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What are the Likely Poverty Impacts of the Current Crises?

This brief is about the likely poverty impacts of the current crisis. It asks, what does the evidence from previous financial crises tell us about the possible impacts on poverty of the current crisis?

Estimates of the poverty impact of the current crisis are becoming numerous and varied. The World Bank (2008) puts the number of new poor people from the crisis at 46–53 million. This is on top of the 130–155 million new poor people as a result of 2008 food and fuel price increases. These are estimates. What does the evidence from previous financial crises say?

How does a financial crisis transmit to household poverty?

Financial crises impact poverty through several transmission mechanisms (see box, right). Baldacci *et al.*, (2002) argue that 60–70 per cent of the poverty impacts of a crisis are due to four factors: unemployment, inflation, reduced public expenditure and GDP contraction. Those households that are adversely hit may respond by trying to increase income. They may do this via family members seeking new or additional work and/or drawing upon savings, credit (if available) and/or selling assets. Or they may try to reduce household expenditures via changes in quantity and quality of diet or the costs of health and children's education (see *In Focus Policy Briefing 7.3*).

Evidence from previous crises

Income poverty impacts

The total number of poor people and the severity of poverty rise dramatically during

How does a crisis transmit to poverty?

A crisis may transmit to poverty through the following:

- Changes in labour demand
- Changes in prices
- Changes in public spending
- Changes in the value of economic, human, social, environmental and financial assets
- Long-term impacts on capabilities (i.e. effects of malnutrition, schooling drop-outs, etc.).

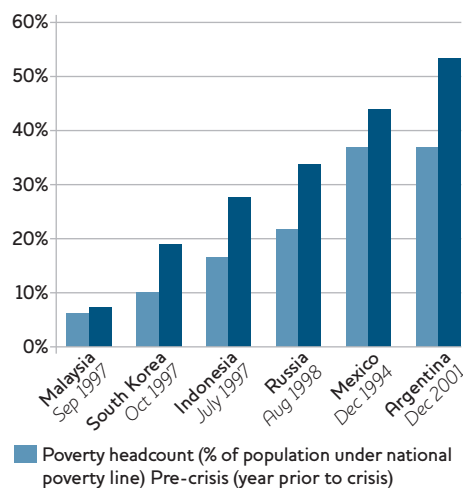
Source: Lustig and Walton (2008)

a crisis (figure 1; World Bank, 2008). Cline (2002) puts the average poverty impact of a crisis at a seven per cent increase in the poverty headcount per country. The IMF (2009) estimates every one per cent contraction in developing countries GDP leads to an increase in poverty of two per cent.

Inequality and non-income poverty impacts

The distributional impacts of crises are highly uneven and income inequality often worsens during a crisis, adding further pressure to poverty levels (Ravallion, 2008). Gendered impacts are particularly evident via labour markets and school drop-outs (World Bank, 1999). Further,

Figure 1: Poverty impacts of selected financial crises



Source: Gottschalk (2004)

major rural and urban variations are often evident because of different impacts on different production and consumption patterns (World Bank, 2008).

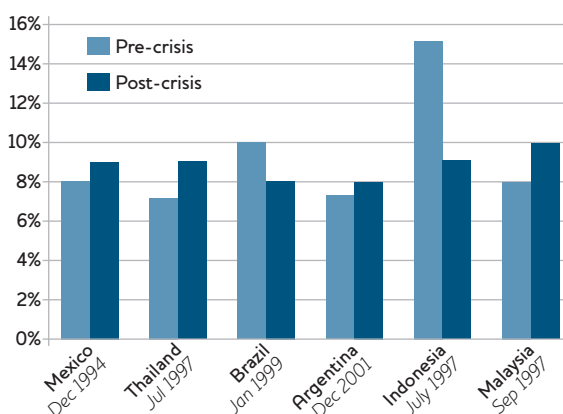
Nutrition, health and education impacts have been evident in previous crises (World Bank, 2008). Such impacts may be long term too because household coping mechanisms typically include decisions related to children and expenditures on food, education and health (see figure 2 overleaf; Mendoza, 2008). There is also

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“ The total number of poor people and the severity of poverty rise dramatically during a crisis ”

strong cross-country evidence of psychological distress, mental health problems and community and intra-household conflict as a result of crises (World Bank, 2008).

Figure 2: Changes in low birth weight babies as per cent of all births during selected financial crises, 1990–present



Source: World Development Indicators (Dec 2008)

However, governments can and do successfully intervene to prevent these kind of impacts (see 7.4). There is evidence in some middle income country crises that education indicators are unaffected or might actually improve (table 1; World Bank, 2008).

Table 1. Primary school completion rate (per cent of relevant age group) during selected financial crises, 1990–present

Country (date crisis began)	Pre-crisis	Post-crisis
Mexico (Dec 1994)	92 (1994)	97 (1996)
Malaysia (Sept 1997)	92 (1995)	94 (1999)
Indonesia (July 1997)	97 (1997)	95 (2001)
South Korea (Oct 1997)	98 (1996)	92 (1999)

Source: World Development Indicators (Dec 2008)

Responses to the current crisis

From the past, we know that the better our ability to track and understand the shifts in poverty at a micro level, the better we are able to respond. Therefore, we suggest two actions:

1. Invest in better poverty and vulnerability early warning tracking systems

Tracking poverty alone is not enough. For each poverty indicator we can propose a corresponding

vulnerability indicator. For example, for income and nutrition poverty we need to track the population immediately above the income and food poverty lines. We also need rapid qualitative appraisals of poverty impacts (see 7.3).

2. Explicitly link these new tracking systems to the following:

- Planning of responses, social protection and pro-poor public expenditures;
- Indicators of the underlying causes of vulnerability such as the indicator sets we have for food security and social protection;
- The Millennium Development Goal (MDG) framework by developing corresponding vulnerability indicators for each MDG.

Ongoing tracking and evaluation becomes particularly important given that the poverty impacts of the current crisis may be worse than previous crises because of the global nature of the crisis (thus export-led poverty reduction will be difficult); because the current crisis follows household shocks in food and fuel prices (with major poverty impacts already); and because aid and public expenditures are under threat (with major poverty implications). Poverty and vulnerability must be carefully tracked and interventions made using this as an evidence base to mitigate the poverty impacts of the current crisis.

Credits

This *In Focus Policy Briefing* was written by **Andy Sumner** and **Sara Wolcott** from the Vulnerability and Poverty Reduction Team at IDS. The series editor is **Clare Gorman**. For other briefs on the crisis see: www.ids.ac.uk/go/infocus7

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Further reading

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