1. Introduction

This book investigates the relationships between rural poverty, risk, and development. Building upon the author’s work in the area, it summarizes the contributions of recent theoretical and empirical work to our understanding of rural poverty and risk in developing countries. Over their lifetime, all men and women are subject to risk. Some external shocks affect their well-being in the most direct manner: illness, accident, death. Other shocks affect their ability to support and feed themselves, either temporarily – unemployment, crop failure, loss of property – or permanently – disability, skill obsolescence. The purpose of this book is to summarize what we know and do not know about the sources of risk faced by the rural poor and the coping strategies they have developed to deal with shocks. We also examine how risk and risk coping strategies impact the rural poor’s capacity to develop. So doing, a better handle can be gained on how governments and international organizations can assist the rural poor to better deal with risk and overcome their poverty.

The book starts in Chapter Two with a brief overview of the issues surrounding poverty and risk in underdeveloped rural areas. Not only is risk higher in poor rural economies, but poor people are also less able to deal with risk. Apart from localized efforts, they are largely left to their own devices as far as socialized care is concerned. Low assets also make it difficult to absorb shocks. Poverty is thus not only associated with higher ambient risk; it also reduces people’s capacity to absorb shocks.

In response, the rural poor have developed a variety of strategies for coping with risk which are discussed in Chapter Three. These multi-faceted strategies include: settling relatively safe areas; breeding plants and species that survive in difficult environments; diversifying sources of income; preserving flexibility and keeping options open; accumulating precautionary savings; forming strong and large households; seeking the protection of the rich and powerful; and sharing risk with a large network of friends and relatives.

These strategies are subject to serious technological, environmental, and economic constraints that limit their effectiveness. These constraints are reviewed in Chapter Four. Commitment failure, in particular, seriously limits society’s capacity to share risk. This may explain the formation of long-term solidarity relationships with networks of friends and relatives.
Moral norms and village ideologies can similarly be seen as attempts to mitigate the perverse effects that self-interest and information asymmetries have on mutual insurance.

Chapter Five examines how wealth accumulation and risk sharing affect the evolution of inequality over time. We first assume risk sharing away and examine how inequality evolves over time when agents accumulate an asset. If asset accumulation is unbounded and the asset yields a positive return, inequality converges to a single value over time. If the asset yields a zero or negative return (for example, grain storage), there is no persistent inequality but inequality is nevertheless correlated over time. If wealth yields a positive return but is in finite supply (for example, land), persistent inequality arises if one agent is more thrifty than the other. Multiple equilibria may obtain. Societies might prevent polarization by closing down markets in such assets.

We then introduce risk sharing. With perfect risk sharing, welfare inequality is constant across time. For continued participation in mutual insurance to be voluntary, asset inequality must remain ‘close’ to welfare inequality. With imperfect commitment, the end result is a hybrid situation half-way between the risk sharing model and the pure accumulation model. If risk aversion is high for poor agents but low for rich ones, patronage arises whereby the rich on average take away from the poor. There is therefore a trade-off between risk sharing and social mobility. We also discuss the possibility of poverty traps and their effect on dynamic inequality. Heavy indebtedness is discussed in this context. We find that access to alternative sources of finance and insurance is key to prevent informal risk sharing from degenerating into exploitative patronage and debt trap.

Chapter Six is devoted to development and growth issues. The relationship between risk, poverty, and economic development is complex but our understanding has progressed dramatically with recent theoretical and empirical advances. Chronic rural poverty, by itself, is unlikely to raise net fertility. It also seldom leads to starvation – except in cases of extreme destitution. Rather, it negatively impacts welfare by raising vulnerability to adverse shocks. The effects of these shocks manifest themselves not only in terms of short-term reduction in consumption but also in terms of reduced ability to deal with subsequent shocks. In this sense, risk is fundamental to the reproduction of poverty over time.

Next, we examine the relationship between rural poverty, risk, and technological innovation. We revisit the traditional risk aversion explanation and discuss many of its shortcomings. We also discuss the relationship between poverty, risk, and experimentation with new technologies and we identify the non-divisibility of technology and its learning process as a major stumbling block on the road to adoption by poor farmers. We argue
that the variance of output is, by itself, unimportant, except inasmuch as it raises fears of bankruptcy. The main factors that hinder technology adoption by poor risk averse farmers are likely to be: large cash outlays, loss of diversification after adoption, and large risk during experimentation and learning.

We then turn toward credit constraints and saving and show that poor individuals with a precautionary motive for saving find it very hard to save enough to finance a large lumpy investment. The link between poverty and low investment apparent in these results is reminiscent of ‘vicious circle’ and ‘big push’ theories of development propounded decades ago.

In the final part of Chapter Six, we discuss the relationship between risk sharing and risk taking. Communities subject to lots of external shocks might fear the concentration of wealth that would naturally arise, were asset and credit markets allowed to freely develop. In order to ensure long-term social cohesion, these communities might institute egalitarian norms that prohibit certain transactions and require the redistribution of material wealth. We then investigate whether egalitarian norms of redistribution dilute incentives to invest. Social stratification based on patronage is likely to be inimical to large scale industrialization but to favour the accumulation of social capital, an essential ingredient in trade.

Lessons are drawn in Chapter Seven. Although we have learned a lot about risk and rural poverty, there remains a lot to be learned. Little is known, for instance, about geographical patterns of rural settlement and resettlement. Yet many areas where the rural poor currently live are unsustainable. In the long run we need to know what will motivate them to move out of these areas. More research needs to be done on financial saving by the poor and the retailing of safe savings instruments to rural areas. The household formation process plays a key role in how individuals cope with risk; unfortunately, we know precious little about what brings individuals together to form household units and how resources are allocated within these units. The formation and maintenance of social networks also deserves further study, as well as the relationship between risk and power. The effect of poverty on development is also not fully understood, with many ideas being proposed but few scrutinized rigorously.

In conclusion, we make a series of specific suggestions regarding policy action by governments and international organizations. These recommendations focus on settlement patterns, disease prevention, savings instruments, divisible technology, and support to existing informal institutions. International organizations must continue to serve in their role of insurer of last resort in times of crisis, with as little of a political agenda as possible. They should also support efforts where cross-country externalities are large and returns to scale important, such as in the eradication of diseases
and pests, the development of vaccines, and agricultural research. They can also assist poor countries gain access to European and US markets for the agricultural products and crafts that the rural poor can produce, such as sugar, vegetable oils, livestock, and feed crops.