ERIK THORBECKE
MACHIKO NISSANKE

The Impact of Globalization on the Poor in Latin America

In 2004 the World Institute for Development Economic Research (WIDER) at the United Nations University initiated a large-scale research program entitled "The Impact of Globalization on the World's Poor," for which we served as codirectors. The main objectives of the project were to produce a set of rigorous theoretical and empirical economic studies, which would deepen our understanding of how conditions facing the world's poor have been evolving under globalization and provide a framework yielding the elements of a strategy that would induce the globalization process to become more pro-poor. In addition to the methodological and conceptual conference held in Helsinki at the end of 2004, the project organized three regional conferences to explore the impact of globalization on Asia, Africa, and Latin America, respectively, in 2005 and 2006.

Because of very significant differences in initial conditions (including natural resource endowments, the quantity and quality of human capital, the institutional framework, and the quality of governance), as well as in internal dynamics of institutional and sociopolitical conditions, globalization has different effects on the poor in different regions of the developing world. Generally speaking, the poor in sub-Saharan Africa were essentially bypassed by the forces of globalization, while most of the Asian poor benefited—none more so than in China. Latin America occupies an intermediate position in

Thorbecke is with Cornell University; Nissanke is with the University of London, School of Oriental and African Studies.

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this continuum.[1] In addition to broad intercontinental differences, the effects of globalization on the poor can be very diverse within each regional bloc and can even vary from region to region within a country.

This paper consists of four parts. The next section analyzes and describes the main channels (or transmission mechanisms) through which the process of globalization affects poverty both directly and indirectly.[2] The paper then reviews the major effects of globalization on the Latin American economy, although few generalizations can be made with much certainty. A subsequent section reviews the findings of eight selected case studies, undertaken under the auspices of the WIDER project. We use these case studies to illustrate and analyze the critical role institutions can play in mediating the impact of globalization on poverty within different Latin American settings. These studies reveal, first, how key institutions can strengthen the positive effects of globalization on poverty reduction and moderate some of the negative effects and, second, how sensitive the link from globalization to poverty, via institutions, is to initial conditions and the specific context. The final section concludes.

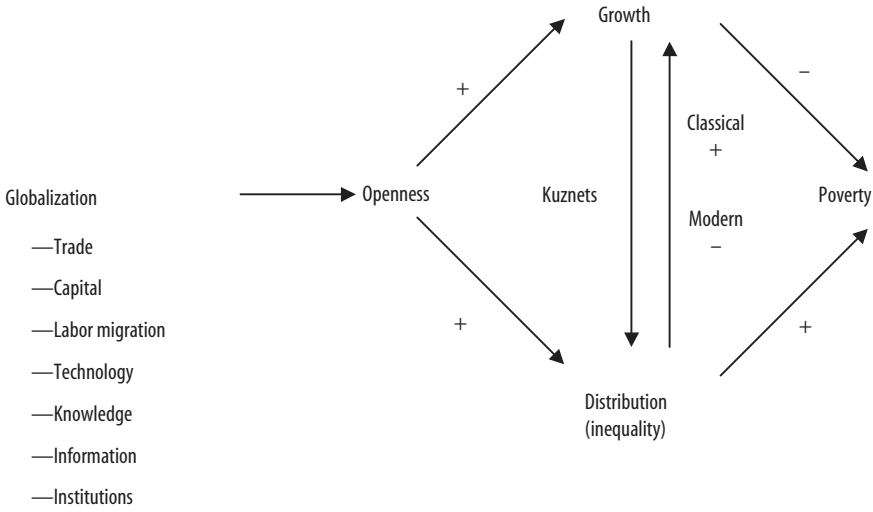
Channels Linking Globalization to Poverty

The globalization-poverty nexus is complex, involving many different channels. The link between globalization (openness) and poverty can be visualized as a large river fed by a variety of economic tributaries. Figure 1 illustrates schematically the various critical links of the causal chain running from globalization (openness) to poverty, focusing on the most critical tributaries and abstracting from several feedback effects among the constituting elements. Increased openness is the primary manifestation of globalization. The major transmission mechanisms from globalization to openness are listed in figure 1 and include changes in the relative prices of factors of production (labor and capital) and commodities; movements of capital and labor across borders and within countries; the nature of technological change and technological diffusion; the impact of globalization on volatility and vulnerability; the worldwide flow of information; global disinflation; and institutions. These mechanisms affect poverty through two different paths: first, through their contributions

1. For a comprehensive discussion of the differential regional impact of globalization on the poor, see Nissanke and Thorbecke (2008).

2. For a more detailed discussion of different transmission mechanisms in the globalization-poverty nexus, see Nissanke and Thorbecke (2006a; 2006b, chaps. 1–2).

FIGURE 1. The Globalization-Poverty Nexus



to the growth channel (shown in the upper part of the diagram) and, second, through their impact on income distribution and poverty (in the lower part of the diagram), since globalization creates winners and losers directly and affects vertical and horizontal inequalities.[3] The links shown in figure 1 are from openness to growth, from openness to income distribution (inequality), from growth to income distribution and vice versa, from growth to poverty, and from income distribution to poverty, respectively. In turn, the two main channels of globalization—the growth and distribution channels—further interact dynamically over time to produce a growth-inequality-poverty triangular relationship. This is captured by the right-hand side triangle of our diagram, which describes the arithmetic-statistical relationship among growth, inequality, and poverty investigated and popularized by Bourguignon.[4]

In the remainder of this section, we first discuss the globalization-poverty nexus through the growth channel and the growth-inequality-poverty triangular relationship. We then move on to a discussion of other channels through which globalization can affect poverty directly by creating winners and losers.

3. See, for example, Ravallion (2004a) for a discussion of how globalization may alter horizontal and vertical inequality.

4. Bourguignon (2004).

The Globalization-Poverty Causal Chain

To analyze the impact of openness through the growth channel on poverty, the globalization-openness-growth-inequality-poverty causal chain has to be scrutinized link by link.

THE OPENNESS-GROWTH LINK. Policies of openness through the liberalization of trade and investment regimes and capital movements have been advocated worldwide for their growth and welfare-enhancing effects on the basis of the propositions embedded in the well-known economic theories of international trade, investment, and finance. Indeed, openness through trade, foreign direct investment (FDI), and financial markets typically increases the flow of goods and capital across national borders and can contribute significantly to economic growth. The direction of causality in this link, however, is still under debate (the present consensus is that trade contributes to growth rather than vice versa), as is how trade and capital flows could be interlinked in a virtuous circle. Furthermore, the positive openness-growth link is neither automatically guaranteed nor universally observable. The growth-enhancing effects of trade openness depend critically on the way and extent to which a country is integrated in the global economy.[5]

Similarly, the transfer of technology, skills, and management know-how that is assumed to accompany FDI often does not occur. The postulated positive effects of portfolio and other capital flows (hot money) on growth have been increasingly challenged in recent years. Even some studies by the International Monetary Fund (IMF) acknowledge that it is difficult to establish a strong positive causal relationship between financial globalization and economic growth.[6] In addition, short-term capital flows contribute to the increased vulnerability to external shocks of the recipient developing countries. Empirical evidence suggests that openness leads to more within-country inequality through the openness-inequality link, as discussed below.

A large number of empirical studies based on cross-country regressions have been conducted to show the beneficial effects of an open economy

5. Sánchez (2003, p. 1979) notes that "the causality link between trade openness and long-run growth is not engraved in stone."

6. For example, see Prasad and others (2003); Kose and others (2006). Nissanke and Stein (2003) present a critical view of the effect of financial globalization on economic development in emerging market economies.

regime on growth.[7] However, many researchers contest the validity of these cross-sectional empirical exercises on technical grounds.[8]

THE INTERRELATIONSHIP OF GROWTH, INEQUALITY, AND POVERTY. The second link in the causal chain from openness to poverty through the growth effect is the interrelationship between growth and inequality. First, there are two conflicting theoretical approaches to relating the causal chain from income and wealth inequality to growth (the inequality-growth link). The traditional approach views income inequality and wealth inequality as necessary conditions for fast capital accumulation and economic growth at an early stage of economic development because of the higher propensity to save among the rich and the existence of investment indivisibilities and incentive effects.[9] From this theoretical perspective, the desirability of an unequal income distribution is rationalized on economic grounds, that is, on the basis of the claim that more poverty today is a precondition to more economic growth and less poverty in the future.[10] In contrast, the new political economy of development theories linking greater inequality to reduced growth operates through a number of subchannels, including the diffusion of political and social instability, which increases uncertainty and lowers investment; unproductive rent seeking activities; high transaction costs; and increased insecurity of property rights.[11] In addition, wide income and wealth disparities can have an impact on education, health, and crime through such manifestations as underinvestment in human capital, malnutrition leading to low worker productivity, stress, and anxiety. These manifestations may, in turn, contribute to lower long-term growth.[12]

7. Dollar (1992); Sachs and Warner (1995); Dollar and Kraay (2002, 2004). See World Bank (2002) for a summary of these cross-country studies on the openness-growth link.

8. See Rodríguez and Rodrik (1999) for an excellent critical assessment of these cross-sectional studies. See also Pritchett (1996) for a detailed discussion and comparison of various measures used in empirical analyses of outward trade orientation in least developed countries. Clearly, the simple trade intensity index (exports plus imports over GDP), which is frequently used to measure a country's outward policy orientation in cross-country regressions, is unsatisfactory and inappropriate for testing the hypothesis on the link between trade openness and growth.

9. See Kaldor (1956) and Aghion, Caroli, and García-Peñalosa (1999) for a discussion of the savings effects and investment effects, respectively.

10. See Thorbecke (2006) for a critical review of the traditional approach to the inequality-growth link.

11. See Thorbecke and Charumilind (2002).

12. See also Aghion, Caroli, and García-Peñalosa (1999).

The rejection of the Kuznets hypothesis of the inverted-U-shaped relationship between growth and inequality by a number of empirical studies spurred the reexamination of the opposite causal flow in the link, that is, the growth-inequality link.[13] Many early development economists noted that economic growth, if left to market forces alone, tends to be accompanied by increased inequality. They considered growth to be inherently disequalizing.[14] According to the new political economy of development approach, growth patterns yielding more inequality in the income distribution would, in turn, engender lower future growth paths, resulting in less of a growth-induced poverty reduction, as figure 1 illustrates.

Thus, while growth may benefit the poor, the ultimate poverty-reduction effects will depend on how the growth pattern affects income distribution. Inequality is the filter between growth and poverty reduction.[15] If growth leads to a significant increase in income inequality, the poor may benefit only slightly or even be hurt by the globalization-induced economic growth. We argue specifically that the pattern of economic growth and development, rather than the growth rate per se, may have significant effects on a country's income distribution and poverty profile, since growth can be pro-poor, distribution neutral, or even poverty increasing at the limit.

The recent debate on the meaning of pro-poor growth is directly related to the complex triangular relationships among poverty, growth, and inequality. (The evolution of this interrelationship is analyzed in detail within the context of Latin America in the next section.) At one extreme is a weak definition of pro-poor growth, by which growth is only required to yield a positive reduction of poverty. A major increase in per capita gross domestic product (GDP) only has to reduce poverty by one person to satisfy this definition. Hence, any positive elasticity of poverty reduction with respect to growth would be considered pro-poor. Although this definition is widely used and has become part of the conventional wisdom, it has led the development community to propose an alternative definition requiring the poor to benefit more than proportionally from growth than the nonpoor (a strong definition). A corollary of this relative definition of pro-poor growth is that it will bring about a more equal (or

13. See Thorbecke and Charumilind (2002) for a comprehensive review of the new political economy literature on the subject.

14. For example, Myrdal (1957); Rosenstein-Rodan (1943); Hirschman (1958), as noted in Milanovic (2005).

15. See Naschold (2004) for empirical evidence showing that in least developed countries, the distribution effects are as important as the growth effects for poverty reduction, while growth effects are larger in other low-income and middle-income countries.

less unequal) distribution of income. In this sense, poverty reduction would require some combination of higher growth and a more pro-poor distribution of the gains from growth.[16] Hence what is relevant for poverty reduction is a distribution-corrected rate of growth.[17] We consider growth to be truly pro-poor if in addition to reducing poverty, it decreases inequality consistent with the strong definition of pro-poor growth. Economic growth can be considered genuinely pro-poor only if that growth is accompanied by a decline in inequality such that the poor benefit relatively more than the nonpoor.[18]

Direct Distribution Channels in the Globalization-Poverty Nexus

In this subsection, we briefly discuss a number of mechanisms through which changes in openness affect income growth for individual households. These channels may be largely responsible for explaining why many poor households have not benefited substantially from contemporary globalization. For example, according to the theoretical prediction embedded in the Stolper-Samuelson theorem, income inequality should decline in developing countries abundantly endowed with unskilled labor in response to an increased demand for unskilled labor, while unskilled labor in developed countries would lose out. However, the empirical evidence reveals that the ratio of the average wage rates between skilled and unskilled workers has been increasing in many developing countries. Several specific features associated with the current phase of globalization explain why such a theoretical prediction does not hold. We highlight below some of the critical channels through which globalization ultimately affects poverty.

TECHNOLOGY AND FACTOR MOBILITY. Since the bulk of technical change emanates from research and development (R&D) activities in developed countries, the nature of technical progress and new technology is heavily biased in favor of skilled and educated labor.[19] Technical change therefore tends to be labor saving and skill biased, while new technology is complementary to capital and skilled labor and is a substitute for unskilled labor. Consequently, technical change tends to increase inequalities in both developed and developing countries.

16. Woodward and Simms (2006) argue that global economic growth would not reduce poverty on account of the disproportionately adverse net impact of climate change and worsening income distribution on the poor.
17. Ravallion (2004b).
18. Kakwani and Pernia (2000).
19. Culpeper (2005).

Technological diffusion and access to new technology is neither universal nor spontaneous, and it has become increasingly skewed and asymmetrical. In particular, intensified privatization of research in biotechnology and pharmacology has adverse effects on the access of developing countries and the poor to new technology, as evident in the debate surrounding the trade-related intellectual property issues (TRIPs) in the World Trade Organization (WTO) negotiations. The widened productivity differences resulting from these asymmetries help explain cross-country wage and income inequality. The initial knowledge gap and unequal, skewed access to technology and knowledge have adverse implications for the world income distribution. This is critical because the current wave of globalization is characterized more by trade in knowledge and information than by trade in goods, which was the case with the earlier wave of globalization.[20]

The perverse factor movements hypothesis could provide another explanation. Capital and skilled labor do not migrate to poor countries, but rather circulate among developed countries. Skilled labor also tends to migrate from developing countries to developed countries, as the massive migration of African nurses and medical doctors to the United States and Europe testifies, while unskilled labor migration is strictly controlled. Unskilled workers from developing countries face increasing obstacles in their attempts to migrate to developed countries. Consequently, wage equalization does not take place through labor migration, as was the case in the previous globalization era.

The process of capital market liberalization brings about a propensity for capital flight to developed countries, particularly during periods of financial instability and crisis. Today's cross-border portfolio capital flows are also characterized by diversification finance rather than development finance.[21] Typical capital transactions increasingly take the form of asset swaps for risk hedging and shedding rather than the financing of productive investment in capital-scarce developing countries—contrary to what the standard textbook theories would predict. FDI has also been dominated by intra-industry FDI (that is, two-way flows of investment among developed countries), compared with FDI flowing mainly from developed countries to developing countries under the previous wave of globalization.[22]

20. Baldwin and Martin (1999).
21. Obstfeld and Taylor (2002).
22. Baldwin and Martin (1999).

The differentiated degree of cross-border factor mobility (skilled labor and capital versus unskilled labor and land) often affects the functional income distribution between labor and capital against the former. Some workers are losing out, as de facto labor mobility takes place through the increasingly free cross-border capital mobility and transnational corporations' ability to relocate production sites in response to changes in relative labor costs. In response, governments of developing countries are less likely to enact regulations to protect and enhance labor rights or protect local environments, for fear of driving away the transnational corporations.[23] The unwillingness or inability to tax international mobile financial capital, stemming from the process of tax competition and the fear of capital flight and asset mobility, has contributed greatly to the erosion of governments' capacity to raise revenues for redistributional purposes.[24] Furthermore, the poor and unskilled are the most adversely affected by asymmetries in market power and access to information, technology, and marketing, as well as the activities of transnational corporations and their dominance in commodity value chains.

VULNERABILITY, INFORMATION DIFFUSION, AND INSTITUTIONS. Globalization can hurt the poor disproportionally and thus increase their vulnerability, by heightening the fluctuations in income and expenditures caused by global shocks, such as the various financial crises that have hit Latin America and Asia in the last two decades.[25] While globalization can be a major engine for growth in the aggregate, it introduces or exacerbates other trends that affect people's well-being, such as the increasing flow of information about the living standards of others, both within and beyond country borders. This flow of information can result in changing points of reference and increased frustration with relative income differences, even among respondents whose own income is rising. Individuals in specific socioeconomic groups and professions increasingly compare their own individual welfare status with that of similar groups in other countries.

23. Basu (2003).

24. Tanzi (2001) discusses various effects of globalization on the tax system under so-called fiscal termites.

25. See Ligon (2006) for a discussion of the effects of risks and uncertainty associated with globalization on the poor. See also Diwan (2001) and Birdsall (2002, 2006) for a discussion of the adverse effects of financial crises, and Montalbano and others (2006) and Winters, McCulloch, and McKay (2004) for the effects of trade shocks on the poor. Kakwani, Côrtes Neri, and Son (2008) examine the effect of shocks associated with globalization on income distribution and poverty in Brazil (see below).

Institutions are another critical factor for determining how globalization affects the poor, since they mediate the various channels and mechanisms through which the globalization process influences poverty. Institutions act as a filter that intensifies or hinders the positive and negative pass-through between globalization and poverty, and they can help explain the diversity, heterogeneity, and nonlinearity of outcomes.[26] The impact of globalization on the poor is mediated by domestic political economy structures and institutions such as social polarization, oligarchic structures, and predatory regimes, which may bias, confiscate, or nullify the gains from globalization for particular groups. The positive effects of globalization on growth and poverty can be found when institutional conditions are characterized by such features as political participation, social cohesion, and management of social conflict arising directly from globalization effects and the availability of safety nets and social protection schemes. We explore the crucial role that institutions can play in amplifying the positive benefits and moderating some of the negative consequences of the forces of globalization on poor households within different specific Latin American settings in a later section.

Latin America's Socioeconomic Performance in the Present Globalization Era

Any attempt to rigorously estimate the impact of the globalization process on socioeconomic performance (and more specifically on poverty) faces the almost insurmountable obstacle of the lack of a plausible counterfactual scenario. To derive robust inferences, one would have to compare the performance under the present forces of globalization to an alternative scenario of no or limited globalization. Within limits, this could be done very approximately and roughly within a computable general equilibrium model for a given country or region of a country, but this task is clearly infeasible for a continent as large and diverse as Latin America.

Instead we use trade openness as reflected by the trade intensity ratio (exports plus imports divided by GDP) as a major manifestation and indicator of the strength of the globalization process. We then compare the extent to which changes in trade intensity are associated or interrelated with changes in growth rates, income distribution, and poverty in Latin America, as a whole, and in selected Latin American countries during six subperiods between 1980

26. See Sindzingre (2006).

and 2006. Any observed association, however, does not necessarily stem from the globalization process, given that it might be the net consequence of a whole series of factors, of which some could be independent of the forces of globalization.

The resulting general picture can usefully serve as a backdrop to the specific case studies discussed later in the paper. These are organized around the theme of institutions that can help strengthen the transmission of positive effects of globalization on the poor and moderate the vulnerability of the poor to shocks linked to the globalization process (such as trade liberalization taking the form of tariff reduction, labor market reforms and reduction in barriers to international migration, the granting of property rights and social protection schemes, and public programs to invest in the human and health capital of the poor). A few case studies undertaken as part of the WIDER research project were selected to illustrate how specific institutions and policies in the above areas affected the poor in different settings.

The Evolution of Trade Openness, GDP Growth, Income Inequality, and Poverty Incidence

The first step is to identify the globalization period under scrutiny. Three different waves of globalization can be identified over the course of the last century and a half. During the first wave, from 1870 to 1914, income convergence among the globalizing countries was driven primarily by migration. Sixty million people, including largely unskilled workers, migrated from Europe to North America and other parts of the new world in this period. The second wave spanned the period from approximately the end of the Second World War to the 1970s. It was based on the availability of cheap labor mainly in East and Southeast Asia to mass produce labor-intensive manufactured products (such as textiles and appliances). The current wave, which started in the 1980s, is characterized more by trade in knowledge and information than by trade in goods, as was the case with the preceding wave of globalization. Our focus is on the present globalization era between 1980 and 2006.

Globalization embraces such an overwhelming set of forces that for analytical purposes the concept has to be defined in a narrow, specific, and operationally useful way. Since an increase in trade intensity is a major manifestation of the globalization process and can be approximately measured, the trade intensity ratio (exports plus imports divided by GDP) has become the most used indicator of globalization in the literature. Although easy to compute, it is incomplete as it only reflects the impact of globalization on

trade. Other weaknesses include not being able to correct for the size of a country. Large countries such as China, India, and Brazil would be expected to have significantly lower trade intensity ratios (TIRs) than small countries such as Singapore, Nepal, and Uruguay. Also, it represents an outcome variable, not the actual trade liberalization policies that trigger the globalization process. As Goldberg and Pavcnik point out, an obvious shortcoming of this concept is that both imports and exports are determined simultaneously with other variables that are the focus of the empirical analysis (such as wages and, by extension, poverty), so interpreting the results is subject to simultaneity bias.[27] Tracing the path of causality under those conditions is a perilous adventure. We hold that the forces of globalization encourage a process of trade liberalization at the country level (particularly tariff reduction), which, in turn, leads to higher TIRs as the country becomes increasingly integrated in the world economy. Thus, in spite of its limitations, we use the trade intensity ratio as a major, but not exclusive, indicator of the strength of the globalization process in the subsequent analysis.

The comparative analysis below follows a number of sequential steps. In each of these steps, we compare the performance of the Latin American and Caribbean region with that of the other major developing regions (namely, sub-Saharan Africa, South Asia, East Asia, Eastern Europe and Central Asia, and the Middle East and North Africa) and with the performance of selected Latin American countries (specifically, Argentina, Bolivia, Brazil, Chile, Colombia, Mexico, and Peru) over six time periods from 1980 to 2006. First, we review the evolution of the TIRs and GDP per capita growth rates and check whether these two variables appear to be positively correlated. Second, we look at the relationships between TIRs and income inequality and between GDP growth and inequality, over time. Finally, we determine whether any pattern can be established between trade liberalization (TIRs) and the incidence of poverty, either directly or indirectly via the growth and inequality channels (see figure 1).

Table 1 summarizes the evolution of trade openness as reflected by TIRs in the major developing regions and selected Latin American countries between 1980 and 2006. It shows that East Asia succeeded in opening up trade earlier and much more intensively than other developing regions: its TIR jumped from 43 percent in 1985–89 to 60.1 percent in 1990–94 and 82.7 percent in 2005–06. Trade intensity started rising in the other developing regions only in 1995–99, with the TIR in the Latin American region

27. Goldberg and Pavcnik (2004).

TABLE 1. Trade Intensity Ratios: Selected Latin American Countries and Major Developing Regions, 1980–2006[a]

Region or country	*1980–84*	*1985–89*	*1990–94*	*1995–99*	*2000–04*	*2005–06*
Latin America and Caribbean	28.2	28.1	30.3	35.1	45.7	49.0
Argentina	13.9	16.4	15.8	21.9	29.9	44.1
Bolivia	50.7	44.0	48.2	49.3	50.0	72.1
Brazil	19.3	16.0	17.9	16.4	26.0	26.5
Chile	45.5	59.7	57.9	56.3	67.0	75.1
Colombia	26.5	29.9	35.1	35.8	41.9	45.7
Mexico	25.3	33.6	36.4	61.8	59.0	63.4
Peru	37.4	30.5	28.2	31.9	35.3	46.4
Sub-Saharan Africa	52.5	49.7	52.3	59.4	66.3	73.5
South Asia	18.5	17.3	22.7	27.5	32.8	45.5
East Asia	40.4	43.0	60.1	60.7	69.6	82.7
Eastern Europe and Central Asia	n.a.	n.a.	57.9	62.7	76.3	77.0
Middle East and North Africa	68.3	48.2	67.7	59.0	67.8	84.6[b]
World total	40.57	37.7	40.3	45.1	51.0	57.5[b]

Source: World Bank, *World Development Indicators,* 2008.
n.a. Not available.
a. The trade intensity ratio is measured as (exports plus imports) divided by GDP. It is calculated from current estimates in U.S. dollars.
b. Only 2005.

gradually climbing from 30.3 percent in 1990–94 to 49 percent in 2005–06. Within the set of Latin American countries in table 1, Chile, Mexico, and Colombia went through a continuous process of trade openness from 1980 on, which was relatively intensive in the case of the first two. In contrast, the relative importance of trade in GDP only started to rise in 1995–99 in Argentina and even later in Brazil, where the TIR stagnated between 16 percent and 19 percent in the four subperiods in the 1980s and 1990s before increasing to 26 percent in 2000–04. Bolivia and Peru only achieved higher trade intensity levels in the most recent subperiod.

The above trends are surprising for the possible disconnect between the timing of trade liberalization policies and the resulting increase in trade intensity. For example, in Brazil average nominal tariffs fell from 43 percent in 1987 to 14 percent in 1995, while effective rates of protection fell from 56 percent to 20 percent in the same period, with no impact on the TIR until 2000–04.[28] Likewise, trade liberalization and large-scale reduction in quantitative trade restrictions began in Argentina in 1990–91, but it took almost a

28. Ferreira, Leite, and Wai-Poi (2007).

TABLE 2. Growth of GDP per Capita: Selected Latin American Countries and Major Developing Regions, 1980–2006
Average annual percent

Region or country	*1980–84*	*1985–89*	*1990–94*	*1995–99*	*2000–04*	*2005–06*
Latin America and the Caribbean	–0.9	0.3	1.6	0.9	1.0	3.7
Argentina	–1.6	–2.8	5.3	1.0	–0.6	7.8
Bolivia	–4.0	–1.2	1.7	1.7	0.7	2.4
Brazil	–0.9	2.5	–0.4	0.5	1.6	1.9
Chile	–0.2	5.6	5.4	3.9	2.8	3.8
Colombia	0.3	2.3	2.4	–0.4	1.4	4.3
Mexico	1.0	–0.8	2.0	1.4	1.4	2.7
Peru	–1.8	–2.1	0.9	2.1	2.2	5.9
Sub-Saharan Africa	–1.3	–0.3	–2.0	0.7	1.5	3.2
South Asia	3.1	3.4	2.6	4.0	3.9	7.0
East Asia	5.8	6.3	7.9	5.7	7.1	8.4
Eastern Europe and Central Asia	n.a.	n.a.	–6.0	1.8	5.4	6.4
Middle East and North Africa	0.3	–1.6	1.6	2.3	1.9	3.0
World total	0.5	2.0	0.7	1.7	1.6	2.4

Source: World Bank, *World Development Indicators,* 2008.
n.a. Not available.

decade before these measures led to any significant increase in the relative magnitude of trade flows. It is likely that actors need time to respond to new policies and signals and that a confluence of other factors affects the link between policies and outcomes. The time lag between the latter two provides yet another illustration of the limitations of the TIR as an indicator of globalization.

Table 2 gives the growth of GDP per capita for the same set of regions and Latin American countries as table 1. The growth performance of the Latin American region was marginal at best: stagnation in the 1980s was followed by an annual growth rate of per capita income of only slightly above 1 percent between 1990 and 2004. It remains to be seen whether the quantum jump to 3.7 percent in 2005–06—caused largely by the price surge in primary products and commodities—is sustainable. The growth performance of the Latin American region was very substantially worse than that of all other developing regions except sub-Saharan Africa, which endured negative growth rates between 1980 and 1994. Within Latin America, by far the most successful country in terms of growth was Chile, which grew at annual rates between

2.8 and 5.6 percent starting in the mid-1980s. In contrast, Argentina, Bolivia, Brazil (first half), Mexico (second half), and Peru displayed negative growth in the 1980s. In the 1990s, Argentina, Bolivia, Mexico, and Peru performed relatively well, while Brazil essentially stagnated. A clear upsurge in growth rates occurred in the current decade in all Latin American countries listed in table 2, except for Argentina in 2000–04. In a number of instances, financial shocks and inconsistent, often populist economic policies have contributed in no small measures to the mixed socioeconomic performance described above.

The World Bank recently issued a major report on inequality in Latin America based on a sample of household surveys for twenty countries at three points during 1989–2001.[29] The report concludes that Latin America and the Caribbean is one of the most unequal regions in the world. Many Latin American countries display higher Gini coefficients of income inequality than most of Africa. The report indicates that inequality rose in most South American economies in the decade ending in 2001. Argentina experienced by far the biggest jump (7.7 Gini points between 1992 and 2001). Venezuela follows, with an increase of about 4.0 Gini points. The income distribution also worsened in Bolivia, Chile, Ecuador, Peru, Uruguay, and possibly Paraguay. Colombia's income distribution remained essentially the same, while Brazil is the only South American country that recorded a clear reduction in inequality in the 1990s.[30]

Table 3 provides estimates of poverty and inequality measures for a large set of individual Latin American countries for selected years in the 1990s and 2000s. The information is drawn from the most recent study by Ferreira and Ravallion on global poverty and inequality, and in a number of instances table 3 contains even more up-to-date estimates than the above World Bank report.[31] The table shows that income inequality rose in nine Latin American countries between the mid-1990s and the mid-2000s. Inequality fell in two countries (Brazil and Mexico) and remained essentially the same in four countries (a change of less than 2.5 percent from the initial Gini). The last decade reveals the beginning of a convergence trend with respect to inequality in Latin America: highly uneven countries (with Gini coefficients above 0.5) became more even and less uneven countries (with Gini coefficients below 0.5) became more uneven. A comparison of Gini ratios in the early 1990s and

29. De Ferranti and others (2004).
30. De Ferranti and others (2004).
31. Ferreira and Ravallion (2008); de Ferranti and others (2004).

TABLE 3. Inequality and Poverty Measures for Individual Latin American and Caribbean Countries, 1990s and 2000s

				International poverty line		*Inequality*	
Country	*GDP per capita*[a]	*Survey year*	*y/c*[b]	*Population below $1 a day (percent)*	*Population below $2 a day (percent)*	*Gini index*	*Mean logarithmic deviation*
Argentina	13,652.41	1996	*y*	1.10	9.80	0.486	0.429
		2003	*y*	6.60	17.40	0.513	0.510
Bolivia	2,579.16	n.a.	*y*	n.a.	n.a.	n.a.	n.a.
		2002	*y*	24.00	42.90	0.602	0.709
Brazil	7,825.78	1995	*y*	10.50	23.30	0.615	0.756
		2004	*y*	7.60	19.80	0.570	0.617
Chile	10,938.57	1994	*y*	0.90	10.80	0.552	0.548
		2003	*y*	0.50	5.60	0.549	0.539
Colombia	6,886.04	1995	*y*	3.10	16.30	0.572	0.611
		2003	*y*	7.60	19.40	0.588	0.669
Costa Rica	9,646.49	1996	*y*	3.60	13.30	0.471	0.419
		2003	*y*	1.80	9.60	0.498	0.459
Dominican Republic	7,617.82	1996	*y*	1.80	11.70	0.487	0.426
		2004	*y*	2.80	16.20	0.516	0.476
Ecuador	3,981.58	1994	*y*	16.80	37.40	0.520	0.511
		n.a.	*y*	n.a.	n.a.	n.a.	n.a.
El Salvador	4,775.52	1995	*y*	20.80	47.10	0.499	0.454
		2002	*y*	20.40	40.50	0.523	0.541
Guatemala	4,150.21	n.a.	*y*	n.a.	n.a.	n.a.	n.a.
		2002	*y*	13.90	32.60	0.553	0.581
Haiti	1,479.34	n.a.	*y*	n.a.	n.a.	n.a.	n.a.
		2001	*y*	52.90	77.60	0.600	0.675
Honduras	3,170.33	1994	*y*	23.70	48.20	0.552	0.573
		2003	*y*	14.10	36.00	0.539	0.523
Jamaica	3,907.43	1993	*c*	4.90	27.50	0.357	0.221
		2004	*c*	0.50	14.40	0.455	0.357
Mexico	9,967.30	1995	*c*	8.40	26.00	0.537	0.528
		2004	*c*	1.90	12.50	0.461	0.379
Nicaragua	3,538.94	1993	*c*	47.90	77.90	0.504	0.452
		n.a.	*c*	n.a.	n.a.	n.a.	n.a.
Panama	7,234.06	1995	*y*	7.40	17.40	0.571	0.645
		2003	*y*	6.00	16.80	0.561	0.603
Paraguay	4,368.11	1995	*y*	19.40	38.50	0.591	0.687
		2003	*y*	13.60	29.80	0.584	0.660
Peru	5,725.07	1994	*y*	9.40	31.60	0.449	0.350
		2003	*y*	10.50	30.60	0.520	0.489
St. Lucia	6,482.11	1995	*y*	25.20	59.60	0.426	0.316
		n.a.	*y*	n.a.	n.a.	n.a.	n.a.
Trinidad and Tobago	14,708.07	1992	*y*	5.10	23.20	0.403	0.288
		n.a.	*y*	n.a.	n.a.	n.a.	n.a.
Uruguay	9,897.78	1996	*y*	0.60	4.60	0.438	0.344
		2004	*y*	0.00	9.20	0.461	0.378
Venezuela	6,485.33	1995	*y*	9.40	28.80	0.468	0.402
		2003	*y*	18.70	40.20	0.482	0.461

Source: Ferreira and Ravallion (2008, table 1).

n.a. Not available.

a. GDP per capita is measured in constant 2000 PPP international dollars.

b. A denotation of *y* or *c* indicates whether the surveys and inequality measures are based on per capita income (*y*) or consumption (*c*).

TABLE 4. Global Comparisons of Poverty Trends: Major Developing Regions, 1981–2004

Poverty measure and region[a]	*1981*	*1987*	*1993*	*1996*	*1999*	*2002*	*2004*
Headcount ratio							
Sub-Saharan Africa	42.3	47.2	45.5	47.7	45.8	42.6	41.1
Latin America and the Caribbean	10.8	12.1	8.4	8.9	9.7	9.1	8.6
South Asia	49.6	45.1	36.9	36.1	34.9	33.6	30.8
East Asia	57.7	28.2	25.2	16.1	15.5	12.3	9.1
Eastern Europe and Central Asia	0.7	0.4	3.6	4.4	3.8	1.3	0.9
Middle East and North Africa	5.1	3.1	1.9	1.7	2.1	1.7	1.5
World total	40.1	28.7	25.6	22.7	22.1	20.1	18.1
Ratio: Sub-Saharan Africa/World	1.05	1.64	1.78	2.11	2.07	2.12	2.27
Number, in millions							
Sub-Saharan Africa	167.5	222.8	252.6	286.2	296.1	296.1	298.3
Latin America and the Caribbean	39.4	50.0	38.8	43.0	49.0	48.1	47.0
South Asia	455.2	471.1	436.7	452.9	463.4	469.6	446.2
East Asia	796.4	428.8	420.2	279.1	276.5	226.8	169.1
Eastern Europe and Central Asia	3.0	1.6	16.9	20.9	17.9	6.0	4.4
Middle East and North Africa	8.8	6.4	4.5	5.4	5.7	4.9	4.4
World total	1,470.3	1,180.7	1,170.17	1,087.8	1,108.6	1,051.5	969.5
Ratio: Sub-Saharan Africa/World	0.11	0.19	0.22	0.26	0.27	0.28	0.31

Source: Ferreira and Ravallion (2008, tables 2 and 4)

a. Income poverty measures are based on the international poverty line (US$1.08 a day, in 1993 PPP dollars)

early 2000s reveals that twelve out of the fifteen Latin American countries analyzed showed either no change or convergence.[32] For example, income distribution became more uneven in three countries with relatively low inequality (namely, Argentina, Uruguay, and Venezuela), while it improved in four economies with moderate to high inequality (Brazil, Colombia, Mexico, and Panama).

The incidence of poverty as measured by the headcount ratio (that is, the dollar-a-day poverty line) declined substantially worldwide, from 40 percent in 1981 to 18 percent in 2004 (see table 4). The headcount ratio fell in every developing region, even sub-Saharan Africa, but Latin America's performance in reducing poverty was still relatively poor. The poverty estimates oscillate around a level of 10 percent from one subperiod to another. While the headcount fell from a high of 12.1 percent in 1987 to a low of 8.4 percent in 1993, the latest estimate of 8.6 percent in 2004 reveals essentially no progress in combating poverty during this eleven-year period. Across Latin American countries, achievements in reducing poverty were decidedly mixed. Of the countries in table 3 for which at least two household surveys are available for

32. De Ferranti and others (2004, table A.6).

the period under consideration, poverty increased in four, fell in nine, and yielded ambiguous results in two (for example, in Peru poverty rose based on the dollar-a-day line and fell using the two-dollar line). In Argentina poverty rose sharply from 1.1 percent in 1996 to 6.6 percent in 2003, while Colombia saw an increase from 3.1 percent in 1995 to 7.6 percent in 2003. Conversely, the headcount ratio fell significantly from 10.5 percent in 1995 to 7.6 percent in 2004 in Brazil and from 8.4 percent to 1.9 percent in Mexico in the same period.

Interrelationship of Trade Openness, Growth, Income Distribution, and Poverty

In Latin America, no clear relationship stands out between the degree of trade openness of a given country (as measured by the TIR) and its GDP growth rate. However, the time trends discussed in the preceding subsection point to a few suggestive observations. First, there was a significant time lag between the initiation of trade liberalization policies and the subsequent increase in the relative magnitude of trade, as the cases of Argentina and Brazil indicate. Thus, whatever causal link might exist between trade openness and growth is likely to occur with a lag. This is not surprising given that the TIR is endogenous and is influenced not only by the trade liberalization process, but also by various other factors such as the domestic business cycle and exchange rates. Second, a comparison of the evolution of TIRs and per capita GDP growth rates for selected Latin American countries (tables 1 and 2) suggests that the direction of influence between trade openness and growth might well go in both directions. For example, Argentina grew extremely fast in 1990–94 when it liberalized trade (at 5.3 percent per capita GDP a year), but its TIR only rose in 1995–99. The evolution of GDP and TIRs in Argentina, Chile, and Colombia could provide some support for the hypothesis that trade liberalization contributes to growth with a lag while facilitating the implementation of a further round of liberalization.

Many economies in South and Central America have historically been linked to the global economy through primary commodity exports. Though the economies in the region are much more diversified in their production and trade structures than countries in Africa, they have been largely vulnerable to external shocks. Many countries in the region were exposed to the deterioration in their terms of trade caused by the sharp drop in prices of a number of primary commodities in the 1980s. In addition, as main recipients of commercial loans based on abundant petrodollars in the 1970s, middle-income countries in the region suffered from the sudden hike in real interest rates at

the end of the 1970s. The resulting severe debt crisis led to the so-called lost decade of economic growth in the 1980s, characterized by negative external resource transfer and low and often negative growth rates in per capita income.

After the belated market-based debt restructuring under the Brady Plan and the sweeping policy reforms of liberalization and deregulation, middle-income economies in the region reintegrated into the global economy as emerging market economies in the early 1990s. Nevertheless, the region's economic integration—spurred by the liberalization and privatization drive and based on the premise of large growth dividends from globalization—has not delivered the promised benefits of sustained economic growth. The average annual growth of per capita GDP was only slightly above 1 percent in the 1990s, as we discussed in the previous subsection. Sánchez succinctly summarizes the prevailing reflection on the region's economic performance over the last two decades of the twentieth century by noting that "Latin America has wholeheartedly embraced the faith in open trade and freer capital markets, and yet subsequent growth is well short of expectation."[33] On the whole, the globalization-induced economic growth in the region has been much more precarious and fragile than that recorded in Asia, at least until 2004.

In contrast to Asia, the Latin American region has experienced not only low growth, but also a low rate of formal job creation in the tradables sector under globalization. In some cases, economic growth was jobless, with a negative rate of formal job creation. Sáinz observes the sharp disparities in performance between large enterprises (often operated by transnational corporations) and small businesses in the region: large enterprises recorded high rates of productivity growth with a shrinking labor force, while the number of small, informal, less productive enterprises continues to grow.[34] Thus, labor markets in the Latin American region are characterized by a high degree of segmentation, together with an increasing casualization of the workforce.

As liberalization proceeds, firms operating in the formal sector are subject to increased international competition, and the informal sector has expanded by absorbing the negative income shocks that occur when workers in the formal sectors are laid off.[35] This process has given rise to the fear of social exclusion of the self-employed, who operate almost entirely in the informal sector. Popli notes that the self-employed now account for one-third of the labor force

33. Sánchez (2003, p. 1977).

34. Sáinz (2006).

35. See Kakwani, Côrtes Neri, and Son (2008) and Gindling and Terrell (2008) for detailed analyses of the effects of globalization, growth, and institutional changes on labor markets in Brazil and Honduras, respectively.

in the Mexican economy and are one of the most vulnerable groups.[36] This process of casualization of the workforce can help explain the reduction in open unemployment in Mexico and other Central American countries in the 1990s, while open unemployment was rising in Argentina, Brazil, Colombia, and other Latin American countries. The informal sector's share in urban employment rose significantly in most countries of the region.[37]

The descriptive statistics in tables 1–3 do not suggest any clear relationship between trade openness, on the one hand, and income distribution and poverty, on the other. Yet certain links can be observed. The most successful and continuous Latin American globalizer, Chile, managed to practically eradicate the incidence of dollar-a-day poverty without, however, being able to reduce its highly uneven income distribution (a Gini of 0.55 throughout the last decade, as table 3 shows). Two other globalizing nations, Brazil and Mexico, were able to reduce both poverty and income inequality significantly. In Argentina and Colombia, where trade intensity rose fairly substantially in 2000–04, poverty increased significantly and income distribution worsened considerably in the former.

Are there plausible explanations for the divergent relationships highlighted above? How did the various globalization transmission channels discussed earlier ultimately affect poverty, given the different initial conditions prevailing across Latin America? Can some of the apparent inconsistencies in the interrelationship between trade openness, growth, income distribution, and poverty be resolved? The remainder of this section explores these issues and proposes some initial conclusions.

Factors Influencing the Differential Impact of Globalization on Poverty

Poverty is influenced by many factors and variables, and the impact of globalization can only be separated from all the other factors to a very limited extent. In what follows, we return to the globalization transmission channels discussed earlier to determine how they operated in affecting poverty in Latin America. We analyze the effects on poverty of different initial conditions across Latin American countries, other manifestations of globalization than trade openness, and the individual growth pattern followed by different Latin American countries.

Ferreira and Ravallion derive three relevant stylized facts from their worldwide review of evidence: "(1) Economic growth tends to be distribution-

36. Popli (2008).
37. ECLAC (2004).

neutral on average in developing countries, in that inequality increases about as often as it decreases in growing economies; (2) measures of absolute poverty tend to fall with economic growth; and (3) the higher the initial level of inequality in a country or the greater the increase in inequality during the growth spell, the higher the rate of growth that is needed to achieve any given (proportionate) rate of poverty reduction."[38] While potentially the most powerful channel in alleviating poverty, the growth engine in most of Latin America sputtered at best and was much too weak, between 1980 and 2004, to have had any significant effect in pulling many households out of poverty (stylized fact 1 above). Moreover, the distribution of income and assets in the region is the most unequal in the developing world and, until the first half of the current decade, it continued to deteriorate in nine Latin American countries, improved in two countries, and remained essentially constant in four countries (see table 3). As the World Bank indicates, "For the majority of Latin American countries, the economic changes of the last half century have been mainly disequalizing."[39] Since the state of income distribution acts as a filter between growth and its poverty outcome, the combination of very low per capita GDP growth rates, high initial income inequality, and generally rising inequality in Latin America over the period translates into a marginal impact on poverty at best (stylized facts 2 and 3 above).[40]

The apparent tendency toward convergence among Latin American countries in terms of the evolving state of their income distributions does not alter the above statement, as it implies greater inequality in many countries even if compensated by less inequality in others. This bleak appraisal of the very limited capacity of the growth and income distribution channels (because of their inherent weakness) to affect poverty at the regional level raises the question of why the performance in terms of poverty reduction was actually so much better in a number of individual Latin American countries than one could have expected based on the aggregate growth and distributional picture. To answer this question, we need to explore how trade liberalization and some other manifestations of globalization affected the growth pattern differently in specific countries characterized by different initial conditions.

The trade literature typically explains the observed increasing income inequality in terms of a wage premium benefiting skilled versus unskilled

38. Ferreira and Ravallion (2008).

39. De Ferranti and others (2004).

40. Incidentally, "the distribution-neutrality of the growth process on average" identified by Ferreira and Ravallion (2008) in their first stylized fact above does not seem to hold for Latin America in the last three decades or so.

workers (or, alternatively, workers in the formal sector versus workers in the informal sector). The increased skill premium is driven by the increased demand for skilled workers, which, in turn, is linked to trade liberalization through an increase in the returns to particular occupations that are associated with a higher educational level, a shift in the production of skill-intensive intermediate goods from developed to developing countries, and skill-biased technological change and the transfer of capital- and skill-intensive technology accompanying FDI flows.[41] Prior to trade liberalization, most Latin American countries heavily protected sectors that use unskilled labor intensively. Under those circumstances, trade liberalization might cause unskilled wages to decline and wage inequality to increase. Argentina provides a good example of this process at work in the 1990s, during the second episode of trade liberalization: inequality increased 7.7 Gini points between 1992 and 2001.[42] In Brazil, effective protection prior to trade liberalization was higher in skill-intensive industries, such that both the wage and income distributions became significantly more even after the trade liberalization episode of 1988–95.[43] As a result of these differences in initial conditions, the poverty head count ratio rose markedly in Argentina and fell in Brazil.

Another characteristic of the Latin American income distribution is the increasing polarization at both ends of the distribution. It is likely that the macroeconomic adjustments brought about by the massive disruptions of global financial crises exacerbated this polarization. While some of these shocks were truly exogenous, at least some of them were self-inflicted and caused by unsound populist monetary policies. This high vulnerability to shocks has undoubtedly made the process of building institutions that could help resolve distributional conflicts more difficult.

Mexico and Brazil were able to achieve a major decrease in poverty between 1995 and 2004 despite unspectacular growth (the headcount ratio fell from 8.4 percent to 1.9 percent in Mexico and from 10.5 percent to 7.6 percent in Brazil). Through social protection schemes and investment in human capital and health such as Mexico's *Progresa* (now *Oportunidades*) and Brazil's *Bolsa Escola* and *Bolsa Familia,* rural poor households, in particular, benefited from a variety of public services and goods. These schemes were essential in reducing rural poverty, which is relatively much higher than urban poverty and only indirectly affected by trade liberalization (since the latter

41. Goldberg and Pavcnik (2004); Harrison and Hanson (1999).
42. See Galiani and Porto (2008).
43. Ferreira, Leite, and Wai-Poi (2007). This case study is discussed in more detail below.

normally reduces tariffs on industrial but not on agricultural goods). The 1990s witnessed noticeable surges in per capita social expenditures through public transfers and human capital formation in many countries.[44] Kakwani, Côrtes Neri, and Son undertake a rigorous empirical analysis of the relationship between growth patterns, poverty, and inequality in Brazil from 1995 to 2004; they provide important insight into the crucial role of incomes derived from social security and other government transfers in cushioning the effects of macroeconomic shocks, triggered by the forces of globalization, among the poorest segments of Brazilian society.[45] Skoufias, Lindert, and Shapiro examine the performance of various public transfer schemes in eight countries in the region.[46] They find convincing evidence that social protection and other public programs investing in the human and health capital of the poor have contributed substantially to reducing poverty in many Latin American countries.

Paradoxically, while the evidence is persuasive that income inequality is high and rising and contributing to perpetuating poverty in a number of Latin American countries, much of the development literature ignores the fact that income inequality and income-based poverty are not necessarily the only or even the best measures of economic and social well-being. Poverty and inequality are multidimensional concepts that can only be imperfectly reflected by money-metric measures. To further muddle the development performance picture, Sahn and Younger find that inequality measured in the health and education dimension fell in Latin America in the 1980s and 1990s, and this decline contributed to a substantial improvement in health and education indicators.[47] They point out that this progress is important evidence of socioeconomic development in Latin America—evidence that a narrow focus on money-metric measures alone would miss. Again, the public programs initiated in the 1980s and the more recent programs discussed above must have contributed significantly to the observed reduction in health and education inequality.

Trade liberalization could potentially lead to a process of labor reallocation, but relatively little reallocation has occurred in Latin America because of fragmentation and rigidities in most labor markets, with the exception of Brazil. Evidence suggests that declines in tariffs are associated with an

44. ECLAC (2004).
45. Kakwani, Côrtes Neri, and Son (2008). This case study is discussed below.
46. Skoufias, Lindert, and Shapiro (2008). This case study is discussed below.
47. Sahn and Younger (2006).

increased probability of informal work, which, in turn, could contribute to inequality.[48] The benefits of more flexible and better functioning labor markets on employment, efficiency, equity, and poverty alleviation could be significant. Likewise, reducing the barriers to international migration can contribute to improving the income distribution and even, in some instances, to alleviating poverty through the flow of remittances sent by the migrants to their families in their countries of origin.

The Role of Institutions: Findings from Case Studies

As described earlier, institutions can play a critical role in mediating the various channels and mechanisms through which globalization affects poverty. Institutions—defined broadly as including policies—can moderate some of the negative effects of globalization on the poor while strengthening and reinforcing some of the positive effects. We have selected eight case studies out of fourteen presented at a 2006 conference in Rio de Janeiro, which we organized under the auspices of the WIDER project.[49] These studies illustrate within different settings how institutions can contribute to rendering the process of globalization more pro-poor. These studies also demonstrate that the impact of globalization on poverty is extremely context specific, reflecting the heterogeneous and complex nature of the globalization-poverty nexus.

We have grouped the case studies into four broad and somewhat interrelated categories: (1) social protection schemes, public transfers, and interaction with labor income to induce a more pro-poor growth pattern; (2) trade liberalization and its effects on income distribution and poverty; (3) more efficient labor markets and migration opportunities; and (4) property rights.

Social Protection Schemes, Public Transfers, and Interaction with Labor Income

Kakwani, Côrtes Neri, and Son analyze the relationship between growth patterns, poverty, and inequality in Brazil during its globalization process, focusing on the role played by the labor market and social programs.[50] Their

48. Goldberg and Pavcnik (2004).

49. A few of the papers presented at the WIDER regional (Latin American) project conference on "The Impact of Globalization on the World's Poor," held in Rio de Janeiro on 23–24 September 2006, were commissioned. We selected the majority (about half a dozen) out of about one hundred submissions generated by a call for papers.

50. Kakwani, Côrtes Neri, and Son (2008).

paper makes two significant methodological contributions: they formulate a new measure of pro-poor growth, and they derive a decomposition methodology that explores linkages between growth patterns, labor market performance, and social policies. An individual's utility function is specified to depend on his or her income, as well as on the individual's sense of deprivation, captured by the number of people who are better off. The authors derive a growth equation consisting of the growth rate of mean income and the growth rate of inequality. The pattern of growth is defined as pro-poor if the former is greater than the latter.

Their decomposition methodology explains the growth of per capita income in terms of four components: the employment rate, hours of work in the labor market, the labor force participation rate, and productivity. Kakwani, Côrtes Neri, and Son also assess the contribution of different nonlabor income sources to growth patterns, with a focus on the expansion of targeted cash transfers and pro-poor social security benefits. The application of this methodology provides important insights into the role of public transfers and safety nets in Brazil over an extended period of negative per capita growth (1995–2004). While labor markets were quite adversely affected, incomes derived from social security and other government transfers played a crucial role in cushioning the effects of macroeconomic shocks (some of which were triggered by the forces of globalization), particularly among the poorest segments of Brazilian society. The lesson for other developing countries is that governments need to take a proactive and pro-poor stance in the face of negative income shocks at the macroeconomic level. The institutionalization of safety nets and transfers benefiting the poor can successfully mitigate periods of financial and economic crisis.

Globalization could adversely affect income inequality and poverty through skill-biased technical change, as well as increased international competition. Skoufias, Lindert, and Shapiro argue that in such cases, effective instruments to redistribute income to the poor through public transfers are critical for alleviating the negative effects of globalization on inequality.[51] The paper explores the redistributive effects of public transfers, in particular social insurance schemes and specially designed social assistance programs. Using household survey data, the authors analyze the simulated impact of fifty-six transfer schemes in eight Latin American countries (namely, Argentina, Brazil, Chile, Colombia, the Dominican Republic, Guatemala, Mexico, and Peru). Mitigating

51. Skoufias, Lindert, and Shapiro (2008).

the negative effects of globalization on inequality is particularly important in Latin America, where there is widespread dissatisfaction with the social injustice resulting from high poverty and inequality levels.

The findings of Skoufias, Lindert, and Shapiro suggest that social assistance programs are far more effective than social insurance schemes at redistributing income and contributing to social welfare, per unit of currency transferred. They also suggest that social assistance programs have a stronger impact on reducing inequality than social insurance schemes; that the impact of social insurance schemes on inequality is fairly small and in some cases negative (Guatemala, Peru), although they reduced inequality in Argentina, Brazil, and Chile; that the poverty impact of public transfers varies significantly across countries in Latin America; and that the relative success of conditional cash transfers in redistribution is driven by the need to clearly define the targeted poor.

The success achieved by Brazil (through its social security program and such schemes as *Bolsa Escola* and *Bolsa Familia*) and Mexico (through *Progresa* and other transfers) contributed significantly to the observed remarkable fall in the incidence of poverty in those countries. The relative share of income from social security income doubled from 10 percent in 1981 to 20 percent in 2004.[52] If the imputed value of the benefits received by the households from the two *Bolsa* schemes were added to their disposable incomes, the rise in the relative share would be even more pronounced. In addition, to the extent that these measures contribute to the health and human capital of poor households and, in particular, to that of their children, they will also accelerate the process of future growth and poverty reduction.

Trade Liberalization and Its Effects on Income Distribution and Poverty

We have already extensively discussed the process of trade liberalization and its impact on growth, distribution, and poverty. Here, we focus on a couple of specific case studies. Ferreira, Leite, and Wai-Poi explore the impact of trade liberalization (a key instrument in the spread of globalization) on wage inequality in Brazil.[53] Using a nationally representative sample of workers in all sectors of the economy, the authors quantify the effects of the 1988–95 trade liberalization episode on the Brazilian wage distribution. Their main finding is that trade reforms did contribute to the observed reduction in income inequality in the last decade through two main channels: trade-induced changes in

52. Ferreira, Leite, and Litchfield (2006).
53. Ferreira, Leite, and Wai-Poi (2008).

employment levels across sectors, industries, and formality categories; and changes in the economywide skill premium, which fell together with the returns to education. The combination of trade liberalization and social programs was instrumental in the observed substantial reduction in inequality and poverty in Brazil since the mid-1990s.

These findings are in conflict with much of the literature on trade liberalization in Latin America, which suggests that liberalization has contributed to an increase in inequality—or at least to widening the gap between skilled and unskilled wages. Ferreira, Leite, and Wai-Poi explain that Brazil was an exception to the Latin American pattern in that effective protection prior to trade liberalization was higher in skill-intensive industries, whereas most other Latin American countries protected low-skill sectors.[54] The lesson for policymakers would seem to be that in countries with stronger protection for skill-intensive industries, trade liberalization does not necessarily imply a mandatory trade-off between gains in efficiency and productivity, on the one hand, and increases in inequality or poverty, on the other. This raises the issue of whether countries that protected low-skill sectors could design the tariff reduction and harmonization process in such a way as to reduce some of the negative consequences for the unskilled and for income distribution in the short and medium terms.

Most of the existing empirical literature on the effect of trade liberalization on inequality in Mexico focuses on wage earners and shows a rise in income inequality on account of an increase in the relative demand for, and the relative returns to, skilled labor. The self-employed, however, account for one-third of the labor force and are one of the vulnerable groups in the economy, as they operate almost entirely in the informal sector. Popli examines the trend in income inequality and poverty among self-employed workers in Mexico from 1984 to 2002, when Mexico opened its economy to the global market through trade and investment liberalization.[55] Because liberalization exposes firms to increased competition, the formal sector has had to reduce wages and lay off workers to remain competitive, causing negative income shocks that have led to the expansion of the informal sector. This process has given rise to the fear of social exclusion of the self-employed.

Popli finds that inequality and poverty increased among the self-employed during the first decade following liberalization. In the second decade, however, inequality started to decrease as the economy stabilized and grew, but

54. Ferreira, Leite, and Wai-Poi (2007).
55. Popli (2008).

poverty kept increasing. To understand these changes in inequality and poverty in relation to self-employed workers, Popli decomposes the inequality and poverty indexes into within and between group effects, employing well-established decomposition methods. Her decomposition analysis reveals that raising relative returns to skilled labor contributed to increasing both inequality and poverty. As the supply of skilled labor rose, inequality started to fall. This is reflected in the narrowing of the gap between the mean incomes of skilled and unskilled self-employed workers. However, she argues that because the self-employed are largely unskilled, their relative lower returns meant a continued increase in poverty for that group. Popli further confirms that there are significant regional differences in the impact of liberalization effects within Mexico. The central and southern states, where the self-employed are concentrated, are lagging behind other regions in benefiting from the forces of globalization. Popli's analysis of the self-employed suggests that the large scale social protection schemes undertaken in Mexico must have acted as a buffer in moderating some of the negative effects of trade liberalization on the overall incidence of poverty.

More Efficient Labor Markets and Migration Opportunities

Aguayo-Tellez, Muendler, and Poole examine how factors relating to globalization affect an individual decision to migrate internally within Brazil, where only 66 percent of the labor force held a formal sector job in 1997 and where considerable economic disparities continue to prevail across regions.[56] The level of per capita GDP in the southern regions is more than triple that in the northern regions. The authors argue that while interstate migration has a long history in Brazil, an accelerated rise in foreign direct investment and export activities, following dramatic market-oriented policy reforms aimed at increasing integration into the global economy, has contributed to a spurt in internal migration of formal sector workers. This migration spurt occurred within the southern states, which were already endowed with a high concentration of well-established firms, and from the southern and southeastern states to the northeastern state, where many foreign-owned and exporting firms have located their operations.

Aguayo-Tellez, Muendler, and Poole test the hypothesis that globalization directly affects formal sector workers' mobility and migration, using a uniquely matched data set of workers and their employers across all states of

56. Aguayo-Tellez, Muendler, and Poole (2008).

Brazil for 1997–2001. Their analysis shows that prospective employment at a foreign-owned firm exerts a positive and significant pull effect on formal sector internal migration flows. They find that rather than responding to spot wage differentials, workers' decision to migrate is likely to be made on the expectation of a steeper wage path, human capital accumulation, or other forms of nonpecuniary compensation at a destination firm, the majority of which is foreign owned. They conclude that globalization acts on internal migration through the growth of foreign-owned firms and employment opportunities as a pull factor. These migratory flows may also have contributed to the process of income convergence between the rural and urban areas of the country, which Ferreira, Leite, and Litchfield cite as an important contributing factor to the fall in income inequality in Brazil in the last decade.[57]

De la Fuente examines the effects of globalization on the poor through one of the manifestations of migration, namely, international remittances.[58] The paper focuses on Mexico, where the flow of remittances from largely U.S.-based migrants has become the dominant source of foreign exchange revenues. The author tests a popular claim that international remittances could become a massive resource transfer mechanism for reducing poverty levels by increasing the incomes of poor households. He formulates and computes a vulnerability to poverty (VTP) index to examine whether the people who are most vulnerable to shocks and to falling into poverty would be likely to receive remittance transfers. This index is a forward-looking measure of the magnitude of the threat of future poverty facing a household, computed from a household panel data set extending from October 1998 to November 2000. The author uses the VTP index as an explanatory variable, along with other characteristics (including household sociodemographic characteristics and the idiosyncratic and covariant risks that households face), in a series of probit and tobit models of remittance transfers.

De la Fuente's analysis suggests that the national and transnational support available to the rural poor through remittances is surprisingly low and that transfers are not going to the poorest members of rural communities in Mexico. His econometric estimation results further reveal that an increase in the threat of future poverty for rural families (that is, a higher VTP) actually reduces their likelihood of receiving transfers, including foreign remittances. On the basis of these results, the author concludes that although remittances are increasingly perceived as one of the main positive effects of globalization

57. Ferreira, Leite, and Litchfield (2006).
58. De la Fuente (2008).

on the rural poor, facilitating foreign remittances for rural recipients should not be considered a safety net against poverty or a substitute for the introduction of publicly funded schemes of social protection and improvements in economic opportunities for the rural poor.

Macours and Vakis explore the impact of seasonal migration on early childhood development in a poor, shock-prone border region of rural Nicaragua.[59] The authors show that seasonal migration can play an important role in protecting early cognitive development of preschool children in poor areas who suffer from severe malnutrition problems. Paradoxically and somewhat counterintuitively, they find strong evidence that mothers' migration has a positive effect on early childhood development, while fathers' migration does not. At least two factors account for this unexpected result. First, seasonal migrant mothers tend to bring more migration income home than migrant fathers, resulting in a direct income effect for the family. Second, the women's migrant earnings may generate an indirect empowerment effect that gives women more influence on how the money is spent, and women tend to allocate a larger share of their budget to nutrition and child care than men. The income and empowerment gains of migrating mothers appear to more than offset the potential negative effects on early child development of the mothers' temporary absence (most children of migrant mothers were left in the care of their grandmothers). The evidence illustrates how one aspect of globalization—namely, increased opportunities for seasonal migration resulting from higher south-south mobility—might positively influence early childhood development and thus reduce poverty in the long run.

The lesson from these studies is that freeing the movement of people within and across regional borders can help create flexible regional labor markets that allow the increasing production of goods for which the region has a comparative advantage. In this sense, globalization could contribute to both efficiency and poverty reduction. At the same time, the study by de la Fuente highlights the dangers of governments' relying exclusively on market forces and assuming a purely passive approach to the forces of globalization. Countries have to implement complementary national policies to improve the functioning of human capital markets and develop competitive technological capabilities.

59. Macours and Vakis (2008).

Property Rights, Exports, and Poverty Reduction

Globalization manifests itself through a variety of channels. Field and Field explore how trade liberalization and other reforms aimed at reducing market distortions have affected agricultural production in rural Peru.[60] The opening up of the economy after 1994 altered the relative prices between traditional agricultural crops and crops produced primarily for export, in favor of the export crops. The econometric results confirm that changes in these relative prices increased the likelihood that households would shift production toward these new export products. These tendencies appear to be strengthened if the farm household obtained title to its property over the period. A lesson to be drawn from this result is that weak property and titling institutions may inhibit the degree to which households can reap the benefits of globalization.

The authors also find that households that began producing an export-oriented crop over the period under consideration were much less likely to be poor at the end of the sample period (2004) than families who were unable to alter production because of location, access to credit, or lack of title to the property. Households that continued to produce traditional crops were caught in a poverty trap. These results illustrate that a passive approach to globalization cannot ensure that poverty will be reduced. The liberalization of markets must be accompanied by appropriate social programs and institutional reforms that address the specific nature of the problems and constraints faced by those socioeconomic groups suffering from poverty.

Conclusions

The case studies reviewed in the preceding section help clarify how certain critical institutions and policies can make the process of globalization more responsive to the welfare of the poor in Latin America. The first and foremost conclusion is that the impact of globalization on poverty depends crucially on the specific context and environment under investigation. Given this qualification and the fact that relatively few generalizations are robust across different socioeconomic settings, we can proceed to explore how the various

60. Field and Field (2007).

globalization transmission channels described earlier in the paper appear to have influenced poverty in Latin America.

Potentially the most important channel is growth. High rates of economic growth, such as those experienced in East Asia in the 1970s and 1980s and in China and India today, translate into significant declines in the incidence of poverty even when the growth process is dampened by increasing income inequality.[61] In contrast, the growth engine in Latin America since the 1980s has been very weak until the last four years. The growth engine clearly sputtered and could not contribute to any significant reduction of poverty. To make matters worse, the growth pattern for most countries in the region was associated with a rise in the degree of income inequality. Between the mid-1990s and mid-2000s, inequality rose in nine Latin American, while it fell in only two countries and remained essentially the same in four countries.[62] The lethal combination of low growth and increased income inequality resulted in very little progress in the reduction of poverty in the region. The headcount ratio (based on a dollar-a-day poverty line) remained essentially the same in 2004 as in 1993, at around 8.5 percent. The aggregate statistics hide the good performance of some individual countries. The best performer by far in terms of growth and poverty alleviation throughout the 1980–2006 period was Chile, where dollar-a-day poverty has been practically eradicated. Brazil and Mexico, in turn, have succeeded in reducing both inequality and poverty very substantially since the mid-1990s despite unspectacular growth.

No clear relationship could be established between the degree of trade intensity (as a proxy for globalization) and growth at the country level. The analysis of the descriptive statistics, however, yielded two hypotheses (which should be further tested): first, there is a significant time lag between the initiation of the trade liberalization process and a subsequent increase in trade intensity; and, second, the direction of influence between trade openness and growth might well go in both directions. The link between trade openness and inequality is explained in the trade literature in terms of a wage premium benefiting skilled workers relative to unskilled workers when the initial conditions before liberalization tend to protect low-skill sectors more heavily than skill-intensive sectors. This situation was characteristic of much of Latin America at the outset of the trade liberalization process, with some exceptions such as Brazil.

61. The positive effects of high growth on poverty reduction in China and India are presently significantly greater than the negative effects resulting from rising inequality.

62. Ferreira and Ravallion (2008).

The case studies reviewed in this paper illustrate how certain types of institutions can help mediate the effects of globalization on the poor. Two case studies focus on the key role that institutions and the policy framework can play in reducing the vulnerability of the poor to a variety of shocks triggered by the forces of globalization. Kakwani, Côrtes Neri, and Son argue that in Brazil in the post-1995 decade, during which labor markets were negatively affected, income derived from social security and other government transfers played a crucial role in cushioning the effects of macroeconomic shocks.[63] Skoufias, Lindert, and Shapiro provide evidence of the effectiveness of social assistance programs throughout Latin America, particularly when they are clearly targeted to the poor.[64] Social protection schemes (such as *Progresa* in Mexico and the *Bolsas* in Brazil) were very probably instrumental in contributing to the substantial reduction in poverty in these two countries.

Ferreira, Leite, and Wai-Poi show that trade liberalization can be a potent instrument to raise growth (efficiency) and reduce inequality simultaneously under the right set of initial conditions—as prevailed, for example, in Brazil in the 1980s, where effective protection prior to trade liberalization was higher in skill-intensive industries.[65] Under different initial conditions, however, trade liberalization can hurt certain socioeconomic groups. This is what Popli found in her study of how globalization affected self-employed workers in Mexico.[66] Increased competition from abroad caused firms to lay off workers, many of whom ended up in the informal sector. As the supply of largely unskilled self-employed workers rose, they received relatively lower returns, which translated into rising poverty.

Internal and international migration, induced by flexible labor markets, is yet another channel through which globalization can affect poverty. Aguayo-Tellez, Muendler, and Poole build a strong case that globalization in Brazil has had a major impact on the internal migration of formal sector workers. Large-scale migration to the poorer northern regions has probably contributed to reducing both inequality and poverty by creating new job opportunities.[67] Macours and Vakis show that seasonal migration by mothers who leave their children behind (usually with the children's grandparents) can play

63. Kakwani, Côrtes Neri, and Son (2008).
64. Skoufias, Lindert, and Shapiro (2008).
65. Ferreira, Leite, and Wai-Poi (2008).
66. Popli (2008).
67. Aguayo-Tellez, Muendler, and Poole (2008).

an important role in protecting the early cognitive development of preschool children in poor areas suffering from severe malnutrition problems.[68] De la Fuente argues, however, that remittances from abroad are not the panacea claimed by some investigators.[69] While undoubtedly contributing to the observed fall in inequality in Mexico in the last decade, the flow of remittances should not be considered a safety net against poverty or a substitute for social protection schemes and public programs that contribute to the educational and health capital of the poor.

The final study by Field and Field shows convincingly that while trade liberalization in Peru shifted relative prices toward exportable goods, weak property rights inhibited the extent to which relatively poor farmers could take advantage of those incentives.[70] This is a good example of the key role that property rights as an institution (in this instance, transparent and legally binding titling) can play in amplifying the potential positive effects of globalization on poverty reduction.

68. Macours and Vakis (2008).
69. De la Fuente (2008).
70. Field and Field (2008).