
Politics, Social Cost-Benefit Analysis and Planners

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This paper explores some of the political assumptions implicit in the use of social cost-benefit analysis (SCBA) and the role of economic planners in using this form of analysis. The paper is written in four parts. The first discusses, briefly, the rationale for the adjustments suggested by the proponents of SCBA. The second discusses the assumptions about the State necessary to justify the use of these techniques as a measure of government objectives. Part three considers whether the assumptions are consistent with the behaviour of the governments of most underdeveloped countries. The last part considers these techniques in relation to the role of planners in the political process.

The rationale

A number of reasons can be given for the increasing attention being given to SCBA in the literature of development economics. In particular it became clear that macro-economic planning did not prevent the introduction, in many countries, of projects which turned out to be expensive failures. In some cases of so-called import substitution, projects turned out to have negative domestic value added. A need was therefore felt for greater use of micro-economic planning techniques. However, in many cases the market prices used in private profitability calculations bore little or no relation to the real cost and benefits to the nation. Techniques were therefore developed to introduce shadow or accounting prices for planning purposes. These efforts culminated in the publication of a number of books putting forward integrated systems of SCBA, the most well known being Little and Mirrlees (1969 and 1974), UNIDO (1972), and Squire and van der Tak (1975). The principal pricing adjustments suggested were:

—elimination of all transfer payments, such as taxes and subsidies, that do not represent resource costs;

—the use of world prices in the valuation of traded goods on the principle that trading possibilities represent the opportunity cost of those goods which enter into international trade;

—use of a measure by which to translate domestic resource costs into world prices. This can be either a standard conversion factor or a shadow

exchange rate depending on the unit of account or numeraire) used;

—the adoption of a shadow wage rate to account for any excess of market wages over the marginal product of labour;

—the use of a rate of discount to take account of the relative value of payments made in different time periods. This may bear little or no relation to internal market rates of interest and, in the first instance, might be an estimate of the opportunity cost of capital;

—the use of a measure (known as the shadow price of investment or the value of public income) by which the value of savings (more precisely, government savings) can be expressed in terms of the average value of consumption in cases where a savings shortage is assumed to exist. This measure also affects the rate of discount used;

—the adoption of an income utility function which relates the value of the consumption of people at different income levels to the value of the average, in the form of an income distribution weight.

Attempts have been made to estimate all these parameters either from existing data such as trade statistics and rural wage rates, or from the revealed preferences of the government, indicated, for example, by taxation exemption limits, the consumption of people with income below this level being assumed to be of at least equal value to government income. The proponents of SCBA suggest that, when the appropriate pricing adjustments are made, the government should select projects according to their present social value (PSV) at the chosen discount rate, or according to the social rate of return where no discount rate is given. The trade-offs between the different possible government objectives, of saving foreign exchange, increasing employment, and growth maximisation subject to considerations of income distribution, are numerically defined by the values given to the various parameters, and the result is held to represent the value of the project according to government objectives.

Few economists would suggest that governments would (or even should) always take decisions solely on the basis of an estimate of a project's PSV. Any analysis of political decision-making would show that the economic considerations which are embodied in the estimate of the PSV are only part of the complex set of factors by

which government decisions are made. However, this would only invalidate the use of SCBA if the government so consistently turned down its recommendations that it became inoperative as a planning technique. In a situation where a government consistently ignores the advice of its planners, it is difficult to conceive of any serious planning. A more important question is whether the political assumptions underlying the adjustments have any validity, and if so in what context.

The assumptions

SCBA can be analytically separated into two stages: economic analysis and social analysis. These two stages are clearly identified in UNIDO (1972) and in Squire and van der Tak (1975), but are less obvious in Little and Mirrlees (1969 and 1974). Economic analysis is primarily concerned with the first five adjustments outlined above, social analysis with the last two. Economic analysis is concerned with the maximisation of national income according to opportunity costs and undifferentiated by its distribution. Social analysis is concerned with the distribution of income between saving and consumption, and between different income groups. The use of economic analysis does not require particularly heroic assumptions about the nature of the State, the major assumption being the desire by governments to maximise national income. This degree of economic nationalism is common to all but the most grossly neocolonial regimes, although the assumption may only relate to one among many government objectives. The results of economic analysis may come up against political opposition in cases where it successfully exposes such activities as transfer pricing or import substitution projects with little or no domestic value added; however, the planning technique in itself merely assumes that the government would like to oppose such activities and this is only an unreasonable assumption when members of the government stand to gain directly from the projects concerned. The major problems in the use of economic analysis appear to lie in relation to the data that should be used, as Sen (1972) and Dasgupta (1972) have pointed out in relation to traded goods; to the sheer organisational and manpower problems involved in undertaking such analyses; and to the relative importance that should be placed on project planning vis à vis other forms of planning.

However, economic analysis contains two major weaknesses, and it is in trying to meet these that the technique has been extended to social analysis. The first weakness is that the use of an opportunity cost rate of discount assumes that the

government is able to ensure sufficient savings to achieve the desired rate of growth, whereas the governments of many underdeveloped countries feel that they are unable to raise sufficient levels of savings to achieve the desired level of investment. In such a context it can be argued that project income in the form of savings is more valuable to them than the generation of additional consumption. The parameter known either as the shadow price of investment or as the value of public income is introduced with the effect (in most cases) of lowering the rate of discount, raising the shadow wage, and reducing the value of any other consumption effects. To justify the use of this parameter as an instrument of government policy it is necessary to assume that the government is politically constrained from using taxation policy and other macro-economic tools to raise the level of savings to that level which it considers optimal, and must, therefore, attempt to do this indirectly through project selection.

The second weakness of economic analysis is that additional consumption by people at widely different income levels is valued equally. Here the implicit assumption is that the appropriate tools for achieving redistribution of income are taxation policy and structural reforms, and that the government is able to use these tools to the extent that it wishes. The economists' objection to this is that governments are frequently unable to achieve desired redistribution objectives directly and that economic theory quite clearly demonstrates the principle of diminishing marginal utility. It is illogical to argue that this principle applies to commodities but not to the income that buys them. A weighting system is therefore proposed (e.g. by Squire and van der Tak, 1975) whereby the value associated with additional income received by individuals is inversely related to their level of income. The usual form of function used, primarily for ease of application, is a constant elasticity utility function.

Why are these adjustments felt to be necessary? It seems that economists have focused on two particular problems which are felt to constrain development. First, accumulation is inhibited by a savings shortage and second, the fruits of development projects are frequently observed to be unevenly distributed. The proponents of social analysis are arguing that the governments of underdeveloped countries are seriously concerned with the distribution of income but are unable to adopt macro-economic policies to influence it because of political weakness. In their attempts to find the necessary parameters they are also equating social cost benefit analysis with government cost benefit analysis. It is with reference to government

policy that the adjustments are made. It could be argued that the equation of government interest with social interest, and the use of distribution weights, implies a consensus, while the assumption of political weakness implies just the opposite.

Do the assumptions make sense ?

The postulate that the governments of underdeveloped countries are interested in both increasing the rate of growth and redistributing the benefits is founded on the rhetoric of political pronouncements rather than on observed actions. It is difficult to find many underdeveloped countries that have shown much interest in taking practical steps to redistribute income away from the elite and towards the poorest sections of the population. The same conclusion can be levelled at the interest in growth. If Baran's concept of surplus is considered, many countries would be able to raise adequate levels of investment *if* effective measures were taken to channel conspicuous consumption, hoarding and non-productive investment to productive use. It is precisely because the governments are not prepared (or in some cases, such as Chile under Popular Unity, are not allowed) to take effective action against vested interests that it is felt necessary to use indirect measures to influence distribution. It is difficult to escape the conclusion that any project that would be genuinely effective in directing income away from the rich towards priority uses in investment and income for the poorest people would not even get as far as the identification stage.

The economist is faced with the possibility that the use of distribution weighting is unlikely to be more than a palliative. Indeed, the interest shown by the large aid donors in SCBA techniques and redistribution has been seen, by some authors, to be more concerned with maintaining rather than transforming the existing structure and dependence of underdeveloped countries (Leys 1975: 8; Thomas 1974: 184-5). Can an economist take seriously the redistributive designs of a government which persistently refuses to undertake a land reform or tax the wealthiest section of the population? If not, it is necessary to justify social analysis on a basis other than fulfilling the objectives of the government. Yet it is information based on the government's observed policies such as the minimum income level on which tax is levied, that is used to calculate the parameters used in SCBA. This is entirely inconsistent: it is precisely because the government is *unable* to redistribute income through taxation that the use of distribution weights is justified.

However, if the economist does not make arbitrary judgements like this he is left with a system of project appraisal that takes no account of the need for a higher rate of savings or a greater measure of redistribution. It is because increasing numbers of economists feel that insufficient action has been taken in relation to redistribution, rather than any fundamental change in the nature of Third World governments, that the techniques of social analysis have been put forward.

Social analysis in a political context and the influence of planners

The above analysis suggests that economists are trying to influence government policies using the government's own rhetoric as justification. To do this they have constructed a model of a constrained but benevolent government, representative of some national interest rather than sectional or class interests. That such governments are rather hard to find scarcely matters: the economist is merely adding his own viewpoint to the many others in the political process.

Much economic theory is written with, at most, a vague conception of the liberal democratic state. Through the internal logic of economic theory (or just from an idea of human justice) it is apparent that, in many countries, there is insufficient overall saving and insufficient consumption by the poorest people. One reason is that the rich (and the army) consume and waste too much and invest too little in productive activity. Social analysis can therefore be seen as an attempt by economists (and the aid agencies that finance their work) to impose this logic on countries that would otherwise do very little about redistribution of income. While government statements are sometimes used to back the judgements up, they really constitute an attempt to impose the priorities of economic planners and aid agencies on recalcitrant governments, for a variety of different motives—such as humanitarianism and the desire to promote political stability—or to prevent revolution.

Where a government rules more by force than consensus it is possible to justify an attempt by economic planners to put forward their viewpoint on the selection of projects. Whether it is democratic or not, planners are not robots and will usually take some point of view. In a country which is ruled by a combination of repression and bureaucracy the viewpoint of the bureaucrats, or the 'econocrats' (Self 1975), will have some impact, and it is legitimate for the planners (not all of whom may be interested in such radical notions as redistribution) to put forward their viewpoint. Can a case then be made for social analysis, despite its dubious political assumptions and the

dangers of excessive influence of 'econocrats', in conditions where the planning process is separated from any control by the people that are planned?

With the existing situation in most underdeveloped countries, social analysis might be justified along two lines. First, that the alternative is a strategy which places no premium on redistribution. In such circumstances, the use of social analysis, even if somewhat arbitrary and undemocratic, is likely to give results that are more beneficial to the mass of the population, despite rather than because of government objectives. The second and perhaps more important justification is that any adequately conducted social analysis should provide valuable information about the distribution effects of development projects, which, if freely available, can be helpful in indicating either the sort of projects to be encouraged, or avoided, or the reforms which such projects make necessary.

Under certain circumstances the assumptions implicit in the use of social analysis may be plausible. This is the case where a government would seriously be interested in raising the level of savings and redistributing income, including the possibility of actually reducing the incomes of the elite, but is actively prevented from doing so by powerful vested interests. In such a case the techniques concerned might be used to indicate a way out of a severely constrained position.

The case for social analysis therefore rests insecurely on the present predicament of the underdeveloped countries, for many of which

redistribution is a slogan to be ignored in practice, while for others the constraints imposed by external forces prevent effective action. It can be shown that the most efficient form of redistribution is through taxation transfers rather than the selection of a set of projects that are sub-optimal from the production efficiency viewpoint (Diamond and Mirrlees 1971). In any society where there is some degree of popular participation in the planning process and where development priorities can be agreed and acted upon, it should not be necessary to use social analysis as a substitute for macro-economic action. The role of social analysis is therefore limited to a transitional phase where the economic planner feels justified in asserting that the government is taking insufficient action in encouraging savings and the redistribution of income and tries to change this, while pretending to implement government policy. He may take this attitude because, by the nature of his job, he has a longer time perspective than the government or he may not be interested in redistribution at all. Whatever the case it is certain that planners *will* give their opinions and that, in the absence of any vehicle for popular involvement, their opinion may be just as relevant as that of the government. It might also be said that the bureaucracy is effectively part of the government. Social analysis *can* be justified, but it is very much a second-best approach in a situation where the mass of the people are excluded from decision-making and where the government is too weak to redistribute income through macro-economic policy.