The Impact of Globalization on the Poor in Latin America

by

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Abstract: This paper consists of three main parts following an introduction. Section 2 analyzes and describes the main channels (transmission mechanisms) through which the process of globalization affects poverty directly and indirectly. Section 3 reviews the major effects of globalization- as proxied by trade intensity- on the Latin American economy, as a whole, and on a number of individual countries in terms of growth, income distribution and poverty between 1980 and 2006. Section 4 focuses on 8 case studies of the impact of globalization within different Latin American settings undertaken under the auspices of a UNU/ WIDER project directed by the authors. These case studies reveal the critical role institutions (social protection schemes, more flexible labor markets and migration opportunities, trade liberalization and property rights) can play in reducing the vulnerability of poor households to global shocks and strengthening the positive effects (pass-through) of globalization on poverty reduction within different context-specific settings. In general, the main globalization channels appeared to have had relatively limited success in reducing overall poverty in the region. Between 1981 and 2004 overall growth was largely anemic and its pattern was not pro-poor, instead bringing about greater income inequality in a majority of Latin American countries. There were some exceptions: the best performing countries were Brazil, Mexico and Chile. The trade liberalization process tended to benefit relatively more the skilled workers than the unskilled workers. Two rays of hope, in an otherwise relatively bleak picture, consist of 1) the safety nets and social protection schemes and other institutional changes implemented in an innovative fashion by some of the larger countries in the region; and 2) the very recent growth surge and acceleration in most of the region. [3]

Key Words: globalization, growth, income distribution, poverty, trade liberalization and Latin America

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1. Introduction

The United Nations Universities' World Institute for Development Economic Research (WIDER) initiated a large scale program of research on 'The Impact of Globalization on the World's Poor" in 2004 under the co-directorship of the two authors of the present paper. The main objectives of the project were to produce a set of rigorous theoretical and empirical economic studies, which would deepen our understanding into how conditions facing the world's poor have been evolving under globalization; and provide a framework yielding the elements of a strategy that would induce the globalization process to become more "pro-poor". In addition to the methodological and conceptual conference held in Helsinki at the end of 2004, the project organized three regional conferences to explore the impact of globalization on Asia, Africa and Latin America, respectively, during 2005 and 2006.

Because of very significant differences in initial conditions (natural resource endowment, quantity and quality of human capital, institutional framework, quality of governance) as well as in internal dynamics of institutional and socio-political conditions, globalization has influenced the poor in different regions of the developing world very differently. Generally speaking, the poor in Sub-Saharan Africa were essentially by-passed by the forces of globalization while most of the Asian poor benefited- none more so than in China. Latin America occupies an intermediate position in this continuum[4]. In addition to broad intercontinental differences the effects of globalization on the poor can be very diverse *within* each regional block as well and even vary from region to region within a country.

This paper consists of four parts. Section 2 analyzes and describes the main channels (transmission mechanisms) through which the process of globalization affects poverty directly and indirectly.[5] Section 3 reviews the major effects of globalization on the Latin American economy – keeping in mind that few generalizations can be made with much assurance. Section 4 reviews the findings of eight selected case studies, undertaken under the auspices of the WIDER project, analyzing and illustrating the critical role institutions can play in mediating the impact of globalization on poverty within different Latin American settings. These studies reveal, first, how key institutions can strengthen the positive effects of globalization on poverty reduction and moderate some of the negative effects; and, secondly, how sensitive the link from globalization, via institutions, to poverty is to initial conditions and the specific context. Section 5 concludes.

2. Channels Linking Globalization to Poverty

What are the transmission mechanisms through which the process of globalization affects poverty directly and indirectly? The globalization-poverty nexus is indeed complex, involving many different channels. In a general sense, the channel linking globalization

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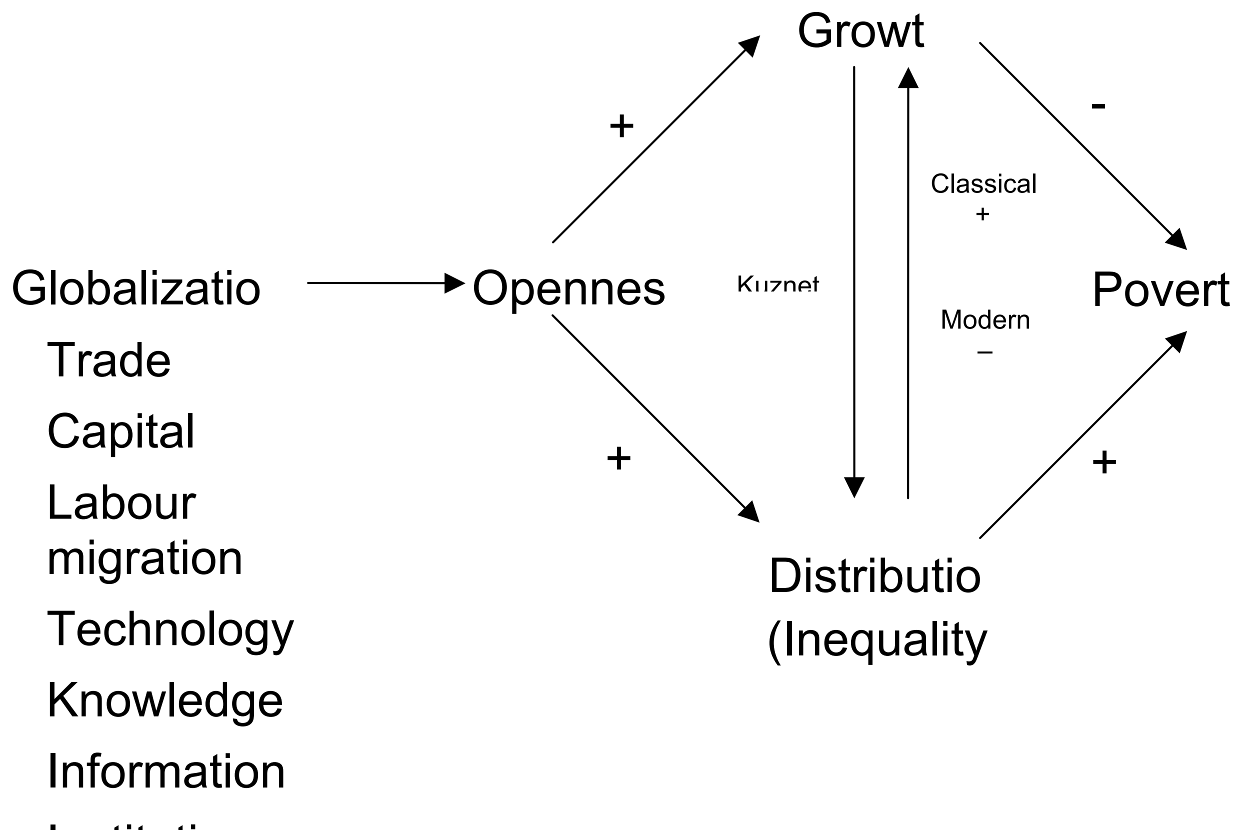
[4] For a comprehensive discussion of the differential regional impact of globalization on the poor, see Nissanke and Thorbecke (2008).

[5] For a more detailed discussion of different transmission mechanisms in the globalization-poverty nexus, see Nissanke and Thorbecke (2006a) and Chapters 1 and 2 in Nissanke and Thorbecke (2006b).

(openness) to poverty can be visualized as a large river fed by a variety of economic tributaries. Figure 1 is our attempt to illustrate schematically the various critical links of the causal chain running from globalization (openness) to poverty, focusing on most critical tributaries and abstracting from several feed-back effects that exist among the constituting elements.

Figure 1: The Globalization–Poverty Nexus



Greater openness is the major manifestation of globalization. The major transmission mechanisms from globalization to openness are listed in Figure 1 and include changes in relative prices of factors of production (labor and capital) and commodities; movements of capital, labor 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. These mechanisms affect poverty through two different paths: first, through their contributions to the growth channel in the upper part of the diagram in Figure 1 and, secondly, through their impact on income distribution and poverty (in the lower part of the diagram) since globalization is also known to create winners and losers directly and affect vertical and horizontal inequalities.[6] The links shown in Figure 1 are from openness to growth, from openness to income distribution (inequality), from growth to

6 See, for example, Ravallion (2004a) for a discussion of how globalization may alter horizontal and vertical inequality.

income distribution and vice versa, from growth to poverty, and from income distribution to poverty, respectively. In turn, the two main channels of globalization- the "growth" and "distribution" channels further interact dynamically over time to produce a growth-inequality-poverty triangular relationship, which is captured by the right hand side triangle of our diagram describing the arithmetic-statistical relationship among growth, inequality and poverty investigated and popularized by Bourguignon (2003).

In what follows, we first discuss the globalization-poverty nexus through the growth channel and the growth-inequality-poverty triangular relationship (Section 2.1). We then move on to a discussion of other channels through which globalization can affect poverty by creating winners and losers directly (Section 2.2).

2.1 The Globalization–Growth–Inequality–Poverty Causal Chain

To analyze 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.

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 being 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.[7]

Similarly, the transfer of technology, skills and management know-how that is assumed to accompany FDI does not occur in a number of instances. 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.[8] In addition, short-term capital flows contribute to the increased vulnerability to external shocks of the recipient developing countries.

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[7] Sanchez (2003) notes that "the causality link between trade openness and long-run growth is not engraved in stone (p.1979)".

[8] 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.

Indeed, there is much empirical evidence that openness leads to more 'within-country' inequality through the openness-inequality link, as discussed below.

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, e.g., Dollar (1992); Sachs and Warner (1995a); Dollar and Kraay (2001, 2002).[9] However, the validity of these cross-sectional empirical exercises has been contested on technical grounds by many researchers.[10]

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 an 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.[11] From this theoretical perspective, the desirability of an unequal income distribution is rationalized on economic grounds, i.e. on the basis of the claim that "more poverty today is a precondition to more economic growth and less poverty in the future".[12]

In contrast, the 'new' political economy of development 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[13] 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[14].

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 the re-

[9] See World Bank (2002) for a summary of these cross-country studies on the openness-growth link.
[10] 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.
[11] See Kaldor (1956) and Aghion et al (1999) for discussion on the savings effects and investment effects, respectively.
[12] See Thorbecke (2006) for a critical review of the traditional approach to the inequality-growth link.
[13] See Thorbecke and Charumilind (2002).
[14] See also Aghion et al (1999).

examination of the opposite causal flow in the link, i.e. the 'growth-inequality' link.[15] Many earlier development economists noted that economic growth, if left to market forces alone, tends to be accompanied by more inequality. They considered growth to be inherently dis-equalizing.[16] 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 illustrates.

Thus, 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.[17] If growth leads to a significant increase in income inequality the poor may benefit only slightly or, in some instances, actually be hurt by the 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 (the evolution of this inter-relationship is analyzed in detail within the context of Latin America in Section 3). 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 positive elasticity of poverty reduction with respect to growth 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 more pro-poor distribution of the gains from growth.[18] Hence what is relevant for poverty reduction is a 'distribution-corrected' rate of growth, [19]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).

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

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

[17] See Naschold (2004) for empirical evidence 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.

[18] 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.

[19] Ravallion (2004b).

2.2 Direct Distribution Channels in the Globalization-Poverty Nexus

In what follows we discuss briefly a number of mechanisms through which changes in openness actually affect income growth for individual households. These channels may be largely responsible for explaining why many poor households 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 labor should experience a decline in income inequality through an increased demand for unskilled labor, while unskilled labor 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. Several specific features associated with the current phase of globalization, explain why such a theoretical prediction does not hold. We highlight below some of the critical channels through which globalization ultimately affects poverty.

Technology and Factor Mobility in the Globalization-Poverty Nexus

Since the bulk of technical change emanates from R&D activities in developed countries in response to local conditions prevailing in these countries, the nature of technical progress and new technology is heavily biased in favor of skilled and educated labor.[20] Hence, technical change tends to be labor-saving and skill- biased, and new technology is complementary to capital and skilled labor, while it is a substitute for unskilled labor. In this sense, 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. Especially, intensified privatization of research in bio-technology or pharmacology 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 issues (TRIPs) in the WTO negotiation. The widened productivity differences, resulting from these asymmetries help explain cross-country wage/income inequality. The initial knowledge gap and unequal, skewed access to technology and knowledge have adverse implications for the 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.[21]

The 'perverse' factor movements' hypothesis could provide another explanation. Capital and skilled labor do not migrate to poor countries as much as among developed countries. Rather, there is a tendency for skilled labor 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 labor migration tends to be strictly controlled. Unskilled workers from developing countries face increasing obstacles in

[20] Culpepper (2002)
[21] . Baldwin and Martin (1999)

their attempts to migrate to developed countries. In consequence, wage equalization does not take place through labor migration, as was the case in the previous globalization era.

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, i.e. 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[22].

Also, the differentiated degree of cross-border factor mobility (skilled labor and capital vs unskilled labor and land) often affects the functional income distribution between labor and capital against the former. Some workers are losing out, as *de facto* labor mobility takes place through the increasingly free cross-border capital mobility and Transnational Corporations' (TNCs) ability to re-locate production sites in response to changes in relative labor 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 labor rights or protect local environments.[23] The unwillingness or inability to tax international mobile financial capital in the process of tax competition and in fear of capital flight and asset mobility, has, among other conditions, contributed greatly to the erosion of the capacity of governments to raise revenues for redistributional purposes.[24] 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.

Vulnerability, Information Diffusion and Institutions in the Globalization-Poverty Nexus

Globalization can hurt the poor disproportionally and thus increase their vulnerability, by generating greater fluctuations 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 decade.[25] Further, while globalization can be a major engine for growth in aggregate, globalization either introduces or exacerbates other trends that affect people's wellbeing as much if not more than income, for example, through the increasing flow of information about the living standards of others, both within and beyond country borders.

[22] Baldwin and Martin (1999)
[23] Basu (2003)
[24] Tanzi (2001) discusses various effects of globalization on the tax system under 'fiscal termites'.
[25] See Ligon (2006) for discussion on the effects of risks and uncertainty associated with globalization on the poor. Further see Diwan (2001) , Birdsall (2002 and 2006) for discussion on the adverse effects of financial crises, and Montalbarno et al (2006) and Winters et al (2004) for the effects of trade shocks on the poor. Kakwani et al (2008) examine the effect of shocks associated with globalization on income distribution and poverty in Brazil (see Section 4 below)

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. Individuals in specific socio-economic groups and professions increasingly compare their own individual welfare status with that of similar groups in other countries.

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 influences 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.[26] 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 and the availability of safety nets and social protection schemes. The crucial role institutions can play in amplifying the positive benefits and moderating some of the negative consequences of the forces of globalization on poor households within different specific Latin American settings is highlighted in Section 4.

3. Latin America's Socio-Economic Performance during the Present Globalization Era (1980-2006)

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 a continent as large and diverse as Latin America.

Instead we use trade openness as reflected by the trade intensity ratio (exports + imports/ GDP) as a major manifestation and indicator of the strength of the globalization process. Next, we compare the extent to which changes in trade intensity are associated or inter-related with changes in growth rates, income distribution and poverty in Latin America, as a whole, and in selected LA countries during six sub-periods between 1980 and 2006. Of course, one has to be careful not to claim that any observed association is necessarily influenced by the globalization process when, in fact, it might be the net consequence of a whole series of factors with some of them independent of the forces of globalization.

[26] See Sindzingre (2006).

The general picture we paint with a broad brush can usefully serve as a backdrop to the specific case studies discussed in Section 4 –organized around the theme of institutions that can help strengthen the transmission of positive effects of globalization on the poor and moderate the vulnerability of the poor to shocks linked to the globalization process (such as trade liberalization taking the form of tariff reduction, labor market reforms and reduction in barriers to international migration, the granting of property rights and social protection schemes and public programs to invest in the human and health capital of the poor). A few case studies undertaken as part of the WIDER research project were selected to illustrate within different context-specific settings how specific institutions and policies in the above areas affected the poor.

3.1 The Evolution of Trade Openness, GDP Growth, Income Inequality and Poverty Incidence during the Current Globalization Era

The first step is to identify the globalization period under scrutiny. Three different waves of globalization can be identified over the course of the last century and a half. During the first wave, from 1870 to 1914, income convergence among the globalizing countries 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. The second wave spanned the period from approximately the end of the Second World War to the seventies and was based on the availability of cheap labor mainly in East and Southeast Asia to mass produce labor -intensive manufactured products (such as textiles and appliances). The current wave, starting in the eighties, is characterized more by trade in knowledge and information rather than trade in goods, which was the case with the preceding wave of globalization. Our focus is on the present globalization era between 1980 and 2006.

Globalization embraces such an overwhelming set of forces that for analytical purposes the concept has to be defined in a more narrow, specific and operationally useful way. Since an increase in trade intensity is a major manifestation of the globalization process and can be approximately measured, the trade intensity ratio (exports + imports divided by GDP) has become the most used yardstick and indicator of globalization in the literature. Although easy to compute, it is incomplete as it only reflects the impact of globalization on trade. Furthermore it suffers from other weaknesses in particular in not being able to correct for the size of a country. Large countries such as China, India and Brazil would be expected to have significantly lower trade intensity ratios (TIRs) than small countries such as Singapore, Nepal, and Uruguay. Also it represents an outcome variable, not the actual trade liberalization policies that trigger the globalization process. As Goldberg and Pavcnik (2004) point out an obvious shortcoming of this concept is that both imports and exports are determined simultaneously with other variables that are the focus of the empirical analysis (such as wages and by extension poverty) so that interpretation of the results is subject to simultaneity bias. Tracing the path of causality under those conditions is a perilous adventure. We would claim that the forces of globalization encourage a process of trade liberalization at the country level (particularly taking the form of tariff reduction) which, in turn, leads to higher TIRs reflecting a greater integration in the world economy. Thus, in spite of its limitations, we shall use the

trade intensity ratio as a major, but not exclusive, indicator of the strength of the globalization process in the subsequent analysis.

The comparative analysis below follows a number of sequential steps. In each of these steps we compare the performance of the LAC region to that of the other major developing regions (Sub-Saharan Africa, South Asia, East Asia, Eastern Europe and Central Asia, and Middle East and North Africa) and the performance of selective Latin American countries (Argentina, Bolivia, Brazil, Chile, Colombia, Mexico and Peru) over six time periods from 1980 to 2006. First, we review the evolution of the TIRs and GDP per capita growth rates and check whether, and the extent to which, these two variables appear to be positively correlated. Secondly, we look at the relationship between TIRs and income inequality, and between GDP growth and inequality, over time. The final step consists of determining whether any pattern can be established between trade liberalization (TIRs) and the incidence of poverty- either directly or indirectly via the growth and inequality channels (see the Bourguignon triangle on Figure 1).

Table 1 summarizes the evolution of trade openness as reflected by TIRs in the major developing regions and selected Latin American countries between 1980 and 2005. It shows that East Asia succeeded in opening up trade earlier and much more intensively than other developing regions: its TIR jumping from 43% in 1985-89 to 60.1 % in 1990-94 and ultimately 82.7 % in 2005-06. Trade intensity started rising in the other developing regions only in 1995-99 with the TIR in the LAC region gradually climbing from 30.3 % in 1990-94 to 49 % in 2005-06. Within the set of LA countries appearing in Table 1, Chile, Mexico and Colombia went through a continuous process of trade openness from 1980 on, as well as a relatively very intensive process in the case of the first two above. In contrast the relative importance of trade in GDP in Argentina only started to rise in 1995-99 and even later in Brazil where the TIR stagnated between 16 % and 19% in the four sub-periods in the eighties and nineties before increasing to 26 % in 2000-04. The other two LA countries in Table 1, Bolivia and Peru only achieved higher trade intensity levels in the most recent 2005-06 time-span.

Table 1: Trade Intensity Ratios: Selective Latin American Countries and Major Developing Regions, 1980-2006

	1980-84	1985-89	1990-94	1995-99	2000-4	2005-06
Trade openness[1]*:* (X+M)/GDP						
Latin America and Caribbean	28.2	28.1	30.3	35.1	45.7	49.0
Argentina	13.9	16.4	15.8	21.9	29.9	44.1
Bolivia	50.7	44.0	48.2	49.3	50.0	72.1
Brazil	19.3	16.0	17.9	16.4	26.0	26.5
Chile	45.5	59.7	57.9	56.3	67.0	75.1
Colombia	26.5	29.9	35.1	35.8	41.9	45.7

Mexico	25.3	33.6	36.4	61.8	59.0	63.4
Peru	37.4	30.5	28.2	31.9	35.3	46.4
Sub-Saharan Africa	52.5	49.7	52.3	59.4	66.3	73.5
South Asia	18.5	17.3	22.7	27.5	32.8	45.5
East Asia	40.4	43.0	60.1	60.7	69.6	82.7
E Europe and Central Asia	..	..	57.9	62.7	76.3	77.0
Middle East and North Africa	68.3	48.2	67.7	59.0	67.8	84.6[2]
World total	*40.57*	*37.7*	*40.3*	*45.1*	*51.0*	*57.5*[2]

(.. not available)

Sources: World Development Indicators 2008

Notes: 1. World Bank *World Development Indicators,* 2008 (calculated from current US$ estimates)
2. Only 2005

What appears surprising in the above trends is a possible disconnect between the timing of trade liberalization policies and a resulting increase in trade intensity. For example in Brazil average nominal tariffs fell from 43 % in 1987 to 14 % in 1995 and effective rates of protection fell from 56 % to 20 % in the same period (Ferreira et al, 2006) with no impact on the TIR until 2000-04. Likewise, trade liberalization and large scale reduction in quantitative trade restrictions began in Argentina in 1990-91 and it took almost a decade before these measures led to any significant increase in the relative magnitude of trade flows. It is likely that it takes some time for actors to respond to new policies and signals and that a confluence of other factors affects the link between policies and outcomes. The time lag between the latter two provides yet another illustration of the limitations of the TIR as an indicator of globalization.

Table 2 gives the growth of GDP per capita for the same set of regions and LA countries as Table 1. It can be seen that the growth performance of the LAC region was marginal at best- stagnation in the eighties followed by an annual growth rate of per capita income of only slightly above 1 per cent between 1990 and 2004. It remains to be seen whether the quantum jump to 3.7 % in 2005-06 -caused largely by the price surge in primary products and commodities- is sustainable. The growth performance of the LAC region was very substantially worse than that of other developing regions except for Sub-Saharan Africa that endured negative growth rates between 1980 and 1994. Within Latin America by far the most successful country in terms of growth was Chile that from the mid-eighties on grew at annual rates between 2.8 and 5.6 per cent. In contrast, in the eighties, Argentina, Bolivia, Peru, Brazil (first half) and Mexico (second half) displayed negative growth. In the nineties Argentina, Bolivia, Peru and Mexico performed relatively well while Brazil essentially stagnated. A clear upsurge in growth rates occurred in the current decade in all LA countries listed in Table 2- except for Argentina in 2000-04. In a number of instances financial shocks and the inconsistent- often populist- economic policies followed by the governments in power have contributed in no small measures to the mixed socio-economic performance described above.

Table 2: Growth of GDP per Capita: Selective Latin American Countries and Major Developing Regions, 1980-2006

	1980-84	1985-89	1990-94	1995-99	2000-4	2005-06
Growth of GDP per capita (average annual)[1]						
Latin America and Caribbean	-0.9	0.3	1.6	0.9	1.0	3.7
Argentina	-1.6	-2.8	5.3	1.0	-0.6	7.8
Bolivia	-4.0	-1.2	1.7	1.7	0.7	2.4
Brazil	-0.9	2.5	-0.4	0.5	1.6	1.9
Chile	-0.2	5.6	5.4	3.9	2.8	3.8
Colombia	0.3	2.3	2.4	-0.4	1.4	4.3
Mexico	1.0	-0.8	2.0	1.4	1.4	2.7
Peru	-1.8	-2.1	0.9	2.1	2.2	5.9
Sub-Saharan Africa	-1.3	-0.3	-2.0	0.7	1.5	3.2
South Asia	3.1	3.4	2.6	4.0	3.9	7.0
East Asia	5.8	6.3	7.9	5.7	7.1	8.4
E Europe and Central Asia	..	..	-6.0	1.8	5.4	6.4
Middle East and North Africa	0.3	-1.6	1.6	2.3	1.9	3.0
World total	*0.5*	*2.0*	*0.7*	*1.7*	*1.6*	*2.4*

(….) not available

Source: World Bank *World Development Indicators,* 2008 (average annual %)

A major World Bank report on inequality in LAC based on a sample of household surveys for 20 countries at three points during the period 1989-2001 concludes that Latin America and the Caribbean is one of the regions in the world with the greatest inequality (de Ferranti et al, 2004). Many Latin American countries display Gini coefficients of income inequality even higher than those observed in most of Africa. The report indicates that inequality has risen in most South American economies during the decade ending in 2001. Argentina experienced by far the biggest jump (7.7 Gini points between 1992 and 2001). Venezuela follows with an increase of about 4 Gini points. The income distribution also worsened in Bolivia, Chile, Ecuador, Peru Uruguay, and possibly Paraguay. Colombia's income distribution remained essentially the same while Brazil is the only South American country undergoing a clear reduction in inequality in the nineties (de Ferranti et al, 2004).

Table 3 provides estimates of poverty and inequality measures for a large set of individual LAC countries for selected years in the nineties and the current decade. The information is drawn from the most recent study by Ferreira and Ravallion (2008) on global poverty and inequality and in a number of instances Table 3 contains even more up to date estimates than the above de Ferranti et al (2004) source. It shows that nine

LAC countries underwent a rise in income inequality between the mid-nineties and the mid-2000's. Inequality fell in two countries (Brazil and Mexico) and remained essentially the same in four countries (a change of less than 2.5 % from the initial Gini). Interestingly enough the beginning of a convergence trend with respect to inequality can be noticed among LAC countries in the last decade. There appears to be a tendency for highly uneven countries (with Gini coefficients above .5) to become more even and for less uneven countries (with Ginis below .5) to become more uneven. A comparison of Gini ratios in the early 2000's with that of the early 1990's reveals that out of the 15 LAC countries listed in Table A.6 of de Ferranti (2004) either no change or convergence could be observed in 12 of these countries. For example, in three relatively low-inequality countries (Argentina, Uruguay and Venezuela) income distribution has become more uneven while improving in four mid- to high- inequality economies (Brazil, Colombia, Mexico, and Panama).

Table 3: Inequality and Poverty Measures for Individual LAC Countries, 1990s and 2000s.

Country	GDP per capita, PPP (constant 2000 international $)**	Survey Year	y/c	International Poverty Line		Inequality	
				Population Below $1 a day %	Population Below $2 a day %	Gini Index	MLD
Argentina	13,652.41	1996	y	1.10	9.80	0.486	0.429
		2003		6.60	17.40	0.513	0.510
Bolivia	2,579.16	..	y	..	..	..	..
		2002		24.00	42.90	0.602	0.709
Brazil	7,825.78	1995	y	10.50	23.30	0.615	0.756
		2004		7.60	19.80	0.570	0.617
Chile	10,938.57	1994	y	0.90	10.80	0.552	0.548
		2003		0.50	5.60	0.549	0.539
Colombia	6,886.04	1995	y	3.10	16.30	0.572	0.611
		2003		7.60	19.40	0.588	0.669
Costa Rica	9,646.49	1996	y	3.60	13.30	0.471	0.419
		2003		1.80	9.60	0.498	0.459
Dominican Republic	7,617.82	1996	y	1.80	11.70	0.487	0.426
		2004		2.80	16.20	0.516	0.476
Ecuador	3,981.58	1994	y	16.80	37.40	0.520	0.511
		..		..	..	..	..
El Salvador	4,775.52	1995	y	20.80	47.10	0.499	0.454
		2002		20.40	40.50	0.523	0.541
Guatemala	4,150.21	..	y	..	..	..	..
		2002		13.90	32.60	0.553	0.581
Haiti	1,479.34	..	y	..	..	..	..
		2001		52.90	77.60	0.600	0.675
Honduras	3,170.33	1994	y	23.70	48.20	0.552	0.573
		2003		14.10	36.00	0.539	0.523
Jamaica	3,907.43	1993	c	4.90	27.50	0.357	0.221
		2004		0.50	14.40	0.455	0.357
Mexico	9,967.30	1995	c	8.40	26.00	0.537	0.528

		2004		1.90	12.50	0.461	0.379
Nicaragua	3,538.94	1993	c	47.90	77.90	0.504	0.452
		..		..	..	..	..
Panama	7,234.06	1995	y	7.40	17.40	0.571	0.645
		2003		6.00	16.80	0.561	0.603
Paraguay	4,368.11	1995	y	19.40	38.50	0.591	0.687
		2003		13.60	29.80	0.584	0.660
Peru	5,725.07	1994	y	9.40	31.60	0.449	0.350
		2003		10.50	30.60	0.520	0.489
St. Lucia	6,482.11	1995	y	25.20	59.60	0.426	0.316
		..		..	..	..	..
Trinidad & Tobago	14,708.07	1992	y	5.10	23.20	0.403	0.288
		..		..	..	..	..
Uruguay	9,897.78	1996	y	0.60	4.60	0.438	0.344
		2004		0.00	9.20	0.461	0.378
Venezuela, RB de	6,485.33	1995	y	9.40	28.80	0.468	0.402
		2003		18.70	40.20	0.482	0.461

Note: y or c in the column 4 shows whether the surveys conducted and inequality measures are based on income (y) or consumption per capita..
Source: Ferreira and Ravallion (2008), Table 1.

The incidence of poverty as measured by the headcount ratio ($1 poverty line) declined substantially world-wide from 40 % to 18 % between 1981 and 2004 as shown in Table 4. The headcount ratio fell in every developing region even in Sub-Saharan Africa. What is perhaps most noteworthy is the relatively poor performance of the LAC region in reducing poverty. The poverty estimates seem to swing up and down like a yo-yo around a level of 10 per cent from one sub-period to another. While the headcount fell from a high of 12.1% in 1987 to a low of 8.4 % in 1993, it is remarkable (and a source of concern) that the latest estimate of 8.6 % in 2004 reveals essentially no progress in combating poverty during this eleven years' period. Across LAC countries achievements in reducing poverty were decidedly mixed. For those LAC countries appearing in Table 3 that could rely on at least two household surveys during the period under consideration, poverty increased in 4, fell in 9 and yielded ambiguous results in two (e.g. Peru where poverty rose based on the $1 a day line and fell using the $2 line). Most noteworthy is the rise in poverty incidence in Argentina from 1.1 % in 1996 to 6.6 % in 2003 and from 3.1 % in 1995 to 7.6 % in 2003 in Colombia. Conversely, the headcount ratio fell significantly in Brazil from 10.5 % in 1995 to 7.6 % in 2004 and from 8.4 % to 1.9 % in Mexico during the same period.

Table 4: Global Comparisons of Poverty Trends: Major Developing Regions, 1981-2004

	1981	1987	1993	1996	1999	2002	2004
Income poverty[1] (headcount ratios)							
Sub-Saharan Africa	42.3	47.2	45.5	47.7	45.8	42.6	41.1
Latin America and Caribbean	10.8	12.1	8.4	8.9	9.7	9.1	8.6
South Asia	49.6	45.1	36.9	36.1	34.9	33.6	30.8
East Asia	57.7	28.2	25.2	16.1	15.5	12.3	9.1
E Europe and Central Asia	0.7	0.4	3.6	4.4	3.8	1.3	0.9
Middle East and North Africa	5.1	3.1	1.9	1.7	2.1	1.7	1.5
World total	40.1	28.7	25.6	22.7	22.1	20.1	18.1
Ratio: SSA/World	1.05	1.64	1.78	2.11	2.07	2.12	2.27
Income poverty[2] (numbers million)							
Sub-Saharan Africa	167.5	222.8	252.6	286.2	296.1	296.1	298.3
Latin America and Caribbean	39.4	50.0	38.8	43.0	49.0	48.1	47.0
South Asia	455.2	471.1	436.7	452.9	463.4	469.6	446.2
East Asia	796.4	428.8	420.2	279.1	276.5	226.8	169.1
E Europe and Central Asia	3..0	1.6	16.9	20.9	17.9	6.0	4.4
Middle East and North Africa	8.8	6.4	4.5	5.4	5.7	4.9	4.4
World total	1470.28	1180.7	1170.17	1087.8	1108.6	1051.5	969.5
Ratio: SSA/World	0.11	0.19	0.22	0.26	0.27	0.28	0.31

Sources: Ferreira and Ravallion (2008)

Notes: 1. Ferreira & Ravallion (2008): Table 2; based on international poverty line ($1.08 1993 PPP)
2. Ferreira& Ravallion (2008): Table 4; based on international poverty line ($1.08 1993 PPP)

3.2 Interrelationship among Trade Openness, Growth, Income Distribution and Poverty

Within the context of Latin America, no clear relationship stands out between the degree of trade openness of a given country (as measured by the TIR) and the GDP growth rate of that same country. Yet a few suggestive observations can be derived from the time trends discussed in the preceding sub-section. First, a significant time lag appears to have prevailed between the initiation of trade liberalization policies and a subsequent increase in the relative magnitude of trade as the previously mentioned examples of Argentina and Brazil suggest. Thus whatever causal link might exist between trade openness and growth

is likely to occur with a lag. This is not surprising given that the TIR is endogenous and is influenced not only by the trade liberalization process but also by various other factors such as the domestic business cycle and exchange rates. Secondly, a comparison of the evolution of TIRS and GDP per capita growth rates for selected LA countries (Tables 1 and 2) suggests what can at best be considered a hypothesis, i.e. that the direction of influence between trade openness and growth might well go in both directions. For example, Argentina grew extremely fast in 1990-94 (5.3 % per capita GDP per annum) during the period it liberalized trade but its TIR only rose in 1995-99. The evolution of GDP and TIRs in Argentina, Chile, and Colombia could provide some support for the hypothesis that trade liberalization contributes to growth with a lag but, in turn, facilitates the implementation of a further round of liberalization.

Many economies in South and Central 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 Africa, they have been largely vulnerable to external shocks. 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 low and often negative growth rates in per capita income reviewed earlier.

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 re-integrated 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 per capita was only slightly above 1 % during the nineties as we saw in the previous sub-section. Sanchez (2003) succinctly summarises the prevailing reflection on the region's economic performance over the last two decades of the 20th century 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 (p.1977)". On the whole, the globalization–induced economic growth in the region has been much more precarious and fragile than that recorded in Asia throughout- at least until 2004.

In contrast to Asia, the Latin American region has experienced not only low growth but also a 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 labor force, while the number of small and

informal low productivity enterprises continues to grow. Thus, labor 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.[27] 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 that the self employed now account for one-third of the labor 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 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).

The descriptive statistics in Tables 1- 3 do not suggest any clear relationship between trade openness, on the one hand, and income distribution and poverty, on the other. Yet certain links can be observed. The most successful and continuous LA globalizer, Chile, managed to practically eradicate the incidence of $1 a day poverty without, however, being able to reduce its highly uneven income distribution (a Gini of .55 throughout the last decade as Table 3 shows). Two other globalizing nations, Brazil and Mexico, were also able to reduce poverty and income inequality significantly. On the other hand, in Argentina and Colombia, where trade intensity rose fairly substantially in 2000-04, poverty increased significantly and income distribution worsened considerably in the former.

Are there plausible explanations for the divergent relationships highlighted above? How did the various globalization transmission channels discussed in Section 2 ultimately affect poverty given the different initial conditions prevailing across Latin America? Can some of the apparent inconsistencies be resolved and a somewhat more transparent picture drawn of the inter-relationship between trade openness, growth, income distribution and poverty? Next we make an attempt in that direction and suggest at least some answers.

3.3 Factors Influencing the Differential Impact of Globalization on Poverty across Latin America

Poverty is influenced by a multiplicity of factors and variables and it is only possible in a very limited way to separate the impact of the forces of globalization from all the others. In what follows, we return to the globalization transmission channels discussed in Section 2 to determine how they operated in affecting poverty within the context of Latin America. Next, we analyze the effects on poverty of 1.different initial conditions across

[27] See Kakwani et.al (2008) and Gindling and Terrell (2008) for detailed analyzes of effects of globalization, growth and institutional changes on labor markets in Brazil and in Honduras respectively.

LA countries; 2.some other manifestations of globalization than trade openness; and 3. the individual pattern of growth followed by different LA countries.

Before attempting to draw some inferences about the impact of the major globalization channels on the poor in LAC it is useful to mention the three stylized facts derived by Ferreira and Ravallion (2008) from their world-wide review of evidence: "1. economic growth tends to be distribution-neutral on average in developing countries, in that inequality increases about as often as it decreases in growing economies; 2.measures of absolute poverty tend to fall with economic growth; and 3. the higher the initial level of inequality in a country or the greater the increase in inequality during the growth spell, the higher the rate of growth that is needed to achieve any given (proportionate) rate of poverty reduction."

While potentially the most powerful channel in alleviating poverty, the discussion in Sections 2 and 3 revealed clearly that the growth engine within most of Latin America sputtered at best and was much too weak, between 1980 and 2004, to have had any significant effect in pulling many households out of poverty (stylized fact 1 above). Secondly, the distribution of income and assets in the region is known to be the most unequal in the developing world and, until the first half of the current decade, has continued to deteriorate in 9 LA countries, improving in 2 countries and remaining essentially constant in 4 countries (see Table 3 and Section 3.1). As the major World Bank study on "Inequality in Latin America" indicates "…for the majority of Latin American countries the economic changes of the last half century have been mainly dis-equalizing." (de Ferranti et al, 2004). Since, as was pointed out in Section 2, the state of income distribution acts as a filter between growth and its poverty outcome, the combination of very low GDP growth rates per capita, high initial income inequality and generally rising inequality that have characterized the structure of growth in Latin America over the period under consideration translates into a marginal impact on poverty at best (stylized facts 2 and 3 above)[28].

The fact that there appears to be a tendency towards convergence among LA countries in terms of the evolving state of their income distributions does not alter the above statement as it implies greater inequality in many countries even if compensated by less inequality in others. This bleak appraisal of the very limited capacity of the growth and income distribution channels (because of their inherent weakness) to affect poverty at the level of the LAC region as a whole raises the question of why the performance in terms of poverty reduction was actually so much better in a number of individual LA countries than one could have expected by focussing only on the aggregate growth and distributional picture. In order to answer this question, we need to explore how trade liberalization and some other manifestations of globalization affected the pattern of growth differently in specific countries characterized by different initial conditions.

[28] Incidentally, "the distribution-neutrality of the growth process on average" claimed by Ferreira and Ravallion (2008) in their first stylized fact above does not seem to hold with respect to Latin America in the last three decades or so.

The trade literature typically explains the observed increasing income inequality in terms of a wage premium benefitting the skilled workers versus the unskilled (or alternatively the workers in the formal sector compared to the workers in the informal sector). The explanation for the increased skill premium is that it is driven by the increased demand for skilled workers which, in turn, is linked to trade liberalization through: 1. an increase in the returns to particular occupations that are associated with a higher educational level; 2. a shift in the production of skill-intensive intermediate goods from developed to developing countries; and 3. skill-biased technological change and the transfer of capital- and skill- intensive technology accompanying the flows of FDI.(Goldberg and Pavcnik, 2004; Harrison and Hanson,1999). In most Latin American countries the initial conditions prior to trade liberalization were that the most heavily protected sectors were those sectors that use unskilled labor more intensively. Under those circumstances trade liberalization might cause unskilled wages to decline and wage inequality to increase. Argentina provides a good example of this process at work during the nineties, coinciding with the second episode of trade liberalization with a resulting large increase in inequality (7.7 Gini points between 1992 and 2001 as described in Section 3.1)[29]. In contrast, the initial conditions in Brazil were such that effective protection prior to trade liberalization was higher in skill-intensive industries with the consequence that the wage distribution and, in turn, the income distribution became significantly more even after the trade liberalization episode of 1988-95 (Ferreira et al, 2008).[30] As a result of these differences in initial conditions the poverty head count ratio rose markedly in Argentina and fell in Brazil.

Another characteristic of the Latin American income distribution is the increasing polarization at both ends of the distribution. It is likely that the macroeconomic adjustments brought about by the massive disruptions coming from global financial crises exacerbated this polarization. While some of these shocks were truly exogenous at least some of them were self inflicted and caused by unsound populist monetary policies. This high vulnerability to shocks has undoubtedly made the process of building institutions that could help resolve distributional conflicts more difficult.

Mexico and Brazil were able to achieve a major fall in poverty between 1995 and 2004 in spite of unspectacular growth (the headcount ratio fell from 8.4 % to 1.9 % in Mexico and from 10.5 % to 7.6 % in Brazil). Through such social protection schemes and investment in human capital and health as the Mexican Progresa (now Oportunidades) and the Brazilian Bolsas, the rural poor households, in particular, benefited from a variety of public services and goods. These schemes were essential in reducing rural poverty which is relatively much higher than urban poverty and only indirectly affected by trade liberalization as the latter normally reduces tariffs on industrial but not on agricultural goods. 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). Kakwani et al (2008) through a rigorous empirical analysis of the relationship between growth patterns, poverty and inequality in Brazil (in a case study discussed in Section 4 below) provide an important insight into the crucial role of incomes derived

[29] See Galiani and Porto (2008)

[30] The Ferreira case study is discussed in more detail in Section 4.

from social security and other government transfers in cushioning the effects of macro shocks, triggered by the forces of globalization, specifically among the poorest segments of Brazilian society during the period, 1995-2004. Skoufias et al (2008) in another case study reviewed in Section 4 also examine the performance of various schemes of public transfers in eight countries in the region. In summary there appears little doubt that social protection and other public programs investing in the human and health capital of the poor have had a substantial impact on reducing poverty in many LA countries.

Paradoxically, while the evidence is persuasive that income inequality is high and rising and contributing to perpetuate poverty in a number of LA countries, 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. Again, the public programs initiated in the 1980's and the more recent ones discussed above must have contributed significantly to the observed reduction in health and education inequality.

Potentially, trade liberalization could lead to a process of labor reallocation But because of fragmentation and rigidities in most labor markets in Latin America relatively little reallocation has occurred - Brazil being one of the exceptions. There is some evidence that suggests that declines in tariffs are associated with an increased probability of informal work which, in turn, could contribute to inequality (Goldberg and Pavcnik, 2004). The benefits of more flexible and better functioning labor markets on employment, efficiency, equity and poverty alleviation could be significant. Likewise, reducing the barriers to international migration can contribute to improving the income distribution and even, in some instances, to alleviate poverty through the flow of remittances sent by the migrants to their families in their countries of origin.

4. The Role of Institutions as Channels to Improve the Pass-through from Globalization to poverty Reduction; Findings from Specific Case Studies

In Section 2 we highlighted the critical role institutions can play in mediating the various channels and mechanisms through which globalization affects poverty. Institutions- defined in a broad sense as including policies- can act as channels in moderating some of the negative effects of globalization on the poor and, alternatively, strengthening and reinforcing some of the positive effects. In what follows we selected eight case studies out of fourteen presented at a conference in Rio organized by the authors of this paper

under the auspices of the WIDER project at the end of 2006[31]. These studies illustrate within different specific settings how institutions can contribute to render the process of globalization more pro-poor. These studies also demonstrate that the impact of globalization on poverty is extremely context-specific, reflecting the heterogeneous and complex nature of the globalization-poverty nexus.

The case studies that follow have been grouped into four broad and somewhat interrelated categories: 1) Social protection schemes, public transfers and interaction with labor income to induce a more pro-poor growth pattern ; 2) Trade liberalization and effects on income distribution and poverty; 3) More efficient labor markets and migration opportunities; and; 4) Property rights.

4.1 Social Protection Schemes, Public Transfers and Interaction with Labor Income to Induce a more Pro-Poor Growth Pattern

Kakwani, Neri and Son (2008) analyze the relationship between growth patterns, poverty and inequality in Brazil during its globalization process, focusing on the role played by the labor market and social programs. The paper makes two significant methodological contributions, first, a new measure of pro-poor growth is formulated and, secondly, a decomposition methodology that explores linkages between three dimensions: growth patterns, labor market performances, and social policies is derived. An individual's utility function is specified to depend on his/her income as well as on the individual's sense of deprivation captured by the number of people who are better off. The authors derive a growth equation consisting of the growth rate of mean income and the growth rate of inequality. The pattern of growth is defined as pro-poor if the former is greater than the latter.

In the second contribution, the growth of per capita income is explained in terms of four components: the employment rate, hours of work in the labor market, the labor force participation rate, and productivity. In addition, Kakwani et al assess the contribution of different non-labor income sources to growth patterns and more particularly on the expansion of targeted cash transfers and pro-poor social security benefits. The application of the above methodology provides important insights into the role of public transfers and safety nets in Brazil during an extended period (1995-2004) of negative per capita growth. While labor markets were quite adversely affected, incomes derived from social security and other government transfers played a crucial role in cushioning the effects of macro shocks (some triggered by the forces of globalization) -specifically among the poorest segments of Brazilian society. The lesson for other developing countries is that in the face of negative income shocks at the macro-economic level related to the process of globalization, governments need to take a pro-active and pro-poor stance. The institutionalization of safety nets and transfers benefiting the poor can act successfully as a buffer sheltering the poor during periods of financial and economic crises.

[31] A few of the papers presented at the WIDER Rio Conference were commissioned. The majority (about half a dozen) were selected by the co-directors of the project (Machiko Nissanke and Erik Thorbecke) out of about one hundred submissions generated by a call for papers.

Globalization could adversely affect income inequality and poverty through skill-biased technical change as well as increasing international competition. In such cases, Skoufias, Lindert and Shapiro (2008) argue that effective instruments to redistribute income to the poor through public transfers are critical as means for alleviating the negative effects of globalization on inequality. The paper explores the redistributive effects of public transfers, in particular social insurance schemes and specifically designed social assistance programs. Using household survey data, it analyzes the simulated impact of 56 transfer schemes in 8 Latin American countries (Argentina, Brazil, Chile, Colombia, the Dominican Republic, Guatemala, Mexico and Peru). Mitigating the negative effects of globalization on inequality is of particular importance in the Latin American region, where there is widespread dissatisfaction with the social injustice resulting from high poverty and inequality levels.

The findings of Skoufias et al suggest that social assistance programs are far more effective than social insurance schemes at redistributing income and contributing to social welfare, per unit of currency transferred. They also suggest that a) social assistance programs have a stronger impact on reducing inequality than social insurance schemes; b) the impact of the latter on inequality is fairly small – and in some cases these schemes actually increase inequality (Guatemala, Peru). In contrast, social insurance schemes in Argentina, Brazil and Chile tend to reduce inequality; c) the poverty impact of public transfers vary significantly across countries in Latin America; and d) the relative success of Conditional Cash Transfers in redistribution is driven by the need to define clearly who the targeted poor are.

It is clear that the success achieved by Brazil (through its social security program and such schemes as Bolsa Escola and Bolsa Familia) and Mexico (through Progesa and other transfers) contributed significantly to the observed remarkable fall in the incidence of poverty in those countries. The relative share of income from social security income doubled from 10 % in 1981 to 20 % in 2004 (Ferreira, Leite and Litchfield, 2008). If the imputed value of the benefits received by the households from the two Bolsa schemes were added to their disposable incomes, the rise in the relative share would be even more pronounced. In addition, to the extent that these measures contribute to the human and health capital of poor households and, in particular to that of their children, they will also accelerate the process of future growth and poverty reduction.

4.2 Trade Liberalization and Effects on Income Distribution and Poverty

While the process of trade liberalization and its impact on growth, distribution and poverty has been extensively discussed in this paper it is useful to focus on a couple of specific case studies. Ferreira, Leite and Wai-Poi (2008) explore the impact of trade liberalization (a key instrument in the spread of globalization) on wage inequality in Brazil. Using a nationally representative sample of workers in all sectors of the economy, the paper seeks to quantify the effects of the 1988-1995 trade liberalization episode on the Brazilian wage distribution. The main finding is that trade reforms did contribute to the observed reduction in income inequality in the last decade through two main channels: 1) trade –induced changes in employment levels across sectors, industries and formality categories; and 2) changes in the economy-wide skill premium which fell

together with the returns to education. The combination of trade liberalization and social programs were instrumental in the observed substantial reduction in inequality and poverty in Brazil since the mid-nineties

The Brazilian experience is in conflict with much of the literature on trade liberalization in Latin America which suggests that it has contributed to an increase in inequality- or at least to the gap between skilled and unskilled wages. Ferreira et al (2008) explain that Brazil was an exception to the Latin American pattern in that effective protection prior to trade liberalization was higher in skill-intensive industries –in contrast with most other Latin American countries. The lesson for policy-makers would seem to be that in countries where protection was stronger for industries intensive in skilled workers there need not exist any mandatory trade-off between gains in efficiency and productivity on the one hand and increases in inequality or poverty on the other following trade liberalization.

Alternatively in countries where sectors intensive in unskilled workers enjoyed more protection prior to liberalization , it raises the interesting question as to whether the tariff reduction and harmonization process over time could be designed in such a way as to reduce some of the negative consequences on the unskilled and on income distribution in the short and medium term.

Most of the existing empirical literature on the effect of trade liberalization on inequality in Mexico focuses on the wage earners and shows a rise in income inequality on account of an increase in the relative demand for, and the relative returns to, skilled labor. As the self employed, accounting for one-third of the labor force, are one of the vulnerable groups in the economy, operating almost entirely in the informal sector, Popli (2008) examines the trend in income inequality and poverty among the self-employed workers in Mexico for the two decades (1984 to 2002), during which Mexico opened its economy to the global market through trade and investment liberalization. As firms are subject to increased competition as liberalization proceeds, the informal sector is seen to expand in the need to absorb negative income shocks as workers in the formal sectors are laid off, giving rise to the fear of 'social exclusion' of the self-employed.

Popli finds that during the first decade following the liberalization, inequality and poverty increased among the self-employed; however, during the second decade, she observes that as the economy stabilized while experiencing economic growth, inequality started to go down, but poverty kept increasing. To understand these changes in inequality and poverty in relation to the self-employed workers, she decomposes the inequality and poverty indices into within and between group effects- employing well-established decomposition methods.

Her decomposition analysis reveals that raising relative returns to skilled labor contributed to increasing both inequality and poverty. As the supply of skilled labor rose, inequality started to go down. This is reflected in the narrowing of the gap between the mean incomes of the skilled and the unskilled self-employed workers. However, she argues that as the self-employed are largely unskilled, the relative lower returns to them

meant a continued increase in poverty for that group. Popli further confirms that there are significant regional differences in the impact of liberalization effects within Mexico. The central and southern states, where the self-employed are concentrated, are lagging behind other regions in benefiting from the forces of globalization. Again the above analysis of the self employed suggests that the large scale social protection schemes undertaken in Mexico must have acted as a buffer in moderating some of the negative effects of trade liberalization on the overall incidence of poverty.

4.3 More Efficient Labor Markets and Migration Opportunities

Aguayo-Tellez, Muendler and Poole (2008) examine how factors relating to globalization affect an individual decision to migrate internally within Brazil, where only 66 per cent of its labor force held a formal sector job in 1997 and considerable economic disparities across regions continue to prevail. The level of per capita GDP in the southern regions is more than triple that in the northern regions. The authors argue that while interstate migration has a long history in Brazil, an accelerated rise in foreign direct investment and export activities in the process of increasing integration into the global economy, following the dramatic market-oriented policy reforms, has contributed to a spurt in internal migration of formal-sector workers. This migration spurt occurred within the Southern states already endowed with a high concentration of well-established firms, as well as from the South and Southeastern states to the Northeastern state, where many foreign-owned and exporting firms started to locate their operation.

Aguayo-Tellez et al test the hypothesis that formal sector workers' mobility and migration is directly affected by globalization, using a uniquely matched data set of workers and their establishments across all states of Brazil for 1997-2001. Their analysis shows that prospective employment at a foreign-owned establishment exerts a positive and significant pull effect on formal-sector internal migration flows. They found that rather than responding to the spot wage differentials, workers' decision to migrate is likely to be made on the expectation of a steeper wage path, human capital accumulation or other forms of non-pecuniary compensation at a destination establishment, the majority of which is foreign owned. Thus, they conclude that globalization acts on internal migration through the growth of foreign-owned firms and employment opportunities as a pull factor. It is also possible that the migratory flows described above contributed to the process of income convergence between the rural and urban areas of the country mentioned by Ferreira, Leite and Litchfield (2008) as an important contributing factor to the fall in income inequality in Brazil during the last decade.

De la Fuente (2008) examines the globalization effects on the poor through one of the manifestations of migration, namely, through the channel of international remittances. The paper focuses on Mexico where the flow of remittances from largely U.S.-based migrants has become the dominant source of foreign exchange revenues. The author tests a popular claim that international remittances could become a massive resource transfer mechanism to reduce poverty levels by increasing incomes of poorer households. To verify this claim, the paper examines whether people who are most vulnerable to shocks and falling into poverty would be likely to receive remittance transfer or not. For this purpose, a 'vulnerability to poverty' index (the VTP index) is formulated and computed.

This index is a forward-looking measure of the magnitude of the threat of future poverty that a household might experience- computed from a household panel data set extending from October 1998 to November 2000. The VTP index is then used as an explanatory variable, along with other characteristics (household socio-demographic characteristics as well as both idiosyncratic and covariant risks that households face), in a series of probit and tobit models of remittance transfers.

De la Fuente's analysis suggests that national and trans-national support available to the rural poor through remittances is surprisingly low and transfers are not going to the poorest members in rural communities in Mexico. His econometric estimation results further reveal that an increase in the threat of future poverty that rural families could experience (a higher VTP) actually reduces their likelihood of receiving transfers, including foreign remittances. On the basis of these results, the author concludes that though remittances are perceived increasingly as one of the main positive effects of globalization on the rural poor, facilitating foreign remittances for rural recipients should not be considered a safety valve against poverty nor a substitute for the introduction of publicly-funded schemes of social protection coupled with improvements in economic opportunities for the rural poor.

Macours and Vakis (2008) explore the impact of seasonal migration on early childhood development within the context of a poor, shock-prone border region in rural Nicaragua. The authors show that seasonal migration can play an important role in protecting early cognitive development of pre-school children in poor areas suffering from severe malnutrition problems. Paradoxically and somewhat counter-intuitively they find strong evidence that mothers' migration has a positive effect on early childhood development while fathers' migration does not. At least two factors account for this unexpected result: seasonal migrant mothers tend to bring more migration income home, possibly allowing them to allocate more income on children's welfare through a direct income and indirect empowerment effect (women as decision-makers in contrast to men tend to allocate a larger share of their budget to nutrition and child care). The income and empowerment gains of migrating mothers appear to more than offset the potential negative effects on early child development that could result from temporary lack of parenting (most children of migrant mothers were left in the care of their grand mothers). The evidence illustrates how one aspect of globalization, i.e. increased opportunities in seasonal migration because of higher South-South mobility, might positively influence early childhood development, and as such long term poverty reduction.

The lessons of these studies is that freeing the movement of people within and across regional borders can help create more flexible regional labor markets that allow increasing production of goods for which the region has a comparative advantage. In this sense globalization could contribute to both efficiency and poverty reduction. At the same time the study of de la Fuente warns us again of the dangers of governments relying exclusively on market forces and assuming a purely passive approach to the forces of globalization. Countries have to implement complementary national policies to improve the functioning of human capital markets and develop their technological capabilities.

4.4 Property Rights, Exports and Poverty Reduction

Globalization manifests itself through a variety of channels. Alfred and Erica Field (2008) explore the impact of trade liberalization and other reforms reducing market distortions on the shift away from traditional agricultural crops and towards those produced primarily for exports within the context of rural Peru. The opening up of the economy after 1994 brought about changes in relative prices between these two types of crops favoring the export crops. The econometric results confirmed that changes in these relative prices increased the likelihood that households would shift production towards these new export products. An interesting additional finding is that these tendencies appear to be strengthened if the farm household obtained title to their property over the period. A lesson to be drawn from this result is that weak property and titling institutions may inhibit the degree to which households can reap the benefits of the forces of globalization.

The authors also found that those households that began producing an export oriented crop over the period under consideration were much less likely to be poor at the end of their sample period (2004) while those who were unable to alter production due to reasons such as location, access to credit or lack of title to property continued to produce traditional crops and were caught in a poverty trap. Hence a passive approach to globalization is not enough to ensure that poverty will be reduced; the liberalization of markets must be accompanied by appropriate social programs and institutional reforms directed to the specific nature of the problems and constraints faced by those socio-economic groups suffering from poverty.

5. Conclusions

The case studies reviewed in the preceding section help us understand better how certain critical institutions and policies can make the process of globalization more responsive to the welfare of the poor in Latin America. The first and foremost conclusion is that the impact of globalization on poverty depends crucially on the specific context and environment under investigation. Given this qualification and the fact that relatively few generalizations are robust across different socio-economic settings, we can proceed to explore how the various globalization transmission channels described in Section 2 appear to have influenced poverty in Latin America.

The most potentially important channel is *growth*. High rates of economic growth as experienced in East Asia in the seventies and eighties and in China and India today translate into significant declines in the incidence of poverty even when the growth process is dampened by increasing income inequality (the positive effects of high growth on poverty reduction in these two countries are presently significantly greater than the negative effects resulting from rising inequality). In contrast, the growth engine in Latin America since the eighties has been very weak- except in the last four years. Clearly the growth engine sputtered and could not contribute to any significant reduction of poverty. To make matters worse the growth pattern for most countries of the region was associated with a rise in the degree of income inequality. The latest and most authoritative source

(Ferreira and Ravallion, 2008) reported that, between the mid-nineties and the mid-2000's, nine LAC countries suffered from a rise in income inequality, while inequality fell in two countries and remained essentially the same in four countries. The lethal combination of low growth and increased *income inequality* resulted in very little progress in the reduction of poverty in the region. The headcount ratio (based on a $1 a day poverty line) remained essentially the same in 2004 as in 1993- around 8.5 %. The aggregate statistics hide the good performance of some individual countries. The best performer by far in terms of terms of growth and poverty alleviation throughout the whole 1980-2006 period was Chile, where $1 a day poverty has been practically eradicated. Brazil and Mexico, in turn, have succeeded in reducing both inequality and poverty very substantially since the mid nineties in spite of unspectacular growth.

No clear relationship could be established between the degree of trade intensity (as a proxy for globalization) and growth at the country-level. Yet the analysis of the descriptive statistics yielded two hypotheses (that should be further tested): 1. a significant time lag between the initiation of the trade liberalization process and a subsequent increase in trade intensity; and 2. the direction of influence between trade openness and growth might well go in both directions. The link between trade openness and inequality is explained in the trade literature in terms of a wage premium benefitting the skilled workers relative to the unskilled workers when the initial conditions before liberalization tend to protect sectors using unskilled labor intensively more heavily than sectors relying more on skilled labor. This situation appeared characteristic of much of Latin America at the outset of the trade liberalization process- with some exceptions such as Brazil.

The case studies reviewed in this paper illustrated how certain types of institutions can help mediate the effects of globalization to the greater advantage of the poor. Two case studies focused on the key role that institutions and the policy framework can play to reduce the *vulnerability* of the poor to a variety of shocks triggered by the forces of globalization. Kakwani et al (2008) argue that in Brazil in the post-1995 decade, during which labor markets were negatively affected, income derived from social security and other government transfers played a crucial role in cushioning the effects of macro-economic shocks. Skoufias et al (2008) provided evidence of the effectiveness of social assistance programs throughout Latin America- particularly when they are clearly targeted to the poor. It is most likely that social protection schemes (such as Progresa in Mexico and the Bolsas in Brazil) were instrumental in contributing to the substantial reduction in poverty in these two countries.

Ferreira et al (2008) showed that *trade liberalization* can be a potent instrument to raise growth (efficiency) and reduce inequality simultaneously under the right set of initial conditions - as prevailed, for example, in Brazil in the eighties where effective protection prior to trade liberalization was higher in skill-intensive industries –in contrast with most other Latin American countries.. However, under different initial conditions, trade liberalization can hurt certain socio-economic groups. This is what Popli (2008) found in her study of how globalization affected the self-employed in Mexico. Increased competition from abroad led to firms laying off workers- many of whom ended up in the

informal sector. As the supply of largely unskilled self-employed workers rose they received relatively lower returns which translated into rising poverty.

Internal and international migration- induced by more flexible labor markets- is yet another institution (channel) through which globalization can affect poverty. Aguayo-Tellez et.al (2008) build a strong case that globalization in Brazil has had a major impact on the internal migration of formal sector workers It is likely that the large scale migration to the poorer northern regions contributed to reducing both inequality and poverty by creating new job opportunities. Macours and Vakis (2008) showed that seasonal migration by mothers leaving their children behind can play an important role in protecting early cognitive development of pre-school children in poor areas suffering from severe malnutrition problems. De la Fuente (2008) argues that remittances from abroad in the context of Mexico are not the panacea claimed by some investigators. While undoubtedly contributing to the observed fall in inequality in Mexico in the last decade, the flow of remittances should not be considered a safety valve against poverty nor a substitute for social protection schemes and public programs that contribute to the educational and health capital of the poor.

The final study by Alfred and Erica Field (2008) showed convincingly, within the context of rural Peru, that while trade liberalization after 1994 shifted relative prices towards exportables, weak property rights inhibited the extent to which relatively poor farmers could take advantage of those incentives. This is a good example of the key role of *property rights as an institution* (in this instance transparent and legally binding titling) in amplifying the potentially positive effects of globalization on poverty reduction.

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