed, of all the institutions that assign and enforce property rights and mediate conflicts among citizens—is influenced by the distribution of political power (or influence, or voice) in society. Unequal distributions of control over resources and of political influence perpetuate institutions that protect the interests of the most powerful, sometimes to the detriment of the personal and property rights of others.¹³

Those whose rights are not protected have little incentive to invest, perpetuating poverty and reproducing inequality. Conversely, good institutions that protect and enforce personal and property rights for all citizens have led to higher sustained economic growth and long-term prosperity. Equity can, once again, help societies grow and develop.

This does *not* mean, of course, that efficiency-equity tradeoffs have somehow been abolished. In some cases, equity enhancements bring immediate—as well as long-run—benefits for efficiency. If we reduce discrimination against women in

one segment of the labor market, such as management, and if this brings a new pool of talent into that segment, efficiency is likely to increase even in the short run.¹⁴ In other cases, however, expanding the opportunity sets for the disadvantaged may require more costly redistribution. To finance better-quality schooling for those who have the least educated parents, and who attend the worst schools, it may be necessary to raise taxes on other people. The basic economic insight that such taxation distorts incentives remains valid. Such policies should be implemented only to the extent that the (present) value of the long-run benefits of greater equity exceed the efficiency costs of funding them.¹⁵

The point is that some of these long-term benefits of pursuing greater equity are ignored in the conceptual calculus of policy design. The fact that better-schooled children who are poor and from a racial minority will be more productive is usually taken into account. But the fact that they may acquire greater political voice and help make social institutions more inclusive—which, in turn, may increase the stake of that group in society, potentially leading to greater trust, less conflict, and more investment—may not be. To the extent that such indirect (but important) benefits of equity-enhancing policies are ignored, too few of them are pursued—even assuming a purely benevolent government.

By placing equity and fairness as central elements of an efficient development strategy, developing countries will be better able to reach sustainable growth and development trajectories. Such equitable growth paths are likely to lead to faster reductions in the many dimensions of poverty, the central objective of development everywhere.¹⁶

The second implication of the existence of inequality traps is that no real-life policy or institution is entirely exogenous: no existing organization or application of a policy idea has been implemented on a purely technocratic basis. All policies and institutions exist because the political system has brought them into being or allowed them to survive. The political system reflects the distribution of power and voice attained at a particular time and place. This

distribution is, in turn, influenced by the distribution of wealth, income, and other assets and outcomes in that society. Such “circular causality” for wealth, income, social and cultural capital, and power, mediated through institutions, evolves throughout time and history.

Acknowledging history and social and political institutions is crucial to avoid policy mistakes. But a fatalistic view of the world is not only wrong, but also counterproductive. To propose policies without understanding history, or the specific context for developing these policies, often leads to failure. But this acknowledgment is not equivalent to the view that no policies should be suggested at all. Such a view fails to recognize how purposeful social and political action can achieve significant policy and institutional changes—and would result in fatalistic inaction.

History is *not* endlessly repetitive and, as this report documents, many countries have taken on the challenge of breaking inequality traps with some success. Groups have also changed their circumstances or changed social and political institutions. Consider the civil rights movement in the United States, the democratic overthrow of apartheid in South Africa, the more participatory budgeting practices in some Brazilian cities, and the reforms in access to land, education, and local government in the Indian state of Kerala. The challenge for policy is to ask when and how such changes can be supported.

A brief preview of the Report

Part I summarizes evidence on inequity within and across countries. Part II asks why equity matters for development, both intrinsically and instrumentally. Part III turns to the policy implications. If unequal opportunities and absolute deprivation are inimical to long-term prosperity—as well as intrinsically objectionable—there is scope for policy and institutional reform aimed at leveling the economic and political playing fields.

An equity lens and the focus on leveling the playing field add three basic points. First, redistributions from richer and more powerful groups to poorer groups that face more limited opportunities are sometimes necessary and should be pursued. Second, when considering policy tradeoffs between equity and efficiency, the full long-term benefits of equity—including on the development of better and more inclusive institutions—need to be taken into account. Third, all categories of economic policy—macro and micro—have effects on both efficiency (and growth) and equity (and distribution). Because our ultimate goal is the reduction of poverty through the equitable pursuit of prosperity, the policy suggestions in these chapters are consistent with good poverty-reduction policies, which the World Bank has been advocating since at least the publication of the World Development Report 1990.¹⁷ These suggestions are also in line with the 2000 World Development Report’s three pillars of opportunity, empowerment, and security.¹⁸