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**Item 3: High-level segment Tackling inequality  
through trade and development: A post-2015 challenge**

**Speaker: University of Florence**

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*Not checked against delivery \**

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# Inequality trends, causes, impact and policies

Giovanni Andrea Cornia  
University of Florence

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Trade and Development Board, High Segment; UNCTAD

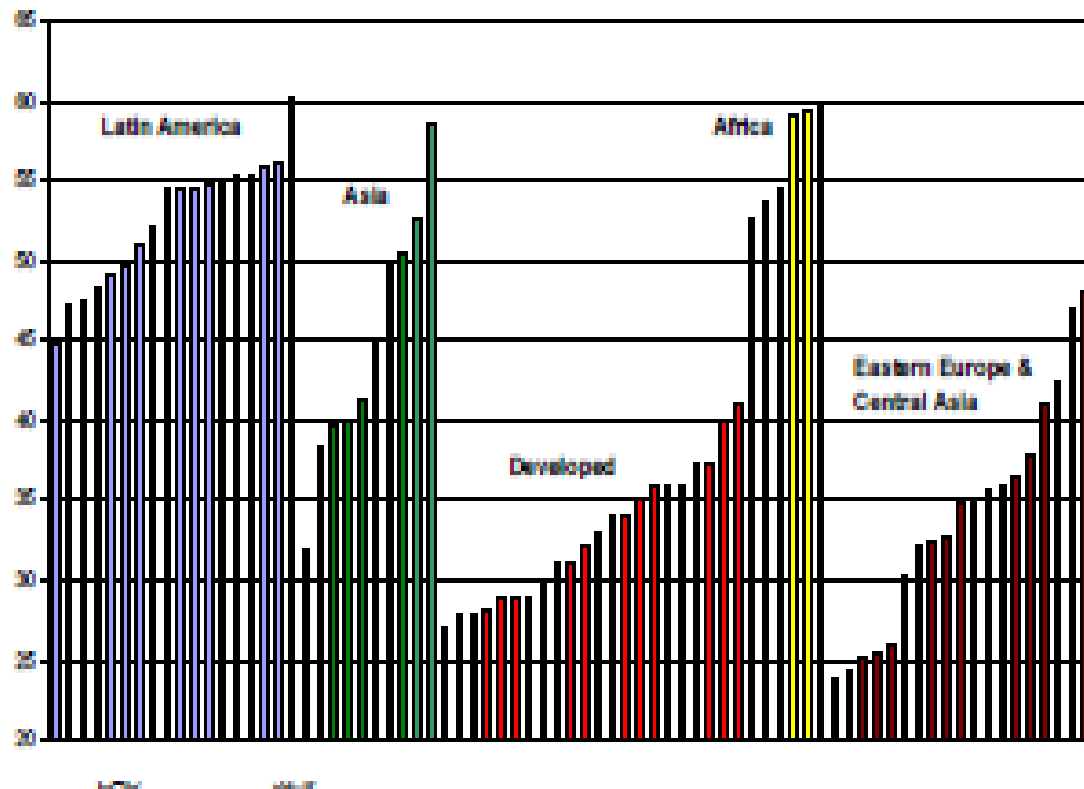
*Geneva 15-09-2014*

# 1. Initial conditions: inequality in OECD/developing regions

OWN CALCULATIONS

Household per capita income distribution

Last available observation



- Initial levels of **within country inequality**

- Much higher in LA, SSA & parts of Asia (SA)

- Due to:

- Asset concentration
- Unequal access to schooling
- Urban-rural gap
- 'Resource curse'

Source: own calculations based on WIDER and SEDLAC (CEDLAS and World Bank).

# Changes during the last 30 years

- In the past economists thought within-country **inequality differed** across nations but was stable in each country. Growth only way to reduce poverty
- Yet, over 1980-2000 **inequality rose** in 73 % of countries with data
- Over 2000- 10, **inequality fell** in LA, SEA, & parts of SSA - while it rose in other regions ... so 50% rise- 50% fall. Rising concern for income inequality ?
- **Convergence** to middle levels of inequality ?
- This bifurcation of trends is a kind of natural experiment, as it **allows to learn about causes of bifurcation** from the countries with falling inequality

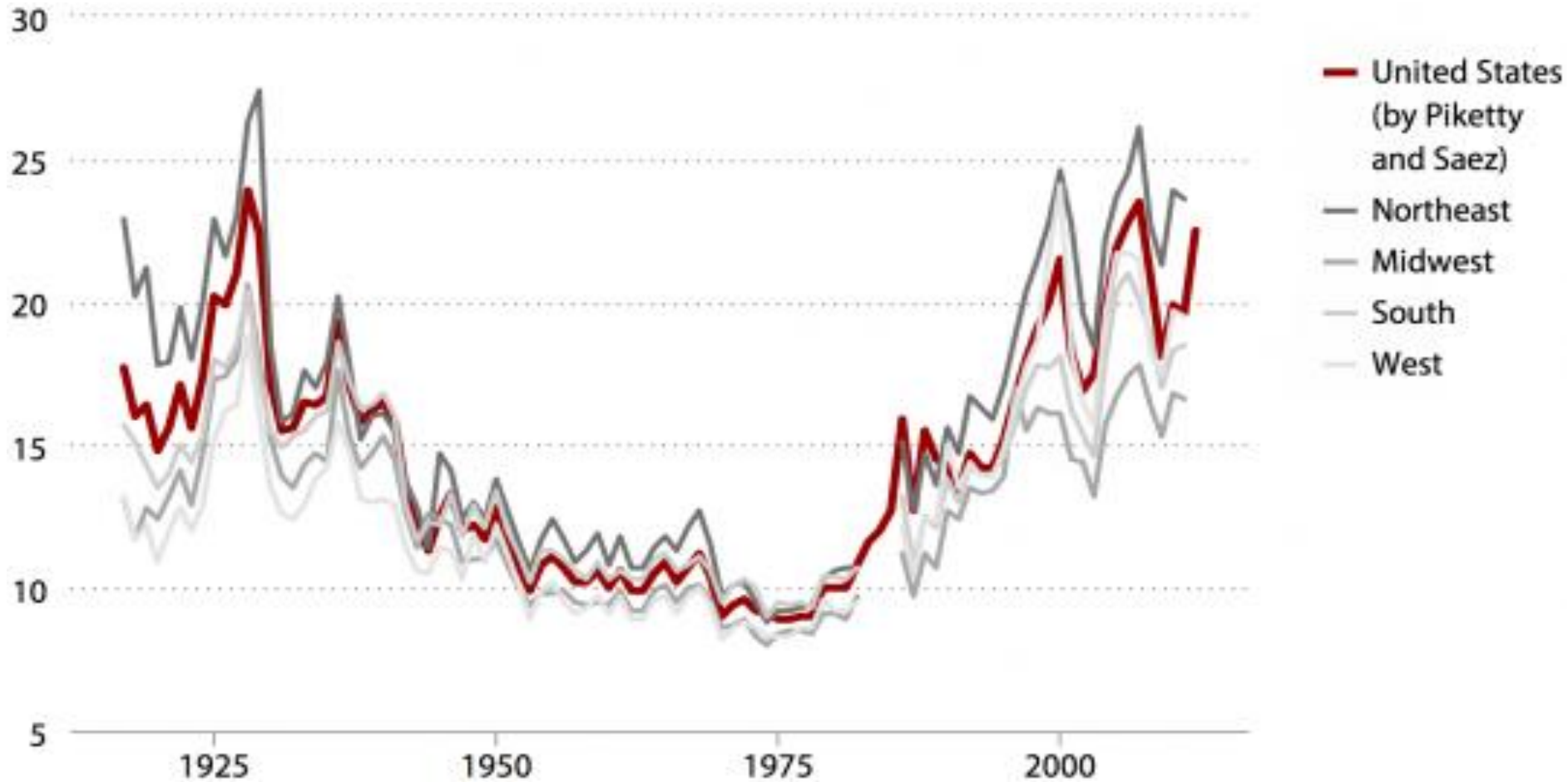
# Trends in n. of countries with rising/falling inequality

Trends in the Gini coefficient of household income/c, 1980-2000 and 2000-2010

	OECD	EE-FSU	Asian Transition	L.A.	MENA	SEA	South Asia	SSA	World
<b>1980s and 1990s</b>									
Period	1980- 2001	1990- 1998	1980- 2000	1980- 2002	1980- 2000	1980- 1995	1980- 2000	1980- 1995	
Rising inequality	<b>14</b>	<b>24</b>	<b>2</b>	<b>14</b>	2	<b>5</b>	<b>3</b>	9	<b>73</b>
No change	1	0	1	<b>1</b>	3	0	0	2	8
Falling inequality	6	0	0	<b>3</b>	3	2	2	8	24
<b>Total</b>	21	24	3	18	8	7	5	19	105
<b>2000-2010</b>									
Period	2000- 2010	1998- 2010	2000 – 2009	2002- 2010	2000- 2007	1995- 2009	2000- 2010	1995- 2007	Total
Rising inequality	<b>9</b>	<b>13</b>	<b>2</b>	<b>2</b>	<b>4</b>	<b>3</b>	<b>4</b>	<b>7</b>	<b>44</b>
No change	4	5	1	<b>1</b>	0	0	1	1	13
Falling inequality	8	6	0	<b>15</b>	<b>4</b>	<b>4</b>	0	<b>13</b>	50
<b>Total</b>	21	24	3	<b>18</b>	8	<b>7</b>	5	<b>21</b>	107

Source: Cornia and Martorano 2012

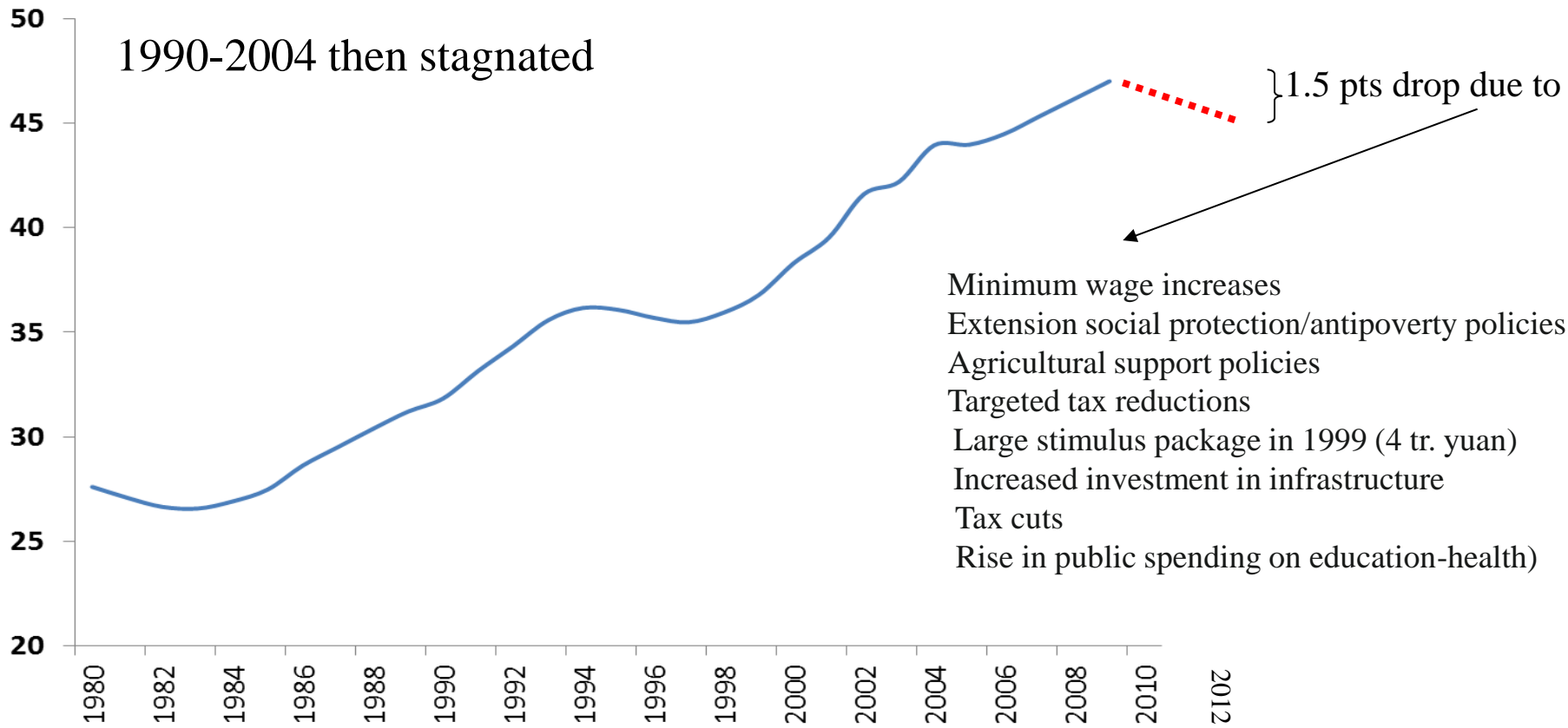
# Rising inequality in the US: Income share of top 1 %, 1917–2011



Source: <http://www.epi.org/publication/unequal-states/>

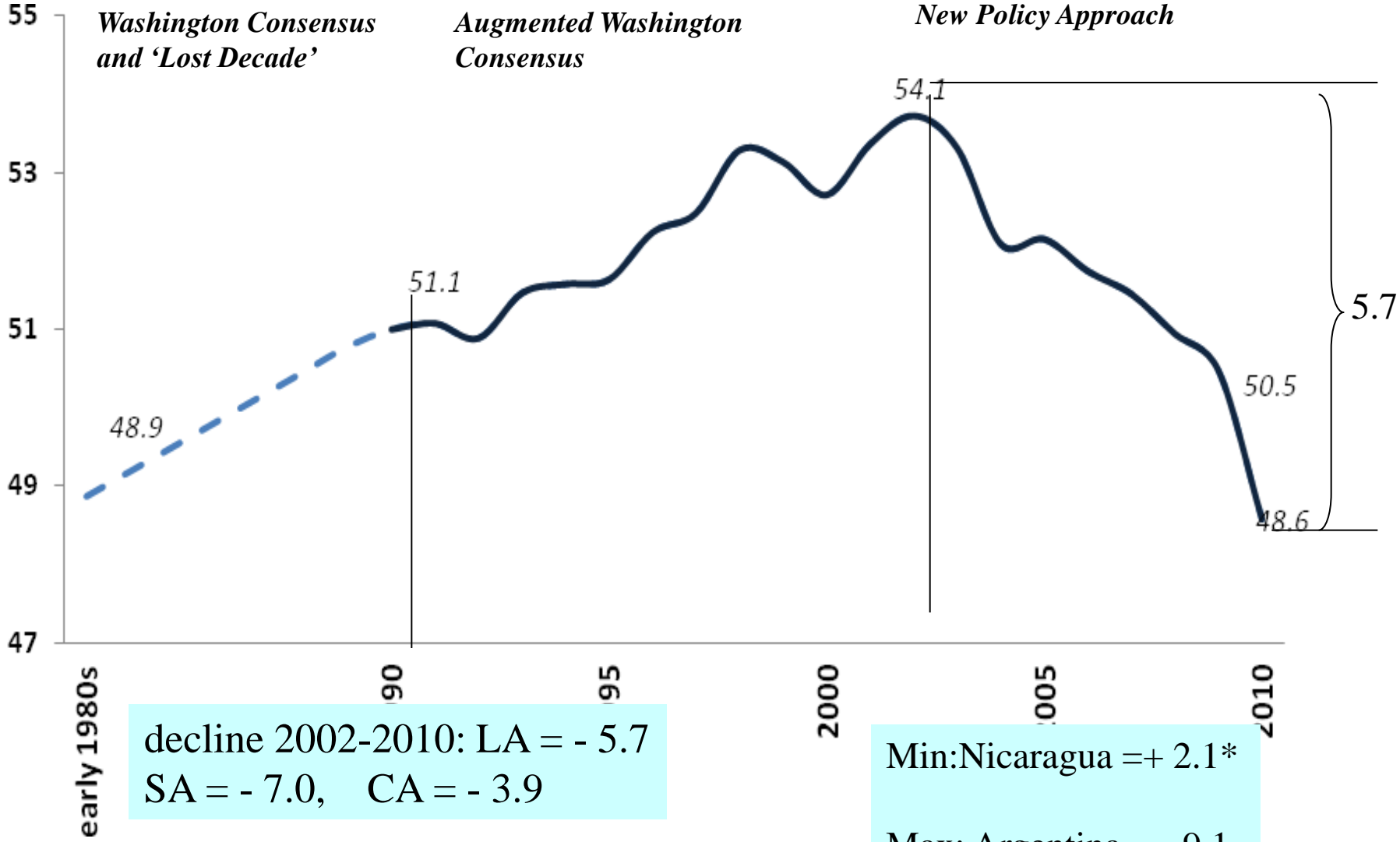
# China: fast rising Gini index, then small fall since 2009

India: Gini rose 7 points btw  
1990-2004 then stagnated



Source: Cornia Martorano 2012 + Nino Zarzua 2014

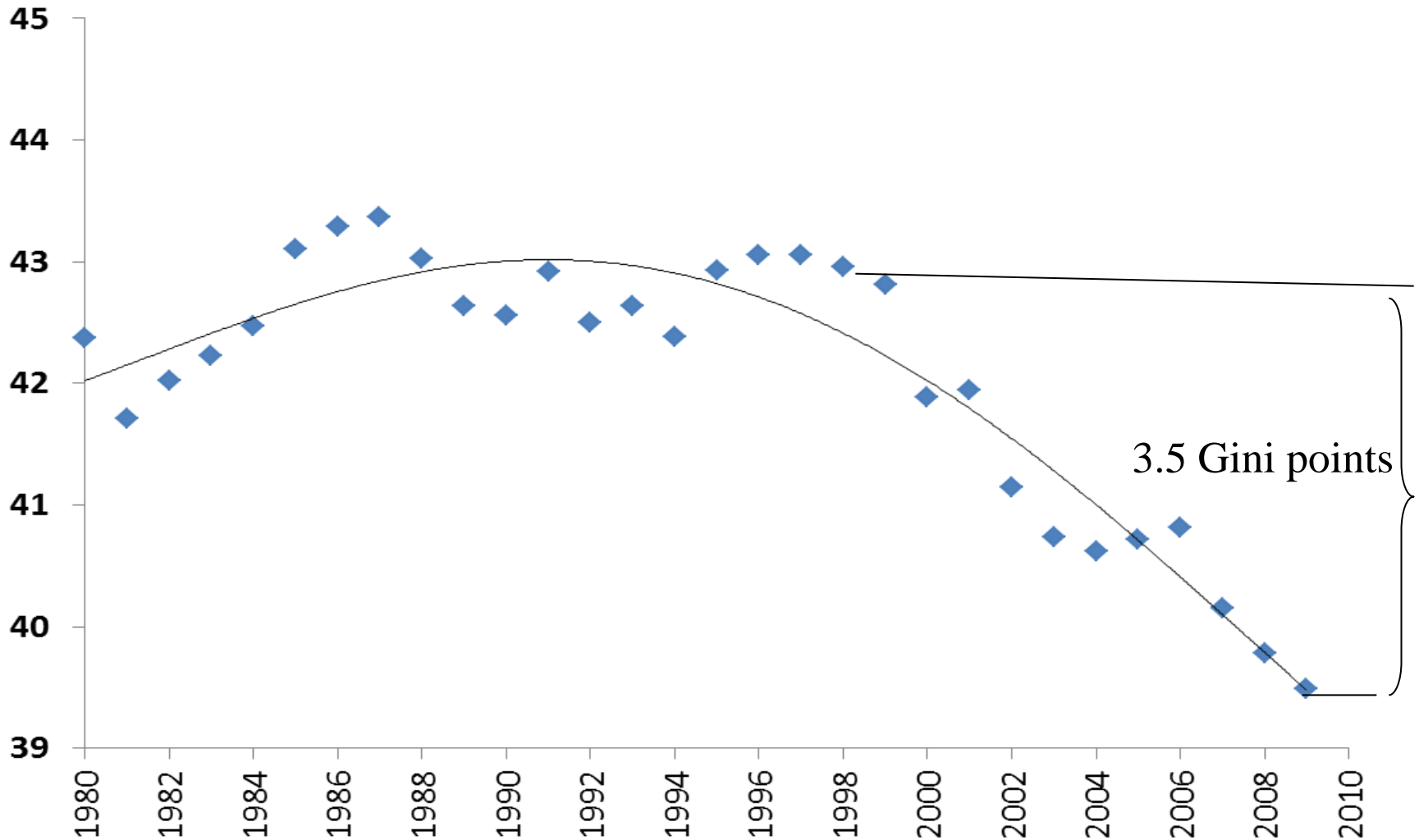
# Trend in av. LA regional Gini of distribution of household income/c



Source: Cornia 2014



# Moderate inequality fall in SEA (Malaysia, Philippines, S.Korea, Thailand)

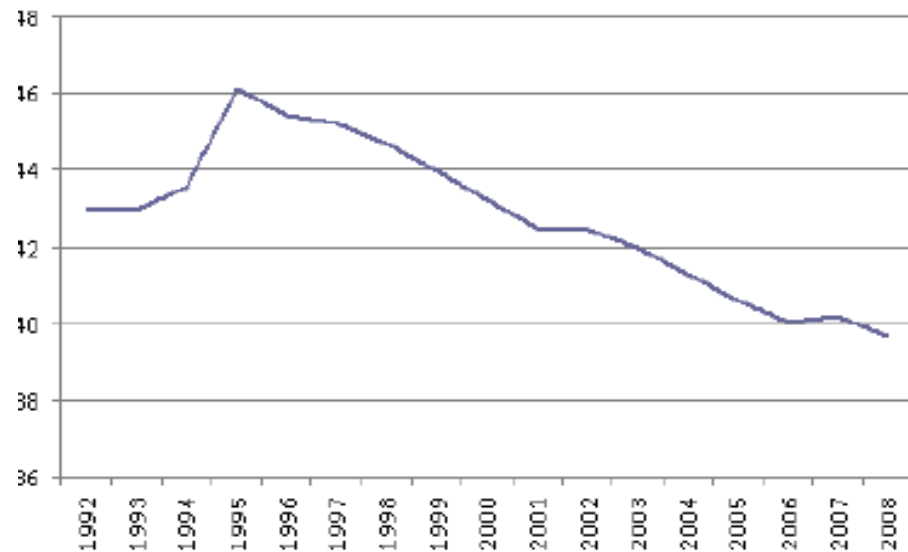


Source: Cornia and Martorano 2012

# Heterogeneous Gini trends in SSA

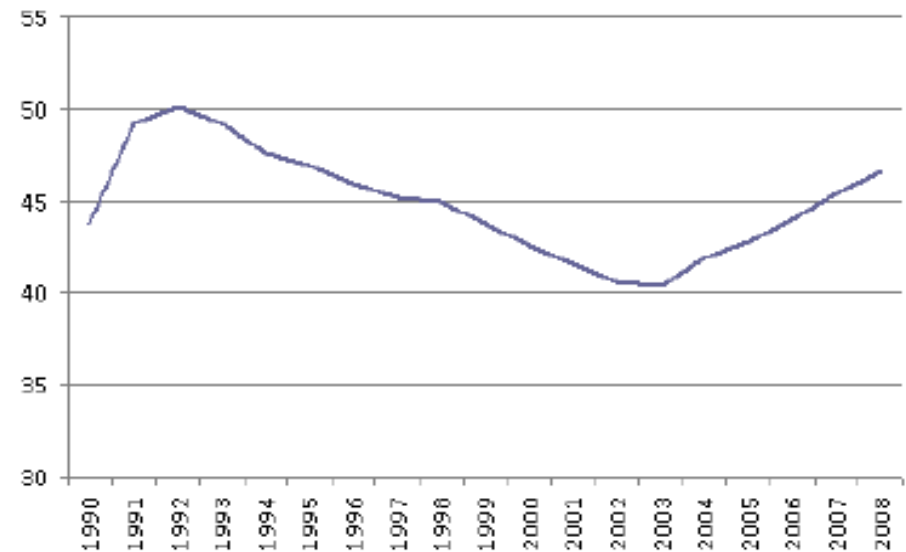
**Panel (a) 'steadily declining'** (8 countries)

Burundi, Cameroun, Guinea, Mali, Niger, Senegal, S.Leone, Swaziland,

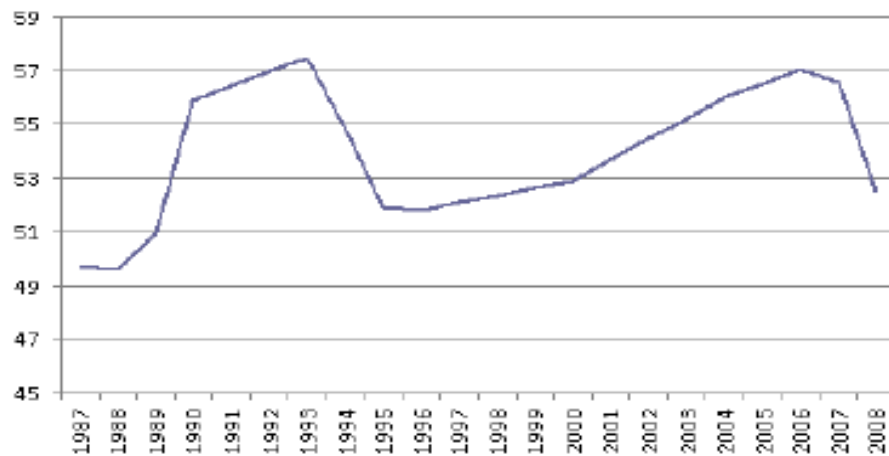


**Panel (b) 'falling, then rising from mid 2000s'**

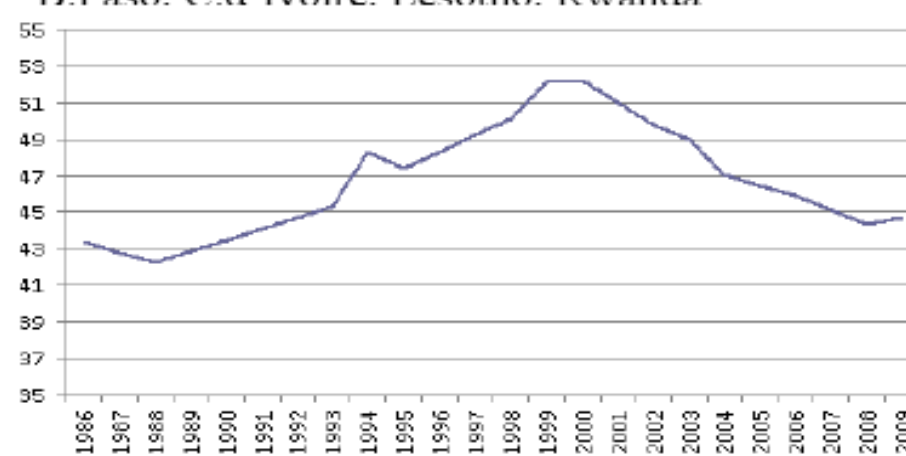
(9 countries): CAR, Ethiopia, Ghana, G.Bissau, Kenya, Malawi, Mozambique, Nigeria, Zambia



**Panel (c): steadily rising:** (4 countries) S.Africa, Mauritania, Botswana, Tanzania

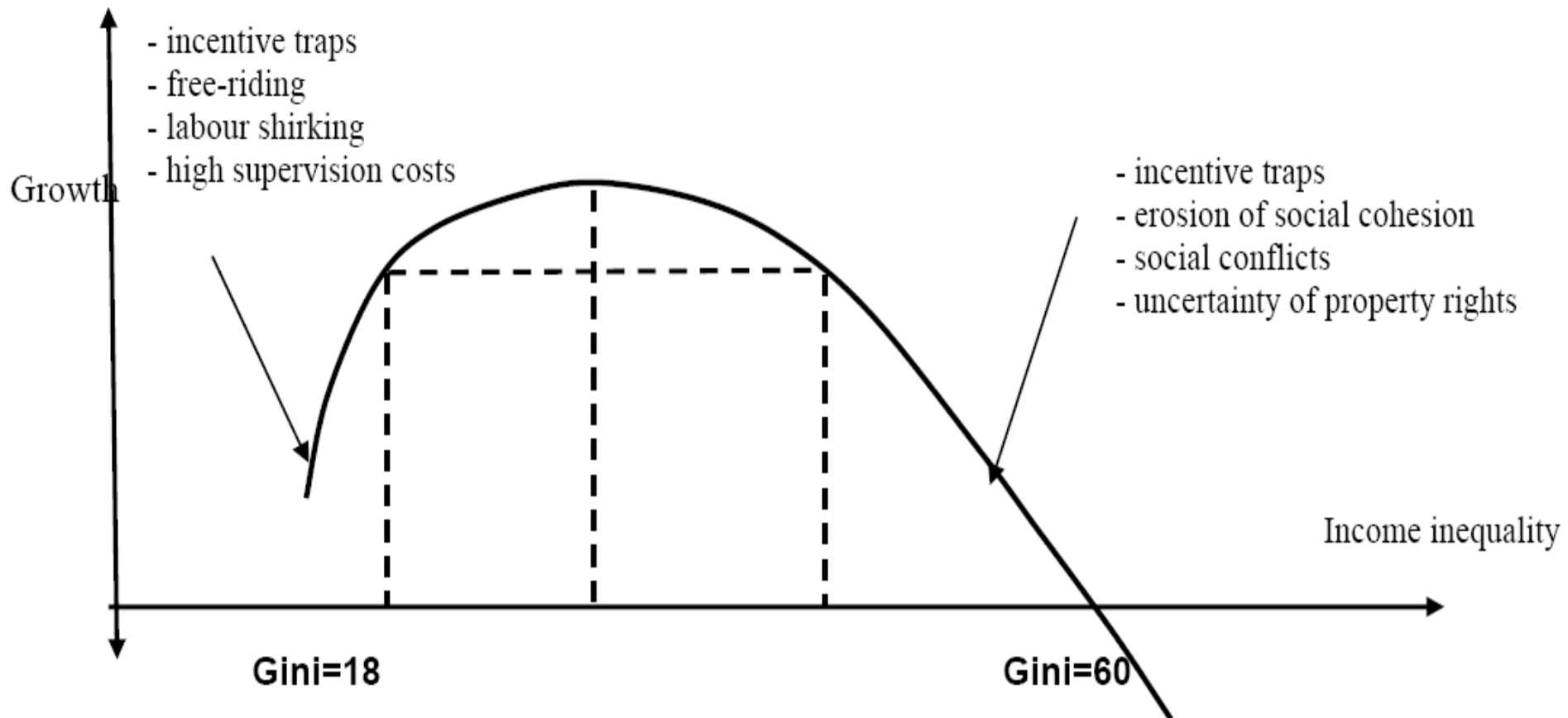


**Panel (d): rising then falling from early 2000s** (5 countries): Angola, B.Faso, C.d'Ivoire, Lesotho, Rwanda



## 2. Impact: Impact of high inequality on growth: beyond Gini 35-40 a rise in inequality reduces growth

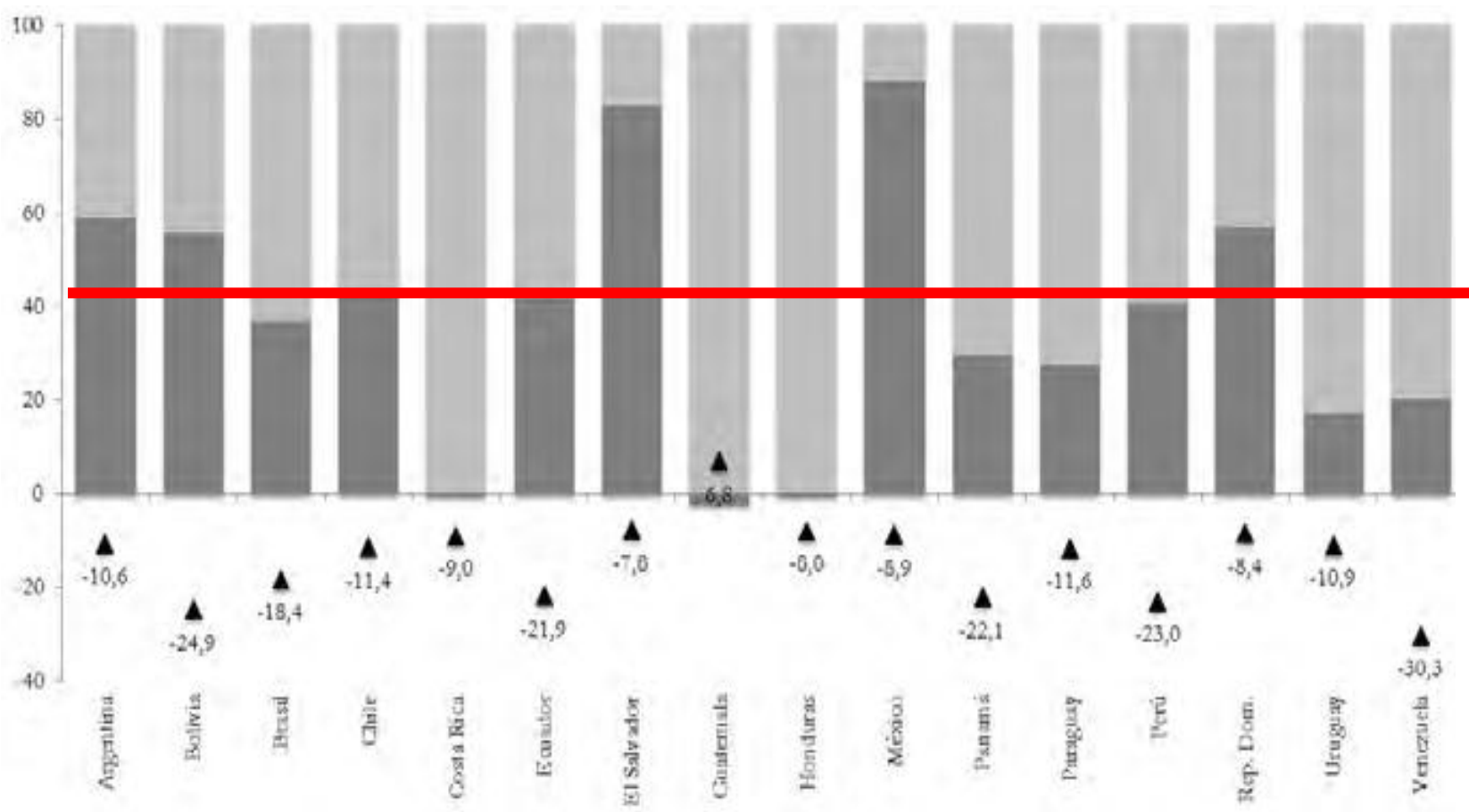
z. Concave relation between inequality and growth



# Impact of falling inequality on poverty:

## Faster rise of Poverty Reduction (40% in LA)

**Dark bar** = distributive effect, **Light bar** = growth effect, **Arrow** = %f poverty drop



Source: Lustig, Lopez-Calva, Ortiz 2014

# Impact of rising inequality from medium level



Social mobility  
Economic growth  
Community life  
Social trust  
Life expectancy  
Educational performance  
Physical health



Rates of obesity  
Abuse of drugs  
Teenage births  
Rates of violence  
Rates of imprisonment  
Incidence of punishment

# 3. Causes of inequality rise 1980-2000

- (i) Skill Biased Technical Change: technological upgrading raised demand for skilled workers while supply stagnated due to low public spending on 2ary/3ary + fall in minimum wages
- (ii) increased South-North exports (with high labour content) and migration depressed low skilled wages in countries of origin/destination.
- (iii) premature adoption of domestic and external liberalization:
  - fast trade liberalization
  - liberalization of FDI + deregulated domestic financial markets
  - Liberalization of wage formation had mixed effects
  - Liberal tax reform reduced tax/GDP ratio and worsened tax incidence
  - Impact of privatization varied according to the approach followed

# Explaining trend bifurcation of 2000-10

Comparing recent experience of LA+SEA (falling inequality) versus China, EE-FSU, SA (rising inequality)

- changing influence of structural causes of inequality ?
- GDP growth differences ? (but China, India: fast growth, Gini rise)
- good global economic conditions (trade, finance, remittances) in 2000s ?
- **better policies ?** → next slide

# ‘Open economy growth with equity’: policies

- Evidence shows inequality can be reduced under open economy conditions + technological shocks if new policy model is adopted:
- Virtuous policy changes observed in SEA & LA :
  - Macroeconomics and trade
  - Labour market
  - Taxation
  - Public expenditure on human capital accumulation
  - Social assistance and insurance



# 4. A new policy approach

## (a) Macroeconomics: 'hybrid model' (WC elements & 'development oriented' macropolicy)

- Prudent budget (1<sup>ary</sup> surplus 3-4% GDP) monetary policy
- Active and progressive tax policy → +tax/GDP ratio +3 to 9 points
- Increasing public expenditure especially on social public goods
- Countercyclical monetary-fiscal policy
- competitive real exchange rate → (+) T, (-) NT → (+) current account surplus
- Better prudential regulation of domestic banks
- Unchanged open trade regime, but changing trade pattern,
- International financing (lower foreign debt reserves accum debt substitution)

## (b) Labor market & income policies

- rise in n. workers covered by collective contracts
- work inspections against informal employment,
- Re-centralisation of wage bargaining in Argentina, Uruguay, Brazil
- rise in minimum wage
- increase in minimum social pensions,

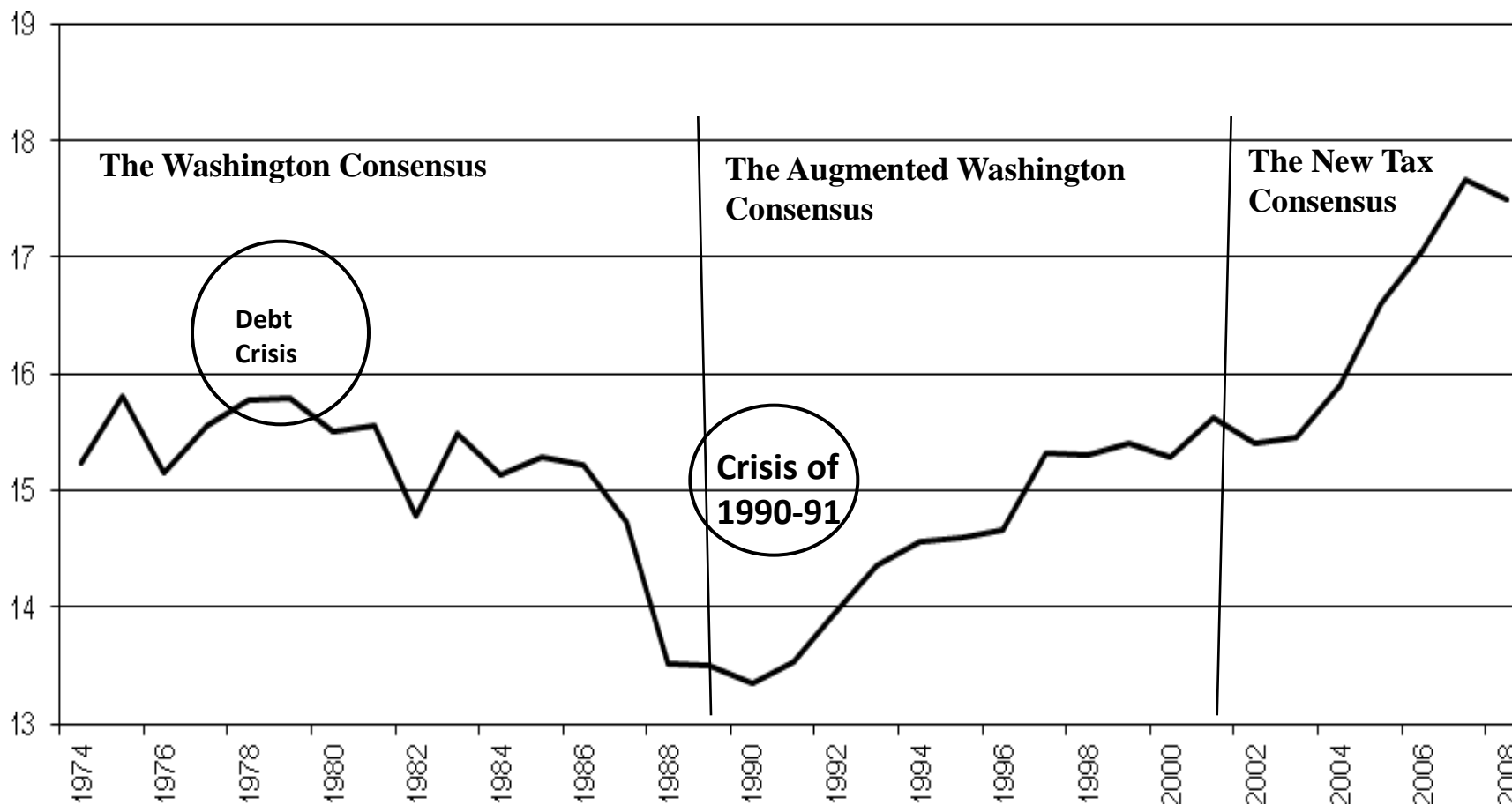
## Index of **real** minimum wages (2000=100), selected countries

	2002	2004	2006	2008	2010
Years of left regimes					
Venezuela (1999)	94.5	92.7	113.9	107.2	93.8
Brazil (2002)	114.3	121.4	145.3	160.8	182.0
Argentina (2003)	81.4	129.8	193.2	253.3	321.3
Uruguay (2005)	88.7	77.5	153.2	176.9	196.8
Costa Rica (2006)	99.5	97.6	99.5	99.5	105.8
Nicaragua (2007)	105.9	113.5	128.5	141.6	174.6
Ecuador (2007)	112.5	122.2	130.0	146.7	161.5
Guatemala (2008)	108.6	117.6	119.6	111.9	122.0
Mexico (--)	101.2	99.1	99.0	96.2	95.6

## (c) Tax policy and rising tax/GDP ratios

- Low initial tax/GDP ratio in relation to intl. norm
  - Tax effort accelerated in 2000s – including greater emphasis on direct taxes (figure on LA)
  - tax/GDP up almost everywhere, but huge variations remain (Mexico, C. America, others) – but flat tax in EE-FSU
  - Higher tax/GDP reduces macro instability, allow countercyclical fiscal policy, raise social expenditure
- $\Delta$  2003–7  $\Delta$  tax/GDP moderately progressive

# Trend in Average Tax/GDP Ratio, 1973-2009, L.America



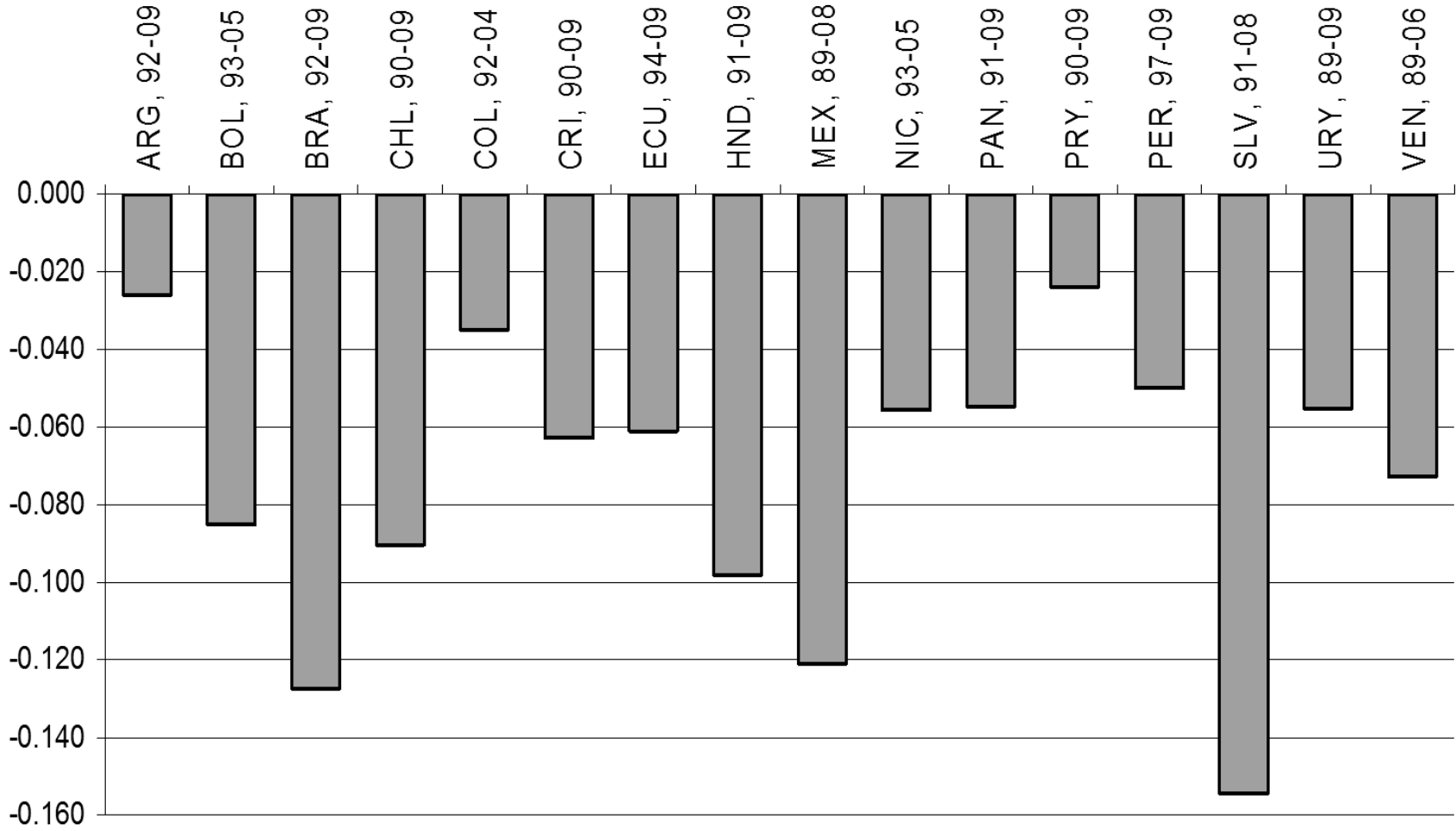
Source: Cornia, Gomez Sabaini and Martorano

## (d) Public social expenditure and redistribution of human capital

- Countries made big invest. in 2ary educ since 1990s chart
- Strong effect on income inequality, current and lagged
- Lower educational inequality → lower wage inequality
- Problems persist in 3ary education (still unequalizing)

Latin America	1990	1995	2000	2010
Av. spending on education p/child 0-14 (\$dollars PPP)	320	511	756	1451
Public expenditure on educ/GDP	2.8	3.3	4.0	4.4

+ public expenditure on educ → fall in Gini education



## (e) Social assistance and income transfers

- extending coverage of **social insurance** to
  - cover people with few years of contributions (in 1990s they worked in informal sector or were unemployed)
- Large increase in well targeted **social assistance**
  - CCT targeted anti poverty programmes (Brazil BF, Mexico, ..(0.5-1.0% GDP)
  - Pure transfers e.g. non-contrib pensions (Argentina, Brazil, Bolivia, Southern African countries, etc)
- Perceptible effect on income inequality, despite low-ish spending



# Long term measures to deal with 'structural inequality'

- Redistribution of assets, correction of mkt failures
  - Land redistribution in Latin America, SSA ...
  - Reduce rural-urban income gap
  - Taxation of resource sector
  - Broaden access to credit/finance/insurance for smallholders & SMEs
  - Accessible secondary and university education
- Active 'open economy industrial policy'
- Reduced dependence on foreign finance (as in E.Asia)