Globalization and Poverty

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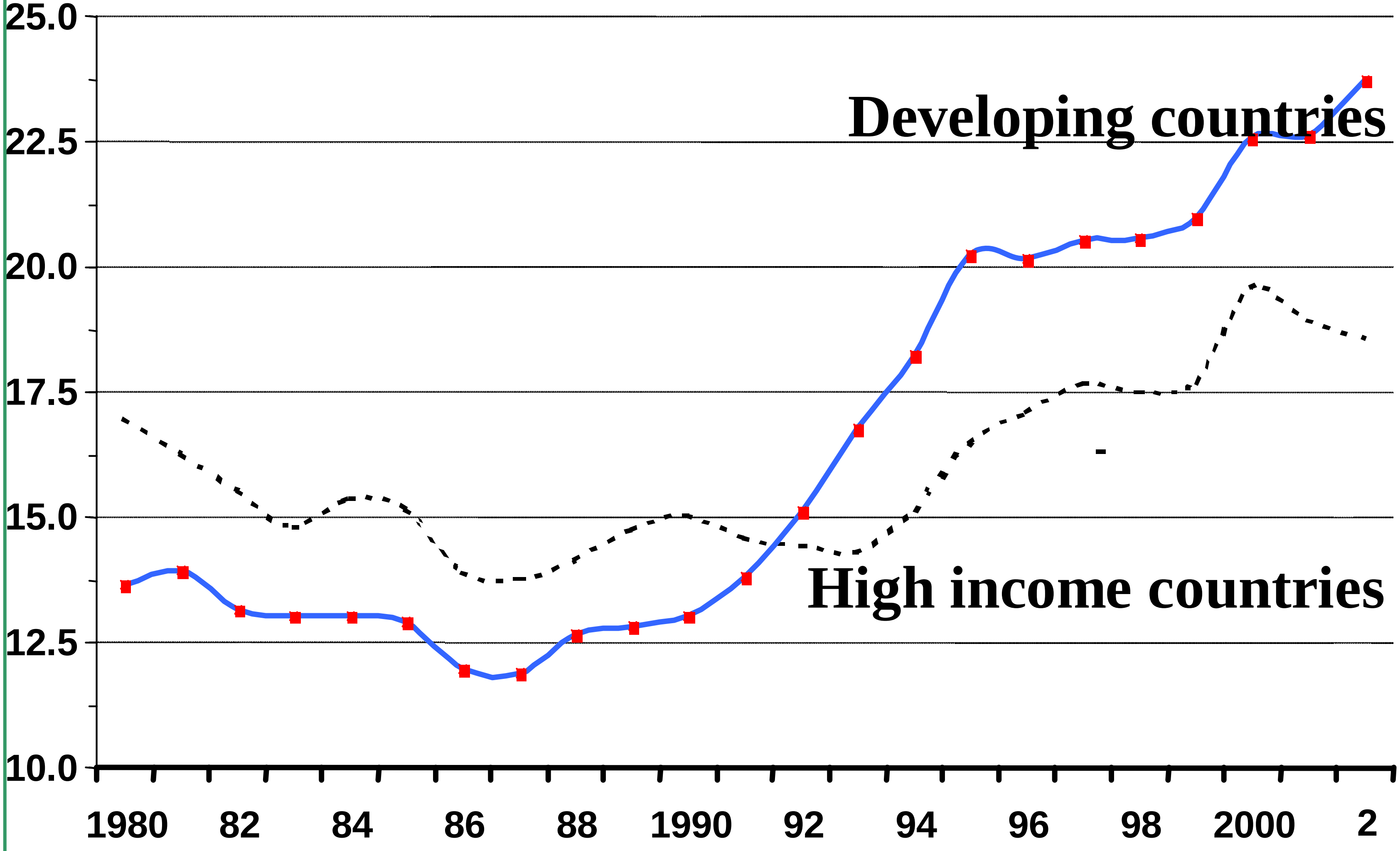
Question: Has Globalization Reduced the Incidence of Poverty?

- Measures of globalization (trade shares, FDI, tariffs, capital flows, capital controls) show increasing openness in developing countries
- World Bank data shows falling incidence of poverty
- Do these trends imply that globalization works as a strategy for poverty reduction?

Increasing Integration of Developing Countries (Export Shares of GDP)



Source: GEP 2003, World Bank data.

My NBER Study: What is the relationship between globalization and poverty?

- Forthcoming book, “Globalization and Poverty”, can be viewed at www.nber.org/books/glob-pov
- What do we mean by “globalization”?
  - trade (tariffs/trade shares)
  - capital flows (FDI, aid, capital flows)
- Topics
  - Theory on poverty-inequality-trade linkages
  - Cross-country evidence on poverty-trade links
  - Country case study evidence from micro data

Why should we care about inequality and not just about poverty?

Ken Rogoff (in his chapter for this volume):

> One has to acknowledge that poverty is fundamentally a relative measure which will probably gain an entirely different meaning as the world economy becomes more integrated…Malthusian notions of poverty are likely to become a distant memory in most parts of the world as global income inexorably expands over the next century, and issues of inequality, rather than subsistence, will increasingly take center stage in the poverty debate.

Ben Bernanke in a recent speech:

> The challenge for policymakers is to ensure that the benefits of global economic integration are sufficiently widely shared--for example, by helping displaced workers get the necessary training to take advantage of new opportunities…

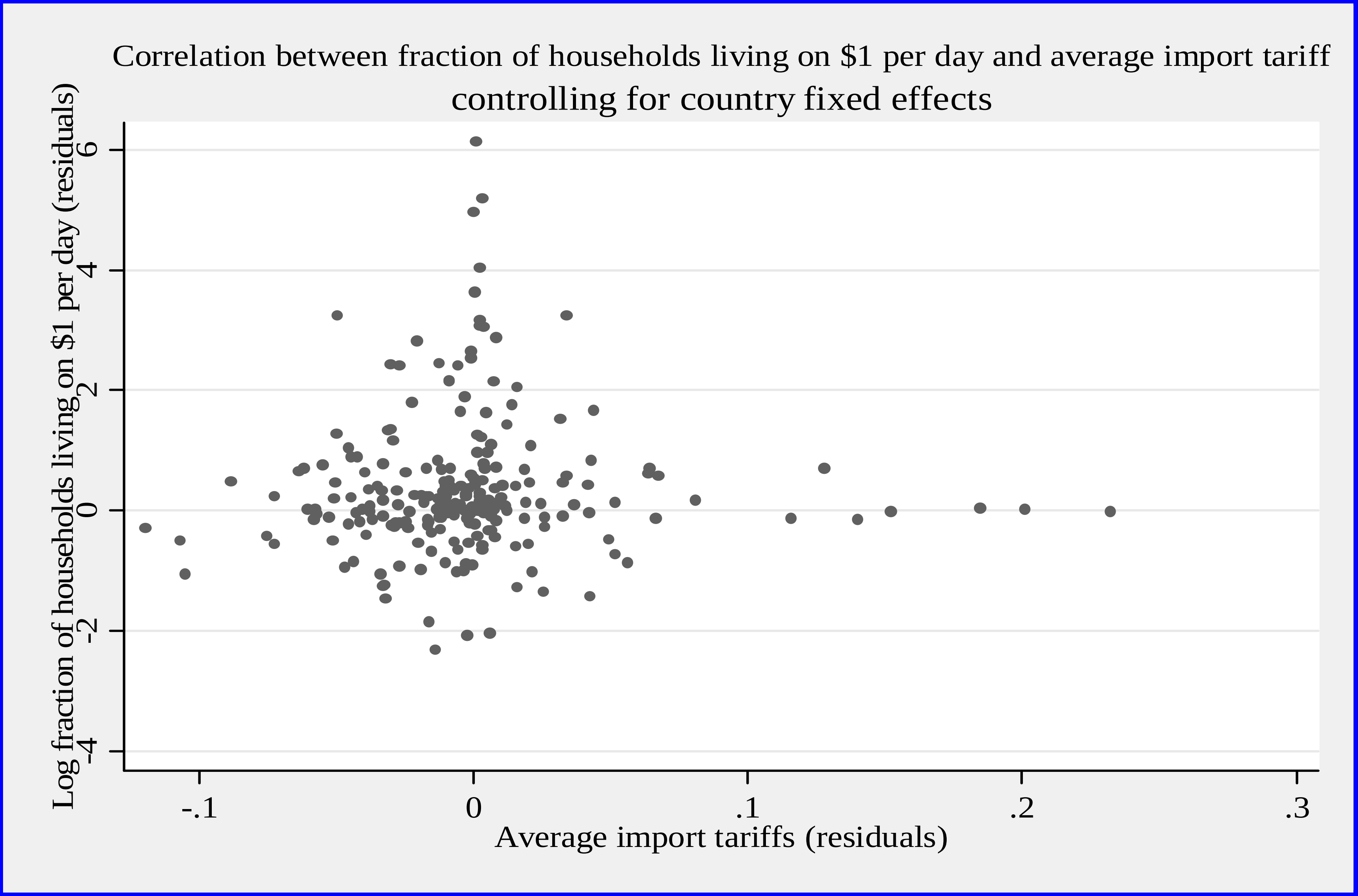
Cross-country results question existing orthodoxy

- Greater openness to trade is associated with higher inequality in poor countries (Milanovic and Squire, Easterly)
- Financial integration is associated with higher consumption volatility for less financially developed countries (Prasad, Rogoff, Wei, and Kose)
- Agricultural support in rich countries *helped* in poor countries, because most poor countries are net food importers (Ashraf, McMillan, and Zwane). OECD subsidies hurt only countries that export primarily food
- No robust impact of openness on poverty reduction

No direct linkages between globalization and poverty outcomes !

- Openness associated with growth
- Biggest driver of poverty reduction is growth ("Growth is good for the poor")
- Very weak *direct* association between openness and poverty outcomes
- Why?
  - Although increased openness to trade promotes growth, not "pro-poor" (inequality rises)
  - Consistent with a negative impact on poor which offsets the gains from growth due to openness

NO Relationship between Trade Policy and Poverty



Country Case Studies Using Household Data

- India
- Colombia
- Ethiopia
- Mexico
- Zambia
- South Africa
- China
- Poland
- Indonesia

Results

- Challenge orthodox perspective on gains from trade for the poor
- Heterogeneity in responses
- BUT poor in expanding sectors gain
- Poor in previously protected sectors lose
- DFI and Aid help the poor
- Currency crises hurt the poor
- Bundling trade reforms with complementary policies is necessary

Why are conclusions based on “Orthodox” view wrong?

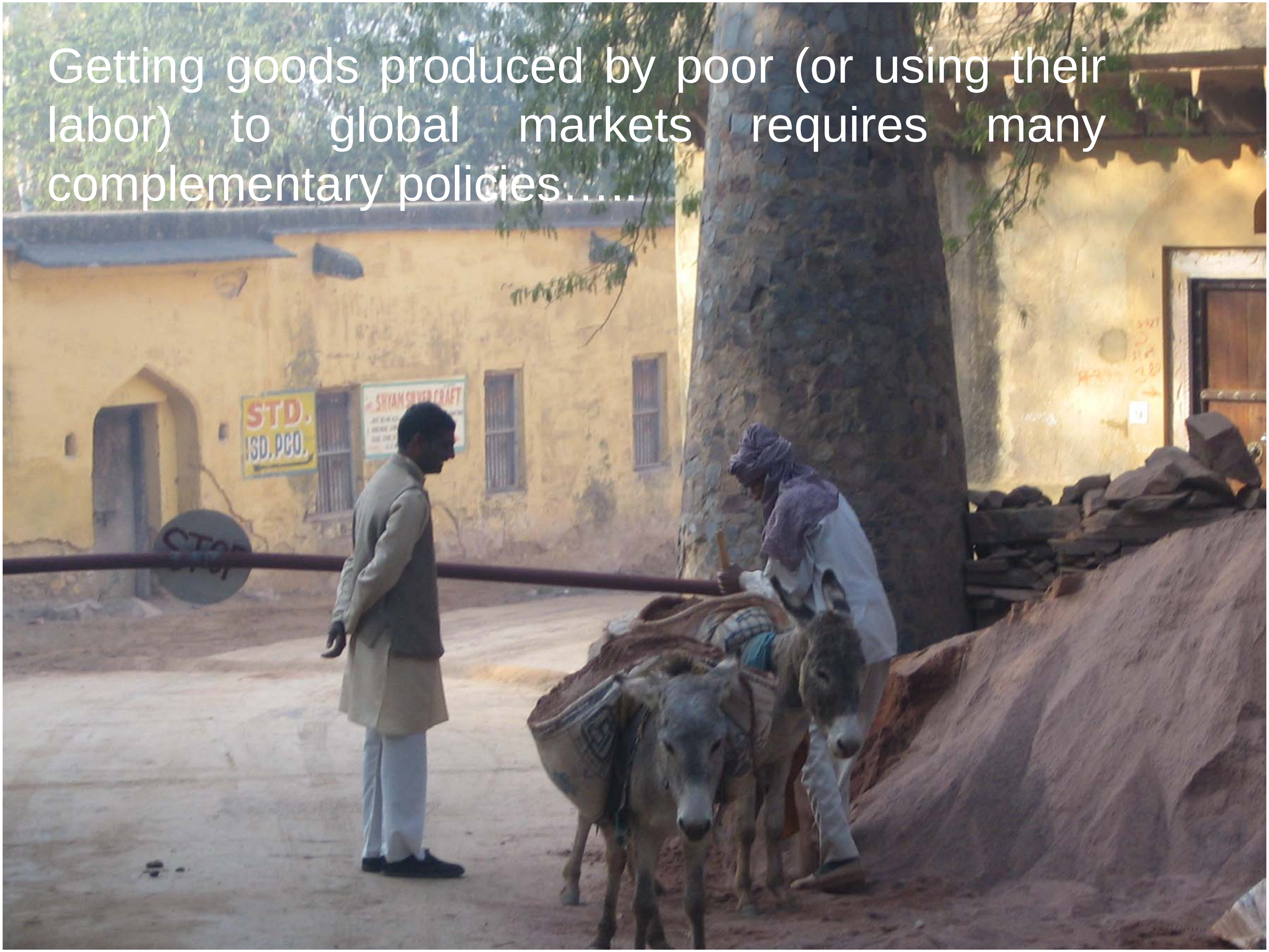
What is the “Orthodox” view? Poor workers gain in developing countries from opening up to trade because these countries export goods that use a lot of unskilled labor (Anne Krueger)

Why is this viewpoint wrong?

- Workers cannot easily relocate to expanding sectors
- Countries protect sectors more that use unskilled labor
- Exporters/foreign firms use skilled labor even in unskilled-labor rich countries
- Getting goods produced by poor (or using their labor) to global markets requires many complementary policies (infrastructure, human capital development)


Exporters and foreign firms use skilled labor
even in unskilled-labor rich countries

Getting goods produced by poor (or using their labor) to global markets requires many complementary policies…..



BUT generally true that poor in expanding sectors gain

- Unskilled in countries with a comparative advantage in exporting unskilled intensive goods to rich countries (Poland)
- Poor wage earners in sectors receiving DFI (Mexico, India, Poland)
- Poor wage earners in sectors with export growth (Mexico, India, Poland, Colombia)

Implication: poor countries need access to rich country markets for poverty reduction

Poor in previously protected sectors lose

- The poor in urban sectors with tariff reductions (Colombia)
- Small farmers competing with higher imports (small corn farmers in Mexico)
- Rural agricultural labor restricted from relocating due to rigid labor laws (India)

Implication: possible to identify the poor who will be hit hardest by trade reforms, and provide social safety nets (Mexico)

Financial Integration: DFI and Aid help the poor, while currency crises hurt the poor

- Foreign investment reduces poverty (India, Mexico)
- Food aid benefits the poor, who are net consumers (rather than net producers) of agricultural goods (Ethiopia)
- Currency crises, premature capital account liberalization costly to the poor (Indonesia)

Bundling trade reform with complementary policies more likely to lead to gains for poor

- Importance of Complementary Policies
  - Lack of labor mobility impedes adjustment. Workers need assistance moving from contracting (import-competing) to expanding (exporting) sectors
  - Exporters need educated workers even in labor-rich countries
  - Lack of complementary inputs (infrastructure, technology, credit) inhibits movements from subsistence agriculture to cash crops
  - Lack of domestic institutions, rule of law, capital market development restricts gains from access to international capital markets
- Income support—carefully targeted—can be an important safety net
- Market access to developed country markets critical (agriculture, textiles)

Concluding Comments

- Trade integration associated with higher growth, growth associated with poverty reduction, but no evidence of significant link between trade and poverty
- Trade and financial integration associated with rising inequality, higher consumption volatility in poor countries
- Simple interpretations of orthodox trade models need to be abandoned
- Poor in expanding (FDI/exporting) sectors gain
- Financial crises hurt the poor
- Poor in contracting (import-competing) sectors lose
- Complementary policies are critical