THE WORLD BANK

INEQUALITY in FOCUS

The Challenge of High Inequality in China

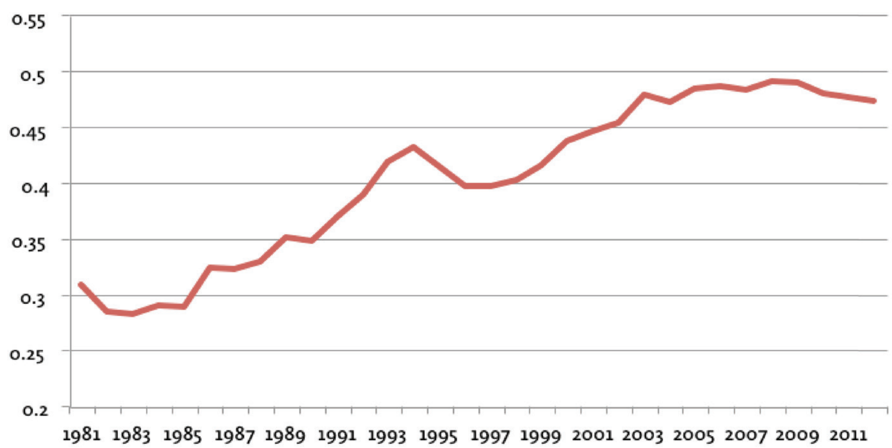
Terry Sicular

In March 2013, before leaving office, China's then-premier Wen Jiabao delivered his final assessment of the state of Chinese society to the National People's Congress. In it, he gave his administration mixed marks on their pledge to reduce income inequality. Wen warned that Chinese development was "unbalanced" and that China "still face(s) many difficulties and problems in (its) economic and social development" (New York Times 2013).

China recently completed a decade under the leadership of former president Hu Jintao and Wen, the former premier. During the period from 2003 to 2013, China pursued a "harmonious society" policy agenda that emphasized equitable growth. China implemented a wide range of policy measures designed to reduce disparities and to protect the economically vulnerable. These measures included agricultural support policies, social welfare transfers, targeted tax reductions, minimum wage increases, and increased spending on poverty alleviation.

Despite these policies, income inequality in China has in recent years remained stubbornly high. As shown in Figure 1, China's Gini coefficient (a measure of inequality ranging from zero, which represents perfect equality, to one, perfect inequality) rose from about 0.3 in the early 1980s to more than 0.45 in the early 2000s. After 2000, the Gini rose further to a high of 0.49 in 2008. Since then it has declined slightly, but remains well above 0.45.[1]

Figure 1 Income Inequality in China, 1981–2012



Sources: Gini coefficients for the years 1986–2001 are from Ravallion and Chen (2007), 2002 from Gustafsson et al. (2008), 2003–2012 from the National Bureau of Statistics.

With a Gini approaching 0.5, China's level of income inequality is in the same ballpark as that of relatively high-inequality Latin American countries such as Mexico (0.51), Nicaragua (0.52), and Peru (0.48), although still lower than Brazil and Honduras (0.56–0.57).[2] China is now among the least equal 25 percent of countries worldwide.[3] Very few Asian countries belong to this group.

What, then, explains inequality in China? Recent research by participants in the China Household Income Project (CHIP) provides some answers. The CHIP is an international collaborative survey research project that began in the late 1980s with the aim of tracking changes in incomes, poverty, and inequality in China. The CHIP organized a series of nationwide household surveys that collect detailed information on incomes and related variables. Although the most recent survey was for 2007, it provides the most up-to-date, nationwide micro-level data. In a new book by Li, Sato,

The author is professor of economics, University of Western Ontario. This article draws on findings from the China Household Income Project (CHIP), an international collaborative survey research project. Fuller analysis of income inequality and poverty based on the CHIP survey data can be found in *Rising Inequality in China: Challenges to a Harmonious Society*, edited by Shi Li, Hiroshi Sato, and Terry Sicular.

and Sicular (2013), these data have been used for an in-depth analysis of the pattern and structure of income inequality. In this article, which draws on findings from this book, I focus on three key sources of inequality in China:

1. Inequality in China is not the result of stagnant or declining incomes among poorer groups, but of more rapid growth in incomes of richer groups.
2. Inequality in China is strongly linked to urban-rural differences.
3. Income from private property is a newly emerging and potentially long-term source of inequality.

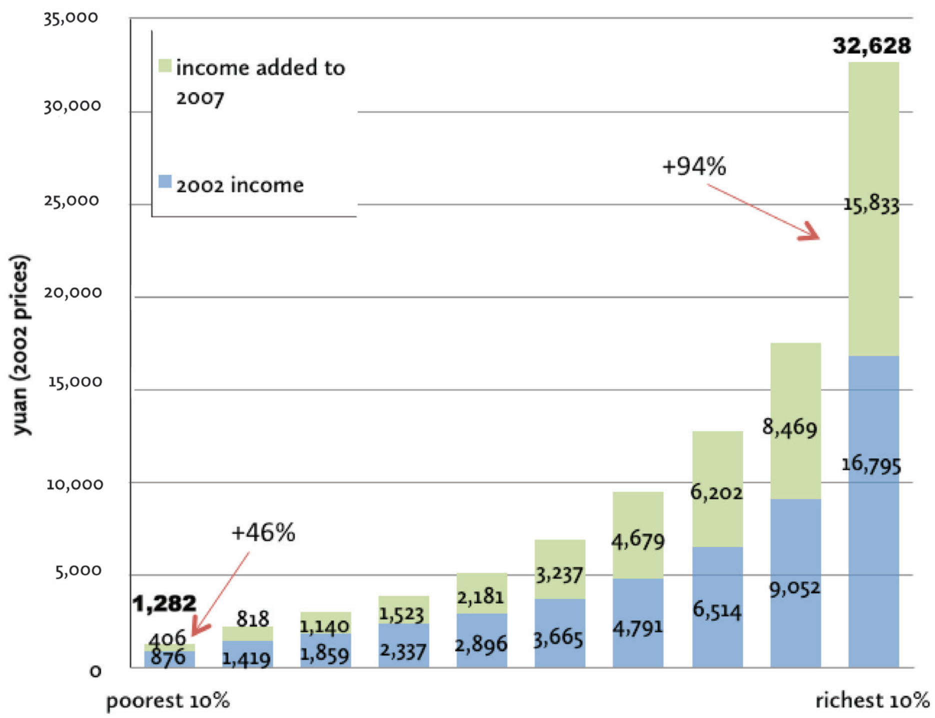
Incomes of the Rich Are Rising Faster than Incomes of the Poor

China's persistently high inequality does not reflect a deterioration of living standards for poorer groups. Between 2002 and 2007, years for which we have CHIP data, growth of per capita household income of poorer deciles in the income distribution was substantial (figure 2).[4] During this five-year period, income increased by nearly 50 percent for the poorest decile, and by nearly 60 percent for the second-poorest decile. Rising incomes for these low-income groups contributed to a marked drop in poverty. Using a PPP (purchasing power parity) $1.25-per-day poverty line, Li and colleagues (2013) estimate that China's poverty rate fell from 19 percent in 2002 to 8 percent in 2007.

Despite the strong income growth for poorer groups, income inequality still increased because the incomes of richer groups grew even faster. Between 2002 and 2007, the richest two deciles of the income distribution saw their income nearly double (figure 2). As a consequence, the income gap between the richest and poorest deciles widened from 19:1 to 25:1, and national inequality increased.

High and rising inequality in China has occurred at a time when inequality in some other parts of the world, notably Latin America, has been declining. The Brazilian experience provides an interesting contrast with China. According to Lustig et al. (2012), between 1998 and 2009, Brazil's Gini coefficient declined by 5 percent. This decline reflected robust growth in the incomes of the poor combined with slow growth in incomes for the rich. From 2001 to 2009, per capita income of Brazilian households in the bottom two deciles increased by 5 to 6 percent per year, while that of households in the top two deciles increased by 1 percent per year (figure 3). In comparison, between 2000 and 2010, China's Gini coefficient increased by nearly 10 percent. This increase was associated with robust income growth for the rich combined with slower, although by no means slow, growth in incomes for the poor. From 2002 to 2007, the per capita income of households in the top two deciles grew by a remarkable 14 percent per year. The bottom two deciles grew by a respectable 8 to 10 percent per year (figure 3). Thus, both China's poorest and richest households experienced faster income growth than their counterparts in Brazil. One could argue, then, that even though the pattern of income growth in China increased inequality, it was preferable to that in Brazil.

Figure 2 Per capita Household Income by Decile, 2002 and 2007

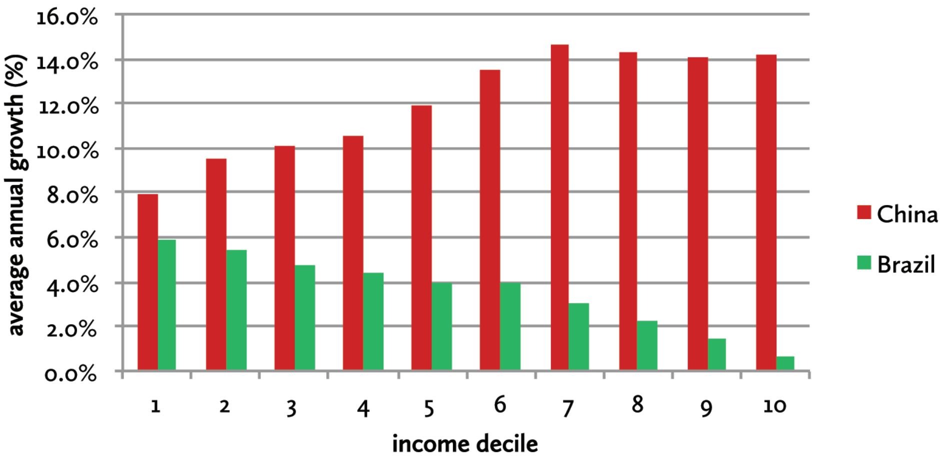


Source: Calculations based on the CHIP data.

The Income Gap between Urban and Rural Households Is Large

China's urban-rural income gap has widened since the early 1980s (figure 4). By 2002, per capita incomes for urban households were, on average, more than three times higher than those for rural households. Since that time, the urban-rural income ratio (measured as the average income per capita of urban households divided by the average income per capita of rural households) has remained well above 3.0. This urban-rural income differential is very high by international standards (Knight and

Figure 3 Growth Incidence Curves for Household per capita Income, China and Brazil



Note: From 2002 to 2007 for China and from 2001 to 2009 for Brazil; in constant prices.
Source: Figure 2; Lustig et al. (2012).

Song 1999, p. 138; see also World Bank 2009b).

China's urban-rural income gap has been a central factor underlying national income inequality in recent years. The gap's contribution to overall inequality was 45 percent in 2002, and 51 percent in 2007 (Li et al. 2013).

Urban-rural differences arise in part from China's household registration or hukou system, established during the Maoist era. The hukou system is an internal passport system that was initially adopted in the late 1950s to control domestic population movements, especially from rural to urban areas. For many years, individuals who wished to move their place of residence were required to apply to the relevant bureaucracies for permission, and approvals were tightly controlled. Since the mid-1990s, the hukou system has undergone a series of reforms that have led to a reduction in constraints on geographic mobility and the rapid increase of rural-urban migration. In fact, earnings from migrant work have become an important source of income in rural areas, contributing to rural income growth and moderating the urban-rural income gap. Nevertheless, barriers to permanent relocation—such as employment discrimination, high housing costs, and low access to public services like education and health care—continue to affect rural migrants. Consequently, most rural-urban migration has been temporary or short-term.

In recent years, the income gap has not been the result of stagnant rural incomes, but rather of faster—indeed very rapid—growth in urban incomes. Between 2002 and 2007, rural incomes grew at an average annual rate of more than 7 percent, but urban incomes grew even more rapidly at 11 percent (in constant prices).

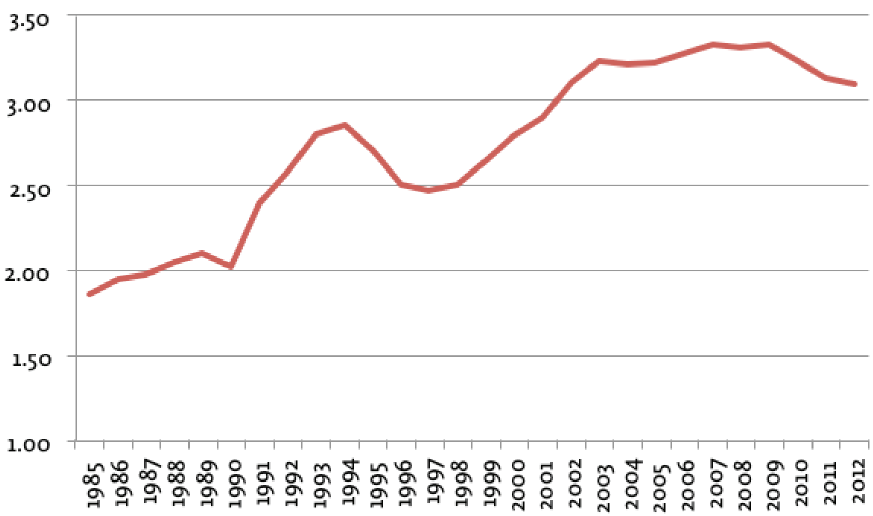
Part of the gap is explained by differences in rural-urban wages and labor earnings. Important in this regard are differences in levels of human capital (Gustafsson et al. 2008; Knight et al. 2013; Sicular et al. 2007). Differences in educational opportunities and outcomes between urban and rural areas persist. Labor earnings, however, are only part of the story. The urban-rural income gap also reflects differences in non-wage income. Urban non-employment incomes—including pensions, government transfers, and returns on private assets such as interest income and imputed rents on owner-occupied housing—have increased rapidly in recent years. By 2007, on average, non-employment income accounted for about 40 percent of urban income as compared to only 15 percent of rural income. Many of these unearned components of income are associated with government policies that have disproportionately benefited the registered urban population, such as the privatization of urban housing, the pension program, and a range of other subsidies and social welfare programs (World Bank 2009a).

China's urban-rural income gap has a distinct regional dimension, though we are unsure as to why. The urban-rural income ratio is largest in western and eastern China (in 2007, 3.85 and 3.44, respectively). Between 2002 and 2007, excluding large municipalities such as Beijing and Shanghai, this ratio rose by a remarkable 43 percent in the east, as compared to 27 percent in the central part of the country, and only 3 percent in the west (Li et al. 2013). The reason for these regional differences merits further investigation.

The Creation of Private Property Is a New Source of Inequality

During the Maoist era, private property was prohibited. In the 1980s, tentative steps were taken to allow private ownership of some forms of property such as livestock, vehicles, and equipment used for family businesses. In the 1990s, new policies opened the way for private ownership of a wider range of assets and on a larger scale. This included the private ownership of urban housing, which began in the 1990s and was basically completed by 2005. Other complementary policy measures promoted the development of urban real estate markets for both residential and commercial property. It was during this time that the government began to foster the development of domestic financial markets and stock markets, and allowed the emergence of private businesses. These changes created new mechanisms for household saving and wealth accumulation, and Chinese

Figure 4 China's Urban-Rural Income Ratio, 1985–2012



Source: National Bureau of Statistics, 2012.

households were rapidly transformed into property owners. In the mid-1990s, few Chinese households owned their homes; only 10 years later, more than 90 percent of Chinese households were homeowners (Sato et al. 2013).

Private property generates income for households through interest earnings, dividends, rents, and capital gains. Because of data limitations and the underreporting of these forms of income in the survey data, some uncertainty exists about their size and distribution. Available estimates, however, show substantial increases in the importance of asset income. For example, Sato et al. (2013) report that the share of asset income in household income nearly doubled in the five years from 2002 to 2007, from about 8 percent to 15 percent.

As in most countries, asset income in China is distributed more unequally than wage earnings and other components of income. Therefore, the growth in asset income for those who own property has contributed to increased levels of inequality. Based on calculations using CHIP data, we found that in 2002 asset income contributed to 8–10 percent of national income inequality; by 2007, it contributed to 13–19 percent.

Concluding Thoughts

China's shift from a low-inequality to a high-inequality economy occurred during a period of rapid macroeconomic growth. This growth contributed to improved incomes for all socioeconomic groups and provided resources for redistributive and social programs.

In the wake of the world financial crisis, however, China has entered a period of slower growth, which creates new challenges for promoting equity. China can no longer rely solely on macroeconomic growth to raise the incomes of poorer socioeconomic groups. The use of public funds for redistributive policies may now involve more difficult political choices.

China currently has a fairly extensive set of social and poverty-alleviation programs in place, many of which were implemented as part of the "harmonious society" agenda. Yet, analysis by the World Bank and others has identified room for improvement in the implementation, targeting, and design of these programs (World Bank 2009a, Li et al. 2013). Such improvements could provide ways for China to maintain and improve distributional outcomes even as macroeconomic growth slows.

Redistributive policies, however, can only do so much in reducing inequality if there are still forces that exacerbate or create new sources of inequality. China's urban-rural income differential and the inequality associated with asset income are two such forces. China's urban-rural income differential reflects the long-term consequences of past and current institutions and policies that have created unequal access between urban and rural residents to education, employment, assets, and social welfare benefits. China recently announced a new policy of accelerated urbanization, with the aim of increasing the share of the population that lives in cities. This new urbanization policy, however, does not appear to address the factors that underlie urban-rural income differentials. It is possible that the new urbanization program will replace the rural-urban gap with an urban-urban gap, wherein the urban population is divided between the privileged, already established urban population, and a new urban underclass composed mainly of migrants and former rural residents.

The evolution of asset ownership by Chinese households is still in its early stages. Yet, we can safely predict that, over time, household wealth in China will increase—and it will do so unequally. A lack of equity in the process of wealth accumulation makes this facet of inequality politically complex and controversial. Timely policy reforms to regularize financial and real estate markets, strengthen property rights especially for rural and poorer households, institute taxation of property and wealth, and limit opportunities for irregular and illegal gains, could help offset the impacts that the expansion of private wealth will have on inequality.

China's new leaders, President Xi Jinping and Premier Li Keqiang, thus inherit from their predecessors continually evolving challenges in reducing inequality. In the context of a changing economy and emerging sources of inequality, meeting those challenges will require new and creative policy approaches.

Notes

1. The Gini coefficients in Figure 1 are calculated using income data from China's National Bureau of Statistics.

2. The Gini coefficients for the other countries reported here are for 2005, are measured over household income per capita, and are

from the UNU-WIDER WIID2c database, http://www.wider.unu.edu/research/Database/en_GB/wiid/ (accessed August 12, 2011). Note that the Gini coefficients for Brazil and Honduras are the highest among all the countries listed in 2005-2006.

3. Based on national Gini estimates reported by the World Bank, http://data.worldbank.org/indicator/SI.POV.GINI/ (accessed June 20, 2013).

4. Estimates of income and inequality based on the CHIP survey data use a fuller definition of income than those based on NBS income data. The CHIP income figures include imputed rents on owner-occupied housing and implicit subsidies on subsidized urban rental housing.

References

Gustafsson, Björn, Li Shi, and Terry Sicular, eds. 2008. *Income Inequality and Public Policy in China*. New York: Cambridge University Press

Knight, John, and Lina Song. 1999. *The Rural-Urban Divide: Economic Disparities and Interactions in China*. Oxford: Oxford University Press.

Knight, John, Terry Sicular, and Ximing Yue. 2013. "Educational Inequality in China: The Intergenerational Dimension." Chapter 4 in Li Shi, Hiroshi Sato, and Terry Sicular, eds. *Rising Inequality in China: Challenge to a Harmonious Society*. New York: Cambridge University Press.

Li, Shi, Chuliang Luo, and Terry Sicular. 2013. "Overview: Income Inequality and Poverty in China, 2002-2007." Chapter 2 in Li Shi, Hiroshi Sato, and Terry Sicular, eds. *Rising Inequality in China: Challenge to a Harmonious Society*. New York: Cambridge University Press.

Li, Shi, Hiroshi Sato, and Terry Sicular. 2013. "Introduction: Rising Inequality in China." Chapter 1 in Shi Li, Hiroshi Sato, and Terry Sicular, eds. *Rising Inequality in China: Challenges to a Harmonious Society*. New York: Cambridge University Press.

Li, Shi, Hiroshi Sato and Terry Sicular, eds. 2013. *Rising Inequality in China: Challenges to a Harmonious Society*. New York: Cambridge University Press.

Lustig, Nora, Luis F. Lopez-Calva and Eduardo Ortiz-Juarez. 2012. "Declining Inequality in Latin America in the 2000s: The Cases of Argentina, Brazil, and Mexico," *World Development*, 44, 129–141.

National Bureau of Statistics. Various years. *China Statistical Yearbook*. Beijing: China Statistical Press.

New York Times. 2013. "China's Wen Warns of Inequality and Vows to Continue Military Buildup." Andrew Jacobs and Chris Buckley. March 4.

Ravallion, Martin, and Shaohua Chen. 2007. "China's (Uneven) Progress against Poverty." *Journal of Development Economics*, 82(1), 1–42.

Sato, Hiroshi, Terry Sicular and Ximing Yue. 2013. "Housing Ownership, Incomes, and Inequality in China, 2002–2007," Chapter 3 in Li Shi, Hiroshi Sato and Terry Sicular, eds. *Rising Inequality in China: Challenge to a Harmonious Society*. New York: Cambridge University Press.

Sicular, Terry, Ximing Yue, Björn Gustafsson, and Shi Li. 2007. "The Urban-Rural Income Gap and Inequality In China," *Review of Income and Wealth*, 53(1), 93–126.

The World Bank. 2009a. *From Poor Areas to Poor People: China's Evolving Poverty Reduction Agenda, an Assessment of Poverty and Inequality in China*. Washington, DC: World Bank.

The World Bank. 2009b. *The World Development Report 2009: Reshaping Economic Geography*. Washington, DC: World Bank.

Inequality and Unrest in Brazil: A Conversation with Ricardo Paes de Barros

Recently, the Inequality in Focus editorial staff interviewed Ricardo Paes de Barros, the secretary of strategic actions in Brazil's Ministry of Strategic Affairs. He is an expert on poverty and inequality issues and has been intimately involved in some of Brazil's signature social policy initiatives, including Bolsa Familia, the national conditional cash transfer program. Foreign Policy magazine recently identified Paes de Barros as one of "the 500 most powerful individuals on the planet." The two-hour interview touched on many issues, but within the context of the widespread popular protests that began in Brazil in June 2013. The initial demands of the protests were for lower-cost public transportation, but eventually evolved into a wide variety of demands on the state. The interview discusses some of the reasons behind these protests, as well as Brazil's current state of development, equality, and social policy. This is a summary of the conversation.

Inequality in Focus: In your opinion, what has been the main cause of the recent protests in Brazil?

Ricardo Paes de Barros: It is important to acknowledge that there is no clear and simple answer to that question, because nobody really knows. The causes are puzzling to many with neither the government nor the opposition ever expecting this. There were never any social or economic indicators that could have predicted this level of discontent. Actually, it is kind of amazing how a country with relatively low levels of unemployment, falling poverty rates, and reduced inequality is experiencing such unrest.

That does not mean that social and economic conditions in Brazil are perfect. Levels of poverty and inequality are still high. But, they are falling. For example, infant mortality rates are very high—still two deaths per thousand—but the rate at which this is declining in Brazil is among the top five fastest in the world.

Still, recent opinion polls show increasing levels of public dissatisfaction with the quality of government services. Interestingly, it seems that the public's opinion of government services is changing much more radically than the actual quality of services. In other words, the satisfaction with the quality of public services has declined rapidly, although the actual measurements of quality have shown improvement.

I think this is the most basic and immediate explanation for the protests. It is purely a change of perceptions—not that quality has deteriorated and people want quality levels back to what they were. It's amazing to what level people's expectations have increased; from an environment in which expectations were holding steady—people were happy—to all of a sudden having a situation where hopes have climbed and where what previously seemed good now seems bad.

IF: What caused this change in perceptions?

PB: Most importantly, because of increasing incomes and economic growth you have 40 million people who have moved out of poverty to the middle class in Brazil. When you take such a large number of poor people and place them squarely into the middle class, then suddenly what was important to them before—surviving—has changed. In a very short period of time you had 40 million more people enter the formal labor market, pay taxes—and who now reflect on how their tax money is used. Before, these people had no time to contemplate these things, they had no idea how much they were paying in taxes, they were more worried about what would happen tomorrow and whether they would have money for food or bus fare.

At the same time that you have these 40 million people moving into the middle class, you have another 30 million people who make up the richest 15 percent of the population and their incomes are not improving much. What is the flip side to reducing inequality? To reduce inequality, you must have an unequal growth rate. If every income group grows equally, you do not reduce inequality. To reduce inequality, poor incomes must grow faster than rich incomes. In Brazil over the last 10 years, the richest 15 percent had a positive growth rate, but well below the national average. This means that for one of the first times in history, the richest 15 percent of Brazilians have seen themselves falling closer and closer to the middle class. As a consequence, they are also less satisfied and increasingly question how their tax money is spent.

Although the spending decisions by the government have not changed much over the past 10 or 20 years, 70 million people have started to reach the conclusion that the allocation of public spending is not exactly what they want. If you look carefully, you can see that there is a general demand to allocate resources differently.

The other contributing factor is that the World Cup has drawn attention to the allocation of public spending. And what people are questioning is why we are spending so much on preparing for the World Cup when resources are so scarce for education, health, public safety, and transportation. Why are we investing more in building roads to the stadium than building roads to work? Although much of this World Cup investment is actually private, it's possible that the recent Confederations Cup football tournament lit the flame in people's heads; not so much about whether the quality of services is good or bad, but whether the allocation of public funds is right or wrong.

But this is all speculation, and all we really know is that we are seeing a movement. Maybe it is a movement that is seeking a slightly modified development path, or maybe it is seeking major change. Maybe all of this has something to do with greater representation and changes in public spending. But it is not yet clear what these messages are. And that is the difficulty in reading too much into the messages.

IF: So should the government respond by shifting its focus more to the provision of "pure" public goods (e.g., justice, law enforcement, logistics, etc.) and away from the provision of private goods (e.g., health, education, transfers)?

PB: Focusing on the provision of "pure" public goods and services is fine for a country with no inequality. In theory, if everyone had equal opportunities, the state could stand in the corner, not worry about redistribution, and focus on the provision of pure public goods and services. This would benefit the entire public equally. However, in a country that has high levels of inequality, like Brazil, the priority must first be to reduce inequality.

What does it mean to reduce inequality? It means that you must improve the situation of the poorest at a faster rate than you do for the richest. To do this, you must target social policy toward the poorest, and not toward everyone equally. In the end, this means that social policy is not designed to deliver pure public goods, but rather to provide publicly funded private goods—like education, health, transfers, etc. —for the most impoverished people. This is what Brazil has done and we have done it quite successfully. We have invested relatively more in publicly funded private goods for the poor than in pure public goods, which would stand to benefit the non-poor the most. Therefore, it is not a huge surprise that the population of a country with an expanding middle class would begin to demand improved transportation services and greater security; that is, more typical "pure" public goods.

I think Brazil had made a decision, which was "we will take seriously the issues of inequality and poverty, and therefore, we will focus our attention on the poor." Much of Brazil's success in reducing inequality was based on the decision to prioritize the needs of the poor above all else. Today's slogan in Brazil is, "A wealthy country is one without poverty."

When you really look at it, it is counterintuitive that such a policy would be politically feasible in a country with only a 10 percent illiteracy rate and only 20 percent of its population squarely living in poverty. However, despite their own self-interests, large portions of Brazilians from all socioeconomic classes believe in this slogan.

IF: But as you mentioned, there is an emerging middle class in Brazil and their values and expectations of the government are changing. What do you believe these new values to be?

PB: If you look at the evidence, the values of the middle class tend to be a mix between the values of the richer classes and the poorer classes. It is a middle group that thinks in the middle. Who hates to pay taxes the most? The rich hate them the most, the poor the least, and the middle class somewhere in the middle. Who thinks the quality of public services is bad? The poor think it's bad, the rich think it's lousy, and the middle class is in between. So far we have not seen any evidence that the middle class is actually revolutionizing, modernizing, or rethinking the values of Brazilian society.

But of course, with the rise of the middle class, the needs and aspirations of the average Brazilian are changing, and this represents a tremendous challenge for public policy. How can you adapt policies to these changes? I think an improved policy is one that is no longer solely focused on the poor but also takes into account the needs of the emerging middle class. The government is very aware of this. So, now Brazil's slogan is changing to, "The end of poverty was just the beginning."

What this means for public policy in Brazil generally is, "How do you handle success?" A successful public policy also means the death of that policy. For example, if you find an excellent remedy for a certain disease and, as a result, cure the disease, you no longer have a need for that remedy. It is the same thing here, Brazil has been successful in reducing poverty, but because of this success the old social policy is less relevant. The question then becomes, "how do you ensure that public policy continues to remedy the problems." Well, you must continue to adapt public policy as success is attained. If you have a new middle class, you have to adjust the policy to address their needs. A continuously new perspective needs to be incorporated into policy making in all facets—from the justice system, to public safety, to public transportation.

Of course, in practice the solutions are not that simple. Redesigning social policy requires other factors as well. How do you adjust the targeting of these policies while maximizing the ability to recover costs? How can you alter public-private partnerships in order to pay for or deliver these new services? Ideally, you want the new social policy to be highly efficient. This means that the communities and the private sector manage these services and the government stays in a position to regulate and fund them.

IF: What would need to happen to be able to more effectively adjust Brazilian social policy?

PB: A constant evaluation of the social and economic situation in Brazil is required, as well as the ability to enact change. For example, I recently visited the mayor of Petrolina, Pernambuco, in northeastern Brazil. He asked me, "Remember how we increased access by families to child care last year? It had such a positive impact: people were happy, and businesses were happy because people didn't have to worry about their children and could show up on time for work. But now I'm doing this other thing." This guy is already on another level. There is nothing like having an active and intelligent mayor interacting with the community everyday to see what problems need to be solved and what changes to policy need to be made.

At the same time, there are things the mayor will not see simply by walking around a city. There may be some environmental problems that are not seen because nobody wants to see them. Maybe a factory is generating pollution, but the factory creates jobs and is a boon for the local economy so nobody wants to acknowledge the negatives. For this reason, using objective data and empirical evidence is also important. In the case of Petrolina, the mayor is tapping into this empirical information as well. For example, he is using census data to identify the scope of the challenges.

What I am saying is this: Empirical evidence is more than welcome and in some cases irreplaceable. But you will never design public policy 100 percent based on evidence, which is often late or incomplete. The idea is to collect as much information as possible while also keeping a keen ear to the ground.

IF: How do you then go about improving public policy evaluation in Brazil?

PB: Brazil, as a nation, is quite good at evaluating public policy. We have the institutions, the money, and the demand to evaluate the performances of both the program managers—like ministers, state secretaries, governors and mayors—and the programs themselves. What Brazil is lacking is an institution, not to evaluate—it is better that the private sector, universities, and nongovernmental organizations do this—but to coordinate all of the evaluation efforts; to determine which evaluations are sound and which are not and to make this information visible to everyone; to create a list of certified evaluators and maybe a list of institutions in search of evaluators; and many other things. So, if you need an evaluation of a certain social program, this agency could not only direct you to it, but also provide a review of the evaluation.

Practically, such an effort could be managed by Brazil's Federal Accountability Office (Tribunal de Contas da União), by the Institute of Applied Economic Research (Instituto de Pesquisa Econômica Aplicada), or by a stand-alone government agency. The point is to have a government agency that regulates, guides, and funds the evaluation process, but doesn't actually do the evaluating. If it did both there would be potential conflicts of interest.

IF: This brings up an interesting question on the role of the public and private sectors in the provision of social services. What do you believe the role of each should be?

PB: What we want is a world of high quality services. To do so you need a fully integrated service. What I mean is a service that is equally accessible to the poor, the rich, and the middle class and of high quality for all. Ideally this would be a service provided by the private sector, paid for by the public sector, and certified and regulated by the public sector. Such a system would be free to the poor—or at least they would be reimbursed for their expenses—while the rich would have to pay the state for the service they are receiving.

Such a system already exists in Brazil for child-care services in Petrolina. In this case, the state has a contract with a private company to construct the child-care center, which is paid for by a state-administered fund specifically used for basic educational services. These private providers are free to earn profits and compete for contracts. Such a system is beneficial because competition will ensure a high quality service. Furthermore, such a system can be easily expanded because the state provides educational funds based on the number of students, not as block sums. So as more students are enrolled in this system, more resources will be diverted to it.

But such a system would be highly difficult on a larger scale. Not because of its design, but because of inequality in Brazil. In order to have a system of equal quality and access for poor and rich alike, you would have to have residential desegregation—not rich communities and poor communities, but rather communities of rich and poor. Ideally, these integrated communities would be a microcosm of Brazil as a whole. In this way, a high quality service can be provided to all. What I mean is that in order to have a public service of equal quality and availability to all you must also have equality. For example, in a segregated world, rich communities would have higher quality schools than poor communities. In other words, if you wanted a world with high quality education that is accessible to all, it would be more important to change the community than it would be to change the school.

Therefore, the main role of the state in social policy is not the management of the service, but the design of it. It may be better that the government leaves the management of the teachers and physicians to the private sector and concentrates instead on what people want and making sure they hire the right agencies to deliver it. In other words, social policy design is not something that can move to the private sector. The market should be used to determine what courses can be taken and private providers can tell the government what they need, but the government would need to regulate the functioning of the market and to guide supply and demand to meet its social goals.

This interview took place on July 19, 2013, between Ricardo Paes de Barros and Pedro Olinto, Fernanda Luchine, and Maximillian Ashwill of the Inequality in Focus editorial team.The interview, in Portuguese, was recorded and transcribed by Fernanda Luchine. The above dialogue is an interpretation of the conversation written by Maximillian Ashwill and Pedro Olinto.

THE WORLD BANK

Poverty Reduction and Equity Department
Poverty Reduction and Economic Management Network (PREM)