No. 0109

Social Protection Discussion Paper Series

Risk and Vulnerability: The Forward Looking Role of Social Protection in a Globalizing World

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March 2001

Social Protection Unit

Human Development Network

The World Bank

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Risk and Vulnerability:
The forward looking role of social protection in a globalizing world

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Paper prepared for "The Asia and Pacific Forum on Poverty – Policy and Institutional Reforms for Poverty Reduction", Asian Development Bank, Manila, February, 5-9, 2001.

Abstract

The paper outlines a forward-looking role of social protection against the background of increasing concerns about risk and vulnerability, exemplified by the recent East Asian crisis, the concerns of the World Development Report (WDR) 2000, the need for a better understanding of poverty dynamics, and the opportunity and risks created by globalization. These considerations and the need for a more proactive approach to lasting poverty reduction have led to the development of a new conceptual framework which casts social protection as social risk management. The paper highlights the main elements of the new conceptual framework and its main strategic conclusions for attacking poverty before addressing crucial issues for its implementation: The need for an operational definition of vulnerability; the use of social risk assessments as an operational entry point for a new policy dialogue; economic crisis management and the lessons for social protection; and the undertaking of social expenditure reviews to enhance the effectiveness of government intervention for addressing risk and vulnerability. The pilot experience with some of these elements yields cautious optimism that a promising road for addressing poverty has been found.

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I. Introduction: Motivation, issues, structure [1]

Social protection is back on the international agenda. The restatement of the international development goals by the international community during the Social Summit 2000 (Geneva 2000 or Copenhagen plus 5) and the refocus by international and bi-lateral organizations on poverty reduction in recent years give social protection, generally defined as public measures to provide income security for individuals an important role in support of these objectives. However, compared to the traditional understanding of social protection (SP), these interventions are now scheduled for a more pro-active and forward looking role. Several developments are responsible for this change in outlook, among the most important are:

(i) The East Asian crisis has brought to the attention of policy makers that high growth rates, while necessary for lasting poverty reduction, are insufficient and that any progress made on the poverty front may be lost quickly under declining output and rising unemployment if appropriate social policy measures are not in place (World Bank, 2000g). Following a large covariate (negative) economic shock, informal safety net arrangements tend to break down, existing public support schemes, where available, are often inappropriate or insufficient, and new schemes tend to prove difficult to establish during a deep and protracted crisis. The conclusion emerges that an ex-ante approach is required which assesses the potential risks and prepares social protection measures, in particular social safety nets, before a major shock hits. This is the main conclusion of a report prepared for the APEC ministers of finance by a group of international organizations.[2]

(ii) The World Development Report (WDR) 2000 on attacking poverty offers the conclusion that sustainable poverty reduction needs a forward-looking approach in social protection (World Bank, 2000a) and signals the change in development thinking during the 1990s. The WDR 1990 proposed a two-part strategy to address poverty: promoting labor intensive growth through economic openness and investment in infrastructure and access to basic social services (World Bank, 1990). Social safety nets were essentially an addendum, understood as ex-post provision of support in response to economic crisis and structural adjustment. Ex-ante income-support measures, risk and vulnerability and the mere concept of social protection were totally ignored. In the WDR 2000, by contrast, social protection is a primary element in the new three-pronged approach, along with opportunity and empowerment. The conceptualization of social protection as "security" incorporates both individual (idiosyncratic) and macroeconomic (covariant) risks, and the proposed underlying social risk management approach has an explicit forward looking agenda, moving from an ex-post poverty toward ex-ante vulnerability considerations. The WDR 2000 suggests that to deal effectively with the diverse risks faced by the

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[1] This draft profited from useful comments and suggestions by John Blomquist, Jeanine Braithwaite, Sudharshan Canagarajah, Margaret Grosh, and Gilette Hall which had to be delivered on short notice. But all remaining errors are mine.

[2] Social Safety Nets in Response to Crisis: Lessons and Guidelines fromAsia and Latin America, Report prepared for the APEC Finance Ministers in collaboration with APEC member countries and a core team from the World Bank, the International Monetary Fund (IMF), the Asian Development Bank (ADB), and the Inter-American Development Bank (IADB), draft, January 2001.

population at large and the poor in particular are confronted with – where feasible and economically useful – in an ex-ante manner.

(iii) The forward looking approach in dealing with poverty mirrors our increasing understanding of poverty dynamics and economic mobility in developing countries. The increasing number of panel data sets signal main regularities across countries. Most importantly, that the poor consists of those who are always poor – poor at all dates – and those who move in and out of poverty, with the latter group tending to be strikingly large (and such movements in and out of poverty can be observed when looking at poverty in absolute or relative terms). The reasons why the poor remain poor, or why some move out of poverty while other move into poverty are beginning to be understood. Beside personal characteristics and endowments (or the lack thereof), there is increasing evidence that seemingly transitory shocks can have long-term consequences.[3] This finding suggests the need for an ex-ante view of poverty – vulnerability – and a thorough investigation about the best social protection/social risk management instruments for dealing with it.

(iv) Last, but not least, there is the perceived strong need to address the increased risks resulting from globalization in an equitable but efficient manner. Recent trends in the evolution of trade, technology, and political systems have made possible great potential improvements in welfare around the world. Globalization of trade in goods, services, and factors of production has the world community poised to reap the fruits of global comparative advantages. Technology is helping to speed innovation and holds the potential to remove the major constraints to development for many people. Political systems are increasingly open, setting the stage for improved governance by holding those in power accountable to larger segments of the population. Taken together, these changes create a unique opportunity for unprecedented social and economic development, poverty reduction and growth. The other side of the coin, however, reveals that the exact same processes that allow for welfare improvements also increase the variability of the outcomes for society as a whole and even more so for specific groups. There is no certainty that improvements will be widely shared among individuals, households, ethnic groups, communities, and countries. Expanded trade or better technology can sharpen the differences between the "haves" and "have-nots" just as it can increase the opportunity for all, depending on the prevailing social context and policy measures. Globalization-induced income variability combined with marginalization and social exclusion can, in fact, increase the vulnerability of major groups in the population. In other words, the risks are as large as the potential rewards. To further complicate matters, the trend towards globalization and the higher mobility of production factors reduces the ability of governments to raise revenues and pursue independent economic policies and, thus, to have national policies to help the poor when they are needed most.

These developments on the policy and research front call for a new approach to social protection: an approach which moves from ex-post poverty to ex-ante vulnerability considerations; an approach which presents SP as a safety-net as well as a springboard for

[3] For a collection of recent papers on these issues see the special 2000 issue by "The Journal of Development Studies" on "Economic Mobility and Poverty Dynamics in Developing Countries", edited by Baulch and Hoddinott.

the poor; an approach focused less on the symptoms of poverty and more on its causes; and an approach which takes account of reality -- among the world population of 6 billion, less than a quarter of individuals have access to formal SP programs, and less than 5 percent can rely on their own assets to successfully manage risk. Meanwhile, eliminating the poverty gap through public transfers is beyond the fiscal capacity of most developing client countries.

These considerations have motivated the development of a new conceptual framework for social protection – social risk management, (SRM) (Holzmann and Jorgensen, 1999 and 2000).

The basic thrust of the SRM framework is supported by two perceptions: (i) The poor are typically most exposed to diverse risks ranging from natural (such as earthquake and flooding) to manmade (such as war and inflation), from health (such as illness) to political risks (such as discrimination), and (ii) the poor have the fewest instruments to deal with these risks (such as access to government provided income support and market-based instruments like insurance). These perceptions have important consequences: (i) the poor are the most vulnerable in society as shocks are likely to have the strongest welfare consequences for them. For welfare reasons, therefore, they should have increased access to SRM instruments; and (ii) the high vulnerability makes them risk averse and thus unable or unwilling to engage in higher risk/higher return activities. Hence, access to SRM instruments would tend to make the poor more risk- taking and thus provide the opportunity to gradually move out of poverty.

The new SRM framework is the basis of the security chapters of WDR 2000, the World Bank's Social Protection Sector Strategy Paper (World Bank, 2001) and six regional Sector Strategy Papers, has inspired the approaches by other multilateral institutions (such as IADB and ADB), and finds increasing resonance with bi-lateral donor institutions (such as DFID and GTZ)[4]. While the basic thrust of SRM and the main strategic conclusions of SPSSP are getting increasing support, they present only the beginning of a journey. In order to make the new framework and its strategic conclusions effective for lasting poverty reduction, much more needs to be done at both the conceptual and operational levels. Examples include an operational definition of vulnerability, piloting of risk assessments and effective social sector expenditure reviews. To this end, the structure of the remainder of the paper is as follows:

Section 2 highlights the central elements of SRM while Section 3 outlines the main strategic conclusions for SP. Sections 4 to 7 outline the main conceptual issues and suggested next steps toward implementation, including the need for an operational definition of the vulnerability concept (Section 4), the use of risk assessments as an entry point for a new policy dialogue with governments (Section 5), the lessons from economic crisis management and what we have learned for social protection (Section 6), and social sector expenditure reviews as means to enhance the effectiveness of public interventions (Section 7). Section 8 presents concluding remarks.

[4] See, for example, ADB (2000), Conway et al. (2000), DFID-OED (2000), and Lustig (2000),.

II. Social Risk Management – A dynamic conceptual framework for social protection[5]

The main elements of the new framework are derived from introducing the notion of asymmetric information in a world of diverse risks in a more explicit way than has been done generally. Compared to an ideal world (a la Arrow-Debreu) this has several consequences for managing risks, most importantly: (i) The sources and the forms of risk matter, e.g. whether a particular risk is idiosyncratic or covariant. For the former, more reliance can be given to informal or market-based RM instruments; for the latter, more government involvement tends to be required. (ii) Since risk is not necessarily exogenous, there are many more strategies to deal with risks than simple insurance, including risk reduction, risk mitigation and risk coping strategies. (iii) As private insurance markets tend not to emerge or break down in view of asymmetric information, there are three main institutional arrangements for dealing with risk: informal, market-based and publicly- provided mechanisms. (iv) There are multiple suppliers of RM instruments (including individuals, households, communities, NGOs, market institutions, government, international organizations and the world community at large) and distinct demanders (such as the formal urban, the informal urban, the formal rural and the informal rural worker). And (v) we must bear in mind the interrelationship between social risk management, social protection, social inclusion, and redistribution.

Social risk management beyond social protection. There are many areas of public policy that impact vulnerability and income variability that are clearly outside social protection, such as macroeconomic stability, preventive measures against natural disasters, and infrastructure investment (for example, roads and water supply). Against the background of the social risk management objectives, this suggests an advocacy and analytical role for social protection (see Section 3).

Social protection and income redistribution. Income redistribution features importantly in social risk management and social protection activities, but it is not necessarily the primary goal. In the social risk management framework income distribution enters as an equity objective linked to adverse risk and emerges as an important outcome of good social protection programs at different levels. The support of the *critically poor* is a main objective of social protection. Since financing cash or in kind transfers requires taxes on workers or non-working wealthy, income redistribution appears as a result. Also, enhancing *risk management* capacity has high *redistributive effects* on individuals' welfare, yet it does not require inter-personal income redistribution to achieve a more equal welfare distribution (Holzmann, 1990). On the other hand, not all redistribution is social protection – for example, redistributive efforts accomplished through a *tax-transfer mechanism* or through the distributive effects of public goods provision lie outside social protection.

Social protection beyond social risk management and redistribution: social inclusion. Even in a minimalist sense, social inclusion, cohesion, solidarity, and stability are the result of well-designed and well-implemented social risk management interventions. For

[5] This and the next section draw on SPSSP (World Bank) and can present only the bare bones of framework and strategic conclusions. For a more comprehensive and analytic presentation of the SRM framework, see Holzmann and Jorgensen (2000).

example, a well-designed income support system for the unemployed not only enhances individual welfare by reducing vulnerability but also achieves social stability as a result. And social assistance and measures that increase access to basic health and education for the poor give parents and their children a better chance of becoming integrated members of society. Another answer is that social protection should go well beyond mere financial and income-oriented considerations and adopt pro-active policies designed to influence the social structure of an economy. This approach would include investments in the sociocultural infrastructure by supporting informal arrangements and upgrading the non-profit sector, and it would also strengthen the "social rights approach" of social policy. Finally, it would adopt an extended view of instruments and institutions to be used under social risk management, including the broad concept of "social capital" (Badelt, 1999).

Sources of Risks and their Characteristics

The capacity of individuals, households and communities to handle risk and the appropriate risk management instrument to be applied depend on the characteristics of risks: their sources, correlation, frequency and intensity. The sources of risk may be natural (for example, floods) or the result of human activity (for example, inflation resulting from economic policy); risks can be uncorrelated (idiosyncratic) or correlated among individuals (covariant), over time (repeated) or with other risks (bunched); and they can have low frequency but severe welfare effects (catastrophic) or high frequency but low welfare effects (non-catastrophic). The main sources of risk and the degree of covariance can range from purely idiosyncratic (micro or individually specific), to regionally covariant (meso), to nationwide covariant (macro) events.

While informal or market-based risk management instruments can often handle idiosyncratic risks, they tend to break down when facing highly covariant, macro-type risks. To take Africa as an example, the main sources of covariant risks that affect poor people are AIDS, wars and conflict, seasonal volatility in prices, drought, and macroeconomic shocks. Idiosyncratic risks include illness and widowhood or the break-up of the family. Since many of the risks faced by poor people are covariant in nature, informal management mechanisms at the family or community level are typically not very effective. Among these risks, at least two are induced by human activity (war and macroeconomic shocks), which need no *ex-post* coping mechanism if they can be prevented from happening in the first place. Access to market-based interventions, such as saving mechanisms or insurance programs, can mitigate some of the risks (seasonal price volatility or illness). This suggests that different strategies and interventions are appropriate depending on the nature of the risks involved.

Social Risk Management Arrangements

Over time different kinds of social risk management arrangements have evolved. These fall into three main categories: (i) informal arrangements, (ii) market-based arrangements, and (iii) public arrangements on a large scale. Each of them has relative strengths and limitations.

Informal Arrangements. These arrangements have existed since the dawn of mankind and still constitute the main source of risk management for the majority of the world's

population. In the absence of market institutions and public provision of support, the way that individual households respond to risk is to protect themselves through informal (family or community) or personal arrangements (self-protection and self-insurance). Although they sidestep most of the information and coordination problems that cause market failure, they may not be very effective in helping the household weather adverse events. Examples of this kind of arrangement include: the buying and selling of real assets (such as cattle, real estate, and gold), informal borrowing and lending, crop and field diversification, the use of safer production technologies (such as growing less risky crops), storing goods for future consumption, mutual community support arrangements, and kinship arrangements through marriage.

Market-Based Arrangements. Individual households will also take advantage of market-based institutions such as money, banks, and insurance companies when they are available. However, in view of these instruments' limitations due to market failure, their usage will be initially restricted but will rise with financial market development. Empirical evidence suggests that the establishment of a sound banking system and non-inflationary policy serves to reduce risk. Because formal market institutions are reluctant to lend to households without secured earnings, microfinance is also an important instrument of social risk management.

Public Arrangements. Public arrangements for dealing with risk came into being with the development of the modern welfare state but are relatively scarce and have very limited coverage in the developing world for fiscal and other reasons. When informal or market-based risk management arrangements do not exist, break down, or are dysfunctional, the government can provide or mandate (social) insurance programs for risks such as unemployment, old-age, work injury, disability, widowhood, and sickness. The mandatory participation in a risk pool can circumvent issues of adverse selection, in which individuals with low risk profiles avoid participation in insurance pools due to premiums while individuals with high risk profiles join in order to gain access to payouts. Since these programs typically apply to those in formal employment, their coverage in developing countries is generally low. On the other hand, governments have a whole array of instruments to help households to cope after a shock hits, such as social assistance, subsidies on basic goods and services, and public works programs. Which of these measures a government chooses to implement depends on its distributive concerns, its fiscal resources, its administrative capacities, and the type of risk involved.

Social Risk Management Strategies

Risk management can take place at different moments – both before and after the risk occurs. The goal of *ex-ante* measures is to prevent the risk from occurring, or, if this cannot be done, to mitigate the effects of the risk. Individual efforts, such as migration, can prevent risks, but, in many cases, this requires support from government (for example, disaster prevention). Mitigating the effects of risk through risk pooling by definition requires people to interact with other individuals, and poor people are typically less able to participate in formal and also informal arrangements. This leaves most poor households with the residual option of coping with the risk once it has occurred. They are normally poorly prepared to do this and, therefore, often experience irreversible negative effects.

Prevention Strategies. These are strategies that are implemented before a risk event occurs. Reducing the probability of an adverse risk increases people's expected income and reduces income variance, and both of these effects increase welfare. There are many possible strategies for preventing or reducing the occurrence of risks, many of which fall outside of social protection, such as sound macroeconomic policies, disaster prevention strategies, public health investments, environmental policies, and investments in education. Preventive social protection interventions typically form part of measures designed to reduce risks in the labor market, notably the risk of unemployment, under-employment, or low wages due to inappropriate skills or malfunctioning labor markets.

Mitigation Strategies. As with prevention strategies, mitigation strategies aim to address the risk before it occurs. Whereas preventive strategies reduce the probability of the risk occurring, mitigation strategies help individuals to reduce the impact of a future risk event through pooling over assets, individuals and over time. For example, a household might invest in a variety of different assets that yield returns at different times (for example, two kinds of crops that can be harvested in different seasons), which would reduce the variability of the household's income flow. Another mitigation strategy is for households that face largely uncorrelated risks to "pool" them through informal and informal insurance mechanisms. While formal insurance profits from a large pool of participants, which results in less correlated risks, informal insurance has the advantage that all the participants have access to more or less the same amount of information.

Coping Strategies. These are strategies designed to relieve the impact of the risk once it has occurred. The main forms of coping consist of individual dis-saving, borrowing, or relying on public or private transfers. The government has an important role to play in helping people to cope, for example, when individuals or households have not saved enough to handle repeated or catastrophic risks. These people may have been poor during their entire lifetime and, thus, had no possibility of accumulating assets. The smallest income loss would make these people destitute and virtually unable to recover.

The Social Risk Management Matrix

The social risk management matrix in Table 2.1 combines arrangements and strategies in various ways that can be refined and adjusted depending on country circumstances and the issue being investigated. The matrix's three by three structure highlights the multidimensional character of risk management and the need to select appropriate strategies based on opportunity costs and comparative advantage. Filling in each cell of the matrix with existing instruments provides a means of examining the status of social risk management in a given country or certain group within a country, and comparing countries makes it possible to assess differences among them and to determine appropriate and useful changes.

While each cell of the matrix can be filled in most countries, and even more so in the regions, since all risk management instruments are likely to be used at any moment in time, the intensity and the scope of application is likely to differ and change over time. The poorest countries will be characterized by a predominance of informal arrangements and public arrangements concentrated on coping strategies. In contrast, richer countries will apply the whole set of public arrangements and strategies, and market based

instruments and strategies geared toward risk mitigation and reduction will grow in importance.

Table 2.1: Strategies and Arrangements of Social Risk Management – Examples

Arrangements/ Strategies	Informal	Market-based	Public
Risk Reduction			
	• Less risky production • Migration • Proper feeding and weaning practices • Engaging in hygiene and other disease preventing activities	• In-service training • Financial market literacy • Company-based and market-driven labor standards	• Labor standards • Pre-service training • Labor market policies • Child labor reduction interventions • Disability policies • Good macroeconomic policies • AIDS and other disease prevention
Risk Mitigation			
Portfolio	• Multiple jobs • Investment in human, physical and real assets • Investment in social capital (rituals, reciprocal gift-giving)	• Investment in multiple financial assets • Microfinance	• Multi-pillar pension systems • Asset transfers • Protection of poverty rights (especially for women) • Support for extending financial markets to the poor
Insurance	• Marriage/family • Community arrangements • Share tenancy • Tied Labor	• Old-age annuities • Disability, accident and other personal insurance • Crop, fire and other damage insurance	• Mandated/provided insurance for unemployment, old age, disability, survivorship, sickness, etc.
Risk Coping			
	• Selling of real assets • Borrowing from	• Selling of financial assets	• Transfers/Social assistance

III. SP as SRM: Main strategic conclusions

Viewing SP within the SRM framework has many strategic implications for addressing poverty in developing but also developed countries. Some seem obvious, other perhaps counter-intuitive, and many will need empirical testing through pilots in real country environments to prove their usefulness. This section will highlight some of the main strategic conclusions from the World Bank's SPSSP, subject to further discussion, extension and improvement.

Social Protection as a Theme

Against the background of the SRM framework social protection emerges as a theme (such as gender) of socio-economic development and poverty reduction. The reason being that the social risk management framework applies to many areas outside the social

protection sector. These include national shocks (resulting from macroeconomic policy, disasters or civil strife), the financial sector and microfinance, rural development, the informal sector, infrastructure investments, health, population and nutrition. If appropriate policies are in place in these areas, then households are much less vulnerable and can smooth much of their consumption with personal instruments. This means that there is a need to build greater awareness of the importance of risk reduction for development. Furthermore, social risk management can be used as an analytical tool to assess interventions in the various sectors. Two examples illustrate the advocacy and analytical role that social risk management can and should play in selected areas outside the traditional remit of social protection:

Economic crises, natural disasters, and civil conflicts are the three most important causes of aggregate shocks and sharp increases in the incidence of poverty (WDR 2000/01, Chapter 9). Between 1990 and 1997, more than 80 percent of all developing countries experienced at least one year of negative per capita output growth as a result of these phenomena. Macroeconomic crises cause poverty to increase, which affects not only current living standards but also the ability of the new poor to rise out of poverty, as has recently been evident in Latin America, Asia, and Russia. Natural disasters repeatedly interrupt advances in economic development, cause sharp increases in poverty in the affected areas, and slow down the pace of human development. Civil conflict has a similar effect on development and poverty in general, but it represents both a source and consequence of low economic performance. Given these circumstances, the following observations and recommendations are suggested:

- Since many of these aggregate shocks are man-made, following from inappropriate macroeconomic policy or political conflict, there is a clear need to encourage governments to adopt preventive policies and to make them aware of the disastrous effects that inappropriate policies have had on economic development in general and on poor people in particular.
- Truly exogenous shocks such as natural disasters also lend themselves to preventive policies, such as the construction of earthquake-proof housing or dams or the relocation of people – often poor people – to areas that are less likely to be affected. While costly (and often beyond the capacity of poor countries) these measures may prove to be cost-effective from a long-term present value consideration.
- The covariate nature of aggregate shocks means that informal or market-based risk management instruments are often ineffective. However, this is not always the case. For example, insurance against natural risks can still function if appropriately structured and priced, and international diversification of assets and fiscal stabilization funds can smooth national consumption in an effective manner. The use of international insurance against natural risks is not yet well developed but should be encouraged since it has the potential to benefit the poor.

Infrastructure investments such as the construction of a road, an irrigation system, or a dam have an important bearing on the development of an economy and on what opportunities are available to the poor. In the past, the central and often only criterion for such an investment has been the estimated rate of return. However, many investments lead to a reduction in vulnerability over the long run. For example, the construction of a road between an isolated village and a market town reduces the vulnerability of the village community by making it easier for people to trade their goods, migrate, and

access financial market institutions and their instruments. Similarly, irrigation projects are a useful investment for reducing high output risk in agriculture when rainfall is unpredictable. The construction of a dam can be the key instrument for preventing flooding in agricultural and residential areas. These risk reduction or mitigation effects of infrastructure are normally not taken into account in assessing the costs and benefits of a potential investment, and the data and analytical toolkits that are necessary to assess the vulnerability effects do not yet exist.

Balancing informal, market-based and government-provided arrangements

None of these arrangements is preferred in all situations, and all of them typically co-exist. While the importance of risk management for economic development is increasingly understood in the development community, there is still insufficient knowledge about which arrangements and instruments best support the development process. The most contentious questions relate to: (i) the role of governments in risk management and (ii) which public interventions strengthen informal and market-based arrangements.

In any given country, whether and which public interventions are appropriate should be guided by the strengths, costs, gaps, and constraints of the existing informal and market-based arrangements. This implies that public interventions are important in those areas where informal and market-based arrangements: (i) do not function properly because of the severity and scope of a particular risk; (ii) reinforce inequities; (iii) are lacking or dysfunctional; and, (iv) can benefit from public action.

While knowledge about governments' capacity to strengthen informal arrangements is limited, there is ample knowledge about public actions that strengthen market-based arrangements. Even with this limited knowledge, it is possible to come to the following conclusions:

- The family in its diverse forms remains the core institution for handling risks, and its capacity to do so will increase as more and better market-based instruments emerge.
- There are various informal arrangements that are effective in managing risk but that may be detrimental to long-term development goals.
- There is a strong role for risk management instruments provided by communities and non-governmental organizations.
- Market-based arrangements, such as sound saving instruments, are crucial for handling a wide range of risks at the personal level and can contribute significantly to reducing poverty.

Balancing Coping, Mitigation, and Risk Reduction Strategies

At face value, the best social risk management would be to make sure that (downside) risks never occur. The next most effective action is risk mitigation, as this reduces the negative effects of risks before they actually happen. Risk coping is essentially the residual strategy if everything else has failed. However, since each of these strategies has both direct monetary and indirect opportunity costs, relying entirely on risk reduction or mitigation may not be either efficient or feasible. The experience of the formerly centrally planned economies has demonstrated that trying to eliminate all risks in advance

through quantity planning, official price setting, and public ownership of productive means has serious costs in terms of lower economic growth.

At the other extreme, many of the current government interventions in developing countries, particularly for the poor, concentrate on risk coping. To increase the effectiveness of risk management strategies, these countries should pay more attention to risk mitigation and reduction. The accumulation of assets (such as land, cattle, and financial savings) and the adoption of policies that discourage dis-investment (such as cutting down trees) are of the utmost importance in this regard. This does not mean that government should forget about social safety nets, since they are clearly necessary, particularly during periods of natural disaster or economic crisis. Rather, government should introduce programs that support coping while also reducing risk (for instance, by subsidizing education).

Concentrating only on helping poor people to deal with a shock once it has occurred runs the risk of reinforcing a poverty trap and perpetuating the vicious cycle of low returns, low risk-taking, and deep poverty. Balancing coping strategies with reduction and mitigation strategies has the potential to trigger a virtuous cycle in which people can undertake activities with higher variability in returns but also with higher absolute returns.

<u>Revisiting social protection as a sector</u>

The risk management framework poses challenges to rethink the role of existing public sector programs and to expand the range of interventions to include informal and market-based activities. First, the framework provides a starting point to understand individual programs and their interaction in terms of helping people manage risk. Second, it extends the sector to include areas of informal and market-based arrangements in which it has much often little experience.

Regarding publicly provided social protection, reassessment of *<u>risk reduction</u>* measures should involve:

- *Assisting governments to make labor markets more equitable and inclusive,* including a review of labor market regulations and a pragmatic and country-based approach to address public labor standards while distinguishing support for market-based and voluntary standards.
- *Enhancing pre- and in service skills building,* which will entail reorienting supported policies to reflect the increased importance of market-driven training and the shift from skills to knowledge.
- *Eliminating harmful child labor*. Removing children from school is a common coping mechanism for poor households, but it endangers the long term potential of the children. Some uses of child labor are so clearly harmful that a major global effort should focus on their eradication.

In terms of *<u>risk mitigation</u>* the new strategic directions should include:[6]

[6] Current work at the World Bank includes a review of non-contributory pension schemes and a review of alternative income support systems for unemployed.

- *Improving old age income security.* The multi-pillar pension system has emerged as a widely recognized benchmark for formal sector pension reform. But reform experience also indicates that coverage is to remain a main issue of concern in developing countries. This calls for stronger emphasis to ensure provision of retirement benefits for the informal sector and lifetime poor (Holzmann and Stiglitz 2001).
- *Providing appropriate unemployment benefits.* Many developing countries are rightly questioning the standard insurance approach to unemployment mitigation. This calls for a careful assessment of the experience of alternative instruments, including public works programs (for informal sector workers) and individual saving unemployment accounts (for formal sector workers).

Revisiting *risk coping* mainly involves safety nets. Promising avenues relate to interventions that help the poor cope while reducing or mitigating future risks (for example, transfers linked to keeping children in school). Key strategic questions include:
- *What is the appropriate balance in supporting different types safety net programs?* The key interventions include transfers in cash or kind, subsidies and public works. Since each has drawbacks and advantages, more and systematically collected and analyzed information on program experience is needed to provide the best possible advice to countries.
- *How much is enough?* While the global financial crisis has emphasized the need for coping programs, care must be taken that they remain appropriately sized and do not hamper other forms of risk management. Such issues must enter the dialogue of development banks with the IMF in crisis situations.
- *How can coping assistance help with risk mitigation and reduction?* From the perspective of the social risk management framework, this relates to how assistance can be provided in a way that not only increases current levels of consumption for poor people but also enables them to better manage risk and climb out of poverty.

The social protection sector has had little experience to date in supporting informal risk management, yet work can and should be started on several fronts, including:
- *Refining the role of social funds.* Considering their increased emphasis on community-driven development, social funds should: (i) expand the menu of eligible projects; (ii) target vulnerability in addition to poverty; and (iii) strengthen support for software aspects that will enhance the flow of services from installed infrastructure.
- *Encouraging legal reform* to protect poor people's (and especially poor women's) property rights to assets, which includes the revision of inheritance laws.
- *Supporting community-based coping related to orphans and AIDS victims* beginning in the parts of sub-Saharan Africa where the traditional coping mechanisms have been put under an unbearable strain.

International institutions, including the World Bank and ADB, have much more experience in supporting market-based reforms, and the challenge will be to incorporate risk management aspects into these reforms without distorting fiscal and financial sustainability. Two potentially promising areas stand out:
- *Developing microfinance within social protection programs.* Recent trends in microfinance (towards instruments such as microsavings and microinsurance) and the

combination of community-based and market-based arrangements (reinsurance) should help develop new models that may meet both financial and social sustainability criteria.

- *Building financial literacy*. Safe financial assets are key to poor people's ability to mitigate risk, and there is a potential role for social protection interventions in bridging the gap between formal financial sector reforms and traditional social protection programs for example, through the promotion of financial sector literacy.

IV. Vulnerability: A concept in need of definition and operationalization

A main objective of the new framework for SP is to move from an ex-post toward an ex-ante approach in poverty reduction. The task for the government in such a forward looking approach is to undertake or facilitate risk management which reduces the potential for poverty related welfare losses before they actually happen. This concern about expected welfare losses is frequently linked with the notion of vulnerability and the unstable nature of poverty, i.e. movements in and out of poverty by individuals and changing welfare position by poor people due to shocks. This section highlights some key empirical features of poverty dynamics and asks how these characteristics can be best translated into an operational definition of vulnerability.

Poverty dynamics and income mobility

The analysis of poverty dynamics and economic mobility has three dimensions (Baulch and Hoddinott, 2000). One is the metric, the way welfare is measured (such as by income, consumption, expenditure and assets). The second is temporal, the time frame over which the metric is assessed. The most important distinction is between cross section and longitudinal data (following households or individuals over time). The third dimension involves the method used to summarize these measures over time. While there is a rich literature to measure poverty in a static and ex-post manner, the literature on the temporary component is thin.

To assess the poverty dynamics in the short run, the approach used in a growing but still small number of panel studies in developing countries consists in estimating the percent of households which are always poor (i.e. poor in any period of time), sometimes poor (i.e. not poor in at least one period) and never poor (i.e. not poor in any of the periods). This categorization is typically done using the metric of income or consumption and a standard poverty line. Comparing 13 panel studies for developing countries in Latin America, Africa, Asia and Russia (Baulch and Hoddinot, 2000, Table 1) confirms the assessment of still other studies that the percent of households which are sometimes poor is surprisingly large. It ranges from 20 to 66 percent, with most countries exhibiting shares of transient poverty between 30 to 50 percent. This contrasts with the share of households which are always poor and which range for most of the investigated countries between 10 and 25 percent. While measurement errors may substantially inflate the estimates of total and transient poverty, studies that explicitly correct for measurement error still find significant shares of transient poor. These findings suggest that an ex-post focus on poverty is likely to concentrate on many individuals that will not be poor in the next period while neglecting those that are not poor now but will be so in the next period.

A similar picture emerges when panel data is used to estimate changes in the relative welfare position of individuals. Comparing eight transition matrices (Baulch and Hoddinot, 2000, Table 4) suggests that less than half of the households remain on the diagonal, that is, maintain their relative welfare position over time, while some 30 to 40 percent move by one quintile, and another 15 to 20 percent move two or more quintiles. Again, these results suggest that significant individual income and expenditure variation occurs over relatively short time periods, underscoring the potential vulnerability of many people.

While the existence of a strikingly large number of transient poor is receiving increasing empirical support, we still do not understand fully what is behind these dynamics. The current wisdom is that poverty reflects a combination of low endowments, low returns to these endowments and vulnerability to shocks, and that these factors are closely interrelated. A further conjecture is that temporary shocks may have long term effects on the ability of the vulnerable to permanently escape poverty, and that these consequences are transmitted intergenerationally. Empirical validation of this conjecture would further strengthen the case for ex-ante policies to prevent or mitigate such events.

Defining vulnerability

The preceding discussion suggests that an appropriately defined concept of vulnerability would be useful in the analysis and design of ex-ante SP policies. A tractable definition would: (i) allow empirically meaningful measurement of vulnerability both statically and over time at the individual and group levels; and (ii) permit an assessment of the impact of SRM instruments on vulnerability. While important work is ongoing inside and outside the World Bank, no such agreed upon definition yet exists.[7]

Reviewing the notions of vulnerability used in the literature reveals many different concepts, depending on the specific application, whether in economics, sustainable livelihood, food security, sociology/anthropology, disaster management, the environment, or the health/nutrition literature (see Alwang et al., 2000). The main tension seems to be between conceptual and empirical strength. No concept employed so far seems to have both.

In its simplest form, vulnerability for an individual or household can be measured as the probability that expected future consumption falls below some minimum level. For a household at time t, let c_{ht} denote per-capita consumption expenditure and let $\underline{c}$ denote the poverty line. Then, vulnerability, v_{ht}, is the probability that the expected per-capita consumption is below the selected poverty line, with an arbitrarily chosen probability threshold $\underline{Pr}$ (of, say, 0, 25 or 50 percent).

$$v_{ht} = \Pr(c_{ht+1} \leq \underline{c}) \geq \underline{Pr}$$

[7] A scheduled workshop for mid-March of this year at the World Bank will serve to present and discuss the different Bank internal definitions/approaches to the vulnerability concept. Currently available economic approaches for definition and measurement include Alwang et al. (2000), Pritchett et al. (2000) and Jalan and Ravallion (2000).

To make this definition operational, we need to assume a particular income generating process for household consumption. This requires us to think a bit about the determinants of household consumption. A households consumption in any period will depend on a number of factors, including its assets, its current income and expected future income (i.e. permanent income). In cases of liquidity constraints or low permanent income, access to risk management instruments will importantly impact future consumption levels and their volatility. Each of these variables will depend on a variety of household characteristics, those that are observable and some that are not observable as well as a number of features of the aggregate macroeconomic environment. This suggests the following reduced form of consumption:

$$C_{ht} = c(X_h, I_h, \beta_t, \alpha_h, \varepsilon_{ht})$$

where X_h represents a bundle of observable household characteristics, I_h the set of observable, available risk management instruments, β_t is a vector of parameters describing the state of the economy at time t, where β_t evolves according to some stochastic process; and α_h and ε_{ht} represent, respectively, an unobserved time-invariant household level effect, and any idiosyncratic factors (shocks) to households which are otherwise observationally equivalent. Based on this simple model, heterogeneity across households and a distinction between the cross-section and intertemporal dimensions of vulnerability can be introduced and models for empirical implementation can be derived (see Chaudurhi, 2000).

Such a measurable definition of vulnerability will hopefully provide insights into how different household characteristics, macroeconomic aggregates and RM instruments influence vulnerability. Results on the latter may help to assess their relative effectiveness and, perhaps, efficiency.

Yet in order to fully examine the interaction between RM instruments, household characteristics and macroeconomic aggregates , and to gain a better understanding about the underlying choice of RM instruments, it will be necessary to have a more explicit model of SRM and vulnerability. This is still missing. One promising approach would be to determine a model in which individuals or households have the possibility to reduce their vulnerability through access to and application of a given set of risk management instruments, with opportunity costs determining the choice of strategies and arrangements. In such a model, it is the interaction between risk exposure and risk instruments which creates vulnerability (defined as hazard, or the expected damage or loss). Risk exposure is the result of the interaction between risk and characteristics, of which some are exogenous (such as gender), some are endogenous and can be changed by individuals as a preventive action (such as the location through migration). The government can enhance the set of risk management instruments against existing resource constraint, opportunity cost considerations and trade-offs to other policy objectives. The tradeoffs for individuals between the choice of different risk management instruments can, for example, be specified in a simple model as proposed by Gill and Llahi (2000), based on Ehrlich and Becker (1972).

V. Risk and Vulnerability Assessments: An new entry point for a analysis and policy dialogue

The view that risks – both their sources and forms - matter for poverty, and that the way out of poverty crucially depends on the availability of appropriate risk management instruments has important implications. It implies that a necessary starting point is a thorough risk assessment which details, measures, and assesses the crucial risks to which the population at large and the poor in particular are exposed. A second stage involves an assessment of the available instruments to address these risks and identification of gaps in existing instruments. Finally, a plan has to be elaborated which defines the priority and the sequence of actions to close the risk-instrument gap. Such a systematic approach may be not only more effective for poverty reduction, but also more palatable for national governments and the conduct of a policy dialogue with international organizations and bi-lateral donors.

This section summarizes current risk assessment efforts in Latin America, and outlines next steps.

<u>Dimensions of risk assessment</u>

There are two main dimensions for risk assessment: top-down and bottom-up. <u>The top-down</u> approach takes a macro-view on the main risks a country or region is subject to, and includes macroeconomic risks (such as inflation, volatility of GDP, and terms of trade shocks), natural risks (such as earthquake, flooding or drought), major health risks (such as HIV/AIDs and other communicable diseases leading to large covariate shocks) and security risks (such as war and civil strife). Data for these risks are largely available from national and international databases and the macro-risk profile of a country can be established from a desk operation. The regional SP sector strategy papers by the World Bank which were developed in parallel to the overall strategy paper include a first approach in this direction (World Bank, 1999a and b, 2000b-e).

Based on these macro-risk profiles of a country, a number of studies can be undertaken to investigate the poverty effects and implications of these risks, and to outline policy actions, many which will fall outside SP as a sector.

At the regional level, a study was undertaken to investigate the opportunities and risks in a globalized Latin America and the Caribbean (De Ferranti et al. 2000). The study asks whether globalization has increased the macroeconomic risks for the region and how the realized macroeconomic risks in the 1980s and 1990s have impacted the poor. It concludes that while the macroeconomic volatility in LAC is high (at least higher than in industrialized countries), it has not risen in the 1990s; in various countries it has even fallen below that experienced in the 1970s. But as documented by surveys, the perception of insecurity has increased and with it the demand for risk management instruments by workers (most importantly for unemployment income support). To deal with existing risks ex ante, it suggests a number of policies, including macroeconomic diversification and liquidity management, and anti-cyclical budgetary policies. With regard to the impact of crises on the poor, the results based on household panel data for

Argentina, Brazil, El Salvador and Mexico are rather differentiated (op. cit., pages 8 and 9):

- First, economic contractions differ substantially in their economic effects on poverty and human capital investment. In deep recessions the poor suffer greater proportional losses in income than the wealthy. In moderate recessions, the opposite appears to happen – in many cases, the greatest proportionate income losses were borne by the rich, while groups such as elderly and single mothers do not appear to be especially badly affected. This finding is not true in every crisis and every setting. For example, conclusions vary by country, and within some countries, between rural and urban areas.
- Second, the poor seem to have gained more during growth periods than is generally acknowledged. This does not mean that the poor should not be helped, it merely implies that from the perspective of poverty alleviation growth policies must be given priority, regardless of concerns of high inequality in the region.
- Third, the poor – like those with more wealth – are reluctant to permanently compromise their family's future during economic crises that are perceived as temporary. This is especially true for parental decisions about children. The poor do not, for example, frequently pull their children out of school during bad times, although they do when the recession is perceived as severe.
- Finally, and unsurprisingly, access to reserves, such as assets and underused family labor, reduces the vulnerability of households to shocks in the sense of having to adjust through reduced consumption or critical investments such as schooling and health. Assets may be the key factor in households weathering large versus moderate contractions. In brief or mild contractions, even the limited assets of the poor can help weather the crisis; in more severe or recurring crises, the poor may eventually exhaust their assets and be forced to suffer drastic declines in their well-being, with adverse long-term effects.

A bottom-up approach of risk and vulnerability assessment asks the poor what they perceive as the most threatening risks for their livelihood. Their assessment may be different from a (distant) government perception or an (even more distant) perception by international institutions and bi-lateral donors. And their assessment provides, perhaps, more direct guidance for policies and the selection and provision of appropriate risk management instruments.

An example of an ex-post risk assessment is based on the 1994-95 Ethiopian Rural Household Survey (Dercon and Krishnan, 2000). As highlighted in Table 5.2, for the rural population natural risks (harvest failure) dominate other concerns, and even policy problems (such as resettlement and taxation) are more serious than labor problems (such as illness, death and divorce). Altogether, agriculture related risks dominate any other concerns in the rural area, including even war and crime. Introducing period-specific risks into the econometric specification further illustrates the effects of shocks such as rainfall (or the lack thereof) and livestock diseases and the lack of consumption-smoothing instruments (op.cit., Table 6).

Table 5.2 Assessed Risk in Ethiopia by Rural Population during Past 20 Years

Type of risky event	Percentage of household	Mode year of most recent severe

	reportedly effected by type of event	event
Harvest failure (due to drought, flooding, etc.)	78	1984
Policy problems (resettlement, taxation, etc.)	42	1985
Labor problems (illness or death, divorce, etc.)	40	1993
Oxen problem (disease, theft, distress sale, etc.)	39	1993
Other livestock (as above)	35	1984
Land problem (land reform, transfer to family member)	17	1989
Asset losses (Fire, theft, villagisation, etc.)	16	1885
War	07	1989
Crime/banditry	03	1986

Source: Dercon and Krishnan, 2000, Table 5, based on data from the 1994-95 Ethiopian Rural Household survey.

Qualitative risk assessments derived from participatory assessments and community consultations in other African countries confirm that the main sources of risk are largely perceived to be co-variate (AIDS, war and civil conflicts, rural risks and macroeconomic shocks), with some idiosyncratic shocks such as illness, widowhood, and old-age also of concern.[8] Similar patterns also emerge for other lower and middle-income regions in South and East Asia, and Middle East and Northern Africa.[9] These findings call for public interventions which may not necessarily put traditional social protection programs in the forefront, but access to water, health and education. The situation in the former communist countries of Europe and Central Asia is somewhat different since the old system tried to eliminate any kind of risk through public ownership of the means of production and planing, while providing a whole range of social protection programs (World Bank, 2000b). Here, a restructuring of these social programs for a market economy is needed and underway. What all regions and countries need is quantitative evidence of risk and vulnerability and qualitative indicators. Pilots in this direction are underway.

Country pilots in LAC

New "Risk and Vulnerability Assessments" are currently being piloted by the World Bank in Guatemala and Columbia, with first results expected to become available during 2001 (Arriagada et al. 2001). The current plan of these assessments is to:

- Construct a typology of vulnerable groups in each country;
- Construct a profile of key risks and assess their impact on the poor and key vulnerable groups;
- Examine household and community level mitigation and coping mechanisms; and

[8] See the African Sector Strategy Paper "Dynamic Risk Management and the Poor: Developing a social protection strategy for Africa", World Bank, 2000d.
[9] See the strategy papers for EAP, SAR and MNA: World Bank (2000c -e).

- Review formal risk management and social protection interventions in each country and assess their effectiveness in reaching and protecting key vulnerable groups.

A major practical challenge for these country pilots is to develop a methodology and a set of indicators for assessing risk and vulnerability using limited cross section and qualitative data. Clearly, panel data would be superior but are not available in either country and many other countries in the region). Even if they were available, they typically would not (yet) contain information about risks, risks instruments and vulnerability. For this reason, existing cross-section data and newly launched survey data have to be used, including:

- Single-cross section household data resulting from recently fielded household surveys that include specially designed modules on risk, vulnerability, and risk management in addition to traditional modules which could also lend information to analysis.
- Participatory qualitative vulnerability assessments that gather information on community perceptions of risk, vulnerability, poverty, and the use of social risk management strategies.
- Other information that is potentially relevant in these countries, such as poverty maps, maps of other vulnerability-related phenomena such as on natural resources and disasters, conflict maps, food security maps (being tracked by WFP and FAO), other household surveys (such as demographic and health surveys, census data, etc.), and other economic data.

Another approach already piloted in various countries in the LAC region (such as Argentina, Jamaica, Mexico, and Uruguay) consists of using secondary information to identify key risks by age group, help identify possible measures to address these risks, and to clarify the role of SP policies (including social insurance and social assistance programs) vis-a-vis other sectors. The secondary information draws on work on poverty assessments, budget analysis work, voices of the poor surveys, information from NGOs, and other sources. Identifying risks by age groups is a simple but useful way to identify sources of vulnerability. As people move through the age profile with given social programs, a readily available indicator for vulnerability can be established. This short-cut in the risk analysis process proved to be very powerful to complement traditional poverty assessments and to engage governments in a discussion about appropriate policy responses. . Table 5.3 presents an abbreviated version of such an age-group related risk-policy response table for Argentina.

Table 5.3: Managing Social Risk in Argentina: Main Risks and Policy Responses (Summary Table)

Age group/ Main Risk	Role for Other Programs	Role for Social Protection Social Insurance	Social Assistance	Number of Indigent & Poor Uncovered
0-5 Stunted development	PHC Services Pre-school education	--	Early Child Development Programs (ECD)	400,000 ind. 1,000,000 poor
6-14 Low education quality	Improve primary school quality	--	--	--
15-24 Low secondary school completion	Improve secondary school access/quality	--	Scholarship/ return to school incentive programs	100,000 ind. 400,000 poor
25-64 Low income (unemployment/under employment)	Labor-intensive growth and labor market reforms	Unemployment insurance	Workfare/income transfers	800,000 ind. 3,750,000 poor
65 and Over Low income	--	Social security (contributory pensions)	Non-contributory pensions (income transfer)	24,000 ind. 200,000 poor
General Population Low access to/quality of health care	Provision of health svcs.	Health insurance --	--	1,700,000 ind. 6,000,000 poor
Low housing quality	Mortgage facilities, infrastructure investment		Housing subsidies	200,000 hh.ind. 800,000 hh. Poor

Source: Argentina – Managing Social Risks (World Bank, 2000f)

Next Steps

The work on risk and vulnerability assessments is just beginning both at the conceptual and operational level. The approach undertaken by the World Bank is to move conceptual and operational work in tandem in order to leverage the gains in understanding. Conceptual work guides the next steps for implementation while operational work and new survey pilots provide the feedback to rethink methodology and the conceptual framework. The success of this approach is likely to be enhanced by:

- Information sharing between regions, international institutions, bi-lateral donors, and others involved in this new approach. This is more easily said than done (even within one institution), but conferences like the Asia Pacific Forum on Poverty are an important step.
- Supporting academic research at the analytical and empirical level, such as the use of panel data to derive vulnerability indicators which allow the use of cross-section data to signal vulnerability; and
- Working very closely with governments to gain their support for the new approach and to disseminate the new thinking and methodology. Within the World Bank this

is done through the World Bank Institute (WBI), and a new seminar and training module is scheduled to be piloted with the African region this year.

VI. Economic crisis management: What have we learned for social protection?

Addressing major financial and economic crises such as the debt crisis in Latin America in the 1980s and mid 1990s and the recent financial crisis in East Asia present a major challenge for social risk management. Such crises stem from large covariate shocks to individuals and households which, if deep and protracted, are likely to exhaust the risk management capacity of individuals and households and their use of informal and market-based arrangements, as well as the capacity of governments. Family and community risk sharing arrangements are less effective in face of covariate shocks, tend to break down, and are typically less effective for the poorest of the poor. Governments are typically not prepared to handle a rising number of needy individuals, both in administrative and budget terms, and quite often programs do not exist that can be expanded. Lacking or having exhausted available risk management instruments, households will have to use short-term coping mechanisms such as taking children out of school and increasing the time spent in the labor market by children and women, selling of productive assets, and reducing nutritional intake with long-term negative consequences for productive capacity and long-term poverty reduction.

This background has motivated the APEC finance ministers to ask the World Bank, the IMF, ADB and IADB to prepare a paper which takes stock of the experience in Latin America and East Asia, and that distills good practices for the region and the world (World Bank et al., 2001). The report of this working group is based on responses to a questionnaire administrated to six APEC countries (Chile, Indonesia, the Republic of Korea, Mexico, Peru, and Thailand) and follow-up missions to these countries during July-August 2000. The report provides a good first review of issues and recommendations, and the main findings include (op.cit, p.18):

- The availability of timely and reliable information on poor and vulnerable groups is critical for the design and implementation of social safety net programs;
- Pre-crisis planning can contribute to the design of effective safety nets. Planning will include an assessment of risks and target populations together with identification of program instruments, financing and a strategy for reducing or phasing out programs after the crisis;
- Ideally, safety net instruments should be in place before a crisis occurs. It is essential that the programs are targeted; provide adequate protection to the poor; avoid creating a culture of dependency among beneficiaries; and are consistent with economic incentives and overall targets of macroeconomic and fiscal policy;
- Social safety nets should build on existing public programs and mechanisms for targeting and delivery. In practice, safety nets will typically comprise a variety of programs and targeting methods. Major social safety net programs include: cash or in-kind transfers, price subsidies, public works, fee waivers for social services, supplemental feeding and nutrition programs, targeted human development programs and microfinance programs, as well as social insurance programs that can reach the poor;

- If adequate pre-crisis planning has not been possible, social safety nets should concentrate on existing programs employing simple targeting methods that can be adapted quickly to increased utilization during crisis;
- Transparency and accountability in the design and implementation of programs and in the use of resources are critical to the effectiveness of social safety net programs. Public information on the different programs and the eligibility criteria should be made available as well as periodic and independent program evaluations;
- Social safety net programs should be coordinated across implementing ministries and departments as well as different government levels to avoid inefficient overlap and administrative waste;
- The building of adequate administrative capacity at the local level should precede decentralization;
- During crises, proportional cuts in social spending in general and safety nets in particular should be avoided. If possible, spending should be maintained or increased and key programs should be protected; and
- The involvement of NGOs, community groups and religious organizations can be promoted to enhance efficiency and accountability, provided their capacity to implement social safety nets is adequate.

Adding support for these conclusions with experiences from other countries, encouraging further technical clarification about design and implementation, disseminating the findings in these countries and beyond, and supporting the implementation in countries would be a major achievement for social protection and lasting poverty reduction.

VII. Social sector expenditure reviews: A means to improve the efficiency of public interventions

The SRM framework suggests that many effective risk management interventions fall outside the traditional social protection domain but are within the social sectors, such as access to basic health, education, water and sanitation. This suggests that an integrated view on social expenditure and financing would be beneficial. Furthermore, the Poverty Reduction Strategy Papers and the underlying process call for a review of budgetary expenditure in order to increase spending effectiveness. This asks for a review of social expenditure and their efficiency in contributing to poverty/vulnerability reduction.

Reviews of total government expenditure and selected policy areas are undertaken by a number of institutions to serve a variety of purposes. The IMF produces the Government Finance Statistics annually with the key objective of making the fiscal accounts consistent with other accounts in the real and monetary sectors to facilitate detection, analysis, and reaction to sources of macroeconomic instability.[10] The World Bank produces Public Expenditure Reviews which examine the structure of expenditures and provide a broad-brushed analysis of expenditure problems (including institutional weaknesses). The ILO produces Social Protection Expenditure Reviews and uses the European System of Integrated Social Protection Statistics (ESSPROS) as a starting point (Hagemejer, 2000). Bilateral donors (such as DFIF, GTZ, CIDA, SIDA, etc) as well as

[10] The new GFS manual enhances the link with the System of National Accounts, inter alia, by moving toward the recording of flows on an accrual basis and by integration of stocks and flows. See IMF, 2000.

multilateral organizations produce other expenditure reviews for loosely defined social sub-sectors in developing countries, most often on education and health, and sometimes on social safety nets or social protection, however defined. However valuable these different reviews by different actors are, they use different definitions and concepts, often are not linked to the development indicators these expenditures affect, and demonstrate the lack of agreement about the best methods to estimate the effectiveness of these expenditures. In addition, expenditure analyses often fail to take into account the (extra-budgetary) spending by bi-laterals and NGOs, or large employer-sponsored programs.

The current state of expenditure reviews calls for the development of a systematic methodological framework of social expenditure, financing and performance reviews in developing countries. A framework is needed which is jointly developed and applied by international organizations, bi-lateral donors and countries to undertake reviews with comparable results. Such a joint methodology would have at least two main effects. It would enable the development of benchmarks for countries, and would facilitate learning from experiences of other countries. Moreover, once a methodology is established, institutions, bi-laterals and countries will be able to outsource these reviews to international and local consultants, whose work and results can be much better benchmarked and hence monitored. Finally, a joint framework would provide a better basis for partnership between international organizations as well as bi-lateral donors, and should contribute to institution building in the joint client countries.

The Social Protection Sector of the World Bank has developed a draft framework which will form the basis of dialogue with ILO, IMF and other partners, and several bi-lateral donors have expressed their interest to join the effort. A first draft for discussion is close to completion and scheduled for consultation in February-March this year (Canagarajah et al., 2001). After revision, the first pilot Social Sector Reviews (SSR) are envisaged for mid-2001. The experience of these pilots would feedback into revising and refining the methodological framework.

The currently proposed approach to conduct a comprehensive SSR is three-layered:

- Identify the scope and structure of a country's social sector;
- Monitor the necessity, appropriateness and capability of social sector programs/interventions to reduce poverty;
- Evaluate the economic effectiveness of social sector programs and interventions provided or financed by the public sector

First, it is necessary to identify all expenditures related to a country's social sector by gathering information on relevant programs or interventions provided or financed by the government or the private sector.[11] The successful conduct of this exercise will enhance the knowledge on the basic composition and structure of a country's social sector expenditures, as well as the provision and financing systems, and will allow analysts to answer basic expenditure-related questions, e.g., on what, how much, by whom, and for whom.

[11] For a review of public and private transfers in the East Asia crisis context, see Sumarto et al. (2000).

Second, all social sector interventions and programs of a country need to be reviewed in terms of their potential to reduce poverty/vulnerability. This involves primarily the assessment of whether social sector interventions/programs in a country meet the prioritized needs of the poor and contribute to improved risk management. Furthermore, in-depth analysis of programs or interventions of the public sector need to be carried out. This comprises the examination of whether public programs or interventions meet the rationale for public intervention, and the actual demand of the poor. Moreover, the objective(s), progress and outcome(s) of each program or intervention will be studied to identify successful and unsuccessful projects. The information gathered by this exercise provides grounds for improving the allocation of resources between public programs.

Finally, all social sector programs and interventions financed or provided by the public sector need to be evaluated in terms of their economic effectiveness, e.g., by use of cost benefit analysis, benefit incidence analysis, tracer studies, etc. The successful conduct of this exercise will provide information on necessary reforms of social sector programs/ interventions in the public sector.

Applying the three-layered methodology proposed here will permit a description of the structure and composition of social sector programs and interventions within a country, as well as an analysis of the appropriateness, capability and effectiveness of public sector programs and interventions to reduce poverty and provide a rationale for necessary reforms of public programs.[12]

The suggested road map for the development of the framework and its implementation is pragmatic. First, after a reasonable and generally agreed draft is available, it is suggested that a review should be piloted in a few countries in each region to test its feasibility and to learn about its usefulness. Second, a sequential approach is suggested: A review would start with an assessment of the main programs before deciding on selective deepening of analysis and follow-ups. Finally, it is suggested that work begin with initial qualitative assessments and memorandum items before deciding on resource-consuming quantitative follow-ups.

VIII. Concluding remarks

This paper has attempted to motivate and document a forward looking approach to social protection. It puts forward the notion that the conceptual underpinnings for a dynamic role of social protection in lasting poverty reduction are to be found in the social risk management framework, a construct that stresses the need to view social protection as a springboard out of poverty.

The new concept is focused on vulnerability – a dynamic view of poverty - and the need to offer risk management instruments to the population at large and poor people in particular in order to reduce future poverty. This forward looking approach promises to

[12] Linking the assessed risks by age group with budgetary costs per capita also provides a first indication about the potential budgetary costs to cover the gap. For an application to social sector programs in the Mexican context, see Hall and Arriagada (2000), Table 6.

be more effective for accelerated and lasting poverty reduction; it also is consistent with the increase in diverse risks facing people in a globalizing world.

While this new view seems promising, many conceptual and operational issues still need to be addressed, but work in this direction has started. This includes, inter alia, development of an operational definition of vulnerability, the design and implementation of risk and vulnerability assessments, the design of appropriate safety nets to respond to major economic shocks, and the conduct of social sector expenditure, financing and performance reviews. Successful conclusion of this work and implementation in developing countries during the coming years should contribute to achieving the poverty reduction goals set at the Social Summit 2000 in Geneva.

To this end, a coalition is needed between multi-lateral development institutions (such as World Bank and ADB) and bi-lateral donors (such as AUSAID, DFID and GTZ), national and international research institutions and donor and client governments. While each will assume a specific role, working jointly on improving the design and implementation of a forward looking social protection approach is important. Only then can the richness of thought and experience be harvested and applied for the benefit of the vulnerable.

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