

Introduction to the OUP volume

Comparative Analysis of the Globalization-Poverty Nexus in Africa, Asia and Latin America.

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1. Introduction

Alongside the issue of climate change, ‘globalization’ and ‘poverty’ epitomise 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. Both the prevalence and the depth of poverty in many parts of the developing world remain unacceptably high.

A question is often raised as to 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 booming 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 the world income distribution and limited- if not a lack of – income convergence among participating national economies and across regions as globalization has proceeded.¹ The regional trends in income inequality measured by the Gini coefficient show that within-country inequality has increased markedly in all regions except in the group consisting of the advanced high income OECD countries since the early 1980s (Milanovic, 2005 a & b, Birdsall, 2006). Within high income countries too, there are many which experienced growing inequality.

The progress on poverty reduction has also been uneven. The share of the population of the developing countries living below US\$1 per day declined from 40 per cent to 21 per

¹ . 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) provide 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 the world’s distribution dynamics, which are characterised by the tendency for stratification and polarisation.

cent between 1981 and 2001 and fell further to 18 % in 2004, but this was mainly achieved by the substantial reduction of the poor in Asia, in particular in China.² Furthermore, over the period 1981-2004, the total number of people living under US\$2 per day actually has 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 % in 1981 to 48 % in 2004.³ There is a clear disparity in the regional trends in poverty reduction. While East Asia and Pacific experienced the sharpest reduction in the number of the poor living below the US\$1 per day, poverty has increased significantly in Africa in terms of poverty incidence as well as the depth of poverty.⁴

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.⁵ 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.⁶ These concerns have generated a passionate debate worldwide as well as a powerful anti-globalization movement.⁷

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.⁸ Globalization is not purely driven by new technological innovations and progress or by 'neutral' market forces and other inescapable sociopolitical forces, as often depicted in popular writings.⁹ In particular, the current phase of globalization is, to

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

3 Chen and Ravallion (2007)

4 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.

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

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

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

8 See Kozul-Wright and Rayment (2004) for an extensive discussion on this policy-induced condition.

9 Helleiner (2001) emphasises 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

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 before 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 over the recent two decades or so, the question how globalization affects the world's poor has become one of 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 a robust insight into this critical nexus. Both concepts are multi-dimensional, and not easily captured in a composite index to be used in a meaningful manner in cross-country comparative studies or regressions.

Building on earlier research projects, the United Nations Universities' World Institute for Development Economic Research (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'.¹⁰ In addition to the methodological

terminological confusion. For discussion on the effects of technological progress on the shrinkage in space and time, see Cairncross (1997), Bairoch and Kozul-Wright (1996).

¹⁰ Machiko Nissanke and Erik Thorbecke are the co-directors of this project. The aim of this research 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

and conceptual conference held in Helsinki, October 2004, the project held three regional conferences focusing on Asia (in Tokyo), Africa (Johannesburg) and Latin America (Rio de Janeiro), respectively, during 2005-6.¹¹

In the project framework paper (Nissanke and Thorbecke, 2006a and b), 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 and 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.

This volume presents thirteen papers selected from the three regional conferences to illustrate the differential effects of globalization on growth, inequality and poverty in Asia, Latin America and Africa.¹² 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.¹³ At an aggregate level, there are discernible characteristics, specific to each of three developing regions, of the ways 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 one 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.¹⁴

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.

¹¹ See Nissanke and Thorbecke (2006d and e) for main findings from 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.

¹² Three separate publications -containing a collection of the papers presented at each of the three regional conferences -will cover region specific case studies other than those included in this volume.

¹³ . 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.

¹⁴ . See also Winters et. al (2004) for a detailed discussion on context-specific effects of trade liberalisation on poverty in developing countries.

The remaining part of this overview chapter is structured as follows: Section 2 presents a short 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 forces unleashed by globalization. Section 4 consists of a synopsis of the thirteen case studies (chapters) from Africa, Asia and Latin America appearing in this volume. On the basis of a comparative analysis of the regional experiences with globalization and case studies, in Section 5, we outline some policy measures which could make globalization more pro-poor.

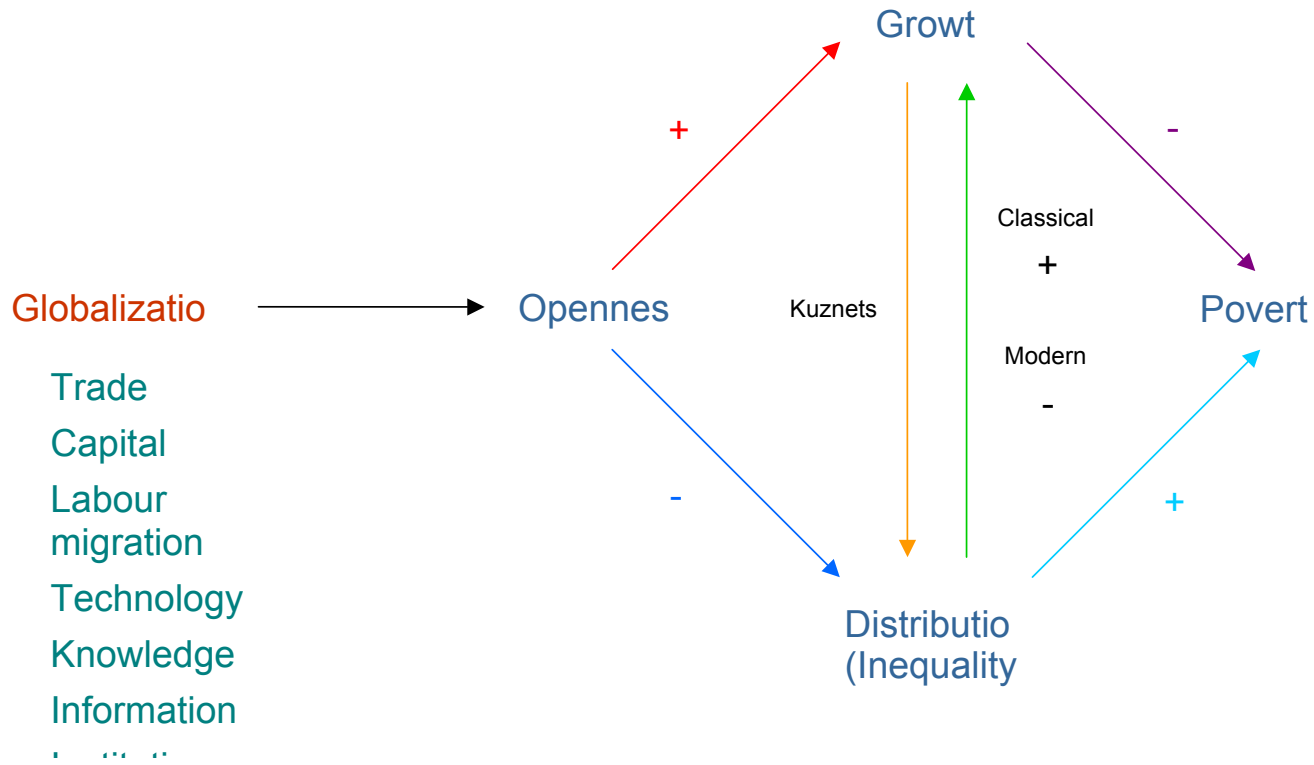
2. Channels Linking Globalization to Poverty

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 analyze 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 illustrates the various links of the causal chain from globalization to poverty as discussed in economic literatures. Greater openness is the major manifestation of globalization. The links shown in figure 1 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.

Figure 1. The Globalization–Openness–Growth–Inequality–Poverty Link



The openness-growth link

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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, as discussed in Section 3 below.¹⁵

Similarly, the transfer of technology, skills and management know-how that is assumed to accompany FDI are 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.¹⁶ 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, 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).¹⁷ However, the validity of these cross-sectional empirical exercises has been contested on technical grounds by many researchers.¹⁸

The growth-inequality-poverty interrelationship

¹⁵ Sanchez (2003) notes that "the causality link between trade openness and long-run growth is not engraved in stone (, p.1979)".

¹⁶ 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.

¹⁷ See World Bank (2002) for a summary of these cross-country studies on the openness-growth link.

¹⁸ 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.

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 a necessary condition 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.¹⁹ From this theoretical perspective, the desirability of an unequal income distribution is rationalised 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".²⁰

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 rights²¹ 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 growth²².

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-examination of the opposite causal flow in the link, i.e. the 'growth-inequality' link.²³ Many earlier development economists noted that economic growth, if left to market forces alone, tends to be accompanied by more inequality. Growth is inherently inequalising.²⁴ 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.

The conclusions drawn from the above analysis challenge the dominant mainstream views in development economics derived from a number of World Bank studies.²⁵ The

¹⁹ See Kaldor (1956) and Aghion et al. (1999) for discussion on the savings effects and the investment effects respectively.

²⁰ See Thorbecke (2006) for a critical review of the traditional approach to the inequality-growth link.

²¹ See Thorbecke and Charumilind (2002).

²² See also Aghion et al (1999).

²³ See Thorbecke and Charumilind (2002) for a comprehensive review of this new political economy literature on the subject.

²⁴ For example, Myrdal (1957), Rosenstein-Rodan (1943) or Hirschman (1958) as noted in Milanovic (2005b).

²⁵ Deininger and Squire (1996); Li, Squire and Zou (1998); Dollar and Kraay (2001, 2002).

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-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.²⁶

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.²⁷ If growth leads to an 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. 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 more pro-poor distribution of the gains from growth.²⁸ Hence what is relevant for poverty reduction is a ‘distribution-corrected’ rate

²⁶ For example, see Ravallion (2002)

²⁷ 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.

²⁸ 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.

of growth,²⁹ 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, as noted earlier. 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, as discussed in Section 3. 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 globalization ultimately affects poverty..

Technology and Factor Mobility in the Globalization-Poverty Nexus

For example, as 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 favour of skilled and educated labour.³⁰ 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. Especially, intensified privatisation 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 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.³¹

²⁹ Ravallion (2004).

³⁰ . Culpepper (2002).

³¹ . Baldwin and Martin (1999)

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, 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 globalization³².

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 equalisation 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 Transnational Corporations’ (TNCs) ability to re-locate 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.³³ 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 redistributive purposes.³⁴ Further, the poor and unskilled are most adversely affected by asymmetries in market

³² Baldwin and Martin (1999).

³³ Basu (2003).

³⁴ Tanzi (2001) discusses various effects of globalization on the tax system under ‘fiscal termites’.

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 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 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. 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.³⁵ 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.

3. Regional Characteristics in the Globalization-Poverty Nexus

3.1 Income Divergence in the South under Globalization

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 be at least partially attributed to the forces shaping the current process of globalization. In particular, the observed "big time" divergence of 'country-weighted between-country' income levels brings into question the validity of the openness-induced income *convergence* thesis, advanced by Sachs and Warner (1995^a) 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

³⁵ See Sindzingre (2006).

convergence club”³⁶. Based on a ‘human development trap model’, Mayer- Foulkes (Chapter 11 in this volume) shows that in the presence of multi-equilibria, development and underdevelopment co-exist 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.³⁷ 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 generally point to the existence of *threshold* effects in the globalization-inequality-poverty nexus, as postulated above 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 nature of integration and specialization of 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 specialisation 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.³⁸ In reality, however, the pattern of specialisation does matter for welfare implications of a trade-induced growth path on at least two accounts.

³⁶ This point was emphasised in Dowrick and DeLong (2001).

³⁷ See four studies on SSA included in Part II of this volume as well as additional six case studies focusing on SSA settings in Nissanke and Thorbecke (2008b), for empirical evidences. Dowrick and DeLomg (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.

³⁸ This two-sector model of international trade can be easily extended to N-sector models (for example, see Dornbusch, Fisher and Samuelson 1977).

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Two sectors need not be symmetrical, first, through the well-known immiserizing effect of trade *à la* Bhagwati, i.e. 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.³⁹

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

If a country follows the Rybczynski 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 characterised 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. Referring to as one of the fundamental differences between the two waves of globalization, Baldwin and Martin (1999) note that in contrast to the experiences under the late 19th-century globalization, when an enormous North-South income divergence was produced as a result of industrialisation of the North at the expense of deindustrialisation of the South, the current wave of globalization has industrialised the South whilst the North is experiencing deindustrialisation.

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

³⁹ See Maizels (1992) and Nissanke and Ferrarini (2001 and 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.

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 *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 benefits of economic growth trickled down to the poor as these developing economies were proceeded to integrate 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 Integration Experiences

Integration experiences in Sub-Saharan Africa (SSA)

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 of 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 Structural Adjustment Programmes 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).⁴⁰ 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 foreign direct investment 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, Sub-Saharan Africa 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.⁴¹ After two decades of reforms dominated by liberalization, privatization and

⁴⁰ . See Chapter 3 by Round in this volume for key aggregate statistics on trends in openness, growth, inequality and poverty.

⁴¹ . 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.

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, 1995, 1997 and 2001, Rodrik et al 2002, among others).

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 favorable 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 Sub-Saharan Africa.

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.⁴² In the past and current debt relief mechanisms, including the HIPC and MDRI initiatives, an effective and flexible facility of *contingency financing* to deal with external shocks on an *ex-ante* basis has been absent.⁴³

The failure of these 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 headcount ratio) in SSA reached 46 % in 2001- the highest of the major regions in the world.⁴⁴ 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 Sub-Saharan Africa (except the region of Southern Africa) in part thanks to the tradition of communal-land holding”. (Milanovic 2003, p. 2). The degree of income inequality in Africa has increased sharply between the 1980s and the 1990s, as shown in Chapter 3 below.

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.

⁴² See Nissanke (1993) for a critical review of macroeconomic adjustment policies over the commodity price cycles in mineral-based developing countries.

⁴³ 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.

⁴⁴ See Chapter 5 in this volume for the effects of globalization on non-income measures of well-being- health and education- in SSA.

Governments in SSA have systematically ignored (if not exploited) their agricultural sectors - failing to undertake pro-poor public investment in rural areas. Rather, they tended to extract a surplus from agriculture. 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.⁴⁵ 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 stabilisation-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.⁴⁶ 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.⁴⁷

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 economic development and poverty reduction. Instead, it 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; extremely under-developed physical infrastructure, and a related high risk investment climate⁴⁸.

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 \$1 a day in China fell from 53 % in 1984 to 13 % in 2003; and in Indonesia from 38 % to 7 % over the same period; Similar progress occurred in Thailand where the headcount

⁴⁵ . This line of characterisation of African states is found in Bates (1981, 1983). See also Teranishi, (1996)

⁴⁶ 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.

⁴⁷ 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.

⁴⁸ See Chapter 4 in this volume for a more thorough discussion of these issues. See also Nissanke and Thorbecke (2008b) for six case studies that examine the effects of different aspects of globalization on poverty in SSA.

ratio dropped from 18 % in 1988 to 1 % in 2003; and in India where it declined from 46 % in 1987 to 31 % in 2003 (Asian Development Bank 2004, 2005). The most recent estimates by the Asian Development Bank indicate that the incidence of extreme poverty as measured by the headcount ratio below the '\$1 a day' poverty line has further declined to 7.1 % in 2005 in China, while extreme poverty has practically disappeared in Thailand. In Vietnam poverty is estimated to have declined from 51 % in 1990 to 7 % in 2005 (Ali and Zhuang, 2007, and Asian Development Bank, 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 foreign direct investment (FDI) in *East Asia* in the 1960s and 70s 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 global experiences suggest that the positive openness-growth link is neither automatically guaranteed nor universally observable as noted in Section 2 above, 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 1997-8, 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 suited to the conditions prevailing in *East Asia* during that period.⁴⁹ The relatively quick turnaround of many emerging economies in *East Asia* in the years following the severe crisis of 1997-8 is often attributed to their strong export performance and renewed adaptability and flexibility in responding swiftly to new opportunities offered by globalization.

⁴⁹ .The eight countries, referred to as the High Performing Asian Economies in the East Asian Miracle Study, are Japan, Hong Kong, the Republic of Korea, Singapore, Taiwan, Indonesia, Malaysia 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).

Second, the structural transformation of most economies in East Asia has been facilitated considerably by the integration/globalization process. As discussed in Chapter 7 by Ozawa, 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 % in 1990 to 7 % in 2005 in East Asia including China, from 24 % to 7 % in South East Asia and from 42 % to 32 % in South Asia respectively.⁵⁰

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 and knowledge, 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 spillovers 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 outposts, health stations, and irrigation systems. In this context, Ozawa argues in Chapter 7 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 continue to reside in the rural areas- 63 percent 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 a) reducing surplus labor in agriculture, and b)

⁵⁰ According to the recent estimates (Asian Development Bank 2007), the incidence of extreme poverty is still very high in both Bangladesh and India, where this ratio is estimated at 36 % in 2005. . The incidence of extreme poverty is still very much prevalent in South Asia, where 476 million still live below the \$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.

through the remittances from migrant workers that presently account for a significant share of rural household income.⁵¹ Further, as emphasized in Chapter 10 by Hayami, 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).⁵² With the current wave of globalization, ‘within country’ income inequality has been steadily rising (Milanovic 2005a).⁵³ 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 1997-8, 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 2008^a) and Chapters 8 and 9 in this volume, 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’ (Asian Development Bank, 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.⁵⁴

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⁵¹. See Sawada and Estudillo (2008) for the effect of migrants’ remittance on poverty in the Philippines.

⁵² Milanovic (2005b) notes that while the disequalising force inherent to economic growth is noted by many classical development writers as discussed above in Section 2, an interesting question remains open whether there are countervailing forces to render growth spatially equalising 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.

⁵³ Strictly speaking the trends in world (global) income inequality depend on which concept of inequality is used for measurement (Nissanke and Thorbecke 2006b and 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.

⁵⁴ Aggrawal (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 .24 to .35 in China and from .25 to .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 (Asian Development Bank, 2007 and 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 (Asian Development Bank, 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).⁵⁵

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.⁵⁶ 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 (i.e. the poor benefit proportionately more than the non-poor).⁵⁷

Indeed, despite the sharp reduction in the incidence of extreme poverty (less than \$1 a day), poverty remains high in many developing Asia, if it is measured on the basis of ‘\$2-a day poverty line. It is estimated that the latter declined from 86 % in 1990 to 77% in

⁵⁵ . See Chapter 8 of this volume for a decomposition analysis of the Indian economy.

⁵⁶ See various chapters in Nissanke and Thorbecke (2008a) for detailed case studies that examine the effects of different aspects of globalization on inequality and poverty in Asia.

⁵⁷ See Kakwani and Son (2008) for a detailed empirical examination of ‘pro-poor’ growth in the Republic Korea, Thailand and Vietnam in the 1990s.

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2005 in South Asia, from 66 % to 43 % in Southeast Asia and from 72 % to 29% 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 wide-spread in Asia as a whole, and the challenge facing policy makers in the region in attacking poverty of this magnitude is non-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.⁵⁸ 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.⁵⁹

Integration Experiences in Latin and Central America

The region of Latin and Central America occupies an intermediate position in its integration experience compared to the other two regions. Like countries in SSA, many economies in Latin 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 SSA, they have been largely susceptible to the ‘global development cycle’, dominated by external shocks (Ocampo and Parra 2006).⁶⁰ 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.

After the belated market-based debt restructuring under the Brady Plan and the sweeping policy reforms of liberalisation 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 liberalisation and privatisation 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. Sanchez (2003)

58 . Campos and Root(1996)

59 See Asian Development Bank (2007) and Ali and Zhuang (2007) for the concept of ‘Inclusive Growth’ and the associated policy strategy advocated for the region.

60 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.

succinctly summarises 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 (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 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 foreign direct investment often took the form of asset acquisition of newly privatised public utilities rather than that of green field investment in productive capital. Operating within the 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 specialise in low-technology manufactures, operating largely assembly plants with little potential of technology and skill transfers (ECLAC 2004 and Sáinz 2006). Thus, during the recent spell of globalization, Ocampo and Parra (2006) remark that, "South America has experienced premature de-industrialisation, while Mexico and Central America avoided this trend by specializing in high-import intensive manufacturing exports, but with limited benefits in terms of growth (p.14)".

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 characterised by a high degree of segmentation in parallel with an increasing casualisation 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.⁶¹ 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 casualisation and informalisation 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 Columbia and other Latin American countries. The share of the informal sector in urban employment rose significantly in most countries of the region (ECLAC 2004).

⁶¹ 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,

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 % and mean of 54.7 % (Palma, 2006). Further, according to the ECLAC study, in the 1990s, the share of total national income accruing to the top 10 % of households continued to rise in most LAC countries. The average income of the richest 10 % of households was 19 times higher than the average income for the 40 % 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).

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.⁶² 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 WDI 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 characterised by a greater income *polarisation*. He explains this polarisation 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 % of GDP in 1976 to just 19 % in 2000. Wages in low-technology manufacturing sector, in which Mexican 'maquila' enterprises specialise, 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.

Further, 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.⁶³ For example, according to the definition used in the ECLAC reports, the percentage of the population in poverty in Latin America was higher in 2003

⁶² . See Harrison and Hanson (1999), Goldberg and Pavcnik (2004) and Chapter 12 in this volume for 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 (See Chapter 12 by Ferreira et. al in this volume).

⁶³ Sanchez (2003).

(44%) than in 1980 (40.5 %).⁶⁴ Poverty incidence is much higher in rural areas (64 %), than in cities (37%), although there is an ongoing increasing urbanisation 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 Progresca 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.⁶⁵

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 macro shocks, triggered by the forces of globalization, specifically among the poorest segments of Brazilian society for the period, 1995-2004. growth. Skoufias et. al (2008) also examine the performance of various schemes of public transfers in 8 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 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

⁶⁴ 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 \$1 a day and \$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).

⁶⁵ 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.

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 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. As will be discussed in Section 5 below, governments have increasingly faced serious constraints both in the fiscal front and monetary policy choices for sustaining public transfer programmes or other social policies in order to address growing inequality and the unacceptable prevalence of poverty.

4. Synopsis of the Book

Chapter 2 by Bhargava examines the effect of globalization on GDP growth rates, inequality and poverty by analysing the statistical relationships among relevant variables with aggregate panel data of 54 developing countries at 5-yearly intervals for the period 1990-2000. Using the trade intensity indices - the ratios of exports and imports to GDP - as representative of globalization measures, he investigates, in particular, the non-linear effects of literacy levels and measures of openness, in the form of trans-logarithmic model.

His empirical results underscore the importance of high literacy rates and life expectancy for developing countries in order to reap the benefits of globalization. Further, while his results reveal that the levels and growth rates of GDP are important for reducing poverty, globalization measured in export/GDP ratio and import/ GDP ratio separately were not significant predictor of poverty measures. This is interpreted as little evidence that globalization has been affecting poverty –either positively or negatively on the aggregate. His model estimated for inequality indicates that imports/GDP ratio and the proportion of the labour force with high skill levels may exacerbate inequality. This leads him to suggest that since the diffusion of technical knowledge to developing countries and the availability of an educated labour force are critical ingredients for economic growth, short-run increases in inequality may be inevitable. Overall, he concludes that developing countries need to invest additional resources in education and health to create a skilled labour force capable of enjoying greater benefits from globalization.

Part II of the book contains four papers examining the globalization-inequality-poverty relationships in Sub-Saharan Africa.

In examining the aggregate economic ‘openness’ indicators and their trends over time, Round in **Chapter 3** observe that : i) Sub-Saharan Africa is not behind other developing regions in terms of a trade intensity index (imports and exports relative to GDP in current US\$) and the average trade intensity has increased in Sub-Saharan Africa in line with the overall global increase; ii) In spite of the increase in trade intensity and inflow of FDI, however, Africa’s share of total world trade has fallen over these two decade.

Though there has been a marked upturn in the growth rates of per capita GDP in the region over the recent years, this is closely associated with the price hike of oil and other mineral commodities in the world markets. The growth rate of real GDP for oil-producing countries and resource-intensive countries in SSA during the period of 2002-5 was 6.2 % and 7.0 %, respectively, twice higher than those achieved by non-oil producing and resource-poor economies in the region

Further, the incidence and depth of poverty have risen in the region. Round reports that the number of poor, measured in income poverty based on the US \$1 a day international poverty line, increased in SSA, almost doubling from about 164 million in 1981 to 313 million in 2001. In terms of the headcount ratio, the poverty incidence in SSA is 46 % in 2001- the highest in the world. He also notes that the degree of income inequality in Africa has also risen sharply between the 1980s and the 1990s and within country inequality in SSA is now higher than in the rest of the world. Thus, he argues that despite considerable variations across countries in the region, empirical evidence and existing studies tend to suggest that globalization may be associated with increasing inequality and poverty in SSA.

However, a key issue in any attempt to estimate the impact of globalization on the poor is the lack of an appropriate counterfactual, i.e. what would have happened in the absence (or under a milder form) of globalization. Hence, Dercon in **Chapter 4**, argues that analyzing “globalization “ as a “natural experiment” is hardly possible and more structural modeling is required to understand its impact. He proceeds to bring forth persuasive evidence on one particular aspect of globalization: the likely impact of trade liberalization on households. Many African countries have been plagued by low or negative per capita growth rates and rising poverty levels. A simple explanation is that such countries suffered from bad policies, not least in terms of trade orientation. But this cannot be the full story as quite a few countries introduced some trade liberalization in the last two decades with very little effect on sustained growth. Dercon offers a related explanation that even with liberalization, growth was stifled by poor infrastructure, low education and corruption.

In particular, a strong case can be made that many African countries suffer from the fundamental disadvantages of location; landlocked, disease-prone, tropical countries with harsh natural environments face a fundamental cost disadvantage. There is much evidence that marketing, transport costs and transaction costs are very significantly higher in Africa than in Asia. In short, the limited scope of globalization in Africa and its slight impact on growth and poverty reduction is seen by Dercon to be the result of a combination of poor initial characteristics, such as inadequate political institutions, greatly under-developed physical infrastructure and a related high risk investment climate.

Africa is clearly not homogeneous. Broadly speaking, one could distinguish three Africas; first, the resource-rich economies such as Nigeria, Congo and Botswana; secondly, Central Africa, with potential access to relatively low cost transport facilities to the rest of the world such as Ghana, Cote d’Ivoire, Kenya and Tanzania; and, thirdly, landlocked Africa lacking harbors and natural resources with as typical examples

Ethiopia, Uganda and Burkina Faso. The development strategies appropriate to each of these groups and the potential gains from globalization differ significantly. In particular some landlocked economies have to rely on their agricultural sector as the sole engine of growth and source of export revenues before they can diversify into the production and export of non-agricultural commodities.

Taking Ethiopia as an example of such an insulated country, Dercon proceeds to analyze the impact of trade liberalization on living standards and poverty during the 1989-1995 period. He concludes that the trade reforms contributed to growth and poverty reduction in the surveyed villages but that the inadequately endowed poor, in terms of land and location benefited least. Further liberalization and engagement with the world economy may offer new opportunities for some rural areas and, more specifically, those areas enjoying good infrastructure and communications. A key lesson is that infrastructural investments appear to be correlated with differential growth experience suggesting that poorly endowed areas within Ethiopia are at risk of becoming even more marginalized during the era of globalization. Also, rural households are becoming more vulnerable to market-related risks triggered by trade induced shocks such as sudden changes in demand or in prices and need new instruments to cope with these emerging risks.

In **Chapter 5**, Sahn and Younger explore how globalization affected non-income measures of well-being-health and education- in Africa over the past 15-20 years. It is important to note that both anthropometry and educational attainment are far less subject to measurement error than income and expenditures measures, and both are directly attributable to individuals so that the difficult issue of intra-household allocation is avoided. The data used in the analysis came from 54 Demographic and Health Surveys conducted in 20 African countries that have at least two surveys. Overall, Sahn and Younger could rely on 32 spells of change in health and education poverty- usually five years long. They expected to find, as they had previously in Latin America, that progress in the provision of public services and the focus of public spending in the social sector would contribute to declining poverty and inequality in health and education, even in an environment of stagnant or worsening income poverty.

Unfortunately, their results indicate that in the area of health, little progress is being made in terms of reducing pre-school age-stunting, a clear and robust manifestation of poor overall health. For children's height there were 13 cases where the headcount ratio worsened, 10 in which it improved and 9 where it remained the same. Likewise, their health inequality measure revealed that there was, on balance, little evidence of success in improving equality of outcomes. With regard to inequality of children's heights the authors found more cases of worsening than improvements. Similar results obtained in their examination of underweight women as an indicator of general current health of adults. The story is somewhat more positive with regard to education. Reflecting the complexity and context-specific nature of the dynamic process, their empirical analysis of the effect of globalization does not suggest that globalization is correlated (positively or negatively) with health and education outcomes. However, the overall picture emerging gives little cause for optimism that Africa has, or will soon reap the benefits of the process of globalization.

In **Chapter 6**, van der Berg, Burger and Louw analyze the impact of globalization in the post-apartheid era on growth, employment, income distribution and poverty in South Africa. The picture they paint is that trade and financial liberalization appears to have positively, but modestly, influenced economic growth. On the other hand, employment was only marginally affected—with the jobs created being largely located towards the upper hand of the skill spectrum. Consequently, South Africans in the upper range of the income distribution seem to have reaped most of the gains from globalization.

The evidence regarding the poverty trend is somewhat ambiguous. However, the authors claim that, on the basis of a different data set than the usual Income and Expenditure Surveys, the headcount ratio fell between 2000 and 2004, from 51 per cent to 47 per cent. Rather than crediting the process of globalization for this reduction in poverty, van der Berg et.al. make a strong case that government action through social grants has been the most important contributor to poverty alleviation. Amongst groups, blacks continue to experience high and increasing intra-group income inequality yet one polarization measure appears to indicate that improvements in living conditions associated with expanding grants and the emergence of a black middle class have dampened to some degree the social tensions associated with material inequality.

Part III of the book contains four papers examining the globalization-inequality-poverty relationships in Asia.

In **Chapter 7**, Ozawa explains the staggered catch-up process and associated growth dynamism in Asia, as a whole and the very substantial reduction of abject poverty that has occurred in tandem in terms of ‘the Flying Geese Paradigm’ of *comparative advantage recycling*. He argues that the economies in this region have effectively initiated a succession of growth spurts based on a strong demand for unskilled labour, driven by exporting labour intensive goods and pro-trade FDI through effective technology and knowledge, skill transfer. In flying geese style (or the hegemon-led growth model), growth clustering develops, in which a hegemon economy (the lead economy or goose) propagates growth stimuli to its closely aligned cohort of countries that are at various earlier stages of development and structural transformation. The stimuli include dissemination of technology, knowledge, information, skills, and demand (via access to the hegemon’s home market), and provision of development finance—and above all, transplantation of growth-inducing institutional arrangements. Ozawa suggests that the region’s synergistic interactions result in agglomeration economies, enabling the *entire* hierarchy of countries to mutually gain, grow, and prosper.

Ozawa further emphasizes that the substantial poverty reduction in East Asia as a whole is not purely a manifestation of market-driven growth effects. In addition, pro-active policy interventions and institutional arrangements were in place to lessen the adverse distributional effect and produce shared, pro-poor growth. Ozawa argues that because poverty reduction is a public good, pro-poor policy interventions and institutional set-ups can always be justified and required to spawn growth-led poverty reduction. For example, the pro-poor pattern of public expenditures in favour of rural poor, such as extensive

public provision of education, physical and social infrastructure was a decisive contributing factor in sustaining the shared growth process in many countries in East Asia.

Chapter 8 by Bhanumurphy and Mitra examines the dynamic trajectory of the interrelationships among poverty, growth and inequality through a decomposition of the changes in poverty into a growth component and a distribution component. They show that the growth effect dominates the inequality (distribution) effects in poverty reduction in the two periods: (i) 1983 to 1993-94 and (ii) 1993-94 to 1999-2000 (the two periods are taken to represent broadly the pre-reform and post-reform periods, respectively). This finding obtains for the rural and urban areas of the 15 major states, and also for the all-India level. Their analysis suggests that the growth/mean effect dominates the inequality effect in both periods. India's economic growth, increased markedly from the 'Hindu rate of growth' of 4 per cent to the 'Bharat rate of growth' of 6 per cent after the deliberate policy shift towards pro-growth and pro-globalization in the early 1990s. This growth acceleration succeeded in reducing overall poverty, despite the rise in inequality in the second period. As the growth accelerated, there was a marked shift in the composition of GDP with a sharp decline in the share of agriculture and a corresponding increase in the share of services. However, since no such a shift was observed in the employment structure with the agricultural sector still absorbing a majority of the labour force, the debate continues whether the increase in output growth is a 'jobless growth' or not in India.

In this context, Bhanumurphy and Mitra also examine the net effect of population mobility on poverty, which depends on the rural and urban components of poverty. This effect is seen to capture the changes in the spatial composition of growth, reflected in terms of rural-urban development disparity which tends to lead to a migration of population from rural to urban areas. The decline in the incidence of poverty (rural-urban combined) depends on whether urban employment opportunities are large enough to absorb the increasing supply of labour migrating from the rural areas. It is conjectured that even when the incidence of urban poverty rises due to the rural-urban migration, the decline in the combined poverty ratio may occur as a result of a fall in the rural poverty incidence following out-migration, as rural poverty dominates the poverty profile for all-areas combined in the Indian economy. In India, the incidence of poverty declined both in rural and urban areas: rural poverty fell from 46 percent in 1983 to 37 percent in 1993-4, and further to 27 percent in 1999-2000, whilst urban poverty was cut from 42 percent in 1983 to 34 percent in 1993-4 and further to 24 percent in 1999-2000.

According to their decomposition analysis, there is a small 'population shift effect' in poverty reduction in the rural areas due to the rural-urban migration, in the first period, but that effect was marginal compared to the growth effect. They conclude that despite some variations across states, overall, the economic growth realized through pro-globalization reforms has produced a large decline in the poverty incidence in India by raising labour productivity and employment opportunities with the shift in value added mix towards industry and tertiary activities such as

information technology, business process outsourcing services, financial institutions, and infrastructure services.

In **Chapter 9**, Hayami emphasizes the employment creating impact of globalization benefiting landless labourers as an important conduit for reducing rural poverty. Using the survey data collected over three decades (1966-1997) in a rice-cultivating village in East Laguna in the Philippines, he examines the transformation of the village community under the forces of globalization manifested through: i) population growth due to the importation of advanced medical and public health technology; ii) the Green Revolution bringing along the transfer of advanced agricultural technology and the introduction of irrigated double cropping; iii) land reform programmes, shifting the land tenure status from sharecropping tenancy towards leasehold tenancy and owner-farming; and iv) expansion of non-farm employment opportunities as well as the greater use of hired labourers who had been negatively affected by the land reforms. The first two channels are considered the outcomes of international knowledge transfer under the current wave of globalization. Whilst the Green Revolution reduced real rice prices received by farmers, it also kept the cost of wage goods, and thus the wage rates in labour-intensive manufactures, from rising. This process allowed this rural community, as elsewhere in East Asia, to gain a competitive edge in producing industrial goods at the lower end of skill requirements, as part of the region's recycling of comparative advantages under the process of globalization discussed above.

Hayami further reckons that the creation of non-farm employment opportunities associated with rural based industrialization under globalization is seen as a most significant and direct factor for creating an opportunity for rural communities to reduce poverty and inequality in East Asia. In this context, he places a special emphasis on the importance of public investment in transportation and communication infrastructure, industrial extension activities and school education as well as building market-supporting institutions to protect property rights and enforce contracts.

Despite the impressive achievement in poverty reduction, the growing inequality under globalization has become a particularly pressing concern in China. Zhang and Wan explain in **Chapter 10** that since the late 1980s the engine of China's economic take-off shifted from agricultural growth spurred by the de-collectivisation of the rural areas to manufacturing exports fuelled by large FDI inflows. At the same time, progress in poverty reduction has stalled in urban China since the late 1980s. Through the estimation of the probability density functions for all the provinces, they find the following characteristics of *urban* poverty in China: i) income of the poor has not grown as fast as average income and the income shares of the poor have fallen accordingly; ii) the income growth of the poor has been particularly slow since the mid-1990s, and in several provinces, real income growth of the poor has stagnated; and iii) the further one moves away from the coast, the less favourable income distribution tends to become for the poor.

Further, they present the results of a number of regression analyses, based on the provincial level data, of the impact of globalization measured in openness to foreign trade and foreign investment on *urban* poverty. Their findings indicate that when the

globalization is separately accounted for in addition to the income growth measured by per capita income, globalization in general, and trade openness in particular, increases the income shares of the poor.⁶⁶ However, their results confirm that the inequality-reducing effect of trade was significantly weakened after 1992. Further, they find that the benefit from globalization accrues to the urban poor in the inland provinces just as much as it does to their counterparts in the coastal region. Hence, they conclude that globalization cannot be simply characterized as a process of pro-rich or pro-coastal provinces in China as popularly feared.

Part IV of the book contains four papers examining the globalization-inequality-poverty relationships in Central and South America.

In **Chapter 11**, David Mayer-Foulkes examines, through a rich theoretical model, how a human development trap can persist throughout the process of globalization. The model can explain persistent income inequality between and within countries, and compare the consequences of different policy regimes such as import substitution and export promotion. By allowing for multiple equilibria, the model shows that development and underdevelopment can co-exist as steady states in the context of globalization. An initial uneven distribution of assets can give rise to a human development trap that divides the population into classes where the lower class (the poor) is caught in a poverty trap from which they can not escape under the prevailing global and national policy regimes.

The model relies on only two types of market imperfections: 1) incomplete markets in human capital investment (poor households can not borrow to educate their children), and 2) innovation provides market power (technological leaders have an inherent advantage). As a result of those reasonable assumptions- negating competitive markets- resources under the impact of globalization will not flow so as to lead to convergence. Instead, divergence and greater inequality within and between countries have characterized the present wave of globalization.

The policy implications of the model are enlightening and potentially operationally useful. A foremost implication is that while globalization (in the form of greater openness and export promotion) is a necessary condition for convergence it is not sufficient. This means that countries have to implement complementary national policies to improve the functioning of human capital markets and develop their technological capabilities. Likewise, supra-national institutions such as the World Bank, the IMF and WTO must commit to balance the incentives for innovation and technological change to ensure that globalization brings economic development to all.

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

⁶⁶ . However, they also conclude that the growth in China has not been pro-poor or distribution-neutral, as the negative signs on per capita income in their regression results are interpreted as an adverse effect of average income growth on the income shares of the poor.

negative per capita growth. While labor markets were quite negatively 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.

In **Chapter 12**, Ferreira, Leite and Wai-Poi 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 Brazilian experience is in conflict with most 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 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.

On the basis of a longitudinal study of the favelas (shantytowns) of Rio de Janeiro spanning over three decades (1969- 2004) and four generations, in **Chapter 13** Perlman derives some fascinating insights on the determinants of geographical and social mobility, how people's lives changed over time and generations and what got better and what got worse over 35 years. A first observation is that at the community (favela) level the improvements in infrastructure and standard of living have been enormous. A comparison of socio-economic status indices at the end and at the beginning of the sample period reveals clear indication of movement away from poverty.

Yet, there are some disappointing trends. Due to the perversity of prejudice, educational gains for favelados are not fully reflected by their income. For every additional year of schooling (after the first four), the gap in expected income between the favelados and non-favelados grows wider. Barriers to upward mobility may have become stronger in the era of globalization and include community-level obstacles (increased violence related to drug and arms traffic and decreased social capital); and economic obstacles

(such as the stigma of favela residence, labor market conditions in Rio and extreme inequality).

The overwhelming finding of the study was that the majority of the respondents across all three generations said that globalization had not made any difference in their overall welfare. Looking at indicators of individual or collective consumption or educational levels one would conclude that there have been striking improvements in well-being. In contrast, looking at unemployment or violence (triggered by the drug trade) one would conclude that life is much worse now. Presumably, in the minds of most favela households these two opposite trends tend to compensate each other.

Perlman interprets the survey results as pointing that even as progress is being made at the material and educational levels, the goal of breaking out of poverty is a moving target. It is quite likely that the increasing flow of information about the living standards of others, both within and beyond country borders triggered by globalization can result in changing reference norms and increased frustration with relative income differences, even among respondents whose own income is rising. Somehow, economic achievements are not capturing the sense of lingering marginalization, disrespect and exclusion the poor feel despite indicators that objectively show that they are now less poor.

Globalization manifests itself through a variety of channels. In **Chapter 14**, Alfred and Erica Field 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 insure 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. Policies towards Making Globalization Pro-Poor

Strategic Policies towards Globalisation

The empirical case studies from the three developing regions under this WIDER research project support our contention laid out at the outset that effects of globalization on poverty is diverse, and in many ways, context-specific.⁶⁷ Indeed, our studies confirm the view that “the forces of globalization as such are not *inherently* beneficial or deleterious for development prospects (Sanchez, 2003, p.1978” *italics added*).⁶⁸

Yet, our comparative analysis of the globalization experiences across the three 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 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.⁶⁹

While the prospect of substantial poverty reduction can be increased considerably, wherever globalisation brings about job-generating economic growth, this potential is realised 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 economy⁷⁰.

⁶⁷. 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.

⁶⁸ 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.

⁶⁹ Making a clear conceptual distinction between ‘non-globalizers’ and ‘unsuccessful globalizers’, Jenkins (2007) 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.

⁷⁰ . 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’.

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.⁷¹ 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 policy makers 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 liberalisation 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 the recent decades. The markets for many labour-intensive products have come to resemble those for primary products.⁷² The entry of China and India into global markets for these products has depressed and will continue to depress real wages and returns 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 above, 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.

⁷¹ . Ocampo and Perra (2006, Tables 2 and 3, and Figure 9).

⁷² . Maizels (1998).

Second, intra-firm trade in parts, components and other intermediate goods and intra-industry trade with highly differentiated products command a predominant share of contemporary global trade. In particular, international trade is less and less conducted in arm's length relationships between firms. Rather a growing share of world trade is accounted for by intra-firm trade undertaken within TNCs. There has been a tremendous growth in offshore-outsourcing and global division of labour, dictated by TNCs' globally integrated production and marketing strategy. TNCs' activities are strategically organised and integrated either horizontally or vertically. In particular, with a sharp decline in transport and communication cost over the recent decades, TNCs have been aggressively organizing their operations vertically by slicing up the production process finely into numerous separate operations and locating them in different parts of the world according to cost advantages of each location.⁷³

In this context, it should be noted that considerable asymmetries in market power and access to information, technology and other intangible knowledge assets between TNCs, on the one hand, and local entrepreneurs, farmers and traders in developing countries, on the other, have resulted in a hugely skewed distribution of gains from trade. This is reflected in the TNCs' dominance in commodity and value chains of traded goods, as well as in frequently observed conditions such as the sharp decline in real wages in export processing zones (Kaplinsky 2000). Under this condition, the benefits of productivity improvements, instead of going to the fragmented producers and farmers, are largely appropriated by the TNCs and global supermarket chains.⁷⁴ This uneven distribution of market power points to the need to improve the negotiating positions of developing-country governments vis-à-vis TNCs, aiming at a strategic, targeted approach to FDI, so that FDI could facilitate skill- and technology-transfer and generate strong positive productivity spillovers benefiting domestic firms.

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.⁷⁵ 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.

⁷³ Krugman (1995) and Kaplinsky (2000).

⁷⁴ See Jenkins (2006) for examples of cases where farmers and workers in Asia and Africa have been increasingly exposed to worsening working conditions provided by TNCs. Carletto et.al (2008) also document difficulties facing smallholders in cultivating non-traditional crops and competing in global markets.

⁷⁵ . In this context, Lin and Liu (2008) argue for the superiority of the comparative advantage-following strategy over the comparative-advantage-defying one.

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 realised. 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 equalising effect.⁷⁶ Thus, at low income levels, openness affects equality negatively, while at medium and high income level it could potentially promote equality.

By demonstrating the possible co-existence of development and underdevelopment under globalization through the human development trap model (Chapter 11 in this volume), Mayer-Foulkes also underscores the critical importance of national policies to enhance human capital endowments and develop technological capabilities. Thus, sizable public investment in skill upgrading, as a specific pro-poor measure, is the key for ensuring positive benefits from globalization for the poor.⁷⁷

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 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 eco-system or new unknown technology with often uncertain pay-offs; and iii) their deteriorating working conditions and weakening bargaining powers in global value chains.⁷⁸ Thus, governments should take a pro-active and pro-poor stance in instituting various schemes

⁷⁶. Milanovic (2002), and Agenor (2002)

⁷⁷ See Chapter 2 in this volume for an econometric study that underscores the need to invest additional resources in education and health to create a skilled labour force capable of enjoying greater benefits from globalization.

⁷⁸ . See various case studies included in Nissanke and Thorbecke (2006d, 2006e, 2008b and d).

of public transfers and safety nets to shelter the poor from these adverse conditions.⁷⁹ 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 proactive 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.

A Quest for Pro-Poor Globalization

Our comparative analysis of the ‘globalization- poverty relationships inevitably raises a critical question whether the present form of globalization/integration is conducive to a process of growth-cum-structural transformation of developing economies, which is capable of engendering and sustaining *pro-poor* economic growth with favourable distributional consequences. With the current wave of globalization, ‘within country’ income inequality has been steadily increasing.⁸⁰ Various project studies suggest that globalization indeed produces adverse distributional consequences at both the national and global levels that could slow down or even reverse the present poverty alleviation trend. As “global markets are inherently disequalizing (Birdsall ,2006: 18)”, market-driven globalization and growth tend to increase inequality everywhere, Asia is no exception to this trend, as discussed in Section 3 above.

Pro-poor globalization can be defined as the *inclusive* process of globalization, wherein sharing opportunities for growth and development take place *ex-ante*, all-encompassing and inclusive of poorer segments of population on a global scale. . *Pro-poor* globalization could remain an *elusive concept*, if the process is left entirely to market forces alone (Nissanke 2007). In order to make pro-poor globalization a *realistic perspective*, there is a need for instituting viable mechanisms for redistribution of assets and income in favour of the poor as well as for social protection of the poor at the national, regional and global

⁷⁹ See Kakwani and Son (2008) and Kakwani et.al (2008), among other project case studies.

⁸⁰ . Strictly speaking the trends in world (global) income inequality depend on which concept of inequality is used for measurement (Nissanke and Thorbecke, 2006b and 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.

levels. Importantly, under pro-poor globalization, it should be possible to make equity and efficiency interact dynamically ex-ante so that a virtuous circle of growth and equity/equality could be created in the process of globalization.

Thus, our quest for pro-poor globalization leads us to revisit the debate concerning the relationships between equity/inequality, on the one hand, and growth/efficiency on the other. The traditional view held by economists on the growth-inequality nexus emphasizes the existence of a fundamental trade-off between productive efficiency/growth and social justice represented by equity/equality considerations, often on grounds of the incentive effects. In contrast, the alternative recent political economy literature suggests instead that there is a long-run complementarity between the two. If there are no clear trade offs on *economic* grounds, equitable and shared growth should be good for efficiency and growth as well. As Thorbecke (2006) argues, “if equality is conducive to growth, it then becomes a *means* towards economic development and future poverty alleviation”, and hence, “the conflict between the ethical objective (norm) of egalitarianism and the economic conditions required for growth disappears (p. 2)”. In this new paradigm, wealth redistribution to the less endowed is, on the whole, growth-enhancing, as redistribution is a key to creating a virtuous circle in the growth-equality nexus.

Notwithstanding the long-run complementarity between the twin objectives- growth and equity, a practical policy choice exists over the actual weight given to the ‘equity’ consideration against the ‘efficiency’ consideration. Such a policy choice would be ultimately determined by the social norms prevailing in a society.⁸¹ However, we should bear in mind, in evaluating the optimal weight to be assigned to each of these objectives, that market forces alone would not lead even to a Pareto efficient equilibrium in the presence of imperfect information and imperfect competition, as demonstrated by recent mainstream economic theories.. As Stiglitz famously remarks, “an invisible hand is not visible, because it does not exist”. Therefore, there is not only a moral case on ethical grounds but also a strong rational economic case on ‘efficiency’ grounds for breaking away from the present mode of globalization.

In making globalization more inclusive and truly pro-poor, we should go probably beyond the minimalist approach outlined by Bardhan (2006) as discussed above. Indeed, if we are serious in our quest for pro-poor globalization, we should search for pro-active ways to create a more inclusive development path for the poor in the process of integration by developing countries. It is also necessary to restructure governance mechanisms over economic policies at both national and global levels.

At the national level, the nation state remains a critical political unit within which citizens can express democratically their choices over economic policies and development strategies. Hence, policymakers need to design and implement an active development

⁸¹ See Thorbecke (2004). Atkinson (1997) also notes the effect of social norms on income distribution. Further, Nissanke and Sindzingre (2006) present a more detailed discussion on policy choices over distributional mechanisms and institutional foundation for equitable, shared growth.

strategy not only to benefit from, but also to help counteract the negative effects of the immutable forces of globalization. Globalization should not be viewed as a reliable substitute for a domestic development strategy (Sanchez 2003). However, under the current wave of globalization, a genuine *policy space* for choice over development strategy has been shrinking for developing countries.⁸² There should be more room for open discussions and debate on different development models, so that governments of low-income countries could have a process of *policy learning* and *policy experimentation*.⁸³ Similarly, there should also be a policy space for *institutional innovations*, as institutional design for economic development has to be context-specific. Rodrik (2004) argues that: “effective institutional outcomes do not map into unique institutional designs (p.9). More innovative institutional structures should be encouraged in order to facilitate pro-poor globalization.

In reality, the policy-space of nation states has been eroded considerably in the name of globalization. It is known that policy makers in open economies face a macroeconomic ‘*trilemma*’ (the ‘inconsistent trinity’ thesis). The thesis stipulates that whilst policymakers typically have three desirable objectives (exchange rate stability, free international capital mobility, and monetary policy independence to engage domestic economic goals), they are in practice forced to give up one objective, since only two out of the three can be mutually consistent. Financial globalization has also led to a loss of fiscal autonomy, under ‘fiscal termites’, when financial openness makes it hard to tax internationally footloose capital relative to labour due to the competition for foreign savings through tax incentives and general financial arbitrage (Tanzi 2000). This often results in fewer available resources to provide social safety nets to people adversely affected by globalization (Rodrik 1997, Bardhan 2006). From a similar perspective, Rodrik (2005) discusses a fundamental political trilemma concerning global governance, suggesting that the nation-state system, deep economic integration, and global democracy are mutually incompatible.

For the WTO and other multilateral agencies to become a truly development forum, it is important to recognize explicitly the hugely asymmetrical unequal economic power relationships existing currently among member countries. These global agencies should endeavour to create a genuine ‘policy space’ to allow developing countries to engage in their development agenda in the integration and globalization process. The current rules and governance should be critically reappraised in this light. The meaningful ‘level playing field’ could be created only if effective and fair ‘differential’ treatments are legitimately instituted as a guiding rule governing multilateral negotiations and institutions.

Furthermore, with globalization, there have emerged a set of cross-border economic issues which can be addressed only at a global level, since they cannot be, by nature,

⁸² Rodrik (2004)

⁸³ Morrissey (2004).

dealt with effectively by individual nation states in isolation. These include addressing global negative externalities such as green-house effects leading to a dramatic climate change or provision of global public goods such as eradication of global poverty, prevention of global financial crises or preservation of global security. It requires an effective system of international coordination and cooperation, as well as cross-border regulations and enforcement mechanisms. A deeper globalization requires a new system of global governance.

Yet, as Stiglitz (2006) remarks, economic globalization has outpaced political globalization by a wide margin. Presently, we are not equipped to deal with these global issues of enormous proportions in a satisfactory and timely manner. The current system of global governance suffers from a democratic deficit.⁸⁴ The governance structures prevailing within many multilateral development institutions are antiquated and not appropriate for dealing with contemporary issues of a global nature, resulting directly from globalization forces. An alternative pro-poor globalization structure, different from the current, market driven globalization form, will need to address these issues.

Finally, in order to address the distributional consequences of globalization, a set of much more effective re-distributional instruments would be required at both national and global levels. Globalization can bring about increased volatility and insecurity for many cohorts, particularly those that are not well positioned to take advantage of the opportunities created by the opening of trade and capital flows. Indeed, as Milanovic (2006) suggests, the relevance of ‘*global* income inequality’ as a valuable concept of measuring the trends in the world income distribution, should increase over time, as people move from using national yardsticks to global ones when comparing their incomes with that of others. Graham (2007) also argues that while globalization is a major engine for growth in aggregate, globalization either introduces or exacerbates other trends that affect people’s well being 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. This flow of information can result in changing reference norms and increased frustration with relative income differences.

If this were the case, as Milanovic (2006) argues, redistribution needs to be globally progressive. The system of foreign aid (the existing form of global resource transfers) is not the most efficient and progressive way to mobilise and utilise resources as a redistributional instrument to address global income inequality. Globalization requires a set of new innovative instruments for financing development as well as for provision of global public goods.⁸⁵ In this context, we should also evaluate various proposals such as a global social contract to finance equal opportunity investments benefiting the weak and the disadvantaged, or instituting appropriate global arrangements to minimise the asymmetric risks and costs of global market failures.⁸⁶

⁸⁴ Nayer (2004) and Stiglitz (2006)

⁸⁵ Atkinson (2005) and Nissanke (2005).

⁸⁶ Birdsall (2006)

An example of an interesting and rather radical global redistributive proposal is that of Basu (2006) who focuses his analysis on the process of marginalization of the poor resulting from globalization. In this process, he argues, some of the poorest people may be subjected to a period of hardship before the benefits of opening-up trickle down. He proposes, in this context, that in place of a country's per capita income, the per capita income of the bottom quintile of the population should be adopted as a normative criterion in evaluating a country's wellbeing. He shows, through a simple model of welfare maximization, that the adoption of the 'bottom quintile income criterion' would lead not only to a pro-poor growth pattern, but that it would also alleviate the erosion of each national government's power to follow an equity-conscious policy. He proceeds to suggest a radical distribution policy whereby workers in all firms as well as currently unemployed labourers be given a fraction of equity earnings from all firms. He envisages that in today's globalizing world, such an equity scheme should be extended to that of inter-country transfers. He suggests that developing rules for some inter-country transfer of equity income would insure that the functional income distribution between capital and labour (especially unskilled labour) would not become too uneven. In order to escape from what amounts to a Prisoner's Dilemma situation, Basu also argues for a creation of a new international co-ordination organization that helps co-ordinate inter-country anti-poverty policies.

While such radical proposals as Basu's can not and should not be seriously considered- let alone endorsed- until they have been subjected to critical scrutiny, it is clear that the world community should start giving serious attention to more enlightened global redistributive measures than prevail today. Some of the existing proposals will require careful and critical investigation, even when they are already anchored firmly in economic theories and are ready for implementation so that sufficient political support can be mobilised.⁸⁷ Indeed, we should get engaged earnestly in a fresh debate on developing new structures of channeling the process of globalization, so that the enormous benefits of globalization can be steered towards a more equitable sharing in favour of the world's poor.

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⁸⁷ See Stiglitz (2006)

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