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Session D
presentation by
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Does Foreign Investment Lower Income Inequality?
New Evidence and Discussion on the Role of Service Offshoring

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14 September, 2018
Motivation(s)

Avenida Italia
Motivation(s)

Inequality is Inefficient, Since it Constitutes an Impediment to Growth, Development and Sustainability bit.ly/2nxn0ZA via @cepal_onu @UNDP @PNUDLAC #SDGs #NextGenUNDP
Theoretical Framework

- (th) Traditional economic: developing countries are abundant in low-skilled labour and FDI (as trade) raises the demand for low-skilled workers. Income inequality decreases (opposite in developed).

- (ee) North-South vertical FDI MNCs offshore labour intensive activities to South. However, for host countries these workers are high-skilled. Income inequality increases in developing countries. Services?
Research Questions

1. What is the effect of **FDI on income inequality**?
2. Is the effect different depending on the level of **economic development**?
3. Is the effect different in mature **service offshoring** locations?

\[
\text{Gini} = \alpha + \beta_1 \frac{FDI \text{ Stocks}}{GDP} + \beta_2 \log(\text{GDP per capita}) + \beta_3 \frac{Trade}{GDP} \\
+ \beta_4 \text{Human capital} + \beta_5 \text{Labor market regulation} + \beta_6 \text{Institutions} \\
+ \beta_7 \text{Democracy} + \beta_8 \text{Inflation} + \beta_9 \text{Transfers and Subsidies}/GDP \\
+ \beta_{10} \frac{FDI \text{ Stocks}}{GDP} \times \log(\text{GDP per capita}) + \varepsilon
\]
## Panel Data Results

<table>
<thead>
<tr>
<th>Dependent Variable</th>
<th>Estimation method</th>
<th>Model specification</th>
<th>Gini Coefficient</th>
<th>Instrumental Variables</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Baseline model</td>
<td>Interaction terms</td>
</tr>
<tr>
<td>FDI Stocks (% of GDP)</td>
<td>Instrumental Variables</td>
<td>Baseline model</td>
<td>-0.046*** (0.016)</td>
<td>-0.203** (0.097)</td>
</tr>
<tr>
<td>GDP per Capita (Log)</td>
<td></td>
<td>14.845*** (2.622)</td>
<td></td>
<td>7.119** (3.279)</td>
</tr>
<tr>
<td>Trade</td>
<td></td>
<td>-0.031*** (0.011)</td>
<td></td>
<td>-0.025** (0.011)</td>
</tr>
<tr>
<td>Human capital</td>
<td></td>
<td>-0.786*** (0.227)</td>
<td></td>
<td>-0.698*** (0.235)</td>
</tr>
<tr>
<td>FDI*Lower-middle-income</td>
<td></td>
<td></td>
<td></td>
<td>0.373*** (0.100)</td>
</tr>
<tr>
<td>FDI*Upper-middle-income</td>
<td></td>
<td></td>
<td></td>
<td>0.188* (0.099)</td>
</tr>
<tr>
<td>FDI*High-income</td>
<td></td>
<td></td>
<td></td>
<td>0.246** (0.098)</td>
</tr>
<tr>
<td>Number of observations</td>
<td></td>
<td>278</td>
<td>278</td>
<td></td>
</tr>
<tr>
<td>R-squared</td>
<td></td>
<td>0.669</td>
<td>0.716</td>
<td></td>
</tr>
</tbody>
</table>
For the Sake of Simplicity

<table>
<thead>
<tr>
<th>Income Group (GNI per cap, 2017)</th>
<th>FDI impact</th>
<th>Marginal effect of 10 pp. increase in FDI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low USD 995 or less</td>
<td><strong>Inequality-narrowing</strong></td>
<td>2.03 decrease Gini</td>
</tr>
<tr>
<td>Lower-middle USD 996 - 3,895</td>
<td><strong>Inequality-widening</strong></td>
<td>1.7 points increase Gini</td>
</tr>
<tr>
<td>Upper-middle USD 3,896 - 12,055</td>
<td>Mixed, robustness check: <strong>inequality-widening</strong></td>
<td></td>
</tr>
<tr>
<td>High USD 12,056</td>
<td><strong>Inequality-widening</strong></td>
<td>0.43 points increase Gini</td>
</tr>
</tbody>
</table>
2) The effect of FDI on income inequality varies according to the level of economic development.

- Low-income countries: low-skilled labour is predominant. FDI is targeted at less-skilled intense activities (e.g. garments, assembly).

- Lower-middle-income countries, low-skilled labour is abundant. FDI is likely vertical. Under the human capital structure of developing countries, offshored activities are intense in high-skilled labour.

- High-income economies: FDI less damaging due to more widespread distribution of wage premiums.

My Own-Little Personal Battle

Traditional Services

Education
Health
Public Services

Knowledge Services

Information Technology
Finance and Accounting
Legal Services
Leo.
“La indignación es el verdadero motor de la acción”.

Mariana Olivera
Creative Mornings MVD

Gracias

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