

Review

Reviewed Work(s): Inequality and Poverty in Malaysia: Measurement and Decomposition by Sudhir Anand

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informative.

The strong point of the book in this reviewer's opinion are the papers by Gordon, Brennan and Buchanan, and Cnossen. Drawing on the earlier work of Starrett, Gordon does a good job of articulating the optimal tax assignment problem when there are distorting taxes and hence, first best equilibrium is ruled out. However as D. B. 'OS has correctly noted there serious follow up work to be done. Gordon's analysis rests on the assumption of an existing Tiebout equilibrium and he also has not dealt with conflicting welfare functions (for the state and federal governments). I might also add that the parallel problem of pricing of public services in a Gordon type of distorted structure has not been attempted, Recent research in this area (see, for example, Murty and Stern (1983)) points both to the necessity of treating prices and taxes in an integrated manner and to the fact that treating taxes in isolation might give us misleading results.

Brennan and Buchanan's paper is the clearest articulation in neoclassical theory, of the need for federalist structures. Having said that, though, one runs up against the main problem with the theory (and hence its articulation)—inadequate treatment of politics and political processes within a federalist structure. One could make a beginning in this direction by adapting the seminar contribution of Aumann and Kurz to federalist structures. The road in this direction is a long one but it is also an exceptionally exciting one.

Cnossen has a bright idea about indirect tax harmonization in the EEC and it is well worth listening in advanced federal countries in general. Based on some meticulous historical and legal research he argues the case—very persuasively—for removal of border controls and their consignment to the books. This is a good idea but one has no data base, really, to suggest how well it may work in practice. In particular I feel agnostic about its resilience to external shocks. It is worth giving a try, though.

RAGHBENDRA JHA

Review of Sudhir Anand, *Inequality and Poverty in Malaysia : Measurement and Decomposition*, (IBRD, 1983).

This painstaking examination of the anatomy of inequality and poverty in Malaysia as revealed by the Post-Enumeration Survey (PES) which accompanied the 1970 Population Census in that country, and the resulting analysis of the 1971 New Economic Policy (NEP) of 1971 (Prongs 1

and 2 of that policy, in particular, which were the inequality-related components of it) is clearly must reading for all those interested in the area of development policy as it relates to inequality. I also recommend it strongly to all research scholars in Economics, as an example of what applied economic research can be at its very best.

The author begins (chapter 2) with a detailed account of the survey design, sampling procedure and income definition used in the 1970 PES, and compares the macro aggregates from the survey with those from the national accounts. He establishes conclusively the non-comparability of the PES with the 1957-58 Household Budget Survey (HBS) and the 1967-68 Malaysian Socio-Economic Sample Survey of Households (MSESH). This contribution alone deserves to be widely read and heeded. It is a common practice to estimate trends in inequality with a passing acknowledgement of the fact that the surveys on which the estimates are based are not comparable. These incomparabilities are often so fundamental as to vitiate all comparative statements, as in the case of the HBS and PES of Malaysia, even though both surveys were concluded by the Government Statistical Department. We cannot conclude from the lower Gini coefficient of the former that inequality worsened in Malaysia over the sixties, because inequality as estimated by the HBS had a downward bias (a bias, further, whose degree cannot be quantified). Anand tells us why in excellent detail in chapter 2. The 1967-68 MSESH is also not comparable with the PES because its coverage extended to cash income alone.

The PES data are then used to construct the anatomy of inequality in Malaysia by per capita household income (chapter 3). An examination of the relative desirability of alternative indices for the decomposition of inequality is followed by a decomposition exercise, using the Theil T index, by race (a central preoccupation in Malaysia) and location. The author finds that as much as 90% of overall inequality is accounted for by *intra*—racial differences, and only 10% by differences between the races. He further finds, even more surprisingly, that much of the intra-race disparity, 86% or more, is accounted for by intra-rural and intra-urban disparities and only 14% (or less) by between-location differences.

The author draws on the above findings in his subsequent analysis of the New Economic Policy of 1971, Prong 2 of which enunciated explicitly a policy of reallocating incremental income so as to raise Malay incomes to parity with non-Malay levels. This objective was sought to be achieved through a system of racial quotas in hiring. Since such preferential hiring will make for a departure from present patterns chiefly at the higher income levels, the policy will merely reduce between-race disparity at the expense of a worsening intra-Malay distribution. It is difficult to agree with the author, however, that the policy might increase overall inequality

in the short-run (p. 102). What happens to overall inequality is a function of the distribution of incremental incomes alone; irrespective of racial allocation. Prong 2 by itself cannot further worsen this, except under special circumstances, such as the possible need to hire more than one Malay to substitute for each non-Malay at the upper income levels.

But Prong 2 will certainly not reduce overall inequality either. This failure might be perfectly acceptable to Malaysians, although the author frequently assumes that the redress of overall inequality is, or could be assumed to be, an underlying policy objective (pp. 103, 275). There are other passages, however, where he concedes that the NEP nowhere makes explicit a concern with overall inequality.

Prong 1 of the NEP aims at a reduction of poverty irrespective of race, and in chapters 4 and 5 the author meticulously delineates a poverty profile of Malaysia, which is an indispensable guide for an informed execution of that policy. Using the simple incidence measure, poverty is worst among Malays and lowest among Chinese. The poor are 78% Malay and 88% rural. This poverty profile does not vary substantially with variations in the poverty line used (the author tries three in all). A breakdown by occupation reveals the somewhat surprising finding that the incidence of poverty among households headed by farmers (62.5%) is higher than among households headed by farm labourers (49.3%). Some effort is unfruitfully expended in chapter 4 on estimating a modified normalisation of the Sen poverty index which attaches equal weights to the income gaps of all persons below the poverty line. The measure is not decomposable, and carries other limitations as well, all carefully pointed out by the author himself. Chief among these is that the index can unfortunately indicate a decline in poverty even with *no change* in their absolute income, as long as the non-poor become better off.

There is of course an intersection between the two Prongs of NEP, and in the concluding chapter (chapter 8) the author estimates the quantitative impact of expenditure directed towards one prong of NEP on the other; thus 0.79 of every Malaysian dollar spent on Prong 1 serves also to reduce racial imbalance, and 0.25 of every Malaysian dollar spent on Prong 2 will serve also to reduce poverty, *provided* all Malay incomes are raised equiproportionately (an assumption unfortunately not likely to be valid in practice).

The author performs a number of other exercises: a decomposition of inequality is done by income recipient (chapter 6), and an earnings function for urban income recipients is estimated (chapter 7) which provides interesting results by race on returns to education. There are important results in these chapters of policy consequence, such as, for example, that there are large intrasectoral differences in worker income. Prong 2

will therefore be more effective if quotas are specified by occupation rather than by sector.

Finally, in the concluding chapter, the author discusses the alternative means by which poverty removal (Prong 1) could be implemented, and identifies the most effective, among them a rebate for smallholders of the export duty on rubber. Some excellent technical appendices present results from the literature on the welfare and other properties of alternative measures of inequality.

All one can ask for is an update of the book on the actual performance of NEP in Malaysia, which has now been in operation for over a decade. There have been two surveys since the PES : the 1975 Household Expenditure Survey (HES) and the 1976-77 Malaysian Family Life Survey (MFLS, which however excluded single-member households). If any one of these is comparable to the PES in his judgement (could MFLS be compared with that subset of PES households that had multiple membership?), we would finally have a two-point answer to two unanswered questions on Malaysian inequality : have disparities in fact worsened over time, and has the poverty removal policy met with any success at all?

Ramesh Bhatia, *Planning for the Petroleum and Fertiliser Industries—A Programming Model for India*, Oxford University Press, Delhi 1983.

Starting on the premise that “investment and operating decisions in the petroleum industry need to be analysed simultaneously with those of petro-chemicals and fertilisers”, this book explores an optimum mix of policy choices relating to foreign trade, process technology and location patterns for these industries. The investment problem is sought to be solved through the formulation of a “static multi-process spatially disaggregated sectoral planning model”. The linear programming framework adopted for this purpose, is in the nature of partial equilibrium sectoral studies, where optimisation has been defined “in terms of selecting plant size, process choice and locations so as to meet estimated regional demands at minimum costs”, with efficiency prices for capital and foreign exchange given exogenously. The objective function stipulates that the sum total of costs of production, net imports and distribution of petroleum products and nitrogenous fertilisers for meeting the projected demands at any given point of time should be the minimum.

By adopting a linear objective function, the model does not permit variation in unit costs with the level of activity. While this may be a reasonable assumption as far as import prices are concerned, it may not