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THE IMPACT OF GLOBALIZATION ON THE WORLD'S POOR

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Moderator:

CAROL GRAHAM
Senior Fellow, The Brookings Institution
Professor of Public Policy, University of Maryland

Panelists:

MACHIKO NISSANKE
Professor of Economics, School of Oriental and African Studies, University of London

ERIK THORBECKE
H.E. Babcock Professor of Economics Emeritus, Cornell University

Discussant:

NANCY BIRDSALL
President, Center for Global Development

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PROCEEDINGS

MS. GRAHAM: Okay. Well, good afternoon. Welcome. I know some of you are still finding your seats, but I think we should get started.

Welcome to our discussion of The Impact of Globalization on the World's Poor. I would say that it's a great book, but as I'm one of the contributors, I'll be more modest than that. But I will say that you have two great editors here to discuss the book. It's obviously on a topic that is of wide interest if you look at the size of the crowd here today.

I'd like to introduce Erik Thorbecke, who is the H.E. Babcock Professor of Economics Emeritus at Cornell University and for those of us who have studied development economics, a very big force in the field for many, many years. And it's been really wonderful to work with him on this. And secondly, his co-editor, Machiko Nissanke, Professor of Economics at the School of Oriental and African Studies at the University of London.

This book grew out of a conference sponsored by WIDER and Helsinki, a conference I was lucky to attend and with a wide range of authors, whose contributions are in the book and are summarized in some of the materials you have.

Erik and Machiko will summarize the book. After that, I might say just a few quick words about my own contribution to the book. And then we're very lucky to have Nancy Birdsall, who is president of the Center for

Global Development, right across the street, former head of research at the World Bank, former executive vice president of the Inter-American Development Bank, another huge force in the development economics field, also a co author and friend, and I'm very pleased that she's here.

So, with that, I will turn it over to Erik – or Machiko. Who's first? Erik.

MR. THORBECKE: Thank you very much, Carol. It's a pleasure to be here. I think the first time that I spoke here was probably 40 years ago, so it feels good to be back. I was asked to say just a few words about WIDER. WIDER stands for the World Institute for Development Economics Research. It's a UN University's center. It's, in fact, the leading center of the UN University system.

It was established in Helsinki in 1985. It does policy and development research, and it has a network of over 200 researchers worldwide. And presently, it has 15 projects ongoing.

Now, the project that I would like to talk to you about today, as Carol mentioned, is on The Impact of Globalization on the World's Poor. And so far, we've had four conferences. The first conference was in Helsinki about two years ago, and this is the one that I will try to summarize here, give you the essence of it here.

Since then, we've had one in Asia looking at the impact of globalization on the poor in Asia. We've had one in Johannesburg looking at the impact of globalization on the African poor, and the last one in Rio on the impact of globalization on the poor in Latin America.

Now, the first question that we should ask is what is globalization? What are its manifestations? And I think many people would agree with the definition which I'm going to give, which is that globalization implies greater integration within the world economy via increased openers to first international trade; trade liberalization; capital and labor movement liberalization; greater international flow of technology; greater international flow of information, knowledge and ideas, what some people have called the internet superhighway.

The questions that are frequently asked and which are at the basis really of the policy debate on globalization are whether the actual distribution of the gains of globalization is fair. I think nobody doubts that globalization on a net basis has had positive gains, including positive gains for the poor.

But I think one important issue is whether the poor have benefited less than proportionately than the non-poor and might under certain circumstances actually have been hurt by the globalization process. I think that in all fairness one can say that the poor benefited on a net basis but less than proportionately compared to the non-poor.

Second question is who bears the cost of some of the negative effects of globalization. And here again, you know, I think it's not unfair to say that the developing world bears the brunt of the negative effects of globalization. And again, we will illustrate this in a few minutes.

Finally, there is the issue as to whether globalization has led to greater within-country inequality in the world. And I think here again the evidence is that in many, many countries, China being the prime example of this, globalization has led to a greater inequality. In the case of China, the coastal provinces benefited greatly from the globalization forces, whereas the inland provinces benefited much less. And the income distribution became more unequal.

But again, one has to be careful not to generalize. Brazil, a country that has probably the highest level of inequality in the world, we find that in the last six, seven years, inequality has come down somewhat.

Now, a key question that we tried to address in the book that we are discussing here are the transmission mechanisms through which globalization affects policy. And there are many channels which we will review very briefly here. The first channel and by far the most important channel is through economic growth, but it also works through inequality, international capital movements, migration, technology, and so on. And as I say, we will go over these channels very briefly.

The first and most important of the mechanism through which the process of globalization affects poverty directly and indirectly is what we call the growth inequality poverty channel. And I'm going to spend just a few minutes on it, because it's a fundamental channel.

If we start with the globalization process, as I mentioned, it means greater openness through trade, capital, labor, technology, knowledge, trade, sometimes has been called the conveyor belt of technology together with trade and together with capital movements. Technology flows to the less rich countries in the world.

So, the issue here is how does this openness, first of all, affect growth. So, I'm looking here at the link between openness and growth. Now, it's very, very clear that the globalization in the sense of greater openness has led to an increase in growth. It has contributed directly to output in the countries that liberalize through greater exports, through more efficient economy. And the issue is absolutely clear. There was a contribution to growth.

But at the same time, if we look at a second causal link from openness to distribution, here, as I pointed out before, the evidence suggests that in many, many instances, greater openness has led to greater income inequality. The income distribution has become more unequal.

Now, a key question is what is a link between a change in income distribution and economic growth. And here, there are two schools of thought. The classical school of thought best represented by somebody like Keldore essentially took the view point that a more unequal income distribution was almost necessary for economic growth, because the rich save a larger proportion of their income than the poor.

So, if you wanted to have larger aggregate saving, a larger flow of investment, you needed a more uneven income distribution. You could say that the impoverishment of the masses was almost a precondition to economic growth.

There is a modern version which looks at it very differently and which essentially takes a position that a more unequal income distribution may lead to social conflict, may lead to political instability, may lead to rent activities -- high rent seeking activities which are quite inefficient and which threaten property rights.

And for all of these reasons and others that I can't go into would have a dampening effect on growth. So, this modern political economy view of the link between distribution and growth suggests that a more unequal income distribution would tend to reduce growth. So again, there is a conflict between the two, but I think there is at least some evidence that the modern view is probably the correct one in some instances.

Now, the next link is from growth to distribution. And here, many of us who were trained earlier are very familiar with the Kooznet's Curve. Kooznet claimed that at an early stage of development, growth is going to be unequalizing, and it's only after a country has reached a certain level of per capita income, a certain standard of living, that it will start reducing inequality. By now, I think many people have dethroned, de-mythed the Kooznet's Curve, and the evidence is not such that there is a law which links growth to distribution.

Now, the next link is from growth to poverty. Now, here again, it's very clear growth is going to reduce poverty, but the question is at what rate. And we will be saying quite a few things about pro-poor growth. What is important here is not the rate of growth per se, but the pattern, the structure of economic growth. For instance, in the Sub Saharan African country, neglecting agricultural growth may lead to stagnation, many lead to the short-circuiting of the development process.

So, the – again, in technical terms, people would say that the elasticity which links economic growth to poverty reduction can vary anywhere from .2 to maybe 3 depending on the pattern of economic growth.

And then finally, the – well, that's it.

So, now let me just go over some of the empirical evidence which we have in the book. I think the first conclusion that comes out of the book is that openness as such is a necessary but clearly not a sufficient condition for successful development. The pattern of economic growth and development rather than the rate of growth per se is going to have significant effects on the country's income distribution and on poverty dynamics.

And finally, for those countries which are at an early stage of development, particularly in Sub Saharan Africa but also in South Asia, other parts of the world, the role of agriculture is absolutely fundamental.

In a very few months, the world development report for 2008 of the World Bank is going to come out. And its theme this year is on the role of agriculture and development. And you will see that they take a very strong position vis-à-vis the role of agriculture at an early stage of development as an instrument to reduce poverty.

Now, there are alternative definitions of pro-poor growth. And the weakest one is that the poor gain from growth, but it doesn't say by how much. The poor might can one percent. The non-poor might can four or five or six percent. And we would say that this is pro-poor.

A somewhat more stringent definition is that the poor gain proportionately more than the non-poor, which is a relative definition. And probably the most stringent definition is that the poor gain absolutely more than the non-poor.

Now, let me give you just a few examples of this. Suppose that in year one the per capita income average of the poor is 100 and the non-poor is 500 and in year 2, it's 101 and 520. Here, the so called weak absolute definition would say that it is pro-poor as long as the poor have gained. But if you look at this, you see the poor only gain one percent, the non-poor four percent.

The relative definition would say that the poor gained more than the non-poor. You can see here the poor gained six percent, the non-poor four percent. And finally, the strong absolute definition of pro-poor growth would call for the poor gaining absolutely more than the non-poor.

Now, in our book, we have taken the position that we meant by pro-poor growth at least the relative definition. In other words, that the poor gained at least as much as the non-poor and note that if they gained more than the non-poor, then the inequality in the income distribution will be reduced.

Now, just very quickly, some empirical evidence. If we look at China, where a fifth of the world population lives, the bulk of the poverty reduction occurred during the phase of agricultural de-collectivization and the freeing of prices before 1980, rather than in the trade liberalization subsequent to trade opening period, which is interesting and again, reinforces the argument that it's the pattern of growth which is very essential.

Since the great majority of the poor live in rural areas, we can ask ourselves under what conditions they may or may not gain from globalization. As consumers, they will gain if prices come down. And this is very important with respect to food. And there is again much evidence in these countries that as food prices come down, particularly rice, the net buyers will benefit and the net sellers will only benefit if the increase in output more than compensates the fall in price. So, there are situations where the net sellers could actually be hurt.

As recipients of public services, the poor can lose from globalization through budget cuts that are mandated by structural adjustment programs, particularly in the health and education field. And they can also be heard by falls in tariff revenues following immediately the trade liberalization. And then finally, as users of common property resources, the poor can be heard by over exploitation of the common resources, particularly deforestation.

Now, one of the studies in the book looks at global value change, particularly for garments, horticulture, and textiles in four developing countries. And what this study shows is that the overall impact on unskilled employment was positive but relatively small. Also, in the case of Kenya and South Africa, skilled workers appeared to have benefited from globalization while unskilled workers were adversely affected.

Now, Machiko is going to follow up and discuss a number of additional channels and also the policy debate.

MS. NISSANKE: I'd like to mention that the growth channel economic clause resulting from openness and integration is most important most of dynamic forces affecting poverty. But if growth process increases in quality together, then its net effect on poverty can be dampened. That's what Erik emphasized.

But there are other challenges through which globalization affect linking to the poverty. And although in our book, we look at the inequality, increase the inequality or movement of inequality, flittering between growth and the poverty reduction. And the actual outcome and pro-poorness of globalization depends how dynamics of income distribution taking place in the globalization process.

But coming to other channels, we looked at the different channels but we are doing that because current phase of globalization has particular specific futures which affect the poverty dynamics in the developing world and it produces as any modern history of globalization, winners, and losers in globally and everywhere.

So, we looked at the international capital movement, but there is a particular pattern that affects the links between globalization levels, poverty, labor pattern, labor mobility patterns, changes in goods prices. This all affect the links between globalization and poverty. Also, the nature of progress, technical progress and how technology is transferred from advanced country to the developing country are how access to that new technology have been managed has major implication for poverty. Also, increased (inaudible), increased information deficient, how institution intermediate globalization and the poverty would make difference through this nexus.

So, using limited time I will go through very quickly what we mean about this. Of course, globalization changes a little the goods' prices as a reactive that if wage goods prices like food would decline particular circumstances integration that would be good for poor. But globalization openness is not only changing goods prices, but complementary changing factor prices, which is a reactive (inaudible) on capital on our natural resources.

So, we looked at these issues and famous (inaudible), which in its pure form if we take it, then unskilled labor is supposed to be winner in low income countries, developing countries and loser in developed countries because of differences in the factor endowment.

But what we of course see is empirical evidence which not necessary that sort of predictions, so of course, not meant to use just prediction but that would have to empirical. But if we use as a benchmark, we can look at that wage gaps between skilled and unskilled labor have been rather increasing in many developing countries, in particular, Latin America, Africa, Brazil, but that's changing in recent years.

There are lots of explanations about this, but an explanation why in Latin America, Africa now unskilled labor cannot come up as a winner is partly because China, India turn into global market with huge reserves of unskilled labor, and that affects the relative prices on labor and unskilled labor in global market.

But also, nature with new technology, it sort of has to be looked at very carefully, what is the influence that makes on poverty and inequality dynamics. And basically, we will say that nature new technology is such that it works in favor of skilled and educated labor.

But first I will come very quickly go through what is international factor mobility, what is a particular characteristic future of factor movement. And that is very important to understand because there is sort of a perverse factor movement taking place. We use words like perverse because it is different from what is predicted by economic authorities that kept low from rich countries to poor countries generally because I can't really discuss in developing countries. But that's not what we observed.

So, skilled labor on the whole tends to migrate to poor countries as much as among developed countries. Do not migrate to poor countries much and that is often kept moves from poor country to rich country as applied to capital, particularly at the time of crisis.

Also, portfolio kept more or less in the current phase, diversification finance rather than development finance, so what money going around the globe at for asset sloping or risk hedging and shedding and not much looked into productive development finance.

Other things we noticed that the direct investment on the global scale, it is still dominated by inter-industry FDI among developed countries, and only very small group of developing countries, emerging country economics are benefiting from FDI.

There is also tendency for skilled labor to migrate from developing countries to developed countries. And we're seeing maybe a lot of African doctors going into US and Europe, Philippine medical doctors all working in the US and that sort of story we all know from news. But also, migration by unskilled workers to rich countries is often hampered by restrictions and different obstacles. So basically, de facto mobility is perverse because it's differentiated asymmetric measures to de facto mobilities. Captors become much more free to move. Skilled labor can move, but not necessary unskilled labor. That is different from previous globalization phase than (inaudible) did take place through labor migration. For example, in the previous globalization era more than 100 years ago, it was 60 million largely unskilled migrated from Europe all the way to new world. That is a (inaudible) taking place.

But the fact we observe now is actually a symmetrical. De facto mobility is not symmetrically, so the de facto labor mobility taking place. Because unskilled labor cannot move freely across border, but it is de facto mobility taking place from transnational corporations ability strategically locating production site and also outsourcing activities and also dominance over that corporations in commodity value change.

And of course, because of that in fear driving away TNC's and interferes with tax competitions, developing country governments are constrained to use their own measures to protect labors, their own labors, or try to increase tax generally or redistribution of the populous. And that makes difference to position of the poor in developing countries.

I will be getting quick. Again, I would like to spend bit time on why technical progress and transfer technology nature of the way it's taking place, that make difference to position of the poor, because the nature of new technology, it's heavily biased in favor of skilled and educated labor. So, generally, technical changes itself emanate from R&D activities in the developed countries in response to its own local developed country conditions. So, it's tend to be labor saving, tend to be skill biased.

So, new technology, it's generally complimentary to capital and skilled labor but it's substitute for unskilled labor. So on the whole, technical changes tend to increase in qualities universally most in developed countries and developing countries. Also, we have to see how R&D activities are taking place.

There are increased privatization over research itself like biotechnology, medical research make it very difficult for developing countries to hold access to this research result and new technologies, and that's create tricks issues. It makes less affordable to the poor. And for example, biotechnology revolution is in the private domain rather than it was a cause of green revolution, then it was public domain. And that sort of things makes difference to the accessibility of new technology for the poor and the developing countries.

So, in the book we studied the contribution, I think it was involved in development issues. There is one chapter which talks about these issues lot and looking at maybe we need much more functioning intellectual property like clearing house have to be established.

Other channels, again, vulnerability issues, poor. While the poor tend to be more vulnerable to shocks and financial crisis particularly, so they have to be protected. And the second other challenge which we want to talk is particular possibility of information diffusion. This is generally good thing, but it changes the perception of people, of the poor as well as non-poor, how globalization affects their positions. So, difference changes enormously.

And that is the one Carol is going to talk after our presentation. So, I will stop here, but there is increased feeding insecurity and fear folding into poor, poverty among non-poor, among low and middle income classes in developing countries. That makes them to feel globalization is not necessary good for them.

Also, the nature of institution. Institution act as a filter, intensifying or moderating the positive and negative pass through between globalization and poverty. Those conditions taking place in the globalization and filter through to poverty that is intermediated by institutions.

So, looking at all these issues altogether, what in the past was pro-poor globalization, pro-poor in the way we defined it making poor to more proportionately benefit from globalization. And we take the view that better global market forces established vicious circle would depend on initial conditions at the time of exposure and effective design implementation policy to manage that integration process.

And that's coming very clearly from comparative studies, comparative analysis between say Asia verus Africa that Africa increased its share of trade, trade openness and GDP enormously, but they are not benefiting from globalization, because the way they're integrated, it's not making benefiting from dynamic forces in globalization.

So, growth is very important. Growth is important. Openness is important. Globalization induced through growth is important channel for reducing poverty. But at the same time, that is not automatic or universal. So, it has to be engaged in that dynamic process.

So, globalization offer potential benefit for those countries which had a strategic position and adjust the past civilization could lead to marginalization. It requires long time vision for upgrading the comparative advantage partly because current phase of globalization is very much driven by technology knowledge transfers. So, unless you get into that beneficiary dynamic course, you cannot benefit from it.

And there is a critical threshold existing for positive effective globalization in poverty reduction, particularly poor without basic education very difficult to get part of benefiting from globalization. So, basically you have to increase human resource capital of the poor. So, as a recommendation that openness is necessary but not sufficient as we mentioned, and agriculture, structure, transformation is very important.

So, policy issues, what are the policy issues? Globalization cannot be taken, that is our view, as a substitute for a domestic diplomatic strategy, meaning that just opening or liberalizing trade investment regime would not entail poverty reduction. And the governments of developing countries need proactive designing implementation pro-poor growth and development strategies.

And one of critical issues facing policymakers in low income countries in home rating their strategic position towards globalization process and how to evolve their advantage, particularly in their abundant factor, unskilled labor.

So, consciously engage in building institutional capacity for successive integrations and pro-poor globalization, develop national level in both first the safety net, social protections that reduce vulnerabilities and share the asset with the poor. But we also have to have a position investment in building primary asset over the poor, education, health, other socioeconomic infrastructure for the poor without which poor cannot participate meaningfully and benefiting from globalization process.

And also labor market fragmentation, discrimination, and factor price mobility differences, that has to be attended. And finally, making globalization work for the poor, you need therefore with acceptable more effective redistribution of (inaudible) at both national and global level.

We didn't have today time to talk about how do go about changing global governance issues. That is not necessary main issue we took up in our book, but of course, that is something we have to think about for making globalization more pro-poor.

Thank you very much.

(Applause)

MS. GRAHAM: Okay. Well, thank you, Erik and Machiko.

I'll be very brief. My chapter was on trying to understand public attitudes about globalization and how those might depart from aggregate assessments of the benefit of the process. And my assumption going into this was that basically even though a lot of the work in this area is looking at the effects of globalization on the poor, who is below the poverty line, that actually understanding public attitudes about the process needs to focus more broadly on the dynamics of poverty and inequality, that there's a lot of change and that in fact, some of this change might have happened anyway, some is globalization induced.

But it's the change that effects how people assess the process, how they assess their lives. This grew out of some work that Nancy and I started almost 10 years ago thinking about income ability, basically saying that you need to understand the effects of inequality on peoples' welfare. You need to unbundle it and think about who's moving up and down the income ladder. Who has opportunities?

And one of the things we find in some of the very few studies we have of income mobility, one in Peru that I'll talk about and some others, is that there's a remarkable amount of movement. There are a lot of people moving out of poverty. Again, some of this may be caused by openness, globalization, and new policies. Some might have happened anyway, some interaction there.

But there's a remarkable amount of movement. We don't get a static picture. So the happy story is that a lot of people move out of poverty. The less happy story is that we also see a lot of vulnerable people, some of whom were formerly middle class, moving all the way back to extreme poverty. So, there's a lot of changing, rewards, and skills – rewards different skill levels. Some of t his came out in Erik and Machiko's conversation.

So, when we think about perceptions, what do we find? Well, these rater cumbersome bar charts here are based on a sample in Peru, where we have objective data for income ability over 10 years. So, we know how much people have moved up or down the income ladder. On this bar here, we have what's happened to people in objective terms, so people that lost and then up here, people that gained. And then here, on this bar, is how they assessed how they did over a 10 year period.

We went back to the same sample of people and asked them compared to 10 years ago, how was your economic situation today? And one of the things we found that surprised us, if you look at the top four bars in the top corner is that roughly half of the people with the most income ability, so the people that h ad done the best in our sample, said their situation today was negative or very negative compared to the past.

This surprised us. We called these people the frustrated achievers. If you look all the way down to the bottom, there are people who had losses that said they did very well. We initially called them the stupids, decided that was not politically correct, and so, we re-labeled them the Pollyannas.

But the people we're really worried about are the frustrated achievers at the top, because here are people that in objective terms seem to be doing well, and yet, they're saying things are very bad. So, then we thought maybe it was just Peru. I'm part Peruvian. Maybe we're a little weird. We got data for another country and also a globalizing country in a big way, Russia, and we found that almost 70 percent, 7-0 percent of the people with the most upward mobility said their situation today was negative or very negative compared to the past.

So, we went back and basically analyzed these groups of people to find out, you know, what – why do they think things are bad. Well, we clearly found that they were very insecure. These frustrated achievers had very high levels of fear of unemployment. They feared losing their jobs. In both contexts, they live in situations where there are no viable safety nets. That's something that

Machiko mentioned in her policy recommendations. So, even if you make it out of poverty, if you lose your job tomorrow, there's nothing to fall back on.

Secondly, we found among other things that they were much more concerned about inequality than the average. Why? We don't know. It could be that awareness and expectations are raised with mobility. They're also raised with more access to the media, again, something that came out in the book.

We have in another study for a Latin America-wide sample, when we look at – we have a media index. So, we measure how exposed people are to different forms of the media and to different information. And we find, indeed, that people in Latin America who have more media exposure are more likely to think the distribution of income in their country is unfair.

So, I could say much more, but the basic story is along with whatever is happening to the poorest people with globalization, there is an insecure and at times, frustrated middle or near middle sector of the population that may be doing all right with globalization but is also very vulnerable to falling back into poverty and is quite frustrated.

And in the end, this group may be more critical in determining the political sustainability of the process than the very poor. So, it's all to say the story is more complicated than just looking at the poor.

And with that, we'll turn it over to Nancy.

MS. BIRDSALL: No PowerPoint, so everybody can back.

Well, thank you very much, Carol and Erik and Machiko and WIDER. I'm a great fan of the work at WIDER.

In particular, I think Erik didn't mention it, but I want to that starting about 10 years ago or more, WIDER really began to generate an important public good, which are the data gathering and improving and consolidating and fine tuning data on income inequality within countries across the world and more recently on wealth inequality across the world. And it is doing that that has generated the sort of industry of researchers, scholars, and students doing empirical work on these issues.

So, it's always a pleasure to have the opportunity to join with this group of people at WIDER who have supported my work indeed also on inequality.

I want to make four points very quickly, and some of them will repeat what you've heard. And the fourth one is the one that hope you'll remember because it's the one that says what ought to happen next in terms of new research and new activism.

But let me start with the first point, which is a summary point. The way I like to think about much of what you've heard is to use the word asymmetric. Globalization is asymmetric in its effects. It has potential effects for everyone, but it's asymmetric at the moment in its actual effects. It is better for those who already have certain assets. It's better for countries that have the key asset of being institutionally solid.

If you are in – so, poor countries with weak governments do not and cannot yet benefit from globalization. You heard that from the presentation. And there is, as a result, some thing that economists refer to as lack of actual convergence between the richest countries and the poorest countries. The richest countries are like first movers. They can benefit because they have solid political institutions.

Now, luckily, we see a few countries, emerging markets, China is an interesting case, India, that have done something about institutional development that has matter. And I think it has to do with not democracy, per se, not accountable political institutions in the context of democracy or human rights, but ensuring investors and small businesses a business friendly environment.

So, there's an important point there in terms of how countries that are now poor could navigate this globalization landscape if they could figure out how to attain somehow a more business friendly environment, rule of law, property rights, that sort of thing.

So, it's asymmetric across countries, and it's asymmetric within countries across people. And as you heard, the key asset for people in a global economy at the moment is education and skills. And we see in every country, it's most dramatic in Latin America, that the key asset is higher education. The returns to higher education across countries in Latin America have been three fold the returns to secondary education or they were in the nineties.

So, those with higher education were already ahead and they're even more ahead, three times more and more ahead, which may also be why a lot of people who had absolute gains with growth in countries in Latin America like Peru are frustrated. Because even if your income went up from $1,000 a year to $1,050 a year with a 5 percent increase, if your neighbor's income went up from $100,000 a year to – what would it be – $105,000, the difference is between $5,000 and $50, so you don't really feel all that much better off. Okay. So, globalization is asymmetric.

Second point, this asymmetry matters within countries because income inequality matters. It is the key transmission mechanism in my view, which translates or not globalization into benefits from the poor. And the reason income inequality matters, I think, although this is hard to show empirically, is fundamentally that power matters and politics matter. And it's very difficult even in the most mature democracies, like the US, to ring fence politics from economic interests.

So, you can imagine in countries that start with high initial income inequality how difficult it is to get to something we would call democratic accountability, one person, one vote. It's just very difficult. It is just natural for those with economic power to highjack the political process and to use it in their own interests.

We were just talking today at the Center for Global Development about the intellectual property rights issue and how it's affecting access to medicines in developing countries. And how important is and what is the power of the pharmaceutical industry in the US? And the US is much more an effective democracy in which there is some accountability to citizens than most developing countries.

So, the problem of inequality as a transmission mechanism is all about power. Now, as you heard, inequality, income inequality, it undermines growth through economic factors such as poor capital markets, but it also undermines growth because of power relations, which lead to policies that are inefficient, protected monopolies, widespread distorting subsidies that don't benefit the poor.

And so it undermines growth because it leads to some inefficiencies. It also undermines poverty-reducing growth, which is the point after all, because the rich highjack – in fact, I think one of the great problems of the 1990's, the reform movement, the structural adjustment movement that was pushed very hard, and reasonably so in my view, by the World Bank and the IMF and the international economic community, is that the reforms, which made sense on paper were often highjacked in developing countries by those with economic power who had political interests in – well, highjacking these reforms then maneuvering them in a way that in the end, they didn't accomplish what on paper they – you would have thought they would accomplish if you were just reading a textbook, I guess is the way to say it.

So, the worst about political power that is allied with economic interests that are concentrated in developing countries is that it undermines public services and the ability of countries to have a domestic social contract in which they guarantee equal opportunities through good education systems and adequate access to health and so on and so on.

These are all familiar issues, but I think what the book has done in a very balanced, very careful, thoughtful way is to lay this out and to add a lot of examples and meat to the discussion, so that it's a great book in that sense for students, for scholars. It brings together theory and empirical work, lots of new ideas. So, I failed to say that at the beginning, and I want to.

And on this issue of why inequality matters, it's really – I think it will be a useful – among other things, a very useful text for students in the next, you know, decade or more. Now, I do think – I want to just refer back to

Carol's reference to the middle sector. I think that we could think a lot more in the development community about what it takes to build a middle class. Maybe it's not that different a question from what does it take to build adequate political institutions. I mean the two support each other.

But it would be a different way – it might bring a different perspective to some issues than the perspective that says what does it take to reduce poverty. And I've been thinking about and working on that, so maybe some of you will have ideas to share.

Let me go to my third point, which is I wanted to just convey something that I think the book doesn't do yet, which I would call now three empirical regularities about inequality in the developing world since I think inequality is the key transmission mechanism between growth and poverty reduction.

I've said a little bit how inequality seems to matter through power politics, but where does it matter and what do we know and understand? What are the empirical irregularities? And I want to mention three.

First, from work at WIDER, it seems to be that inequality reduces growth in countries with high inequality – high income inequality. For those of you who know these issues, a genie coefficient of .45 or above. Although that's probably a little bit of misplaced concreteness, the point is that below – sort of levels of inequality such as we see in South Asia may not per se be an impediment to growth.

But the levels of inequality we see in Latin America and much of Sub Saharan Africa do seem to be empirically a problem in that through these various mechanisms, be it power relations, be it poor capital markets, high inequality matters. So, that's the first.

The second, high inequality seems to matter most in the low income countries. That is, countries that were at about $3,000 per capita income -- in PPP terms, in $2,000. So, it doesn't matter as much in the US and in Europe. And it may not even matter as much in some of the upper middle income countries as it does at these lower levels of income.

And that's obviously because of these asymmetries that I referred to, that where markets are working better, where political institutions are working better, and where because that's been true for a long time, countries are richer than the asymmetries of inequalities don't kick in in the same way. You have to have an interaction of inequality with a poor capital market or with poor government policy in providing access to education or whatever.

So, how many people in how many countries have these two characteristics? I forget. It's in a paper on our website, but I forget. But it's something like 15 to 20 percent, concentrated in Latin America and Africa or, if we add China, closer to 40 percent of the developing world's population.

And why might we add China? Because in China, the latest measurements suggest that the genie coefficient of income inequality has risen to almost .45, that critical level that I mentioned. It's risen very dramatically as many of you all know in the last decade. So, we're not talking anymore about a trivial number of people in a trivial number of countries. The third empirical regularity is that inequality has been increasing within developing countries. And that's a bit of a surprise because 10 years ago, basically the view was that inequality didn't' change much within countries, that there were tremendous inequalities across countries, but that these genie measures and other measures of inequality were high in Latin America, low in South Asia, and not very much changing.

But of course, we see China, and now we see in India also that although the measure hasn't increased to that critical level I mentioned of .45, inequality has been rising very quickly in India and of course, with marketization in Eastern Europe and elsewhere.

So, let me go to my fourth point, which is thoughts on how to deal with this challenge that we have about ensuring that globalization's potential is realized for everyone, including the poor and maybe the incipient middle class.

And here's where I think the book does less, but you can't expect one book to do everything, so maybe this is the next book. It touches on some of these issues but in more of an ad hoc way. And I think what we need now is really some thinking about what are the implications of this story for what countries should do, although Machiko certainly went into that but also what the international community should do.

So, on what countries should do, I think actually I won't repeat the point she made very nicely that globalization is not a substitute for a domestic development strategy. And the Chinese and the Indians are struggling with that right now. There's no substitute for the slow, hard slog of institutional change. It's one of those problems where you know you have to be developed to benefit from globalization. If you're underdeveloped, then you can't benefit as well. So, you have to figure out with these additional pressures that globalization brings, also how to develop and acquire these institutions that are the key asset at the country level.

Let me go to what could be done at the international level. And here, I think I'll just reel off a number of points, including some that are mentioned in the book, although I lost my notes about that, but I'll try to remember. One is that we really do need international mechanisms to manage market failures.

The classic case is climate change. You know, I suppose you could climate change is in some vague way, one result of a more active, deeper, richer global market. And the effects of climate change are going to be stunningly and chillingly asymmetric, because poor people in developing countries do not have the assets to adjust. So, from a welfare point of view, it's really going to undermine what otherwise might be success in the war – or the battle against poverty.

So, we need much more thinking about these – it's the global public good, how to manage a problem, a challenge like global climate change. It's not – it's exactly the same issue as managing through a better international financial architecture the problems in global financial markets, which also reflect basic missing markets and market failures that we all understand at the local level. That's why we have banking supervision and so on.

And then there's this whole set of actions that I would call managing collective action on say tax harmonization on the supply of corruption from the rich world, which makes it too easy for say predatory leaders in natural resource rich developing countries to get – you know, capture private rents.

The recovery of assets, which is a good initiative recently announced I think through the World Bank, led among others by Ngozi Okonjo Iweala of Nigeria, recovery of the assets that have been illegally put abroad.

The odious debt issue is an example where there's probably better ways to coordinate internationally an arrangement that would create disincentives for lending to bad leaders.

International oversight of these oil funds, the one in Chad, the one in Azerbaijan, the oil fund that ought to have been developed in Iraq, these oil funds for some period of time, I think, need international oversight. I don't think it should be thought of as undermining the sovereignty of a country. I think it should be thought of as protecting the rights of citizens within a country, their sovereign rights to share in the benefits of an asset that they have.

Prenab Bardon in his essay mentions the need for an antitrust agency at the international level that would prevent monopolies from capturing the rents in global markets that otherwise they are capturing. I think he has the example, you know, sort of four agriculture or food industries capture 90 percent or have 90 percent of the market in the distribution of foods around the world. Maybe it's not even four.

So, all of these coordination collective action problems need to be thought through much more aggressively at the global level.

And the second part is for the rich countries, and here's where the Center for Global Development is also trying to be more active, is to do no harm. You know, we don't need to have protection, the kinds of poor access to rich country markets that harm competition and undermine potential for poor farmers and poor producers in general in the developing world.

We have limits on immigration, which was mentioned that are really – we need to think that through. We are doing harm to the poor and the unskilled when we have such closed markets. Supply of corruption the Foreign Corrupt Practices Act, the TRIPS issue, you know, is – I mentioned it already as an abuse in my view of the economic power of the US, which is being incorporated in the Free Trade Agreements even now that are finally going to get agreed to in Panama and Peru.

So, it's a very big agenda for the developing community. I'm glad there are so many people here, presumably students and activists who will support those of us at places like Brookings and the Center for Global Development, who are struggling with these issues, doing research, trying to gather evidence, and think through good ideas for how to ensure that globalization does reduce poverty in the developing world.

Thank you very much.

(Applause)

MS. GRAHAM: Thank you very much, Nancy and Erik and Machiko.

We now have about 15-20 minutes for questions. Just two operating rules. I'd ask the panelists please to use the mikes that are on your chairs and whoever asks a question, please, there are a couple of Mikes floating around. Adriana has one; Christy has another. So, please identify yourself if you could and say who you'd like to address the question to.

SPEAKER: Yes. I'm a former (inaudible) of the World Bank a couple of years ago and now stranded here. There is a big debate and a lot of frustration in our countries – I come from Latin America – coming out from that they're embedding in globalization so many different things. So, there's such an importance of being able to weed out what is really globalization about.

When, for instance, we read in a Forbes Magazine that a carnal slave in Mexico has been able to turn himself into second richest man over a decade by being in the telecommunications sector of Mexico Loan, obviously, that has nothing to do with globalization. That has nothing to do with it whatsoever. That has to do with lack of regulations or whatever you want to say, but it's not.

So, one way of really helping out is to try to make clear what is globalization and what is not and try to open up the debate. And that is as important in my country, in my Latin America as it is probably up here, because the same need for information is needed before protectionism breaks out everywhere. Thank you.

MS. GRAHAM: I'll take that as a comment unless somebody wants to –

MR. THORBECKE: No. I mean, we defined globalization in a fairly broad, but yet, I think clear way, which is greater integration through openness and the manifestations of openness were trade liberalization, capital liberalization, and greater flow of technology across borders, greater flow of information across borders.

And you’re quite right when you say that when it comes to domestic issues, privatization, for instance, which makes it possible for somebody to overnight become a billionaire, may only be very indirectly related to the forces of globalization.

MS. GRAHAM: Okay. Question over there?

MR. MICHAEL: Hi. I’d like to ask both the authors for some clarification of a point. I’m Jim Michael with DPK Consulting. It seems to me that there’s a risk of interpreting the book as saying that if there are aspects of globalization that inherently contribute to inequality, you shouldn’t do them, like being open to technology flows because technology benefits those who are better off rather than those who are at the lower end of the income scale. And it seems to me then you would have less growth.

And rather, it seems to me the lesson here is that you should have an economy that is open to technology and growth and you should be investing the gains and the benefits of that growth to assure better participation in that growth by the poor and reduce poverty.

But it was a little bit unclear. And I would appreciate –

MR. THORBECKE: No. I mean –

MR. MICHAEL: -- clarification on that point, please.

MR. THORBECKE: Yeah. I think we would agree absolutely fully with you. I mean some people have described globalization as a force similar to gravity. It’s here to stay. And it’s also very clear, and I tried to say that at the outset that on a net basis, globalization has been a force to reduce poverty. But, it can be made much more effective.

And it requires not only interventions at the national level of the types Machiko described, safety nets, greater investment in education, health – Nancy also talked about this – but is also requires steps at the international level, such as the agricultural protectionism, which obviously makes it very difficult for African countries that have a comparative advantage in certain food crops to really compete on a fair basis in the world markets.

So, I think the – it’s not that we say globalization is bad for the poor, no. But globalization could with proper interventions, inter-domestic and at the international level be made a much more efficient instrument in reducing worldwide poverty.

MS. NISSANKE: I just want to add that our book is really trying to see, understand this integral – all of these different forces to understand mechanism through which globalization might effect position, relative position of the poor in the global community. But that doesn't mean that we take a view that globalization itself to be blamed.

What we are saying, there are those channels that mechanism operating and aren't working in development economics. How to make globalization to work for the majority and the poor, and that is the position. Of course, growth or globalization clearly inequality, then what we should do to make it more beneficial for everyone including the poor.

So, that is the position of our book. So, we are not saying that because globalization create inequality, we shouldn't have openness or we shouldn't have something else, but in fact, we are saying that this is a state, this is a tendency, but if integration works, then our question is how to deal with it, the consequences of that forces. And that's the way we approach it.

MS. GRAHAM: Nancy?

MS. BIRDSALL: Yeah. I think as a third party I can attest, Jim, that the book is very careful on this issue to avoid seeming to say that globalization is bad. You know, just a reflection on this problem and the dialogue about the effect of globalization on the poor and the reality of the – I mean, I think we’re at a point in time in which we need to be a little bit less fearful about every seeming to say, you know, that globalization isn’t good.

I think there’s – you know, it’s taken since the fall of the Berlin Wall, almost 20 years for the economics community to shed itself of the fear that if you talk about inequality, you will be seen as some kind of a wild-eyed socialist. So, it’s – now, we’re at a point where we need to similarly shed our fear that if you discuss the channels carefully and in a thoughtful balanced way by which globalization might produce some losers, that you will be accused of being anti-market or – we’ve got to stop that, you know – as – this is a – at Brookings and WIDER and it’s – we have to be analytic about this and move on to just what Machiko said, what are the channels, so we can work with countries to prevent them.

And I think the one thing I would say about the book is that it is so careful, it’s never really that bold on this is about politics and power; it’s not just about technical fixes. It’s there in the book. It’s there, but it’s very subtle and careful.

MS. GRAHAM: Okay. Well, that seems to have gotten some people.

That gentleman back there who’s had his hand up for a while?

MR. GUYOSO: My name is Antonio Guyoso. I am a professor at (inaudible) Graduate School of Management. If you look – if one looks at the European economic community, one could define it as globalization small within a broad region. And one of the characteristics of the European community is that they have cross border social protection mechanisms that help those countries which are poorer as a relative.

And my question is as we look at all of these figures and globalization at large, should we think as developed countries benefits on the need also to implement social protection mechanisms to bring some equalization of the possibilities for other countries to benefit as well?

MS. GRAHAM: Can I say a word on that? Just the prerogative of the chair.

I think there are many of us that would love to think about it, and there are people that have probably thought about some mechanisms. And I'd go back to Nancy's point, it's all about politics and power there. And in a context where it's difficult to get people to think about redistribution within their own societies, we're steps away from that, and it doesn't mean we shouldn't be making some progress on it conceptually.

MS. BIRDSALL: Can I just add something? You know, I think it's a great point, because one way to think about it is unfortunately, in the US, we've had this idea called trade adjustment assistance, which would provide protection for workers who clearly lose their jobs because their factories close down and move somewhere else. And you know, the US Congress, the taxpayers have never been able to bring themselves to put nearly enough resources, even into domestic trade adjustment systems.

On the other hand, the Europe example, we should think about much more. The Europeans are planning to spend 40 billion dollars in the next five years in Poland on what they call the Cohesion Program. They spend in Spain, which of course is much richer and closer in every way to the original members of the EU than is Mexico to the US, let alone Malawi to you know, the UK. The spent more than 10 billion dollars a year in the nineties on these transfers. So, it can be done.

Surely, in the US, you could think of the US states like being the equivalent in some ways. It just started in the 18th century instead of the 20th century. There are huge transfers that go on from New York State to Mississippi or whatever. So, conceptually, its' possible. I think it's time to put it on the agenda and start putting the numbers together and thinking about it.

MS. GRAHAM: No. I think it's conceptually possible. I think one of the things we –

MS. BIRDSALL: And maybe practically it will take 20 years, 30 years.

MS. GRAHAM: No, no. What's interesting, though, is the examples you cite are people redistributing to people who are part of their community or sort of people like them. And everything we know, even about welfare spending within the US is welfare spending is higher for states that are more homogenous.

The same goes in Latin America. Welfare spending is higher in countries that are more homogeneous. So, the further away the country, the more distant it is from the median voter, I think the harder it is to make it work. I'm not saying it's impossible, but it's –

MS. BIRDSALL: Well, luckily, Mexico is becoming more and more like us and us like Mexico, so that might be the right –

MR. THORBECKE: If I may just add one word to what has already been said. A prime example, I think, of a potentially successful social protection mechanism would be a case where a shock, let's say a financial crisis – an international financial crisis hits a group of households so badly that they have to take their children out of school, then have a social protection mechanism that would pay that household to keep the child in school, because in some cases, the impact of taking a child out of school may be irreversible. The child may never go back to school or even if the child goes back to school, there's a loss of human capital.

Now, it seems to me that the first step before we even start thinking of some kind of an international harmonization scheme that would work among countries would be to do much more of it within countries. Progressa in Mexico has been quite successful. A number of Latin American countries are starting to copy it. The World Bank now has a little group that is working exclusively on social protection schemes.

So, I think let's start at the country level and then move to the inter-country level.

MS. GRAHAM: Machiko?

MS. NISSANKE: Yes. I just want to add because it came up. I did do at the very end of my presentation, I talked about it's needed to think about redistribution mechanism at national level, global level. And your question is tie up to that that we have to think about the willingness and the ability to deal – how to deal with side effect of that mechanism wealth creation, and whether we are as a society willing to redistribution gains all inclusive.

And I think economics is come up a long way on this. Before, it was equity; efficiency was just a tradeoff. You had to take one or another. But now, research is such and Erik has done great work on this that actually there is economic ground, economic reasons why creating more equity, more equal society is good for growth.

If we look at from way, I – we hope that our book will create some platform to think through that better we can think about the global creating of mechanisms for more global equity efficiency, both together changing something which we feel economically as well as on ethical ground, which make much more sense. And that's what we are trying to do through our book, get you involved in that debate. Thank you.

MS. GRAHAM: Okay. We're running out of time, so I'd like to take two more questions at once and collect them and let the panel respond. So, we'll take one from over there?

MR. THORBECKE: Carol, this gentleman keeps trying to.

MR. KARIM: My name is Abdul Karim and I'm from Morocco. I'm here as a student attending Indiana State University. So, my question is –

MR. THORBECKE: I can't hear.

MR. KARIM: Okay. My question is a kind of a general one and one of (inaudible), so how far do you think have economically strong countries like United States, Japan, Britain, and many other countries, how far have these countries gone into the process of ensuring economic stability and social prosperity for other underprivileged countries like especially in Asia and Africa?

MR. SMITH: Bruce Smith, George Mason University. I'd like to disagree a bit with Nancy's formulation there that it's either practical or very politically useful to focus on these redistribution policies. You know, maybe that's something that's attractive to intellectuals, but the way it works out politically is that this works against trying to mobilize energies behind completion of the Doha Round.

And I think in a larger scheme of things it's more important to try to get the trade liberalization, particularly since the comments we've stressed on agriculture. If we could liberalize trade, get the developing countries trading with each other on agriculture and finally living up to our bargain of giving them access to advance country markets, that would be a much more immediate payoff in terms of reducing poverty and be worrying about, you know, trying to develop some elaborate measure and equity and so forth.

Trade adjustment experience in the US is not very felicitous because there isn't even the intellectual apparatus of distinguishing what's a trade impact from what's an impact within our domestic economy. So, let's put our energies for the immediate on trying to get the Doha Round ratified and get some umph behind it for the Brazil, India, the Europeans and ourselves.

MS. GRAHAM: Okay. Last comments from the panel on any of those questions.

MS. BIRDSALL: I don't see it – on this last point, I don't see necessarily a tradeoff between getting it – getting clarity on the transmissions mechanisms by which globalization might produce losers as well as winner and pushing for a more liberal free trade international order. I don't see a tradeoff. I think we both are – both make sense.

MS. GRAHAM: I might add to that there's some work done – it's on developed countries primarily. But it shows that countries that have higher levels of trade adjustment assistance, however efficient or not it is, are more pro-globalization, that people are more likely to vote for openness if they don't fear it.

Okay. So, just before concluding, I would like to take a second to thank Kristie Latulippe from Brookings, Adrianna Pita and the Brookings communication team, and Aura from WIDER for their wonderful work in pulling this together and also in putting together a reception, which is next door, and all of you are invited to stop by that if you'd like. And thanks very much.

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