Poverty rates have been falling all over the world in recent years, but, outside of China, the absolute numbers in poverty continue to increase (see Chen and Ravallion, 2008). The number of people living on less than $1.25 a day (the World Bank’s official poverty line) is approximately 1.4 billion, and 2.6 billion live on less than $2 a day. Poverty alleviation in poor countries is surely the greatest humanitarian challenge facing the world in the 21st century. As Paul Collier wrote in his best-selling book *The Bottom Billion* (2007): ‘an impoverished ghetto of 1 billion people [is] increasingly impossible for a comfortable world to tolerate’. The World Bank has expressed the same sentiments. When it published its 2000/2001 *World Development Report* with the title ‘Attacking Poverty’, the then President of the World Bank, James Wolfensohn, wrote: ‘poverty amidst plenty is the world’s greatest challenge. We at the World Bank have made it our mission to fight poverty with passion and professionalism, putting it at the centre of all the work that we do’. Rather than relying on ‘trickle down’ from fast GDP growth to poverty reduction, the World Bank Report advocated a three-pronged ‘bottom-up’ approach to poverty reduction, namely: promoting opportunity; facilitating empowerment, and enhancing security. There is now broad support for this approach, combined, of course, with appropriate macroeconomic policies, but the question still remains of how best to achieve these goals; what works and what doesn’t?

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This is the background to Banerjee and Duflo’s book, *Poor Economics*, the distillation of years of research since together in 2003 they founded the Abdul Latif Jameel Poverty Action Laboratory (J-PAL) which is a network of affiliated academics in five offices around the world, and which uses randomised control trials (RCTs) to enable anti-poverty policies to be based on scientific evidence rather than hunch or custom. As they argue, ideology, ignorance and inertia often explain why good-intentioned policies fail. RCTs can help to understand the causes of poverty; the solution to poverty; whether people live in poverty traps and need help or incentives to get out, or, if they are not in a trap, why they remain poor. As of 2010, researchers had completed, or were engaged in, over 240 experiments in forty countries. The authors themselves report work largely from an eighteen country data set.

The book has received much adulation and many prizes, and there is no doubt that the detail is fascinating, but the question remains: will it radically change attitudes and policies towards poverty reduction in poor countries? This is where doubts start to creep in. Apart from the fact that the results of many of the RCTs could have been predicted in advance, there are well-known limitations of such trials. First they don’t address the general equilibrium effects, or secondary repercussions, of particular programmes. This is no more evident than in the field of education where the use of vouchers to induce children into higher quality private education may be to the detriment of the public education system and lead to an overall welfare loss. Secondly, the evaluation of a trial itself may cause both the treatment and comparison groups to alter their behaviour for the period of the experiment, leading to false inferences. Thirdly, it may be difficult to generalise the results of RCTs because they are context specific. Evaluation may be conducted on only one specific sample; the programme may be implemented in such a way that it can’t be replicated, and if a very *specific* programme is implemented, a slightly different programme may not have the same results. To be fair, the authors themselves, and Duflo et al. (2009), recognise the criticisms and limits of RCTs but maintain that when replication experiments are made, the results generalise quite well. For example, the original PROGRESA programme in Mexico for getting children into school with cash bonuses has been replicated elsewhere in Latin America, all with similar results. Remedial education programmes, and de-worming trials, tend to produce the same results in
different contexts. It is also possible to support the generalisation of RCTs by constructing theoretical behavioural models and seeing whether predictions from the models are the same as found using RCTs. This has been done in the case of the school/work choice for children, with promising results.

With these caveats in mind, let us consider the authors’ findings and policy recommendations. The book addresses chapter by chapter eight major topics: hunger; health; education; population; risk; lending and borrowing; saving, and entrepreneurship.

One of the most common conceptions is that poor people go to bed hungry every night. But one of the first interesting facts in the book, for the layperson at least, is that even very poor people don’t spend all their income on food. This can mean one of two things: either poor people have enough to eat after all, or, even if people are hungry (however defined), they are taking rational decisions about how they allocate their income. It is reported that in the Philippines, 2000 calories can be bought for as little as US20 cents. The authors recognise, however, the important distinction between different categories of people, particularly between children and pregnant mothers on the one hand and the rest of the population on the other, because it is poor nutrition in the womb and infancy which leads to individual and economic damage in later life. The overall conclusion is that governments and aid agencies need to rethink food policy and target only vulnerable groups. This is common sense.

Improving children’s health is a major challenge. Nine million children a year die before their fifth birthday through preventable diseases, treatable with low-cost remedies e.g. chlorine in water; bed nets against mosquitoes; de-worming pills and so on. The reason these cheap preventive measures are not widely used is not because poor people don’t care about their health but because of: firstly poor professional health care by nurses and doctors; secondly, money is spent on expensive cures rather than cheaper alternatives, and thirdly because people think that if something is cheap it is valueless. Belief systems play an important role in health care, but the authors find that often there is not much conviction behind beliefs so that some reward for taking cheap prophylactics as a bribe frequently works. Experiments show, for example, that immunisation camps are very successful where people are
rewarded for attending. The policy conclusion is twofold: firstly, raise and regulate the quality of treatment that people receive, and secondly, make it as easy as possible for the poor to obtain preventive care e.g. free chlorine dispensers next to water sources; free de-worming pills: free nutritional supplements, and rewards for immunisation. Again, non-controversial conclusions.

The education of poor children presents another major challenge. The authors describe most school systems in poor countries as ‘wasteful and unfair’. Pupil and teacher absenteeism is high; the quality of teaching is poor; parents don’t push their children because the perceived rate of return is low, and education is geared to the clever. RCTs show, for example, that the availability of textbooks only seems to matter for children already doing well. Since parents bear the cost of education and children reap the benefit, the main policy proposal is that governments should make it financially worthwhile for parents to send children to school. Conditional cash transfers already exist in some countries (e.g. Borsa Familia in Brazil and OPORTUNIDADES in Mexico), but interestingly RCTs indicate that the conditionality requirement doesn’t matter very much. What is important for families is the cash, and the children go to school without ‘forcing’ them.

The poor typically have large families, but why do some parents have more children than others? Are they unable to control their own fertility, or is it choice? The authors maintain it is mainly the latter. Families have children for investment. When family size goes down, precautionary saving (for old age?) goes up, and this is one reason the authors find that smaller families don’t necessarily mean that remaining children are better educated or looked after. The saving is not for them! This is perhaps a surprising result; that large family size has no impact on the education of children. The research also shows that the provision of family planning services makes very little difference to fertility unless people want them. Typically, males want more children than females, and experiments show that if women are seen alone for family planning advice, they are more likely to practice contraception and reduce fertility. The authors stress the need to target teenage pregnancies, but find that HIV/AIDS education programmes seem to have little effect. What appears to work is paying for school uniforms for girls to stay in school, and off
the streets. This is likely to be one area, however, where the results of RCTs are likely to be very context specific.

The poor live surrounded by huge risks to their livelihoods, and the way they typically cope is by diversifying their activities. They may have different plots of land in different parts of a village, producing different crops, or they may work on the land but also have part-time work or a one-person business in the city. This, of course, is very inefficient from an economic point of view because the advantages of specialisation are lost, but is rational behaviour in the face of risk. The question is why is more formal insurance not available to poor people? The authors offer several explanations: the traditional problem of moral hazard; adverse selection, and fraud, among others, but they also find that the demand for insurance is weak because people don’t understand the concept: they don’t trust insurance companies to pay out, and in really bad situations (such as crop failures) they expect government to step in and compensate. The major policy conclusion is that governments have a role in assisting the development of insurance markets by education and subsidising insurance premiums.

One way for poor people to expand their asset base is to borrow. On average, the poor borrow mainly from money-lenders, followed by friends and family. Only about five percent of poor people are able to borrow through formal financial channels because information and monitoring costs of lending to poor people are high. This has always been the challenge of the micro-credit movement: how to lend to poor people at reasonable rates of interest. The authors are interested in whether micro-credit works and they report results of the Spandana programme in Hyderabad (India) where 52 neighbourhoods were chosen at random to receive micro-credit help and 52 other neighbourhoods were taken as a control group. After eighteen months there was clear evidence of micro-finance working but not dramatically. People, perhaps surprisingly, still continued to borrow from money-lenders at exorbitant rates of interest because of the rigid rules and time costs imposed on micro-credit borrowers. The authors conclude there is a tension between the spirit of micro-credit and true entrepreneurship, but ‘there are very few programmes targeted at the poor that have managed to reach so many
people’. They give the green light to expansion of the micro-credit movement, notwithstanding some of the recent controversies surrounding it.

The alternative to borrowing for investment is prior saving, but poor people find it hard to save partly because of the natural preference for present rather than future consumption (even though returns on present saving can be high e.g. investment in fertilisers), and partly because the formal banking system is not interested in encouraging small saving or dealing with small accounts. The authors argue the case for institutions in poor countries to ‘lock-in’ savings to a fixed date, and/or until a fixed amount of saving is reached. They hold out great promise for cell-phone banking. Indeed, they venture the view that ‘micro-saving is poised to become the next micro-finance revolution’.

The authors pour scorn on the idea that the poor are ‘natural entrepreneurs’ (as claimed by Muhammad Yunus, founder of the Grameen Bank). There is certainly no shortage of small businesses, but they are mostly tiny. The majority have no paid staff; they make very little money, and they don’t survive long. Also, given the opportunity to invest more, many businesses don’t take it because they don’t want to grow. For those which do want to expand, getting over the finance threshold by saving or borrowing can be hard. The reason why most poor people run a business in the first place (approximately twenty percent of the rural poor operate a non-agricultural business) is that they want a job to supplement a meagre income; it doesn’t reflect an entrepreneurial urge as such. The problem is that most poor countries don’t generate enough ‘regular’ jobs in the private sector or government (which is the job that most would prefer). To make life easier for the poor, the authors suggest subsidised migration of rural workers to the cities, but they don’t think through what the consequences might be. Given the grim conditions of urban life, it surely makes more sense to take work to the workers.

As one approaches the end of the book, full of experimental results, case studies, and anecdotes, it is still not entirely clear what works and what doesn’t work to lift people out of poverty, and what the policy implications are. And can changes be implemented within the existing institutional frameworks of countries? The last chapter gives the opposing views of William Easterly and Jeffrey Sachs on these issues. Easterly is a well-known critic of
RCTs arguing that they are infeasible for many of the big questions in development economics, such as the economy-wide effects of good institutions or good macroeconomic policies. Rodrik (2012) argues in the same vein that micro anti-poverty programmes often treat the symptoms of poverty rather than their causes, and that poverty is best addressed not by helping the poor to be better at what they are already doing but by getting them to do something different. This may require policy intervention by governments at the macro, rather than micro, level to encourage, for example, the diversification of production. Micro-development economists, he says, ‘need to recognise that while randomised evaluations are tremendously useful, the utility of their results is often restricted by the narrow scope of their application’.

Easterly and Rodrik both agree that without proper institutions and absence of corruption, pro-poor policies won’t work. Sachs takes the opposite view that poverty itself is a major cause of corruption so that tackling poverty directly from the ‘bottom up’ will empower civil society and governments to maintain the rule of law. Banerjee and Duflo’s view is that institutionalists are over-pessimistic: that it is possible to reduce corruption and improve accountability within existing frameworks e.g. by replacing paper voting with electronic voting and by inviting people to village meetings by letter which is shown to increase attendance and participation. Good policies are sometimes instituted in bad environments (e.g. education and child nutrition in Suharto’s Indonesia), and bad policies can be pursued in good environments because governments don’t understand the nature of the problem and what works and what doesn’t. In other words, there is no guarantee that good institutions will necessarily work well in practice: it depends how they operate on the ground. In the end, the authors agree with both Easterly and Sachs: ‘careful understanding of the motivations and constraints of everyone (poor people; civil servants; tax payers; elected politicians, and so on) can lead to policies and institutions that are better designed, and less likely to be perverted by corruption or dereliction of duty. These changes will be incremental, but they will sustain and build on themselves. They can be the start of a quiet revolution’.
What is still missing from the book, however, is a summary at the end, for each of the topics discussed, of the way forward. Which anti-poverty policies are most effective and which policies should be discarded? Some costing of alternative policies would also be useful. Despite the reservations raised, Poor Economics is undoubtedly one of the most interesting and thought-provoking books to have been written in the field of development economics for a long time.

References


