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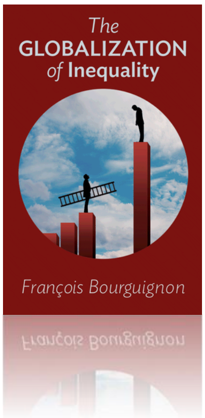
60 Book reviews on global economy and geopolitical readings

Fundación REPSOL

Obra Social "la Caixa"

The Globalization of Inequality

Bourguignon, François, (2015), Princeton University Press, Oxfordshire.



"After two centuries of steady economic growth, global inequality has significantly decreased over the last twenty years. But this should not mask the fact that a small number of less populous countries have fallen significantly behind the rest of the world. In other words, certain poor countries have only marginally benefited from global rise in prosperity... The decrease in global inequality should not distract us from this worrisome situation."

"Is inequality between countries in the world on the verge of being supplanted by inequality within countries?"

Summary

Will the 21st century be remembered for the globalization of inequality? Are we heading towards a world in which the inequality that has developed between nations over the last two centuries will gradually transform into inequality within these nations themselves? In *The Globalization of Inequality,* François Bourguignon adopts a succinct and accessible approach to this highly interesting and complex subject. On a global scale, the signs are positive, since there has been a steady decrease in inequality *between* countries over the course of the last two decades. However, a review of data *within* states is less encouraging. After a significant lessening of inequality midway through the 20th century, followed by a period of stability, inequality has now started to increase in the majority of countries.

Through an exhaustive analysis of the national and global trends that have influenced this process, Bourguignon presents the complex and paradoxical links between the positive effects of a vibrant world economy that has raised the living standards of more than half a billion people in emerging countries such as China, India and Brazil, while simultaneously contributing to growing inequality within nation-states. Without going into great depth, he seeks to put forward solutions that will offset the negative effects of this process. According to the author, these solutions include policies of redistribution through taxes and transfers; policies that reduce differences in the quality of education and professional training and access thereto; income tax policies (above all, taxation of wealth); and policies that regulate the financial market.

One point that is made very clearly in *The Globalization of Inequality* is that it is becoming increasingly difficult in today's globalized world to separate the national factors from the international factors that contribute to the generation of inequality. Furthermore, globalization is part of the problem, but also part of the solution. The author therefore stresses the need to complement national efforts with concerted efforts on an international scale. Although an international taxation system that could be applied by every country may still be a utopian idea, Bourguignon is optimistic in the light of recent initiatives to regulate the international flow of capital and tax havens; he considers that, today, attention must be focused on making capital movements more transparent. In this way, national governments would maintain a certain degree of autonomy with respect to taxation and, consequently, a certain degree of control over inequality in their respective countries.

The author

François Bourguignon is a professor at the Collège de France, Paris, and former director at the Paris School of Economics. From 2003 to 2007, he was chief economist and senior vice-president of the World Bank. In 2010, Bourguignon was made a Chevalier of France’s National Order of the Legion of Honour.

Key ideas and opinion

Globalization is seen by some as a panacea; by others as an instrument for modernization; and even as a deadly threat: the cause of economic crises, the destruction of the environment, the excessive power of the financial sector, de-industrialization and many other ills of contemporary society, including an explosive rise in inequality. There is no doubt that debate about the effects of globalization is heated and leaves no one indifferent. In *The Globalization of Inequality*, François Bourguignon aims to shed some light on this debate. Globalization is a complex historical phenomenon that has existed, in some shape or form, since the beginning of human society. But it is only in recent centuries that it can be tracked with more precision. No one denies that it exists, and there is little doubt that it will continue. However, the real question is whether, as it is often claimed, globalization is responsible for an unprecedented rise in inequality within states over the last two decades. **Does today’s globalization spell the end of equality? If it continues, will it destroy any hope of social justice?**

In order to answer these questions, Bourguignon considers it essential to distinguish, in the first place, between inequality *between* countries and inequality *within* countries. Upon analysis, two clear trends may be observed. **On the one hand, after growing consistently over the course of two centuries, inequality *between* countries has begun to decline**. Twenty years ago, average living standards in France and Germany were twenty times higher than in China or India. Today, this gap has been cut in half. **On the other hand, inequality has increased *within* many countries**. In the US, for example, inequality has risen to levels that have not been seen in almost a century. In the great majority of OECD countries, the GINI coefficient of disposable income per adult has risen by more than two percentage points during the last two decades. In countries such as **the US, the UK, Germany, the Netherlands, Italy** and, surprisingly, in **Scandinavian countries**, it has risen by more than four points. Inequality also increased in a large number of developing countries between 1980 and 2000. In **China**, the GINI coefficient climbed from 0.28 to 0.42 during this period. In **India, Indonesia** and **Bangladesh**, a similar increase was recorded. In **Africa**, some of the countries that have shown the highest rates of growth also reveal the strongest divergence in standards of living, examples here being Ghana, Kenya and Nigeria. In **Latin America**, inequality increased considerably in the 1980s, when the region suffered a severe balance of payments crisis and draconian structural adjustment reforms. In the 2000s, inequality decreased in the region, but even so, it remains at a substantially higher level than in any other region, with the possible exception of Africa.

Since the increase in inequality within countries tends to coincide with the acceleration of globalization, we tend to conclude that globalization is responsible for inequality. This conclusion is drawn, paradoxically, despite the fact that globalization has also contributed to a drop in inequality worldwide. In Bourguignon's opinion, this is because we have a tendency to look to our surroundings rather than beyond them. For this reason, the rise in national inequality is eclipsing the drop in global inequality, leading public opinion to conclude that we are living in an increasingly unequal world. **Nevertheless, the relationship between globalization and inequality is more complex than it might seem**. Of course, the expansion of international trade, the mobility of capital and labour, and the spread of technological innovation have contributed to reducing the gap between developed and developing countries. However, at the same time, these factors have affected the distribution of income within countries. Logically, **other factors such as technological progress, the local capacity to generate economic growth, specific strategies for development and redistribution policies also influence inequality** at both the national and international levels. Bourguignon therefore concludes that **the question that needs to be asked is: how big a role has globalization played?**

In answering this question, there are two key factors to consider: exogenous changes that affect all countries and political reforms that were implemented on a national scale. With respect to exogenous changes, the author highlights the fact that the 1980s and 1990s saw a radical change in the world economy, with a large number of countries such as China, India and the Soviet bloc opening up to international trade. This opening up process in a considerable number of nation-states with unskilled or semi-skilled labour led to the relocation of the world's production activity. Bourguignon stresses, however, that **we must reject the commonly held view that accelerated globalization**

has impoverished developed economies to the benefit of emerging economies. In general, both groups have gained through the expansion of trade. In the **developed economies**, although certain sectors of the economy suffered in the face of new competition, others benefited – in particular, goods and services that are capital-, skill- or technology-intensive. In addition, prices for a large number of goods, which are now imported, dropped, leading to a rise in average purchasing power. Of course, Bourguignon insists, these gains were unequally distributed among the population, and some sectors benefited more than others. However, on the whole, globalization had a positive net effect on the economy. For the **emerging countries,** the opening up of markets contributed to the restructuring and modernization of their economies, and resulted in the transfer of jobs from low-productivity agricultural or artisanal sectors to a better paid industrial sector. In short, the opening up of countries to international markets, the development of trade, and technological advances have had an effect on both developed and developing economies, modifying the quantity of goods and services exchanged and produced, as well as employment, prices and salaries.

In addition, François Bourguignon emphasises that the institutional environment has changed over the last few decades at both the national and international levels. The defining change was the **deregulation of markets and the process of economic liberalization launched by the US and the UK at the end of the 1970s**. The purpose of these reforms was to relax what were seen as the overly strict regulations that states had imposed on markets in the aftermath of the financial crisis of the 1930s and World War II, and to liberate individual initiative from a stifling level of regulation. The author notes that, according to empirical data, **this deregulation contributed to an increase in wage inequality and, in some cases, increased inequality of living standards**. For example, in the US, the fall in the minimum wage in the 1980s and 1990s and the erosion of trade union power were responsible for 20% and 30% of the growth in wage inequality. **Emerging and developing countries also implemented significant reforms along the same lines, often imposed from outside in return for assistance from international financial institutions such as the International Monetary Fund and the World Bank**. These reforms led to profound institutional changes: commercial and financial liberalization, deregulation of goods, capital and the labour market, privatization, removal of subsidies to producers and consumers, cuts in social spending, etc. **Most of these reforms contributed significantly to the rise in inequality. Nevertheless, the author stresses that it would be a mistake to claim that these programmes were entirely responsible for the rise in inequality**.

In fact, many of these countries, especially those in **Latin America**, were in a difficult economic situation and reforms were needed. Moreover, **it is quite likely that inequality would have worsened regardless of these reforms**. In **Africa**, where countries were less developed, inequality was less sensitive to the reforms that came as pre-conditions to aid from development agencies. This does not mean that Africa did not suffer from the market liberalization measures. Indeed, Bourguignon notes that

African growth in the 1980s was severely slowed and possibly even reversed due to the reforms, but also due to unfavourable terms of trade. According to the author, the problem is that **the evolution of distribution in this part of the world has not been tracked with the precision necessary for detailed analysis**. In **Asia**, **the evolution of countries differs considerably from the above examples,** although institutional reforms were also implemented there. In **China**, for example, these institutional changes represented, above all, a transition from a centrally planned economy towards a market economy. The liberation of individual initiative in a country where before there had been little or none could only generate inequality. To a lesser extent, this applies to **India** as well, since it too was over-regulated. In both cases, Bourguignon stresses, it is difficult to disentangle what part of the inequality is due *stricto sensu* to the freeing of market forces, what part is due to the opening up of international trade and foreign investments, and what part is the direct result of the development process. This said, these phenomena themselves are not completely independent of globalization and the competition it has triggered.

Bourguignon considers that globalization is the background for almost all that has happened in recent decades. It has changed the international climate for national economies and has profoundly modified their structures. It has induced financial liberalization in a large number of countries. It has weakened the taxation system on the pretext of maintaining national competitiveness and the capacity for innovation in an environment of growing international competitiveness. The author underlines that, on many occasions, these reforms undertaken in the name of economic efficiency have contributed to an increase in inequality without significantly improving the efficiency they targeted.

But **how can we maintain the trend towards increased global equality while curbing the rise in national inequalities?** In the author's opinion, it is fairly likely that the convergence between emerging economies and advanced economies will continue in the next few years, and perhaps even accelerate. However, **Africa may be the exception, with its current development being based on exporting raw materials**. A large number of African countries have shown growth since the beginning of this millennium, largely due to high commodity prices. This said, it is fairly unlikely that this situation will continue in the long term. Yet, if global poverty is to drop and global inequality to continue decreasing, the growth of these countries must remain high. Of course, growth is the responsibility of the countries themselves, but **Bourguignon is quick to point out that in poor countries, it is heavily influenced by the international economic climate. Since it is difficult to intervene and control commodity prices, it is worth looking at what kind of support the international community** (above all, developed countries, but also emerging countries) **can offer for these poor countries' development**.

At present, development aid is the only instrument of redistribution from rich to poor countries. However, Bourguignon notes, **its effectiveness and size are quite limited**. Rich countries allocate about 0.35% of their GDP to development aid, around $130 billion in total. In contrast, the French system of taxes and transfers redistributes around 15% of the income of the richest 20% to the rest of the population. This figure represents a level of redistribution that is 45 times greater than redistribution on an international scale. Even so, Bourguignon stresses, for the countries receiving this aid, the sums of money **can account for 15% of national income, and sometimes as much as half the government budget**. Although there is some debate about the effectiveness of development aid, it cannot be denied that a large proportion of this aid has contributed to the alleviation of poverty and to improving access to health and education for the most disadvantaged. For this reason, **in the author's opinion, it cannot be considered to have been of no use whatsoever, even if it has not generated immediate economic growth**. In Bourguignon's view, it is important to **ensure that aid is not diverted, that its volume is sufficiently high, and that it is concentrated on the poorest countries**. It is essential to make a distinction between recipient countries whose leaders behave predatorily – in which case strict conditions and effective regulatory mechanisms must be imposed; and those whose governments are more transparent and development-oriented – the latter should be given greater freedom in the management of aid, which would be tied to specific targets.

Any restriction established by rich countries on imports from poor countries will also have a negative effect on living standards in the latter. In this respect, the increasing restrictions imposed by developed countries on the immigration of unskilled labour have prevented potential migrants from developing countries from improving their standard of living and the well-being of their family through the transfer of remittances. In addition, although important progress has been made in the liberalization of trade, this process remains incomplete. Bourguignon highlights the fact that many developing countries still have limited access to the manufactured goods of developed countries. For several years now, the **Doha round** has been attempting to improve this situation. However, the negotiations have failed because they have focused almost exclusively on the relationships between developed countries and emerging economies. **The access of developing countries to the markets of advanced economies must be a priority, as should some coherent form of protection for their domestic markets**.

At a national level, the author also proposes key measures to redress inequality, such as redistribution policies through taxation and transfers. Bourguignon criticizes the fact that over the last three decades there has been a kind of "contagion" of tax reforms among developed countries, which have tended to decrease the progressiveness of redistribution, insisting on the need to make a concerted effort to tip the scales back in the other direction. In emerging and developing countries, the lack of redistribution mechanisms limits the ability of the state to reduce inequality. Nevertheless, Bourguignon highlights the progress made in recent decades by emerging economies, particularly through their programmes of conditional monetary transfers to the lowest percentile on the salary scale. These programmes linked monetary transfers to children's education and medical examinations. In Mexico, for example, this strategy has increased schooling by 10% among 12 to 17-year-olds and reduced ill-health by 20% among children under the age of 5.

Beyond taxation, political leaders who wish to halt the rising inequality need to rely on policies that promote equality in access to and quality of services. Since international competition makes it difficult to regulate the intergenerational transmission of wealth through estate taxes, **these policies must focus primarily on education, health and job training (or retraining)**. The problem, according to Bourguignon, is that the **results of these policies take time to manifest themselves** and they are only an indirect response to the *unequalizing* effect of globalization. **In the short and medium term, taxation is the only effective means** of correcting inequalities, although it is constrained by globalization itself. Therefore, the author notes, it is important to make harmonized efforts focused on redistribution polices and the fight against inequality. **The initiatives recently undertaken by developed countries to regulate the international flow of capital and tax havens are encouraging in this respect and, according to Bourguignon, they must be given priority, especially since the idea of an international taxation system remains utopian.**