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Does Foreign Investment Lower Income Inequality?

New Evidence and Discussion on the
Role of Service Offshoring

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Motivation(s)



Avenida Italia



Motivation(s)



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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?

$$\begin{aligned} \text{Gini} = & \alpha + \beta_1 \text{FDI Stocks/GDP} + \beta_2 \log(\text{GDP per capita}) + \beta_3 \text{Trade/GDP} \\ & + \beta_4 \text{Human capital} + \beta_5 \text{Labor market regulation} + \beta_6 \text{Institutions} \\ & + \beta_7 \text{Democracy} + \beta_8 \text{Inflation} + \beta_9 \text{Transfers and Subsidies/GDP} \\ & + \beta_{10} \text{FDI Stocks/GDP} * \log(\text{GDP per capita}) + \varepsilon \end{aligned}$$

Panel Data Results

| Dependent Variable Estimation method Model specification | Gini Coefficient Instrumental Variables | |
|--|--|-----------------------------|
| | Baseline model | Interaction terms |
| | FDI Stocks (% of GDP) | -0.046*** (0.016) |
| GDP per Capita (Log) | 14.845*** (2.622) | 7.119** (3.279) |
| Trade | -0.031*** (0.011) | -0.025** (0.011) |
| Human capital | -0.786*** (0.227) | -0.698*** (0.235) |
| FDI*Lower-middle-income | | 0.373*** (0.100) |
| FDI*Upper-middle-income | | 0.188* (0.099) |
| FDI*High-income | | 0.246** (0.098) |
| Number of observations | 278 | 278 |
| R-squared | 0.669 | 0.716 |

For the Sake of Simplicity

| Income Group (GNI per cap, 2017) | FDI impact | Marginal effect of 10 pp. increase in FDI |
|---|---|--|
| Low USD 995 or less | Inequality-narrowing | 2.03 decrease Gini |
| Lower-middle USD 996 - 3,895 | Inequality-widening | 1.7 points increase Gini |
| Upper-middle USD 3,896 - 12,055 | Mixed, robustness check: inequality-widening | |
| High USD 12,056 | Inequality-widening | 0.43 points increase Gini |

Patterns of Difference

2) The effect of FDI on income inequality **varies** according to the level of economic development.

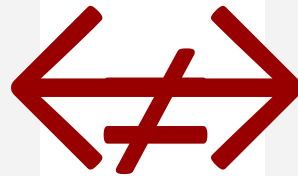
- Low-income countries: low-skilled labour is **predominant**. FDI is targeted at **less-skilled intense** activities (e.g. garments, assembly).
- Lower-middle-income countries, low-skilled labour is **abundant**. FDI is likely vertical. Under the human capital structure of developing countries, offshored activities are intense in **high-skilled labour**.
- High-income economies: FDI less damaging due to more **widespread distribution** of wage premiums.

3) Service Offshoring? **Fail**. Hence. **Guess: Increase**

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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