Food Subsides, Growth and Poverty
A Critique on Neoliberal Institutional Structure

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The relationship among payment style of subsidies, economic growth and poverty is a matter of challenge among economists and policy makers. Neoliberal Institutional Structure in framework of what is called "Washington Consensus" and "structural adjustment policies and economic stabilization" argues on economic advantages of removing food general subsidies so necessity of replacing a most liberalized food markets with regulated food security policy. This paper gives a historical background of this approach and criticizes it's policy recommendation and shows following it has led to a deep crisis in global food market in 2007 with sharply rising of poverty and dying of some people around the world due to lacking of access to food.

Keu Words: Subsidies, adjustment and stabilization policies, poverty, food Crisis

Introduction

The relationship between subsidies targeting and poverty reduction aim is a matter of challenge among economists. Economists with a Neoclassical approach argue that removing general subsidies and replacing them with targeted subsides is the best policy aiming to reduce the poverty. On the other hand, economists with heterodox approaches argue that reducing poverty needs a redistributive policy which in essence is different of recommended policy of first group. From this perspective, there are different challenges which shed a strong doubt on the mainstream recommendation including identification problem, administrative costs, inflationary effects of prices liberalization, stimulating effect of this policy on speculative activities and lees stability at food markets. Moreover, there are institutional and structural barriers in many developing economies which don't allow to price policies to work well. Removing these kind of bottlenecks should be in agenda to address right the poverty and also to pave the way for price policies in the case. Indeed, there are two kind of hypothesis in explaining the low growth and more poverty of developing countries: price inefficiency against to structural-organizational or institutional inefficiency.

First part of paper provides the historical background of "structural adjustment policies and economic stabilization" with its theoretical foundations and also its recommendations to addressing the poverty. In Second part _ initial inequality, growth and poverty_ it is argued that poverty is mainly rooted in uneven distribution of assts and incomes so in this case price liberalization may have negative effects on poor. Third part includes the preconditions of a success and efficient targeting subsidies policy and show there are important problems regarding to these preconditions. The food crisis of 2008 which led to dying of poor along political instability in some developing countries, as a result of this recommendation policy, is argued in forth part of paper. Final part includes the conclusion.

Structural Adjustment and Economic Stabilization Policies (SAESP)

The policy of removing general subsidies and replacing it with targeted subsides is an element of SAPES. This approach rooted in "Washington Consensus" appeared in early of 1980th and recommended to countries from developed to developing in order to address the high trade and budget deficits along the low efficiency and growth. It has two components: stabilization and adjustment. International Monitory Found is responsible for implementing the stabilization and World Bank for the adjustment components . Stabilization has three elements as follow: 1. Demand restriction, 2. Switching policies with an emphasize on devaluation and adjusting the currency and 3. The policies related to supply side in long run with an emphasize on financial reforms as well as trade liberalization. This component aims to reduce the trade and budget deficits and improve the efficiency and growth. Adjustment component has same three elements with this difference that World Bank mainly focuses on third element. (see: Stewart, 1996; Mohan et al 2000; Taylor, 1988; Schydlowsky, 1995). During the decades 1980_90, SAPES were recommended by these international economic institutions and developing countries have had to implement them in order to get the IMF and WB's "structural adjustment loans". According to IMF (1986), the element of demand restriction has had the most emphasize during 1980_84. In all of 93 finalized contracts between these institutions and countries in this period demand restriction were applied in a of all cases (100 percent), public expenditure reduction in 92.4 percent and budget deficit reduction in 82.8 percent (table 1).

Table 1. Characteristics of fund-supported Programmes, 1980-84, (ninety-three agreements)

items	percentage
A. Demand restraints	
1. Limit on Credit explosion	100
2. Restraint in public expenditure	92.4
3. Deficit reduction	82.8
B. Switching policies*	
1.Increase rate reforms	62.4
Exchange rate reforms	50.4
Wage restraint/guidelines	47.3
C. Long run efficiency**	
1. Sectoral restructuring	68.9
2.Financial reforms	51.6
3.Trade liberalization	48.4

Source: IMF, 1986, Table 12 (quoted: Stewart, 1995, p. 9)
*Also have demand restraint and efficiency effects
** May also have switching effects

In the case of World Bank loans and contracts the most emphasize is on long run efficiency. According to WB (1992) during 1980_88 and 1989_91 in 78 and 72 percent of contracts enforced between WB and the countries this element is emphasized. (Table 2).

Table 2. World Bank: Loan agreement conditions
(as a percentage of all conditions)

items	percentage	
A. Demand restraint	38	42
1.Deficit reduction (fiscal policy)	36	39
	2	3
B. Switching policies*		
1.Exchange rate policies**	4	5
2.Wage policy	2	3
	2	2
C. Long run efficiency	78	72
1. Trade policies**	16	10

2. Sectoral policies **, of which	25	23
_Industry	3	2
_energy	3	7
_agriculture	18	10
3. Financial sector reform	10	11
4. Rationalization of government administration	10	15
5. Public enterprise reforms	17	13
D. Social policy reforms	3	7
E. Other	4	5

Source: World Bank, 1992A, Table A2.1 (quoted: Stewart, 1995, p. 10)
*Also Have demand restraint effects
**Also have switching effects
***Also have efficiency effects

According to Joan Toye (1994) the most ten important elements of " structural adjustment loans " are as follow: removing import quotas (57%), improve export incentives (76%), reform the fiscal system (70%), improve financial performance of public enterprises (73%), revise agricultural pricing (73%), shift public investment (59%), revise industrial incentives (68%), increase public enterprise efficiency (57%), and improve marketing and other support for agriculture (57%). Reduction of general subsidies as a part and also deficit budget control and improving the efficiency through " getting to prices right" is one of the important preconditions of these institutions in paying the loans.

Theoretical Framework of SAESP

The theoretical foundation of SAESP is rooted in macroeconomics "Monetarism", "Supply-side" and 'Rational Expectations" schools as well "New Neoclassical Political Economy" . The first school giving a new and modern formulation of "Quantities Money Theory" argues that the main reason of inflation is related to inappropriate money supply in compare to changes of productive capacities and economic growth; generalizing this theory to an open economy it also argues that the inappropriate growth in money supply leads to more imported goods and higher trade account deficit which would result in reduction in foreign reserves and eventually vulnerability of economy against to exchange speculations and attacks. From this perspective, the main reasons of financial imbalances (budget deficits) and account of payments (current account) is rooted in imbalances between supply and demand sides of money which should be removed by using the stabilization elements of SAESP. At the same time, in framework of MacKinnon-Show hypothesis it's argued that state intervention in capital market leads to "financial Suppression" and inefficient resource allocations in financial markets which eventually result in high inflation rates.

From Supply _Side school perspective, state intervention in economy leads to more expenditures than tax revenues ;on other hand, interventional state needs more expenditures should be financed through higher tax rates which has negative effects on investments and economic growth; and when investments goes down the tax base decreases which implies on less tax revenues. This analysis is formulated in framework of well known “Lufer Curve”; There is an adverse U curve shape between tax revenues and tax rate; when tax rate, in horizontal axis, passes optimum rate tax revenues goes down. The conclusion is that tax rate should higher margin of profit and encourage the investments. decrease in order to make strong incentives to investors; and also in this line of analysis, the barraging power of labor union should be controlled in order to make capital accumulation or to have sufficient “ income policies”; high barraging power of these institutions which is considered as a reason for high wages and low profits.

The rational expectation theory is another theoretical foundation of SAESP in which there is a high emphasize on capability of market mechanism to settle the imbalances and getting to equilibriums. From this perspective, every state intervention aiming to improving macroeconomic situation dose not have effect on real economy due to this reason that economic agencies would be able to predicate the non real effects of these kinds of policies and make them failure. For instance, if state aims to decrease unemployment rate through an expansionary monetary policy, the economic agents would predicate it’s inflationary effects and based on this prediction will arrange their economic decisions which would accelerate the inflation; at the end, what’s remain is inflation not low unemployment.

Beside these macroeconomic perspectives, New Neoclassical Political Economy is also another theoretical foundation of SAESP. This approach by introducing the concept of “rent seeking” and this assumption that there is no difference between state agencies and private agencies in terms of following the personal interests and maximizing the profits has tried to show that all of state interventions in forms of imposing tariffs, controlling exchanges and interest rate, using of multi exchange and interest rate systems , paying subsides by fixing the prices, and nationalizing the ownerships only lead to more rent seeking by the relative authorities. The policy recommendation from this perspective is same to previous perspectives: removing all of these interventions through liberalization and privatization and minimizing state in framework of state as night watch not more than it.

From these perspectives markets should be liberalized through these policies: financial liberalization and removing controls on interest rate, devaluation of exchange and removing the fixed exchange system, getting to prices right including foods and energy and removing all of price controls and general subsidies, controlling the barraging power of labor and wages, following an contraction money and fiscal policy, trade liberalization and privatization all are rooted in the Neoclassical or New classical Macroeconomic theories. Using the words of Albert Hirschman (1991) these theoretical foundations of SAESP could categorized in three kind of thesis: “Perversity”, “futility” and “jeopardy”.

> “According to perversity thesis, any purposive action to improve some feature of the political, social, or economic order only serves to exacerbate the condition one wishes to remedy. The futility thesis holds that attempts at social transformation will be unavailing, that they will simply fail to “make a dent”. Finally, the jeopardy thesis argues that the cost of the proposed change or reform is too high as it endangers some previous, precious accomplishment’ (p.7).

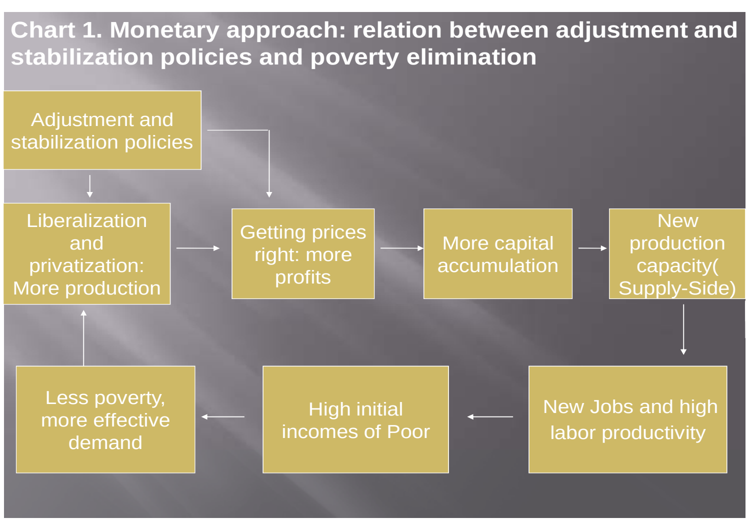
The mainstream Neoclassical debate on the negative role of state in recourse allocation is placed in framework of first thesis; the rational expectation theory is placed in framework of second thesis and supply side theory along Neoliberal hypothesis on negative relation between state intervention and economic and political freedom, for instance debates of Friedman and Hayek, is placed in framework of third thesis.

Targeting of Subsidies , poverty and SAESP

In framework of theoretical foundations of SAESP paying subsidies through stabilizing the prices leads to price disturbances and misallocation. Low economic growth and efficiency, poverty and also even structural bottlenecks such as inelastic supply side of economy in different sectors are related to price disturbances. Getting to prices right not only is necessary to improve the efficiency and growth but to overcome the poverty.

From this perspective, liberalization and privatization in one hand improves the organizational and management structures of firms and getting to prices right on the other hand removes high resource misallocation and leads to efficient allocation and also shapes a correct incentive system. Reducing of losses and getting to profits in losing firms and improving the rate of profits in other firms is the next result of implementing the SAESP. More capital accumulation is logical result of these changes: establishing good macroeconomic environment, appearing strong incentive system, and reforming of organizational and management structures. This economic growth could be accompanied by decreasing poverty through job creation and paying more wages to labor; and increasing initial incomes of poor and labor along other social groups and classes means more effective demand for produced goods/commodities and services by new increased production capacities in supply side.

It could be mentioned that the main conclusion of this perspective is that if state intervention in it's different forms be removed market mechanism would be able to make a commutative circle which leads to more growth and less poverty at every stage. The diagram 1. Pictures the casual relationships between SAESP, efficiency, growth and poverty.



Source: Dini and Lippit, 2009

Milton and Rose Friedman (1980) clearly recommends on removing general subsidies and replacing it with cash subsidies in order to restructure the social welfare system and get to high economic efficiency:

> The program has two components: first, reform the present welfare system by replacing the ragbag of specific programs with a single comprehensive program of income supplements in cash- a negative income tax linked to the positive income tax; second, unwind social security while meeting present commitments and gradually people to make their own arrangements for their own retirement" (p120)

SAESP performance in the 1980th and emerging of cash subsidies debate

As mentioned above stabilization element of SAFSP indeed is a contraction policy aiming to control the budget and trade deficits. The consequences of this policy during the 1980th was falling of capital accumulation due to falling of public expenditures in one hand, and rising of poverty mainly due to liberalizing the food prices and falling of real wages in other hand. (see: Stewart 1996; Mohan et al, 2000). World Bank and IMF in a joint study (1989) pointed out:

> Declining per capita incomes accompanied by worsening social indicators, particularly sub Saharan Africa and Latin America…. Some of the poor and did benefit, but many vulnerable groups were hurt by measures associated with adjustment. By the mid-1980, it became clear that given the time and effort required to turn deeply troubled economies around, it would be morally, politically and economically unacceptable to wait for resumed growth alone to reduce poverty" (quoted: Stewart, pp. 7-8

In 1990 Camdessus, managing director of IMF, accepted:

> The recognition that macroeconomic policies can have strong effects on the distribution of income and on social equity and welfare. A responsible adjustment program must take these effects into account, particularly as they impinge on the most vulnerable or disadvantaged groups in society.(Ibid, p.8)

The above confirmations on negative effects of adjustment policies on poverty and indeed rejecting the possibility of poverty reduction through "trickle down effect" appeared after critiques particularly UNICEF's report entitled "Adjustment with a Human Face" (1987). This reports although accepts the necessity of adjustment but criticizes the World Bank and IMF policy package and recommends these policies:

> -More expansionary (and by implication less deflationary) macro-economic policies in order to raise output, investment and human needs over the period of adjustment;
> -Greater utilization of meso-policies in order to prioritize policies in favor of the poor;
> -Sectoral policies should be designed in order to restructure the productive sectors so as to raise the level of employment and income-generating activities;
> -Compensatory programmes to protest basic health and nutrition of the poor through public works pregammes and nutritional interventions;
> -Finally, the monitoring of the human situation, especially living standards. Health and nutrition of the poor. (Mohan et al, p 70)

Effecting by this report and World Bank and IMF started to argue on necessity of targeting of subsides and paying cash subsidies to poor in order to compensate the negative effects of adjustment policies. Although this revision seems to be a step forward but paying cash subsidies without having other elements of UNISEF package could minimize the positive effects of this program. Indeed, this revision has been in the line of Fridmans approach to restructuring social welfare system: minimizing state intervention in economy, getting to more privatization and liberalization in economy in order to get to more efficiency, paying more attention to controlling inflation by reducing the liquidity so reducing state expenditures including welfare budget and paying cash subsidies as negative tax. Comparing these elements with the UNESEF package clearly show that there is great difference between these two approaches. UNICEF in framework of a regulated institutional structure although accepts the necessity of price adjustments but still argues on the necessity of state intervention in providing public goods including health and education and also job making.

Primary income inequality, growth and poverty

One of the main claims of ASEP polices is that there is a high inequality in terms of access to subsidized commodities between low and high income groups. Although the aim of generalized subsides is to help the poor but it mainly beneficiated the rich who are able to consume more so it argues it would be better to liberalize the prices and de subsidized the commodities and pay cash subsidies to the poor. This strategy help the economy system to target the poor and reallocate the financial founds to them instead of the rich; At the same time as discussed above the resource allocation would be improved through getting to prices right. Indeed, this paradigm tries to address the challenge of inequality and poverty through a price policy rather than paying more attention to main reason of poverty which is related to great gap in terms of property ownership. As Adam Smith (1776) says :

> Wherever there is great property there is great inequality. For one very rich man there must be at least five hundred poor, and the

> affluence of the few supposes the indigence of the many. The affluence of the rich excites the indignation of the poor, who are often both driven by want, and prompted by envy, to invade his possessions.

With respect to cash effectiveness of cash subsidies in reducing of inequality it would be argued If there is a high degree of inequality in assets the primary effect of cash subsidies as a transfer payment policy- which is accompanied by price liberalization in markets including food markets- on welfare of poor could be compensated by secondary inflationary effect of this policy. Price liberalization in this situation leads to more return rate of property and income share of rich in a way that the income inequality if dose not tend to increase at least remains unchanged. As Mierdhal using the concept of "cumulative causality" argues when there is high inequality in terms of economic power price reforms without of any redistribution of assets could performs against itself. According to Stewrst and Streteen (1976) effective redistribution policy needs not only a combination of assets redistribution and technical reforms and sufficient incentives but also needs continually reforms.]

As different studies (Karshenas, 1993; Ali and Elbadewi, 1999; Griffin, 2000; Dagdeviren, 2001) show that primary inequality in high and meddle income economies has negative effect on growth and poverty because it has negative effects on capital accumulation in human capital, social solidarity and social and political environment. Indeed, in these economies poverty is inelastic to growth. Although studies show in low income economies redistribution of assets and wealth could have negative effect on physical capital accumulation but as Sen (1999) argues even in these kind of economies making sufficient capital accumulation in human capital which is a precondition to tackle the poverty should not be delayed up to a time that economy become rich; It's possible to improve the quality of life using a strong social service plan which includes education and health care as the main components. Table 3 shows although depending on economic situation of an economy there should be different kinds of policies to tackle the poverty in all kinds of economies health and education along infrastructure and public services are effective in reducing the poverty through accelerating economic growth.

Table 3: Summary of Feasibility of Redistribution Instruments by Category of Country

Group of country	Redistribution of current income and assets(middle-income countries)	Growth with redistribution policies(middle and most low income countries)	Growth without redistribution: countries (very low- income countries
Progressive taxation	Yes	Yes for some countries	No
Transfer payments	Yes	Yes for some countries	No
consuner subsidies	Yes	Yes	Yes for some countries
Land reform	Yes, but nor always relevant	Yes	No for most countries
Education and health	Yes	Yes	Yes
Infrastructure and public works	Yes	Yes	Yes

Source: Hulya Dagdeviren et al (2001),

Global food crisis as historical testimony for explanatory sufficiency of SAESP and NIS

While a part of economists where doubting on the efficiency of ASESP in terms of technical issues including possibility of identification poor (stewart, 1996), the administrative and psychological challenges of paying cash subsidies (Stewrt 1996; Sen,), "staple food prices soared on world markets during the world food crisis of 2006 to 2008 . World maize prices increased 54 percent from August 2006 to February 2007, followed by an increase in world wheat prices of 125 percent from May 2007 to March 2008. World rice prices increased by 203 percent from October 2007 to April 2008, and then maize prices increased by 59 percent from their already elevated levels between December 2007 and June 2008 (all of these price increases are in nominal terms). Thus, prices for all three cereals more than doubled in a span of less than two years. Subsequently, world cereal prices plummeted in the second half of 2008 before recovering slightly or leveling off in the first few months of 2009" (Dawe and Morrales-Opazo, 2009). Although the prices started to decrease since June 2008" they are still 71% higher than in 2005. Lower international commodity prices have not yet translated into lower domestic food prices in many low income countries. FAO has warned that a new price surge is possible during 2009. Once more, poor farmers will not benefit because they are not integrated into markets and the poorest people who spend 60 to 80% of their income on food will face hunger and malnutrition." (Oxfam, 2009).

As result, some people died in some developing countries due to their inability to cover the high increased prices of food with their fixed nominal income. According to estimation of FAO at least 100 Million people have gone under the risk of hunger. In the words of Josette Sheeran (2008), the head of the UN's World Food Program:

> "This is the new face of hunger....There is food on shelves but people are priced out of the market. There is vulnerability in urban areas we have not seen before. There are food riots in countries where we have not seen them before"

This statement which is in the line of Sen (1999) when argues that many starvations have accrued in history while there have been enough food in the supply side at macro economy level. The case of US as a main exporter of food precuts clearly shows that increasing trend of poverty and hunger during the global food crisis is mainly related to inability of economic system in making able these people to access the food in this kind of situation. As we argued above when there is high inequality in assets, a inflationary situation could suffer the poor while there is a kind of cash subsidies. Emphasizing on liberalizing the markets including food markets as high as possible have had different negative effects: first, in supply side of agriculture sector it led to increase of fertilizers and coproduction costs in this sector which effected mainly small farmers as a part of poor; second, it led to establishing of speculative activities in food markets which has had important effects on rising of global prices; third, it has become as an ideology that there should not be any state intervention in order to organize the food security policy by regulating the food market keeping the food prices more stable.(Ghosh, 2008; Magdoff, 2008).

The world food crisis with deep consequences for the poor around the world confirms that markets including food markets need to be governed. Now, this is the point that is confirmed even by pro Neoliberal Institutional Structure. For instance, Jeffrey Sachs (2007) confirms that:

> "The whole thing was based on the idea that if you take away the government for the poorest of the poor that somehow these markets will solve the

problems....But markets can’t step in and won’t step in when people have nothing. And if you take away help, you leave them to die

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