Impact of Globalization on the Poor in Africa, Asia and Latin America

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1 Introduction

Alongside the issue of climate change, 'globalization' and 'poverty' epitomize two of the most pressing international development issues today. Despite the enormous potential of globalization in accelerating economic growth and development through greater integration into the world economy, the spread and transfer of technology, and the transmission of knowledge, its impact on poverty reduction has been uneven and even marginal in some regions such as in much of sub-Saharan Africa (SSA). Both the prevalence and depth of poverty in many parts of the developing world remain unacceptably high.

A question often raised is whether the actual distribution of gains from globalization is fair and, in particular, whether the poor benefit proportionately less from globalization—and whether they could actually be hurt by it under some circumstances. The risks and costs brought about by globalization can be significant for fragile developing economies and the world's poor. The downside of globalization is most vividly illuminated at times of periodical global financial and economic crises. The costs of repeated financial crises fuelled by the globalization process have been borne overwhelmingly by the developing world in recent decades, and often disproportionately so by the poor who are the most vulnerable. On the other hand, the benefits from globalization during boom times are often not shared widely and equally in the global community.

The fear that the poor have been bypassed, or actually hurt, by globalization was highlighted by the findings from a number of recent studies, which point towards a continuing prevalence of high inequality in world income distribution and limited—if not a lack of—income convergence among participating national economies and across regions.[3] The regional trends in income inequality measured by the Gini coefficient show that within country inequality has increased markedly since the early 1980s in all regions except in the group consisting of the advanced high income OECD countries. (Milanovic 2005a, 2005b; Birdsall 2006). Within high income countries too, there are many that experienced growing inequality.

3 See Nissanke and Thorbecke (2006b) for a review of literature and more detailed discussion on the concepts used for analysing the trends in world inequality and empirical evidence. Milanovic (2005a, 2006) provides a detailed empirical analysis of 'global' income inequality. For the historical trends towards income divergence see Pritchett (1997). Quah (1996) also discusses the twin peaks in world distribution dynamics, which are characterized by the tendency for stratification and polarization.

The progress on poverty reduction has also been uneven. The share of the population of developing countries living below US$1 per day declined from 40 per cent to 21 per cent between 1981 and 2001 and fell further to 18 per cent in 2004, but this was mainly achieved by the substantial reduction of the poor in Asia, in particular in China.[4] Furthermore, over the period 1981–2004, the total number of people living under US$2 per day has actually increased worldwide by about 100 million to 2.5 billion in 2004, while the share of the world's population receiving less than US$2 per day fell from 67 per cent in 1981 to 48 per cent in 2004.[5] There is a clear disparity in the regional trends in poverty reduction. While East Asia and the Pacific experienced the sharpest reduction in the number of poor living below US$1 per day, poverty has increased significantly in Africa in terms of poverty incidence as well as the depth of poverty.[6]

Though any trend in poverty and income inequality observed so far cannot be exclusively or even mainly attributed to the 'globalization' effect as such, these various estimates can not dismiss the concerns raised that the globalization process, as it has proceeded so far, may have had adverse effects on income distribution and on poverty among some segments of the population.[7] Indeed, while most objective observers would argue that globalization is likely to have contributed to poverty alleviation on a net basis, it is also known to have created winners and losers at numerous levels throughout modern history.[8] These concerns have generated a passionate debate worldwide as well as a powerful anti-globalization movement.[9]

The extent of controversy surrounding this debate reflects the fact that globalization is not a process, proceeding neutrally in a policy vacuum. Rather, it is a policy induced condition.[10] Globalization is not purely driven by new technological innovations and progress or by 'neutral' market forces and other inescapable socio-political forces, as often depicted in popular writings.[11]

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4 Chen and Ravallion (2004, 2007). Chen and Ravallion (2007: 2) show that 'when China is excluded, the number of people living on less than US$1 a day is fairly static with no clear trend'.

5 Chen and Ravallion (2007).

6 See Wade (2002) and Deaton (2001, 2002) for critical discussions of the World Bank's estimates of global poverty and inequality used in these studies.

7 The losers could include some of those who have actively participated in the process of globalization (see Aggarwal 2008 for such an example).

8 See Williamson (2002), among others, for winners and losers from globalization in modern history.

9 For a critical literature review of the effect of globalization on inequality, see for example Culpeper (2002) where a set of triangular relationships between globalization, growth, and inequality is systematically discussed.

10 See Kozul-Wright and Rayment (2004) for an extensive discussion.

11 Helleiner (2001) emphasizes the need to distinguish two different phenomena associated with the term 'globalization'. Whilst the first is referred to as the shrinkage in space and in time that the world has experienced as a consequence of technological revolutions in transport, communications, and information processing, the second usage points to policy choices and external liberalization involving political, economic, and social choices. As he notes, despite this clear distinction, the recent association of external liberalization *policies* with the technology-driven *fact* of globalization has contributed to the terminological confusion. For discussion on the effects of

In particular, the current phase of globalization is, to a certain extent, an outcome emerging from the global consolidation and diffusion of the economic policy paradigm, emphasizing benefits and positive features of the liberalized policy regime. This paradigm has been questioned previously in the context of the fiercely contested debate among development economists on the appropriate roles of markets versus states.

As the process of economic integration has intensified since the 1990s, the question of how globalization affects the world's poor has become one of the central issues in international political economy and international relations, as many of the current problems facing the global community are related to how fair the international economic and political system is perceived *vis-à-vis* the poor in developing countries. However, the precise nature of the various mechanisms through which globalization has altered the pattern of income distribution and the conditions facing the world's poor are yet to be carefully analysed. This is because the globalization–poverty relationship is complex and heterogeneous, involving multifaceted channels. It therefore poses a challenging task for economists, both theoretically and empirically.

Indeed, it is highly probable that these relationships are non-linear in many aspects, involving several thresholds effects. Each subset of links embedded in the *globalization (openness)–growth–income distribution–poverty nexus* can be contentious and controversial. Besides the 'growth' effects of globalization on poverty (that is, the effects of globalization on poverty filtered through economic growth), the process of increased integration within the world economy is known to create winners and losers directly through other channels, affecting both vertical and horizontal inequalities (Ravallion 2004a). Because these multifaceted channels interact dynamically over space and time, the net effects of globalization on the poor can only be judged on the basis of context specific empirical studies. Cross-country studies requiring precise measurements and definition of the two key concepts—globalization and poverty—tend to fail to give robust insight into this critical nexus. Both concepts are multidimensional, and not easily captured in a composite index that may be used in a meaningful manner in cross- country comparative studies or regressions.

Building on earlier research projects, the United Nations University World Institute for Development Economic Research (UNU-WIDER) initiated a project on 'The Impact of Globalization on the World's Poor' in 2004. The main objectives of the project were to produce a set of rigorous theoretical and empirical economic studies, which would: (i) deepen our understanding into how conditions facing the world's poor have been evolving under the forces of globalization; and (ii) provide a framework yielding the elements of a strategy for 'pro-poor globalization'.[12] In addition to the methodological and conceptual project conference held in Helsinki, in October 2004, the programme comprised three regional project conferences focusing on Asia (held in Tokyo), Africa (Johannesburg), and Latin America (Rio de Janeiro) during 2005–

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technological progress on the shrinkage in space and time, see Cairncross (1997) and Bairoch and Kozul-Wright (1996).

12 Machiko Nissanke and Erik Thorbecke are the co-directors of this project. The aim of the project is to focus on the predominantly economic manifestations of globalization, hence, it does not attempt to provide a fully comprehensive and multidisciplinary treatment of the impact of globalization on poverty. It would have been overly ambitious to take on board the task of assessing the effects on poverty of all other dimensions of globalization such as cultural, social, and political.

06.[13] The project generated over the course of 2004-2007 a total of approximately sixty case studies which have come out or will come out in three volumes and three special issues of journals.

In the project framework paper (Nissanke and Thorbecke, 2006a, 2006b), various channels and transmission mechanisms are identified and explored through which the process of globalization affects different aspects and dimensions of poverty in the developing world. The fourteen papers appearing in the first two project volumes (Nissanke and Thorbecke 2006d, 2006e) explore through either general conceptual and analytical discussions or through detailed empirical analyses several of these distinct channels operating within the globalization–inequality–poverty nexus.

Significant differences in initial conditions—natural resource endowment, quantity and quality of human capital, institutional framework, quality of governance—as well as distinct internal dynamic processes of institutional and socio-political change triggered by the forces of economic integration have influenced the poor in Asia, Africa, and Latin America very differently.[15] At an aggregate level, there are discernible characteristics, specific to each of the three developing regions, of the ways in which globalization has affected the poor. This merits a comparative analysis of each region's experiences with globalization and integration.

While there are clear inter-continental differences in the effects of globalization on the poor it is also true that significant differences can prevail *within* each regional block as well. Focusing on different manifestations of globalization and channels through which the latter affects poverty, the case studies in the present volume cover the spectrum from broad macroeconomic regional and country analyses to micro-oriented village studies in each of the three continents. The case studies illustrate clearly that the impact of globalization on poverty is extremely context specific, reflecting the heterogeneous and complex nature of the globalization–poverty nexus.[16]

The remaining part of this overview paper is structured as follows: Section 2 presents a brief summary of our analysis of channels and transmission mechanisms through which the process of globalization affects different aspects of poverty in the developing world. Section 3 provides a comparative analysis of the main characteristics of the ways by which the poor in three different regions are affected by globalization. On the basis of a comparative analysis of the regional experiences with, we conclude with an outline of some policy measures that could make globalization more pro-poor.

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13 See Nissanke and Thorbecke (2006d, 2006e) for the main findings of the papers presented at the conceptual and methodological conferences in Helsinki. Nissanke and Thorbecke (2006c) formulate a preliminary policy framework for encouraging globalization to be more pro-poor.

15 In presenting their cross-country regression analyses on the globalization–inequality–poverty nexus for developing and transitional economies from different regions, both Heshmati (2006) and Kalwij and Verschoor (2006) underscore the significance of regional variations.

16 See also Winters et al. (2004) for a detailed discussion on context-specific effects of trade liberalization on poverty in developing countries.

2 Channels Linking Globalization to Poverty

What are the transmission mechanisms through which the process of globalization affects poverty directly and indirectly? The first and most important of these mechanisms is the globalization–growth–inequality–poverty channel. Other channels in the globalization–poverty nexus operate, respectively, through changes in relative prices of factors of production (labour and capital) and commodities; movements of capital and labour migration across borders and within countries; the nature of technological change and technological diffusion; the impact of globalization on volatility and vulnerability; the worldwide flow of information; global disinflation; and institutions.

2.1 The Globalization–Growth–Inequality–Poverty Causal Chain

To analyse and understand the impact of openness through the 'growth' channel on poverty, the *globalization–openness–growth–inequality–poverty* causal chain has to be scrutinized link by link. Figure 1.1 illustrates the various links, from globalization to poverty, as discussed in the economic literature. Greater openness is the major manifestation of globalization. The links shown in the figure are from openness to growth, from openness to income distribution (inequality), from growth to income distribution and vice versa, from growth to poverty, and from income distribution to poverty.

[[insert Figure 1.1 about here]]

2.1.1 The Openness–Growth Link

Policies of openness through liberalization of trade and investment regimes and capital movements have been advocated worldwide for their growth and welfare enhancing effects on the basis of the propositions embedded in the well-known economic theories of international trade, investment, and finance. Indeed, openness through trade, foreign direct investment (FDI), and financial markets typically increases the flow of goods and capital across national borders and can contribute significantly to economic growth. However, the direction of causality in this link is still debated (the present consensus is that trade contributes to growth rather than vice versa) as well as how trade and capital flows could be interlinked into a virtuous circle. Furthermore, the positive openness–growth link is neither automatically guaranteed nor universally observable. The growth enhancing effects of trade openness depend critically on the way and extent to which a country is integrated into the global economy, as discussed later in Section 3.[17]

Similarly, the transfer of technology, skills, and management know-how that is assumed to accompany FDI is not necessarily automatic or guaranteed. Furthermore, the postulated positive effects of portfolio and other capital flows (hot money) on growth have been challenged and increasingly questioned in recent years. Even some IMF studies acknowledge that it is difficult to establish a strong positive causal relationship between financial globalization and economic growth.[18] In addition, short term capital flows contribute to the increased vulnerability to external shocks of the recipient developing countries. Indeed, there is much empirical evidence that openness leads to more 'within-country' inequality through the openness–inequality link.

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17 Sanchez (2003: 1979) notes that 'the causality link between trade openness and long run growth is not engraved in stone'.

18 For example, see Prasad et al. (2003) and Kose et al. (2006). Nissanke and Stein (2003) present a critical view on the effect of financial globalization on economic development in emerging market economies.

A large number of empirical studies based on cross-country regressions have been conducted to show the beneficial effects of an open economy regime on growth, for example., Dollar (1992), Sachs and Warner (1995a), and Dollar and Kraay (2001, 2002).[19] However, the validity of these cross-sectional empirical exercises has been contested on technical grounds by many researchers.[20]

2.1.2 The Growth–Inequality–Poverty Interrelationship

The second link in the causal chain from openness to poverty through the growth effect is the interrelationship between growth and inequality. First, relating the causal chain from income and wealth inequality to growth (the 'inequality–growth' link), there are two conflicting theoretical strands. The traditional approach views income inequality and wealth inequality as necessary conditions for faster capital accumulation and economic growth at the earlier stage of economic development due to the higher propensity to save among the rich as well as the existence of investment indivisibilities and incentive effects.[21] From this theoretical perspective, the desirability of an unequal income distribution is rationalized on economic grounds, that is. on the basis of the claim that 'more poverty today is a precondition to more economic growth and less poverty in the future'.[22]

In contrast, the 'new' political economy theories linking greater inequality to reduced growth operate through a number of sub-channels, including: the diffusion of political and social instability leading to greater uncertainty and lower investment; unproductive rent seeking activities; high transaction costs; and increased insecurity of property rights.[23] In addition, wide income and wealth disparities can impact on education, health, and crime, respectively, through such manifestations as underinvestment in human capital, malnutrition leading to low worker productivity, stress and anxiety. In turn these manifestations may contribute to lower long term growth.[24]

The rejection of the Kuznets hypothesis of the inverted U-shaped relationship between growth and inequality by a number of empirical studies provided much impetus to re-examine the opposite causal flow in the link, that is the 'growth–inequality' link.[25] Many earlier development economists noted that economic growth, if left to market forces alone, tends to be accompanied by more

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19 See World Bank (2002) for a summary of these cross-country studies on the openness–growth link.

20 See Rodriguez and Rodrik (1999) for an excellent critical assessment of these cross-sectional studies. See also Pritchett (1996) for a detailed discussion and comparison among various measures used in empirical analyses of outward trade orientation in LDCs. Clearly, the simple trade intensity index (exports plus imports/GDP)—a standard variable frequently used to measure a country's outward policy orientation in cross-country regressions—is unsatisfactory and inappropriate to be used for testing the hypothesis on the trade openness–growth link.

21 See Kaldor (1956) and Aghion et al. (1999) for discussion on the savings effects and the investment effects respectively.

22 See Thorbecke (2006) for a critical review of the traditional approach to the inequality–growth link.

23 See Thorbecke and Charumilind (2002).

24 See also Aghion et al. (1999).

25 See Thorbecke and Charumilind (2002) for a comprehensive review of this new political economy literature on the subject.

inequality. Growth is inherently inequalizing.[26] Hence, according to the new political economy of development approach growth patterns yielding more inequality in the income distribution would, in turn, engender lower future growth paths resulting in less of a growth induced poverty reduction, as Figure 1.1 illustrates.

The conclusions drawn from the above analysis challenge the dominant mainstream views in development economics derived from a number of World Bank studies.[27] The latter argue that there is no clear association between inequality and growth; the long term distribution is broadly stable and liberalization does not affect distribution; and that growth is distribution neutral: hence growth is the only realistic option. For example, the Dollar and Kraay studies (2001; 2002) state that 'since the share of income going to the poor does not change *on average* with growth, the poor benefit from growth', and 'trade is good for growth and growth is good for the poor'.

However, the methodology used in yielding these results and more particularly the underlying econometric techniques have been challenged. A critical question in understanding the *growth–inequality–poverty interrelationship* is whether or not inequality is an impediment to poverty reducing growth, or in other words, whether high inequality attenuates the *growth elasticity* of poverty. Several empirical studies confirm that the elasticity of poverty with respect to growth is found to decline with the extent of inequality.[28]

Thus, we argue that while growth may benefit the poor, the ultimate poverty reduction effects will depend on how the growth pattern affects income distribution. Inequality is the *filter* between growth and poverty reduction.[29] If growth leads to an increase in income inequality the poor may benefit only slightly or, in some instances, actually be hurt by globalization induced economic growth. We argue specifically that the *pattern* of economic growth and development, rather than the rate of growth *per se*, may have significant effects on a country's income distribution and poverty profile, as growth can be pro-poor, distribution neutral, or even at the limit poverty increasing.

Indeed, the recent debate on the meaning of *pro-poor growth* is directly related to the complex triangular relationships among poverty, growth, and inequality. At one extreme pro-poor growth can mean that growth is only required to yield a positive reduction of poverty. In this sense, it would be enough for a major increase in GDP per capita to reduce poverty by one person to satisfy the above definition. Hence any elasticity of poverty reduction with respect to growth algebraically larger than zero would be considered as pro-poor. This is a *weak* definition. Although widely used and part of the conventional wisdom, it has elicited a reaction within the development community leading to an alternative definition of pro-poor growth requiring the poor to benefit more than proportionally from growth than the non-poor (a *strong* definition). A corollary of this relative definition of pro-poor growth is that it will bring about a more equal (or less unequal) distribution of income. In this sense, poverty reduction would require some combination of higher growth and a

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26 For example, Myrdal (1957), Rosenstein-Rodan (1943), or Hirschman (1958) as noted in Milanovic (2005b).

27 Deininger and Squire (1996); Li et al. (1998); Dollar and Kraay (2001, 2002).

28 For example, see Ravallion (2002)

29 See Naschold (2004) for empirical evidences showing that in least developed countries the distribution effects are as important as the growth effects for poverty reduction, while growth effects are larger in other low income and middle income countries.

more pro-poor distribution of the gains from growth.[30] Hence what is relevant for poverty reduction is a 'distribution corrected' rate of growth,[31]and in our view, growth is considered truly pro-poor if in addition to reducing poverty, it also decreases inequality consistent with the strong definition of pro-poor growth. Economic growth can be considered genuinely pro-poor only if growth is accompanied by a decline in inequality, in such a manner that the poor benefit relatively more than the non-poor (Kakwani and Pernia 2000).

2.2 Other Channels in the Globalization–Poverty Relationship

In addition to the 'growth' conduit, there are other major channels through which globalization affects poverty. These channels may be largely responsible for explaining why the poor have not emerged as larger beneficiaries of contemporary globalization. For example, according to the theoretical prediction embedded in the Stolper–Samuelson theorem, developing countries abundantly endowed with unskilled labour should experience a decline in income inequality through an increased demand for unskilled labour, while unskilled labour in developed countries would lose out. However, the empirical evidence reveals that the ratio of the average wage rates between skilled and unskilled workers has been increasing in many developing countries, (see Section 3). Several specific features associated with the current phase of globalization, explain why such a theoretical prediction does not hold. We highlight next some of the critical additional channels through which globalization ultimately affects poverty.

2.2.1 Technology and Factor Mobility in the Globalization–Poverty Nexus

As the bulk of technical change emanates from research and development (R&D) activities in developed countries in response to local prevailing conditions, the nature of technical progress and new technology is heavily biased in favour of skilled and educated labour.[32] Hence, technical change tends to be labour saving and skill-biased, and new technology is complementary to capital and skilled labour, while it is a substitute for unskilled labour. Hence, technical change tends to increase inequalities in both developed and developing countries.

Furthermore, technological diffusion and access to new technology is neither universal nor spontaneous; it has become increasingly skewed and asymmetrical. Intensified privatization of research in bio-technology or pharmacology especially have adverse effects on access of developing countries and the poor to new technology, as evident in the debate surrounding the Trade-Related Intellectual Property (TRIPs) issues in the WTO negotiations. The widened productivity differences resulting from these asymmetries explain cross-country wage/income inequality. The initial knowledge gap and unequal, skewed access to technology and knowledge have adverse implications for world income distribution. This is particularly critical since the current wave of globalization is characterized more by trade in knowledge and information rather than trade in goods, which was the case with the earlier wave of globalization.[33]

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30 Woodward and Simms (2006) argue that global economic growth would not reduce poverty on account of the disproportionately adverse net impact of climate change and worsening income distribution on the poor.

31 Ravallion (2004b).

32 Culpeper (2002).

33 Baldwin and Martin (1999), Solimano (2008).

The ‘perverse’ factor movements hypothesis could provide another explanation. Capital and skilled labour do not migrate to poor countries as much as among developed countries. Rather, there is a tendency for skilled labour to migrate from developing countries to developed countries, as the massive migration of African nurses and medical doctors to the US and Europe testifies, while unskilled labour migration tends to be strictly controlled. Income convergence among the globalizing countries during the first wave of modern globalization was driven primarily by migration. Sixty million people, including largely unskilled workers, migrated from Europe to North America and other parts of the new world between 1870 and 1914. In contrast, the extent of cross-border mobility differs significantly between skilled and unskilled labour in the current phase of globalization. Unskilled workers from developing countries face increasing obstacles in their attempts to migrate to developed countries. In consequence, wage equalization does not take place through labour migration, as was the case in the previous globalization era.

Furthermore, the process of capital market liberalization brings about a propensity for capital flight to developed countries, particularly during periods of financial instability and crisis. Today’s cross-border portfolio capital flows are also characterized by *diversification* finance rather than *development* finance (Obstfeld and Taylor 2001). Typical capital transactions today have taken increasingly the form of asset swapping for risk hedging and shedding rather than financing productive investment in capital scarce developing—contrary to what the standard text book theories would predict. FDI has also been dominated by intra-industry FDI, that is two-way flows of investment among developed countries in the current wave of globalization, compared with FDI flowing mainly from developed countries to developing countries under the previous wave of globalization.[34]

Furthermore, the differentiated degree of cross-border factor mobility (skilled labour and capital vs. unskilled labour and land) affects the functional income distribution between labour and capital against the former. Wage equalization does not take place through labour migration, as was the case in the previous globalization era. Some workers are losing out, as *de facto* labour mobility takes place through the increasingly free cross-border capital mobility and trans-national corporations’ (TNCs) ability to relocate production sites in response to changes in relative labour costs. In response to the associated footlooseness of production sites and in fear of driving away TNCs, governments of developing countries are less likely to enact regulations to protect and enhance labour rights or protect local environments.[35] The unwillingness or inability to tax international mobile financial capital in the process of tax competition and in fear of capital flight and asset migration, has, among other conditions, contributed greatly to the erosion of the capacity of governments to raise revenues for redistributional purposes.[36] Further, the poor and unskilled are most adversely affected by asymmetries in market power and access to information, technology and marketing as well as TNCs activities and the dominance of TNCs in commodity value chain.

2.2.2 Vulnerability, Information Diffusion, and Institutions in the Globalization–Poverty Nexus

Globalization increases uncertainty via the greater variation in income and expenditure caused by global shocks, such as the various financial crises that have hit Latin America and Asia in the last two decades. Further, while globalization can be a major engine for growth in aggregate, globalization either introduces or exacerbates other trends that affect people’s well-being as much if

34 Baldwin and Martin (1999).

35 Basu (2003).

36 Tanzi (2001) discusses various effects of globalization on the tax system under ‘fiscal termites’.

not more than income, for example, through the increasing flow of information about the living standards of others, both within and beyond country borders. This flow of information can result in changing reference norms and increased frustration with relative income differences, even among respondents whose own income is rising.

Institutions are also a critical factor for determining how globalization affects the poor, as they mediate the various channels and mechanisms through which the globalization process affects poverty. Institutions act as a filter, intensifying or hindering the positive and negative pass-through between globalization and poverty, and can help explain the diversity, heterogeneity, and non-linearity of outcomes.[37] Thus, on the one hand, the impact of globalization on the poor is mediated by domestic political economy structures and institutions such as social polarization, oligarchic structures, and predatory regimes, which may bias, confiscate or nullify the gains from globalization for particular groups of poor. On the other hand, the positive effects of globalization on growth and poverty can be found when institutional conditions are characterized by such features as political participation, social cohesion, and management of social conflict arising directly from globalization effects. In particular safety nets and social protection schemes can reduce significantly the vulnerability of the poor to external shocks triggered by the forces of globalization.

3 Regional Characteristics Influencing the Globalization–Poverty Nexus

3.1 Income Divergence in the South under Globalization

Any attempt at estimating rigorously the impact of the globalization process on socio-economic performance (and more specifically on poverty) faces the almost insurmountable obstacles of the lack of a plausible counterfactual scenario. In order to derive robust inferences, one would have to compare the performance under the present forces of globalization to an alternative scenario of no or limited globalization. Within limits this could be done very approximately and roughly within a computable general equilibrium model for a given country or region of a country but this task is clearly infeasible for continents as large and diverse as Latin America, SubSaharan Africa and Asia.

Instead we attempt to describe some major recent socio-economic trends in each of these continents that one can legitimately claim were influenced by the globalization process even if they were, in fact, the net consequence of a whole series of factors with some of them independent of the forces of globalization. The general picture we paint with a broad brush can usefully serve as a backdrop to the specific case studies generated under the present WIDER project that link more closely specific manifestations of globalization (such as trade liberalization taking the form of tariff reduction, financial liberalization and international labor migration) with context-specific outcomes within different settings ranging from micro-oriented village studies to macro-oriented country studies.

From our discussion so far it is clear that both economic theories and empirical evidences point to the complex and heterogeneous relationships underlying the globalization–inequality–poverty nexus. The recent large increase in world income disparity between the rich and the poor can at least be partially attributed to the forces shaping the current process of globalization. In particular,

37 See Sindzingre (2006).

the observed 'big time' divergence' in inter-country income levels (when each country is weighted equally) brings into question the validity of the openness induced income *convergence* thesis, advanced by Sachs and Warner (1995a) and others.

The reality is that the mere adoption of open trade and investment regimes does not guarantee, or necessarily promote, developing countries' entry into the 'income convergence club'.[38] Based on a 'human development trap model', Mayer-Foulkes (2008) shows that in the presence of multi-equilibria, development and underdevelopment coexist as steady states under globalization. His analysis leads him to conclude that globalization is a necessary, but not a sufficient condition for convergence to development. Indeed, many poor countries that have opened their economies since the 1980s have fallen behind, not having succeeded in reaching the take-off point, necessary for benefiting from positive forces of globalization.[39] In addition, many countries that have seen a substantial increase in their trade/GDP ratios have undergone a worsening of their income distribution. Sanchez (2003) reports the results of a cross country regression analysis that show: (i) integration into the global economy has had deleterious consequences for low income countries. Among these, more open economies have experienced increased inequality and lower growth; (ii) amid middle income countries, more integration is associated with increased growth and lower inequality. Though it is well recognized that cross-country regressions tend to produce rather disparate results, depending on data, model specifications and selected estimation periods, empirical studies of countries and regions generally point to the existence of *threshold* effects in the globalization–inequality–poverty nexus, as postulated in Section 1.

It can be argued, therefore that the conundrum of the persistent 'non-convergence' of world per capita income should be explicitly addressed in terms of structural features of the global economic relationships as they evolved over time and institutional and socio-political conditions found in participating countries. The income convergence trend among nation states, to the extent that it has been observed historically, is likely to be explained more effectively by the specific nature of the integration and specialization process followed by sub-groups of countries, rather than by the degree of openness of the trade and investment regimes *per se*, as often claimed.

First, countries need to have reached the take-off point before they can take advantage of the potential benefits of openness and globalization. One of the critical reasons why globalization may not be working for low income developing countries lies in the fact that the effects of international trade on growth are critically dependent on the pattern of specialization and integration. By treating two sectors symmetrically, the conventional Heckscher–Ohlin trade model (consisting of two countries, two sectors and two factors) shows that two countries equally reap aggregate gains from trade through efficiency gains.[40] In reality, however, the pattern of specialization does matter for welfare implications of a trade induced growth path on at least two accounts.

38 This point was emphasized in Dowrick and DeLong (2001).

39 See six case studies focusing on SSA settings in Nissanke and Thorbecke (2008b) for empirical evidence. Dowrick and DeLong (2001) go further to suggest that many poor countries that have opted for opening their economies since the 1980s have fallen behind, not just relatively but absolutely in terms of both income levels and structural development.

40 This two-sector model of international trade can be easily extended to N-sector models (for example, see Dornbusch et al. 1977).

Two sectors need not be symmetrical, first, through the well-known immiserizing effect of trade *à la* Bhagwati that is the terms-of-trade (TOT) effects. Though many dismiss the likelihood of such an effect in a small economy, low income countries dependent on the exports of a limited range of primary commodities face a deterioration of TOT through the ‘fallacy composition effect’. In the 1980s and 1990s, many primary commodity exporting countries, which implemented structural adjustment programmes, underwent simultaneous export drives, leading to depressed prices in many export commodities.[41]

Furthermore, two sectors are not necessarily symmetrical because of the possible differential impact of dynamic scale economies- that is dynamic externalities through technological spill-overs and the accumulation of knowledge capital. As the endogenous growth theory emphasizes, it is the difference in the scope for scale economies that largely accounts for diverging growth rates among countries in the current phase of globalization. A country specializing in an industry endowed with a larger positive externality would experience a faster growth rate compared with the trading partner that specializes in an industry with a weaker externality. Thus, the growth rates of the two trading countries could differ considerably, depending on the pattern of specialization.

If a country follows the Rybczinski line dictated by static comparative advantage with given relative resource endowments, the country with an initial comparative advantage in ‘non-dynamic’ sectors may end up in a low equilibrium trap through the evolving patterns of production and trade. Similarly, the effects of FDI on host economies diverge enormously, depending on the sectors into which TNCs are attracted to move in and invest. Low income developing countries tend to attract natural resource based FDI in extracting mineral resources or FDI geared towards the lower end of TNCs’ vertical integrated global operations (their global value chain) such as simple assembly line operations. These sectors and activities are characterized by little dynamic externalities and knowledge and skill spill-overs.

Seen from this perspective, openness *per se* is not sufficient to ensure that development will follow from integration into the global economy. Baldwin and Martin (1999) note that in contrast to the experiences under the late nineteenth century globalization wave, when an enormous North-South income divergence was produced as a result of industrialization of the North at the expense of deindustrialization of the South, the current wave of globalization has industrialized the South whilst the North is experiencing deindustrialization.

In reality, however, the globalization experiences in the South tend to be very heterogeneous. In this context, we argue that developing countries have to undergo substantial changes in trade and production structure, so as to be able to reap more benefits from the dynamic forces unleashed by the current phase of globalization and experience income convergence. Indeed sharp divergences have emerged in the development paths followed by different countries in the South over the recent decades. These divergences can be explained by the distinct internal patterns of economic growth and the forms of integration adopted. As a consequence some countries in the South were able to benefit from *virtuous* cycles of globalization- induced growth, while others were left behind in

41 See Maizels (1992) and Nissanke and Ferrarini (2001, 2004). In this context, Birdsall (2002) also draws attention to the fact that measured by the trade-GDP ratio or tariff rates, most commodity-dependent countries have not been more reticent than less commodity-dependent countries about participating in international trade, but the former group has failed to grow (especially after 1980), as they have remained dependent on exports of primary commodities.

vicious cycles of globalization- induced decline. Not only did the growth rates diverge widely but there emerged a marked difference in the extent to which and ways through which benefits of economic growth trickled down to the poor as these developing economies were integrating into the global economy. The sharp differential impact of the forces of globalization on the poor in the developing world can be analysed by focusing on the integration experiences of three broad regions (continents): Africa, Asia, and Latin America, respectively.

3.2. Comparative Globalization Experiences

3.2.1 Integration Experiences in Sub Saharan Africa

Following largely an inward oriented development strategy in the early decades of the post independence period, the majority of SSA countries failed to take advantage of the potential provided by the dynamic growth spurt that characterized the global economy in the 1970s and 1980s. The region was largely marginalized and experienced slow growth and stagnation. With growing recognition of their disadvantageous position, most SSA countries over the past two decades have searched for ways to accelerate their participation in the global economy. Indeed, most economies in SSA significantly liberalized their trade and investment policy regimes as part of SAPs since the mid 1980s. Today, SSA is not behind other developing regions in terms of trade openness, as conventionally measured through a trade intensity index (imports and exports relative to GDP).[42] In spite of the increase in trade intensity, however, Africa's share of total world trade has fallen over the last two decades. Many countries in SSA have also intensified their efforts to attract FDI with the help of various fiscal and other incentive measures. However, FDI flows to the region so far have been largely limited to extraction of oil and other natural resources.

Despite some improvements in aggregate measures of integration intensity, SSA presents a clear example in support of the argument that the shift to an open policy regime alone is not sufficient to bring about economic growth and consequent poverty reduction.[43] After two decades of reforms dominated by liberalization, privatization and deregulation, the economies of SSA have not yet been able to escape from the 'growth tragedy' syndrome—the term popularly used in characterizing the region's dismal economic performance in the comparative growth literature.

A large number of studies have emerged seeking to explain the differences in economic performances across developing countries through theoretical modelling and cross-country regression analyses in a framework of endogenous growth theory. These studies have extended further the list of factors contributing to the overall weaker growth performance of many African economies to include an array of variables such as natural and institutional endowments, the quality of institutions and governance and geography (Acemoglu et al. 2001a, 2001b; Sachs and Warner, 1995b, 1997, 2001; Rodrik et al. 2002, among others).

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42 See Chapter 3 by Round in this volume for key aggregate statistics on trends in openness, growth, inequality and poverty.

43 See Fosu and Mold (2008) and Asiedu and Gyimah-Brempong (2008) for empirical studies of the impact of trade liberalization and FDI flows on employment and poverty reduction. Both studies suggest insignificant contribution, sometimes adverse effects, of trade and investment liberalization on employment in SSA.

Referring to these studies and based on their analyses carried out within the AERC Growth project, O'Connell and Ndulu (2000) and Ndulu (2006) provide additional reasons for the slow growth of the SSA economies in terms of sovereign fragmentation, ethno-linguistic fractionalization and more generally geographical disadvantages. These conditions are seen to result in an uncharacteristically high cost of development in the region and could largely explain the lower rates of economic growth and investment, and very low productivity of investment in SSA compared with other developing countries. O'Connell and Ndulu observe that both the growth rates and investment efficiency in SSA are about half of the average obtained in other developing regions.

The recent upturn in economic growth recorded in many natural resource-rich economies in SSA is closely associated with the price hike of oil and mineral commodities in world markets. The sustainability of these high growth rates is very much dependent on a continuation of favourable exogenous factors unless the present windfalls from commodity booms are used purposely to help diversify and transform the existing economic and trade structures. Highly competent macroeconomic management over the commodity price cycle is required to avoid the 'Dutch disease' often associated with commodity booms. Otherwise, the foundation for long term economic development of these natural resource-rich economies would remain fragile.

Indeed, today, several decades after gaining political independence, the high primary commodity dependence remains one of the most conspicuous characteristics of the trade linkage of countries in SSA with the rest of the world. As UNCTAD (2002) suggests, any low income countries dependent on primary commodity exports and natural resource based structure could be locked in an *international poverty trap* through integration. It is not a mere historical accident that the beginning of the debt crisis in many countries in SSA in the late 1970s coincided exactly with that of the 'commodity crisis' (Maizels, 1992). The reluctance on the part of the international development community to acknowledge and deal with the commodity related issues effectively and in a timely fashion has entailed a huge cost in terms of forgone development opportunities to these low income countries in SSA.

The demand management of commodity dependent economies governed by external shocks should be *counter-cyclical* to the commodity price movements. Yet, at times of an externally induced balance of payment crisis accompanied by a sharp drop in domestic demand, in the absence of alternative financial facilities, these countries have been forced to adopt stabilization policy measures that aims at a further contraction in aggregate domestic demand.[44] Debt relief mechanisms, such as the HIPC and MDRI initiatives that are effective and flexible facilities of *contingency financing* to deal with external shocks on an ex ante basis have been largely absent in SSA.[45]

The failure of SSA economies to diversify and undergo structural transformation, and hence, to benefit from the technology driven, highly dynamic aspects of the on-going globalization process has led to major drawbacks in terms of low economic growth and persistent poverty. The incidence and depth of poverty has deepened in the region. According to estimates provided by Chen and Ravallion (2004), the number of poor below the US$1 a day international poverty line almost doubled in SSA from about 164 million in 1981 to 313 million in 2001. The poverty incidence (the

44 See Nissanke (1993) for a critical review of macroeconomic adjustment policies over the commodity price cycles in mineral-based developing countries.

45 See Nissanke and Ferrarini (2007) for a proposal of enacting a flexible, state-contingent debt relief mechanism in order to avoid the recurrence of debt crisis for HIPCS.

headcount ratio) in SSA reached 46 per cent in 2001—the highest of the major regions in the world. Ali and Thorbecke (2000) argue that poverty in SSA is both most prevalent and severe in rural areas.

Furthermore, as Milanovic (2003) notes, countries in SSA display a relatively high intra-country inequality. This can be seen as a puzzle as Africa should be a low inequality continent according to the Kuznets hypothesis because 'African countries are poor and agriculture based, and also because the main productive asset—agricultural land—is relatively evenly distributed in most of SSA (except the region of Southern Africa) in part thanks to the tradition of communal land holding'. (Milanovic 2003: 2). The degree of income inequality in Africa has increased sharply between the 1980s and the 1990s, as shown in Chapter 3.

There is no doubt that sustained poverty reduction requires economic growth. However, as discussed in Section 2, the *pattern* of growth does significantly affect the rate of poverty reduction. In this context, it can be argued that Africa's growth has been distinctly against the poor not only in terms of its ability to deliver the required growth rate to ensure that the poor could benefit from economic growth, but also in terms of its pattern. Economic growth in SSA, where it has occurred, has not been translated into significant poverty reduction. Critically, the nature and pattern of integration of the SSA economies into the global economy, the slow rate of structural transformation and the neglect of the agricultural sector all combined have not been conducive to generating *virtuous* cycles of globalization induced growth and poverty reduction.

Governments in SSA have systematically ignored (if not exploited) their agricultural sectors—failing to undertake pro-poor public investment in rural areas, rather, tending to extract a surplus from agriculture at an early stage of development. It has also been argued that divisive fiscal instruments such as subsidies or preferential credits were more extensively used by politicians in SSA than other regions as the favoured mechanisms to buy political support or to appease various interest groups.[47] Furthermore, with the advent of the debt crisis in the 1980s, fiscal retrenchment (hence reduced spending on rural infrastructure) has been consistently pursued as part of the stabilization-cum-adjustment policies. Governments were typically left with little capacity and resources to undertake public investment on a sustained basis. Under such conditions, it is difficult to expect structural transformation to take place. The majority in rural areas were de facto disenfranchised from the developing process. Private agents and rural farmers were likely to have refrained from making forward looking productive investments.[48] Today, many parts of SSA remain isolated from global markets and the global community as the region's access to information and technology is limited.[49]

On the whole, while globalization has made some contribution to economic growth in SSA, it has not yet facilitated the process of structural transformation required for countries in SSA to reach the take-off stage and accelerate the process of economic development and poverty reduction. Instead it

47 This line of characterization of African states is found in Bates (1981, 1983). See also Teranishi (1996)

48 See Nissanke and Aryeetey (2003) for detailed discussion on the relationships between private agents and governments in SSA in a comparative perspective with that found in East Asia.

49 See Oduro and Osei-Akoto (2008) for a detailed case study in Ghana which shows how an effective participation of the rural economy in globalization has been hindered by the absence of infrastructure and other market supporting institutions.

has increased intra-country inequality and done very little to reduce poverty. Whilst the impact of globalization on poverty is extremely context specific, the limited scope of globalization in SSA appears to be generally the result of a combination of poor initial conditions, such as fundamental disadvantages of location (disease-prone tropical countries with a harsh environment); inadequate political institutions; poor governance; extremely underdeveloped physical infrastructure, and a related high risk investment climate.[50]

3.2.2 Integration Experiences in Asia

Asia is the region widely regarded as having benefited most from the dynamic *growth* effect of the recent wave of globalization, which has also resulted in a very substantial reduction of abject poverty in many economies: poverty based on the headcount ratio of US$1 a day in China fell from 53 per cent in 1984 to 13 per cent in 2003; and in Indonesia from 38 per cent to 7 per cent over the same period; a similar progress occurred in Thailand where the headcount ratio dropped from 18 per cent in 1988 to 1 per cent in 2003; and in India where it declined from 46 per cent in 1987 to 31 per cent in 2003 (ADB 2004, 2005). The most recent estimates by the Asian Development Bank (ADB) indicate that the incidence of extreme poverty as measured by the headcount ratio below the 'US$1 a day' poverty line has further declined to 7.1 per cent in 2005 in China, while extreme poverty has practically disappeared in Thailand. In Vietnam poverty is estimated to have declined from 51 per cent in 1990 to 7 per cent in 2005 (Ali and Zhuang 2007; ADB 2007). Clearly, poverty has been steadily declining over the last three decades in most of Asia.

Furthermore, the growth pattern achieved through increased trade and FDI in *East* Asia in the 1960s and 1970s was especially seen as highly inclusive, and often viewed as a model of 'shared growth' (Ahuja et al. 1997; Campos and Root 1996, World Bank 1993). Yet, there is growing evidence that more recently inequality has been rising as part and parcel of the integration process in many parts of Asia. Hence, it is critically important to examine the mechanisms at work in the globalization–poverty nexus in Asia.

First, while many country experiences suggest that the positive openness–growth link is neither automatically guaranteed nor universally observable as noted in Section 2, there is very little disagreement over the powerful growth enhancing effects of openness through trade and FDI in the case of most Asian countries. In particular, following aggressively an 'outward oriented development strategy', most *East* Asian economies had not only managed the process of integration into the world economy much earlier than other developing countries but also upgraded their form of linkages to the global economy in the years of their rapid economic growth.

Furthermore, prior to the financial crisis of 1997–98, many of the East Asian economies registered not only 'admirable' growth performances but also accomplished a substantial poverty reduction process through dynamically evolving changes in their socio-economic structures. A number of earlier studies (World Bank 1993; Ahuja et al. 1997; Campos and Root 1996) attributed this successful growth performance to an appropriate set of economic policies and institutions well

50 See Nissanke and Thorbecke (2008b) for six case studies that examine the effects of different aspects of globalization on poverty in SSA.

suited to the conditions prevailing in East Asia during that period.[51] The relatively quick turnaround of many emerging economies in East Asia in the years following the severe crisis of 1997–98 is often attributed to their strong export performance and renewed adaptability and flexibility in responding swiftly to new opportunities offered by globalization.

Second, the structural transformation of most economies in East Asia has been facilitated considerably by the integration/globalization process. As discussed by Ozawa (2008), the catch-up process and associated growth dynamism in Asia, as a whole, can be examined in terms of the 'Flying Geese Paradigm', wherein a sequence of staggered catch-up growth has successively taken place in the region since the end of the Second World War. In addition, as Ozawa observes, poverty alleviation has been occurring, in flying-geese style (i.e., in tandem with growth) among these rapidly catching-up Asian economies. The incidence of extreme poverty is estimated to have dramatically declined from 33 per cent in 1990 to 7 per cent in 2005 in East Asia including China, from 24 per cent to 7 per cent in South East Asia and from 42 per cent to 32 per cent in South Asia respectively.[52]

Thus, the growth performance—accompanied by a substantial reduction of abject poverty—in East Asia can be explained in terms of the region wide *comparative advantage recycling* in production and export of labour intensive goods. The process involves a strong demand for unskilled and semi-skilled labour, driven by exporting labour intensive goods and attracting pro-trade FDI, bringing about effective technology, knowledge and skill transfer. Most of the East and South-East Asian economies have successfully gone through the structural transformation of their production and trade structures with continuous upgrading of their human skill endowments and technology/knowledge base. By relying on their fast evolving dynamic comparative advantages these countries were able to maximize the benefits from dynamic externalities. Their increasing specialization in sectors with large spill-overs and dynamic externalities was conducive to engendering a pattern of equalizing growth.

Third, in most of East Asia, the pro-poor pattern of public expenditure in favour of the rural poor at early stages of development produced and sustained the 'shared' growth process for some time. There were concerted efforts on the part of governments to facilitate building primary assets of the poor through such measures as an equitable distribution of land (through appropriate land reforms); extensive public provision of free and universal primary education; promotion of small scale enterprises and development of rural infrastructure—roads, irrigation, schools, agricultural support

51 The High Performing Asian Economies in the East Asian Miracle Study are Hong Kong, Indonesia, Japan, the Republic of Korea, Malaysia , Singapore, Taiwan, and Thailand. Perkins (1994) groups these eight economies into three quite distinct categories and models: (i) the manufactured export-led state interventionist models of Japan, Korea, and Taiwan; (ii) the free port service commerce dominated model of Singapore, and Hong Kong; and iii) the natural resource-rich model of Indonesia, Malaysia and Thailand. The East Asian Miracle has been subsequently subjected to several critical evaluations. For a summary of these critical reviews in a comparative perspective, see Nissanke and Aryeetey (2003).

52 According to the recent estimates (ADB 2007), the incidence of extreme poverty is still very high in both Bangladesh and India, where this ratio is estimated at 36 per cent in 2005. The incidence of extreme poverty is still very much prevalent in South Asia, where 476 million still live below the US$1 a day poverty line today. In India the headcount ratio declined but the number of poor increased from 374 million in 1990 to 397 million in 2005.

outposts, health stations, and irrigation systems. In this context, Ozawa argues that the observed pro-poorness of growth in East Asia is not purely a manifestation of market driven growth effects.

Fourth, notwithstanding the ongoing urbanization process, the great majority of the poor in Asia continues to reside in the rural areas—63 per cent at last count (Cook 2006). Yet, the accelerating rural to urban migration in response to the rapid expansion of job opportunities has contributed both to economic growth in urban areas and to the alleviation of poverty in rural areas by (i) reducing surplus labour in agriculture, and (ii) through the remittances from migrant workers that presently account for a significant share of rural household income.[53] Further, as emphasized by Hayami (2008), the employment creating impact of globalization benefited landless labourers both in urban and rural areas as an important conduit for reducing rural poverty.

Yet, it is widely acknowledged that globalization and market driven economic growth tend to increase inequality, as 'global markets are inherently disequalizing' (Birdsall 2006: 18).[54] With the current wave of globalization, 'within country' income inequality has been steadily rising (Milanovic 2005a).[55] Asia is no exception to this trend. In the early period, the prevailing initial conditions of lower levels of inequality in income and productive assets as well as public policy and institutional arrangements in many high performing East Asian economies were known to be extremely favourable to the generation of a process of relatively *shared* growth (World Bank 1993). However, the growing inequality in East Asia, including China, Thailand and Indonesia was already evident before the financial crisis of 1997–98, and the rising spatial disparity in growth performance was seen as a characteristic phenomenon (Ahuja et al. 1997). The financial crisis did undoubtedly exacerbate this trend in the region.

As detailed in a separate volume (Nissanke and Thorbecke 2008a), although both China and India have accelerated the catching up process, resulting in a very fast growth in their mean national incomes, income inequality among provinces and states as well as interpersonal inequality has been rising in both countries in recent decades particularly after a decisive step was taken towards opening the respective economies. It is true that the rising inequality in most developing Asian countries is the result of 'the rich getting richer faster than the poor' than that of 'the rich getting richer and the poor getting poorer' (ADB 2007). However, the rising inequality could put a brake on economic growth as it tears apart social cohesion required for economic development in the region. The poor in Asia, as elsewhere, have been particularly subject to increased vulnerability from globalized market forces.[56]

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53 See Sawada and Estudillo (2008) for the effect of migrants' remittance on poverty in the Philippines.

54 Milanovic (2005b) notes that while the disequalizing force inherent to economic growth is noted by many classical development writers as (see Section 2), an interesting question remains open whether there are countervailing forces to render growth spatially equalizing in the long run. Krugman and Venables (1995) argue that centripetal forces and centrifugal forces in a spatial economy will produce an inverted U-shaped trend in global inequality as market-driven globalization proceeds in the long run.

55 Strictly speaking the trends in world (global) income inequality depend on which concept of inequality is used for measurement (Nissanke and Thorbecke 2006b; Milanovic 2005a). Among different estimates, the 'between country' inequality weighted by population but ignoring 'within-country' inequality shows a declining trend largely driven by the China factor, while all other estimates show clearly that the world inequality has been increasing.

56 Aggarwal (2008).

There is growing evidence that 'within country' inequality has been rising at an accelerated pace across most developing economies in Asia over a roughly 10-year period from the early 1990s to the first half of the 2000. Cook (2006) notes that the Gini coefficient of income inequality increased in most Asian developing countries between 1980 and 2002, for example, from about 0.24 to 0.35 in China and from 0.25 to 0.32 in Bangladesh. According to the most recent estimates, among 21 developing countries, 15 countries registered a rise in the Gini coefficient. The sharp increase of 5–10 percentage point in the Gini coefficient is observed in 5 countries, including Nepal and China (ADB 2007; Ali 2007). Growing inequality is observed both in terms of income inequality and non-income inequality such as in health and education.

Thus, it appears that economic growth over the recent decades in Asia has so far produced a marked reduction in poverty despite the adverse distributional changes against the poor. That is, growth produced the adverse distribution effect, but the former was so vigorous that it more than compensated for the latter (ADB 2004). A number of empirical studies have been carried out to examine this dynamic trajectory of the interrelationships among poverty, growth, and inequality in Asia by decomposing the changes in poverty into two components: the growth component and the distribution component. The results of the earlier decomposition study for five countries in East Asia (Malaysia, Thailand, Indonesia, rural China, and the Philippines) generally confirm that growth was sufficiently buoyant to more than compensate for greater income inequality and keep poverty reduction on track (Ahuja et. al. 1997).

Overall, the process of integration of many Asian economies into the global economy has generated such a strong growth impact that the poor were not left out from its beneficiary effects.[58] This is particularly so when economic growth was accompanied by increasing employment opportunities for the poor. At the same time, the Asian experience underscores the importance of policy and institutional measures to build up productive assets of the poor through substantial investment in education, health, extension services and infrastructure as well as through the redistribution of assets in favour of the poor, for example, through land tenure reforms. However, there is also mounting evidence that the distribution effect engendered by the globalization process is generally not in favour of the poor, and that growth has been increasingly disequalizing over time in the region. The pattern of growth in Asia has been pro-poor according to the weak definition but not according to the strong definition of pro-poor growth (that is the poor benefit proportionately more than the non-poor).[59]

Indeed, despite the sharp reduction in the incidence of extreme poverty (less than US$1 a day), poverty remains high in many developing countries in Asia, if it is measured on the basis of the US$2 a day poverty line. It is estimated that the latter declined from 86 per cent in 1990 to 77 per cent in 2005 in South Asia, from 66 per cent to 43 per cent in Southeast Asia and from 72 per cent to 29per cent in East Asia (dominated by China) over the same period. The reduction in this measure is appreciable in particular in East Asia, but poverty is still widespread in Asia as a whole, and the challenge facing policymakers in the region in attacking poverty of this magnitude is non-

58 See Nissanke and Thorbecke (2008a) for detailed case studies that examine the effects of different aspects of globalization on inequality and poverty in Asia.

59 See Kakwani and Son (2008) for a detailed empirical examination of 'pro-poor' growth in the Republic of Korea, Thailand, and Vietnam in the 1990s.

trivial. The 'inequality increasing' effect of globalization should be attenuated by public policy measures to ensure that benefits from globalization induced growth are shared more equally and equitably. In this context, it is worth remembering that the pattern of *shared* growth from wealth sharing policy measures provided legitimacy for governments to pursue pro-growth and pro-business economic policy in the early drive for rapid industrialization in many countries in East Asia.[60] Sustaining the shared growth process is hence critical for ensuring economic growth to continue under this era of globalization. Alternatively, growing inequalities can weaken social cohesion and risk reducing the momentum for economic growth and integration in the region.[61]

3.2.3 Integration Experiences in Latin America

The region of Latin America occupies an intermediate position in its integration experience compared to the other two regions. Like countries in SSA, many economies in Latin America have been historically natural resource based in their linkage to the global economy through primary commodity exports. Though the economies in the region are much more diversified in their production and trade structures than those in SSA, they have been largely susceptible to the 'global development cycle', dominated by external shocks (Ocampo and Parra 2006).[62] Many countries in the region were exposed to the deterioration in their terms of trade caused by the sharp drop in prices of a number of primary commodities in the 1980s. In addition, as main recipients of commercial loans based on abundant petrodollars in the 1970s, middle income countries in the region suffered from the sudden hike in real interest rates at the end of 1970s. Resulting from the ensued severe debt crisis, the region had to endure the 'lost decade' of economic growth in the 1980s characterized by negative external resource transfer and negative growth rates in per capita income. The annual average growth of GDP in the eighties for the LAC region was barely above 2 % resulting in stagnant per capita income.

After the belated market based debt restructuring under the Brady Plan and the sweeping policy reforms of liberalization and deregulation, middle income economies in the region reintegrated into the global economy as emerging market economies in the early 1990s. Yet, the region's economic integration spurred by the liberalization and privatization drive and based on the premise of large 'growth' dividends from globalization has not delivered the promised benefits of sustained economic growth to these economies. The average annual growth of GDP during the nineties was only around 3 %. Sanchez (2003) succinctly summarizes the prevailing reflection on the region's economic performances over the last two decades, by noting 'Latin America has wholeheartedly embraced the faith in open trade and freer capital markets and yet, subsequent growth is well short of expectation'. On the whole, the globalization–induced economic growth in the region has been much more precarious and fragile than that recorded in Asia throughout the last three decades.

Under the impetus of highly volatile portfolio capital flows, economic growth has been interrupted by the periodic crises in capital accounts of balance of payments since the mid 1990s. Much of the eagerly anticipated increase in FDI often took the form of asset acquisition of newly privatized public utilities rather than that of green field investment in productive capital. Operating within the

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60 Campos and Root (1996)

61 See ADB (2007) and Ali and Zhuang (2007) for the concept of 'inclusive growth' and the associated policy strategy advocated for the region.

62 Ocampo and Parra (2006) attribute the cycles of growth spurts and collapses of many developing economies since 1950s to their susceptibility to external shocks originating from the global economy, and accordingly identify a 'global development cycle' that circumscribes the growth possibilities of these economies on a sustainable basis.

global production network, TNCs in the manufacturing sector in the region have adopted new production technology with little fresh employment created. TNCs in Mexico and the Caribbean tend to specialize in low technology manufactures, operating largely assembly plants with little potential of technology and skill transfers (ECLAC 2004; Sáinz 2006). Thus, during the recent spell of globalization, Ocampo and Parra (2006: 14) remark that, 'South America has experienced premature deindustrialization, while Mexico and Central America avoided this trend by specializing in high import intensive manufacturing exports, but with limited benefits in terms of growth'. It is still too early to judge whether the growth spurt starting in 2004 (yielding a growth rate of GDP of around 5 % a year over the last four years) is fuelled by the globalization process and is sustainable. Clearly the growth transmission channel described earlier has, at least until very recently, been much too weak to play a significant role in reducing poverty in the region.

In contrast to Asia, the Latin American region has experienced a very low rate of formal job creation in the tradable sector under globalization. In some cases, economic growth was 'jobless', with a negative rate of creation of formal job. Sáinz (2006) observes the sharp disparities in performance between large (often operated by TNCs) and small enterprises in the region: large scale enterprises recorded high rates of productivity growth with a shrinking labour force, while the number of small and informal low productivity enterprises continues to grow. Thus, labour markets in the LAC region are characterized by a high degree of segmentation in parallel with an increasing casualization of the workforce.

As firms operating in the formal sector are subject to increased international competition as liberalization proceeds, the informal sector has expanded by absorbing negative income shocks as workers in the formal sectors are laid off.[63] This process has given rise to the fear of 'social exclusion' of the self-employed, operating almost entirely in the informal sector. Popli (2008) notes the self employed now account for one-third of the labour force in the Mexican economy and are one of the most vulnerable groups. This process of casualization and informalization of the workforce can help explain the reduction in open unemployment in Mexico and other Central American countries during the 1990s, while open unemployment was rising steadily in Argentina, Brazil, and Colombia, and other Latin American countries. The share of the informal sector in urban employment rose significantly in most countries of the region (ECLAC 2004).

While the distribution of income and assets in this region is known to have historically been the most unequal in the developing world, many empirical studies confirm that income and asset inequality has continued to rise significantly during the integration process after 1980. In the second half of the 1990s, all Latin American countries were grouped at the very top end of the world inequality ranking according to World Bank's WDI data set—with a median Gini of 56.7 per cent and mean of 54.7 per cent (Palma 2006). Further, according to the ECLAC study, in the 1990s, the share of total national income accruing to the top 10 per cent of households continued to rise in most LAC countries. The average income of the richest 10 per cent of households was 19 times higher than the average income for the 40 per cent of households with the lowest income in the late 1990s in the region as a whole. This ratio was notably higher in Brazil, Bolivia and Nicaragua (ECLAC 2004).

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63 See Kakwani et al. (2008) and Gindling and Terrell (2008) for detailed analyses of effects of globalization, growth and institutional changes on labour markets in Brazil and in Honduras respectively.

The increased income inequality is often explained by the widening income gaps between skilled and unskilled workers as well as between the formal and informal sectors reflecting the differences in human capital endowments.[64] Brazil's experience since the late 80's provides a revealing counter evidence marked by a falling wage inequality and income inequality (after 2000) as Ferreira et.al (2008) make clear in their case study discussed in Section 4- illustrating thereby the risk of blanket generalizations.

However, Palma (2006) challenges the power of these explanations for the pattern of income distribution, exclusive of other factors, arguing that the effects of globalization on income distribution in the region are most pronounced at the extreme ends of the income distribution. For example, the enormous increase in the share of the top decile relative to the bottom decile hardly reflects where either skilled or unskilled members of the former labour force are located. Using the World Development Indicators data set, he estimates the median income ratio of the top decile to the bottom decile in Latin America to be 58.1, compared to 12.5 in non-Latin American developing countries. In other words, Latin America is characterized by a greater income *polarization*. He explains this polarization by the way the economies in Latin America have integrated into the global economy, citing the Mexican case where the share of wages fell from 40 per cent of GDP in 1976 to just 19 per cent in 2000. Wages in low technology manufacturing sector, in which Mexican 'maquila' enterprises specialize, stagnated, while large productivity gains were appropriated in a sharp rise in profit margins. In short, globalization in the region appears to have shifted the functional income distribution decisively against labour. In short, globalization, at least partially, through its technology transmission channel appears to have shifted the functional income distribution decisively against labor in the region and the rising income inequality dampened further the poverty alleviation effect of a modest growth performance.

Paradoxically, while the evidence is persuasive that income inequality is high and rising and contributing to perpetuate poverty in the region, much of the development literature ignores the fact that income inequality and income-based poverty are not necessarily the only or even best measures of economic and social well-being. Poverty and inequality are multidimensional concepts that can only be imperfectly reflected by money-metric measures. In this context and to further muddle the development performance picture Sahn and Younger (2006) found that during the eighties and nineties, inequality measured in the health and education dimension fell in Latin America and that this decline contributed to a substantial improvement in health and education indicators. They pointed out that this progress is important evidence of socio-economic development in Latin America- evidence that a narrow focus on money-metric measures alone would miss.

Despite the increasing focus of many governments on poverty reduction rather than addressing the high income inequality, there was only a modest reduction in poverty incidence, if any. Rather, most estimates tend to suggest that poverty today is worse than 30 or 40 years ago.[65] For example, according to the definition used in the ECLAC reports, the percentage of the population in poverty

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64 See Harrison and Hanson (1999), Goldberg and Pavcnik (2004) and Chapter 12 in this volume for a literature review and empirical evidence in Mexico, Colombia, and Brazil respectively. In fact Brazil provides an interesting exception, where the wage inequality fell after trade liberalization in the late 1980s. Brazil also experienced a reduction in income inequality—one of the highest in the world—after 2000. (Ferreira et.al. 2008)

65 Sanchez (2003).

in Latin America was higher in 2003 (44 per cent) than in 1980 (40.5 per cent).[66] Poverty incidence is much higher in rural areas (64 per cent), than in cities (37 per cent), although there is an ongoing increasing urbanization of poverty trend due to the rural–urban migration. It is worth noting that while some major efforts have been in place in recent years to redress income inequality through such schemes as the Brazilian Bolsa or the Mexican *Progresa* in the field of education, inequality in non-income measures such as education, nutrition, health, and access to utilities remains high and persistent. The poor are particularly disadvantaged in accessing these public goods. While a claim has been made that increasing international remittances could become a massive resource transfer mechanism to reduce poverty levels by increasing income of poorer households, de la Fuente (2008) shows that remittances are not going to the poorest members in rural communities in Mexico.[67]

During the 1990s, there were some noticeable surges in social expenditures per capita through public transfers and human capital formation in many countries (ECLAC 2004). Through a rigorous empirical analysis of the relationship between growth patterns, poverty and inequality in Brazil, Kakwani et al. (2008) provide an important insight into the crucial role of incomes derived from social security and other government transfers in cushioning the effects of macroshocks, triggered by the forces of globalization, specifically among the poorest segments of Brazilian society for the period, 1995–2004. Skoufias et al. (2008) also examine the performance of various schemes of public transfers in eight countries in the region. The latter found that on the whole, public transfers in the region have not yet managed to redistribute income to the poor significantly as social insurance schemes tend to dominate public transfers and are less effective than specifically designed social assistance programmes targeting the poor directly. They argue that in many countries in the Latin America and the Caribbean (LAC) region, social insurance schemes are regressive by limiting coverage to workers in formal labour markets, which exclude most of the poor, as well as by paying highly generous unit benefits to those in the upper quintiles of the income distribution. Mitigating the negative effects of globalization on inequality and the poor is of particular importance in the LAC region, where there is today widespread dissatisfaction with the social injustice associated with high poverty and inequality.

In this context, it should be noted that over the last three decades, the course of macroeconomic adjustments necessitated from, and the institutional effects of, the massive shocks coming from global financial and commodity markets have considerably exacerbated the distributional conflicts inherent to the region's economies (Ocampo and Parra 2006). At the same time, the process of building developmental nation states and other institutions that could resolve the distributional conflicts through a set of public transfers and social policies has been significantly and repeatedly disrupted by periodical external shocks and frequent (almost continuous) macroeconomic adjustments necessitated by these shocks. In short, the high vulnerability to external shocks—the

66 The poverty line estimates used in ECLAC are drawn to determine whether or not minimum basic needs of household members, including nutritious needs, is satisfied. It is based on national household surveys conducted in member countries. Comparing its own poverty line estimates with the international poverty lines, the US$1 a day and US$2 a day poverty lines used by the World Bank, ECLAC suggests that the World Bank systematically underestimate the actual number of the poor in the region (See ECLAC 2004: chapter 1, 'Methodological Annex', for the methodology used to arrive at the poverty line estimates by the ECLAC Secretariat).

67 However, effects of migration and worker' remittances on inequality and poverty can be diverse and context-specific even within he LAC region. See Aguayo-Tellez et al. (2008) and Macours and Vakis (2008) for the case of inter state migration in Brazil and seasonal migration in rural Nicaragua.

direct consequence of the way the LAC economies have integrated into the global economic system—has considerably impaired the institution building process towards a more equitable society. Governments have increasingly faced serious constraints both in the fiscal front and monetary policy choices for sustaining public transfer programs or other social policies in order to address growing inequality and the unacceptable prevalence of poverty. At the same time it is clear that the inconsistent (stop and go) and populist economic and monetary policies followed by many Latin American regimes have contributed in no small measure to the mixed socio-economic performance described above. There appears little doubt that with sounder policies and governance the net and overall impact of globalization would have been more favourable to most segments of the population.

4. Strategic Policies to Induce Globalization to be more Pro-Poor

The empirical case studies from the three regions in this UNU-WIDER research project support our contention laid out at the outset that the effects of globalization on poverty are diverse, and in many ways, context specific.[69] Indeed, our studies confirm the view that 'the forces of globalization as such are not *inherently* beneficial or deleterious for development prospects' (Sanchez 2003: 1978).[70]

Yet, our comparative analysis of the globalization experiences across the three developing regions also suggests that globalization works best for the poor through the 'growth' channel when globalization induced economic growth generates secure employment opportunities continuously at a steady rate for a growing population and labour force. On the whole, the employment creating effect of growth is pronounced in East Asia, where globalization has brought about a substantial poverty reduction due to vigorous growth despite the increasing inequality. The process of poverty reduction in the Asia and Pacific region has closely followed the waves of employment creations for unskilled labour and the poor in tandem with the evolution and shifts of comparative advantages within the region in the ever accelerating integration process. In contrast, such a poverty reduction process through globalization could not be achieved in SSA and ECLAC regions, where liberalization of trade and investment regimes failed to produce either strong or significant employment creating growth. Instead it has resulted in 'jobless' growth, casualization of employment and informalization of their economies. This observation leads us to argue that the

69 See Ravallion (2006) and Bardhan (2006) for the detailed discussion on the tenuous but complex nature of the openness-poverty relationships. Winters et al. (2004) also present a careful examination of multiple mechanisms found in the link between trade liberalization and poverty.

70 See also Chapter 2 in this volume for a cross-country econometric study that suggests globalization on its own has made little difference to poverty either positively or negatively on aggregate.

employment creation effect achieved through globalization induced economic growth is a most direct and powerful channel through which globalization can make a noticeable dent on poverty.[71]

While the prospect of substantial poverty reduction can be increased considerably, wherever globalization brings about job generating economic growth, this potential is realized only when economic growth is characterized by a relatively high 'employment elasticity'. However, such growth outcome cannot be necessarily guaranteed whenever globalization/integration is embraced, on its own, as a development strategy. Instead, the dynamic integration experiences in Asia point to the need for policies of *strategic integration*, not policy of *passive integration or de-linking* from the global economy.[72] Such a strategic position should, first of all, aim at facilitating the transformation of production and trade structures from the narrowly based commodity dependence that is bound to expose economies to external shocks. In terms of sustained economic growth, developing countries that have successfully diversified their exports structures into manufactured goods, in particular, increasingly into medium and high technology sectors, have systematically outperformed those dependent on primary commodities, and natural resource based processing goods.[73] Thus, whether global market forces establish a virtuous circle or vicious circle depend not only on the initial conditions at the time of exposure but also importantly on the effective design and implementation of policies to manage the integration process. As Kaplinsky (2000) notes, 'the issue confronting policymakers is not *whether* to integrate into the global economy but *how* to integrate so as to have a stable foundation for sustainable and equitable growth'.

Clearly, a strategic position towards globalization cannot be equated with a mere adoption of liberal trade and investment regimes, or a simple fine-tuning of the pace and sequence of liberalization measures. At the same time, there is no place for an old style, poorly designed and implemented protection policy, which is mired in unproductive rent seeking activities, patron-client relationships between governments and private agents or consolidation of 'vested' interests of the protected sectors. Import substitution strategy can work only when protection is granted to firms with a clearly specified 'graduation' clause in a performance based system. That is, protection should always be seen as temporary and `time-bound' by agents in return for better performances.

In particular, national integration strategy should be designed in the light of the skewed nature of the on-going process of globalization. First, dynamic externalities and rent-rich activities are increasingly concentrated in high skill, knowledge intensive sectors. In short, the skill and technology related divide has become wider over recent decades. This trend is clearly reflected in the continuously declining terms of trade of less skill intensive manufactured goods relative to high skill and technology intensive goods over recent decades. The markets for many labour intensive products have come to resemble those for primary products.[74] The entry of China and India into global markets for these products has depressed and will continue to depress real wages and returns

71 Making a clear conceptual distinction between 'non-globalizers' and 'unsuccessful globalizers', Jenkins (2006) also emphasize the role of employment creation of labour-intensive exports of manufactures and agricultural products as an important differentiating factor between the successful globalizers in Asia and the unsuccessful ones in Africa.

72 Indeed, not integrating into the global economy is not a viable or attractive development option for any nation. Deardorff and Stern (2006) show that 'outsiders' are likely to be harmed, through the terms-of trade- effects, by multilateral MFN tariff reductions as well as preferential trading arrangements (PTAs) between 'insiders'.

73 Ocampo and Perra (2006: tables 2 and 3, and figure 9).

74 Maizels (1998).

in these low technology and low skill sectors. On the other hand, a number of primary commodities have been experiencing a sharply upward phase in their commodity price cycles since the early 2000s, in the face of the surge in demand for raw materials and other commodities from fast growing economies in Asia such as India and China. Consequently, many natural resource based economies in SSA and Latin America are presently enjoying a period of ‘growth spurts’ associated with the ‘commodity’ boom. However, as discussed before, though the current price trend may continue for some time, it is difficult to sustain economic growth that is capable of creating job opportunities for growing labour force, exclusively on the basis of the primary commodity boom. Broad based development of these economies would require a strategy of using resource rents and windfalls for economic diversification.

Generally, given the observed trends towards inequality both globally and within many nations, developing countries have to take strategic steps to position themselves more favourably in the globalization process, in order to derive greater benefits from globalization’s dynamic forces. They need a long term vision for upgrading their comparative advantages towards high value added activities by climbing the technology ladder step-by-step through learning and adaptation.[77] To succeed, developing country governments should consciously engage in building institutional capacities for integration, including a capable nation state that is ready to take on the enormous challenges posed by globalization. The positive benefits from globalization are neither automatic nor guaranteed, whilst passive liberalization would risk perpetual marginalization.

Furthermore, since openness could potentially benefit the poor in countries which have already reached the take-off stage, it is very critical that in addition to a long term vision for strategic integration, low income countries should embark on the path towards *structural transformation* of their agrarian economies, as a necessary condition for successful integration. The importance of this critical step in relation to the globalization–poverty nexus is underscored by the fact that there are critical *thresholds* that need to be reached before the positive effects of globalization on poverty reduction can be realized. The non-linear Laffer-type relationship between globalization and poverty shows that openness helps those with basic and higher education, but reduces the income share of those with no or little education and it is only when basic education becomes the norm for the poor that openness exert an income equalizing effect.[78] Thus, at low income levels, openness affects equality negatively, while at medium and high income level it could potentially promote equality.

In conjunction with building assets of the poor in their human capital base, there is a complementary need to invest in rural physical and social infrastructures and create market supporting institutions, so that the poor can be connected and networked beyond isolated communities and villages. In terms of inter-sectoral flows, a continuing *gross* flow of resources

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77 In this context, Lin and Liu (2008) argue for the superiority of the comparative advantage-following strategy over the comparative-advantage-defying one.

78 Milanovic (2002), and Agenor (2002)

80 See various case studies included in Nissanke and Thorbecke (2006d, 2006e, 2008b, 2008d).

should be provided to agriculture—irrigation, inputs, research, and credit—to increase this sector's productivity and potential capacity of contributing an even larger return flow to the rest of the economy and hence provide a *net* agricultural surplus to finance the subsequent development of the rest of the economy.

Finally, our project case studies unequivocally point to the need for instituting safety nets and appropriate regulations to protect the poor from large downside risks associated with globalization. Clearly, globalization has significantly increased the vulnerability of the poor in all three developing regions through channels such as: (i) the increased scale and frequency of macroeconomic shocks; (ii) larger exposure to changes in the ecosystem or new unknown technology with often uncertain pay-offs; and (iii) their deteriorating working conditions and weakening bargaining powers in global value chains.[80] Thus, governments should take a pro-active and pro-poor stance in instituting various schemes of public transfers and safety nets to shelter the poor from these adverse conditions.[81] In this context, Bardhan (2006) argues that the distributional issue raised in the debate is not an argument against globalization (open trade and investment regimes) per se but for pro-active public programmes to protect the poor.

All in all, our comparative analysis of the three regions suggests that governments of developing countries need to pursue both strategic integration and an active domestic development agenda to ensure that the poor benefit from globalization, while they are adequately protected from negative impacts. Bardhan (2006) notes that globalization should not be allowed to be used, either by its critics or by its proponents, as an excuse for inaction on the domestic as well as the international front. What is *at minimum* called for is liberalization to be accompanied by a comprehensive policy package for enhancing the capability of the poor and instituting a safety net for people who lose from the globalization process. In order to achieve this goal, the capacity of the nation states should be strengthened rather than weakened.

5. Measurement Issues

To be Completed

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[81] See Kakwani and Son (2008) and Kakwani et al. (2008), among other project case studies.

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Figure 1.1 The Globalization–Openness–Growth–Inequality–Poverty Link