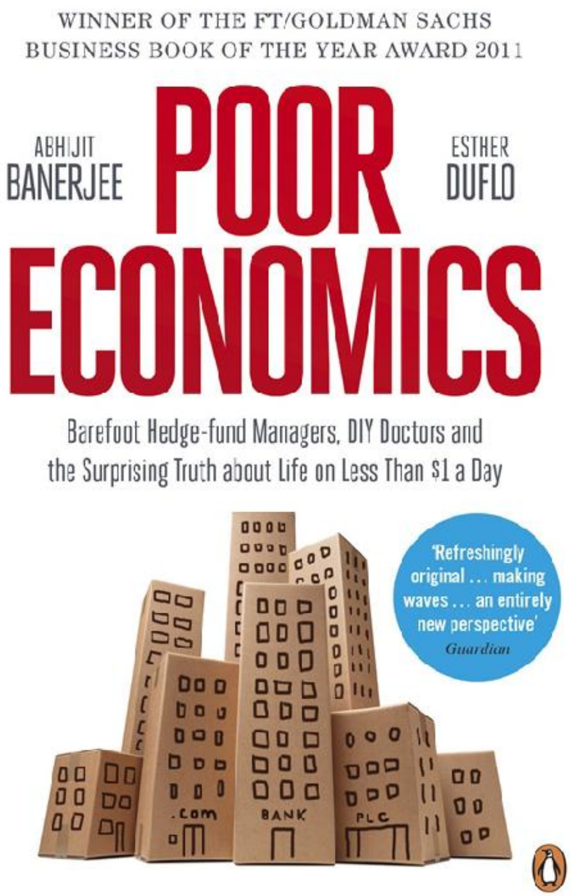


Poor Economics

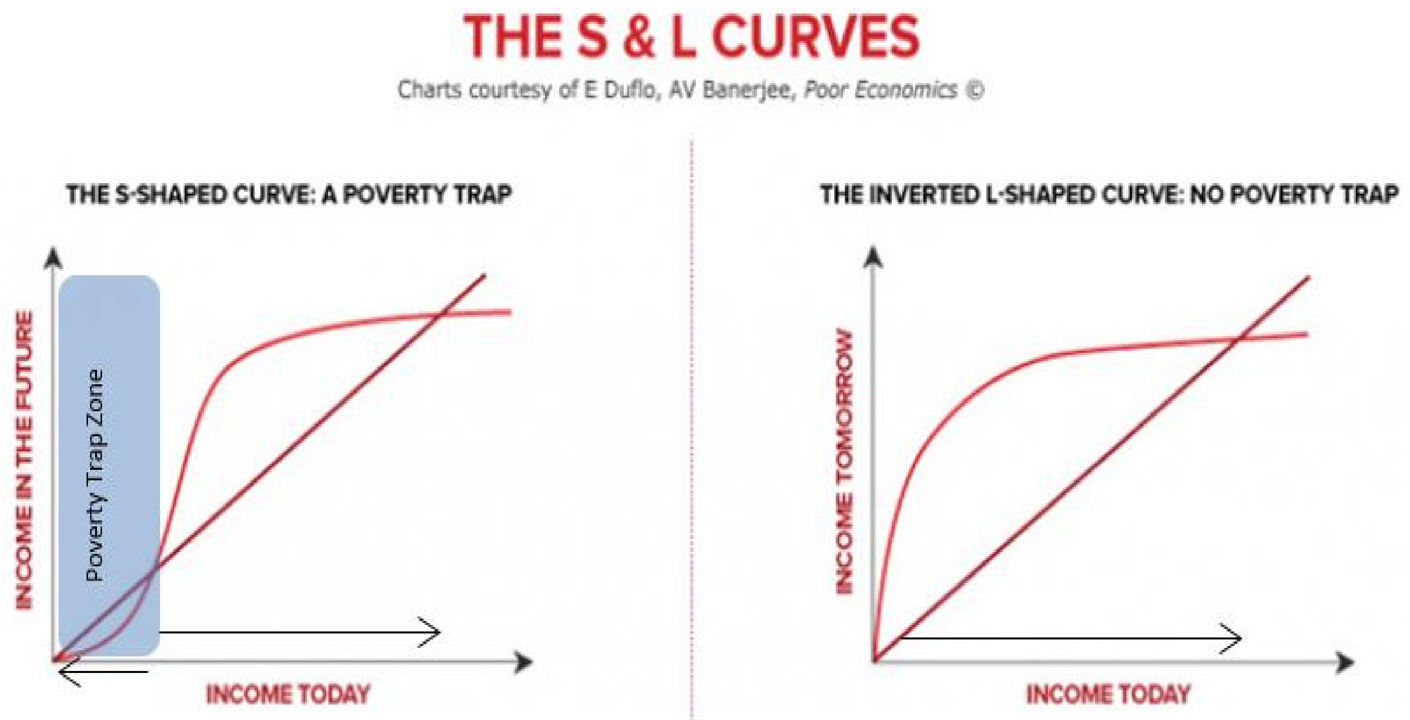
Abhijit V. Banerjee and Esther Duflo

The myths about what it is like to live on very little and the paradoxical aspects of life below the poverty line.

Poverty Trap

- There are 2 opposite views to end the poverty:
  - Left (i.e. Jeffrey Sach, UN, WHO, etc)
    - Spending more on aids
    - Introducing what are best for the poor and providing things to the poor
    - The poverty gap exists → S-shaped curve
  - Right (i.e. William Easterly)
    - Stopping aid
    - Government is corrupt → let the market go
    - There is no poverty gap → L-shaped curve

Poverty Trap



Hungry

- More than a billion people suffer from hunger
- But the world’s food production is enough to provide at least 2,700 kcals per person per day
- The studies show there are plenty of food for the poor and they actually eat enough.
- The problem is that they don’t eat well.

- WHY?

Health

- 9 billion children die before 5
- 1.5 billion children die because of diarrhea
- But it’s easy and cheap to cure and prevent
- Where are the problems?
  - Money?
  - Consciousness about health?
  - Healthcare accessibility?
  - Quality of healthcare?
  - Beliefs?

Education

- There are 2 ways to define problems of Education:
- Top-down Approach (Supply Side)
  - Infrastructure?
  - Quality of teachers?
  - What else?
- Bottom-up Approach (Demand Side)
  - Return on education?
  - Opportunity costs?

Population Control

- Large family really causes a problem?

- less capable in controlling fertility rate
- Early pregnancy

- SOLUTIONS?
  - Kenya: Uniform
  - Brazil: TV-drama

Risks

- Risk is the core problem of the poor and it is unavoidable for the poor.
- They use “diversification” to reduce the risk
    - Diversifying occupation
    - Diversifying farming plots
    - Migrating and the family stays behind
    - More children to spread the risks
- What about insurance?

Loans

- The poor are trapped by the high interest rate
  - Asymmetric information
  - No collaterals
  - High likelihood to default
- Private banks don’t want to lend to the poor while government subsidised interest rate is not effective
- Microfinance (Muhammad Yunus)
  - Group lending

Saving

- Why don't the poor save?
- There are 2 constraints:
- External constraint
  - Little access to saving
  - High administration cost
  - Low income
- Internal constraint
  - Unconscious of benefits
  - Impatience and little self-control
  - Time inconsistency and present bias

Entrepreneurship

- The poor are mostly an entrepreneur to a small business
  - small business → low scale → low growth → high margin rate of returns (think about L-shaped curve!)
  - Still, overall rate is low
- The poor are risk-adverse so they don't want to invest in a big business
- View about their self-employed occupation
  - They don't want their kids to be self-employed
  - They want their kids to have a stable job such as teacher, government officer and etc.

PUZZLE 1

Why don't the poor eat more/ better?

- 30% slack in budget for greater food purchase or saving – why then periods of hunger? Why no improvement in quality of food consumed?

  - Eating more or eating better does not help much (in incidence of sickness or productivity)? E.g. nutrition explains only a very small part of health gains worldwide over the past few decades. But some improvements in nutrition (reduction of anemia) directly linked to increased productivity.

  - Lack of saving for difficult times (no self-control around current consumption of non-food) does not fully explain this finding – because poor HHs do spend on entertainment, even save up for events, gadgets, etc.

  - The need to spend surplus on entertainment rather than on more/ better food - is it because the poor want to keep up with their neighbours?*

PUZZLE 2

Why don't the poor expand cultivation?

- Rural poor cultivate the land they own – no more no less – why?
  - Agency problems associated with renting out land?
  - Even though too little land relative to available family labour, still don't purchase land (lack of access to credit)
  - Few options to insure against risk – so get a second, temporary, non-agric job, while still holding onto some minimal farm production

Why so little specialization?

- Risk spreading very difficult, so cannot put all eggs in one basket; hence, shuttling between agric and non-agric jobs
- Occupations (farming, tiffin sales) tend to leave periods of time vacant ; hence pursue other jobs
- Also cannot raise the capital needed to expand business/ specialize in one occupation

Why so many entrepreneurs?

- Few specialized vocational skills, little capital, rigidities in local labour market (e.g. if you are a woman), so being a small-scale entrepreneur easier than finding a job

- Due to riskiness of borrowing for expansion, limit business to own/ family labour (do not employ others) – reinforces lack of jobs, and proliferation of other small-scale entrepreneurs

Why don’t the Poor invest more in Education?

- Children are going to govt primary school – but parents aren’t reacting to the poor quality by shifting children to pvt/ better schools or putting pressure on the govt to improve quality. Why?
    - Poor parents, often illiterate themselves, may have a hard time recognising that their children are not learning much
    - Not sure if they can trust pvt schools, especially since teachers there seem to have lower qualifications
    - Unclear on how best to organise to reform govt school quality

Why don’t the Poor save more?

- Why don’t the poor show more evidence of accumulation for the future, by cutting non-food expenditure (alcohol, tobacco)?
  - Saving at home is hard (live in non-lockable houses, need to share with relatives/ friends who ask for funds)
  - Have to battle temptation to spend surplus that is in-hand (small expenses that the rich may take for granted – e.g. chocolate for children)
  - Poor appear to be aware of temptations to spend: In Hyd survey, 28% mentioned at least one item they would like to cut (44% alcohol and tobacco; 9% sugar, tea and snacks; 7% on festivals; 7% on entertainment)

Why don't the Poor migrate for longer?

- Low levels of long-term migration among the poor – why?
  - Value being close to own social network, especially when that is the major source of informal insurance
  - Making money in better-paying locations is a priority, but not enough to endure poor working conditions and personal difficulty (living away from loved ones) for long periods

Designing ‘better-fit’ programmes

- Study of fertilizer use in Kenya – use of fertilizers increases yield by 75% on average; showed proof on trial plots with randomly selected farmers; but farmers who participated in the study only 10% more likely on average to use fertilizer in next season (despite recorded gains)

- When asked why, farmers replied that they had insufficient money – but fertilizer could be purchased in small packets (with little savings)

- So introduced a programme to sell fertilizer vouchers just after harvest, when farmers had money in hand – uptake of fertilizer increased dramatically (40% purchased)

- Used the voucher as a commitment device – farmers did not then exchange it for other items for immediate consumption, but instead stored and used fertilizer on land in a few months’ time

Policies

- In developing countries, there are poor governing management and poor policy implementation
- Need decentralization

- Democracy
  - The power should be given to people and the policies should come from people's opinions
- Political constrains are real and hard to be solved
  - But once we can solve these, we'll be able to solve other problems (at least, the policies are better-designed and efficient)