Econ 133 – Global Inequality and Growth

Global inequality and factor mobility

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What we've learned so far:

- The world as a whole is very unequal
- Global individual income inequality has been roughly stable over the last two decades
- A key dimension of global inequality is the inequality in average income across countries

Roadmap

This lecture: how factor mobility affects world inequality

- Labor mobility (= migration)

- Capital mobility (= cross-border investments)

Impact on inequality across countries? Inequality within countries?

1 Global inequality and migration

- Strong restrictions on migration: major departure from equal rights ideal in today's global society

- Two effects of immigration:

  – In source countries

  – In destination countries

1.1 The effect of immigration in destination countries

- In 2015 migrants made up 15% of US population

- Yearly net immigration flow into the US $\approx$ 1 million

- About a third of new arrivals are undocumented immigrants from Mexico and Central America with low education

- Card (2009) analyzes the effect on US inequality

- Empirical strategy: comparison of major US cities

- Los Angeles has 48% immigrants vs. Detroit: 11%.

- How does the wage of native workers compare?

- Key finding: net impact of immigrant inflows on mean wages of native workers is small

Two key reasons for low impact of immigration on wages of natives:

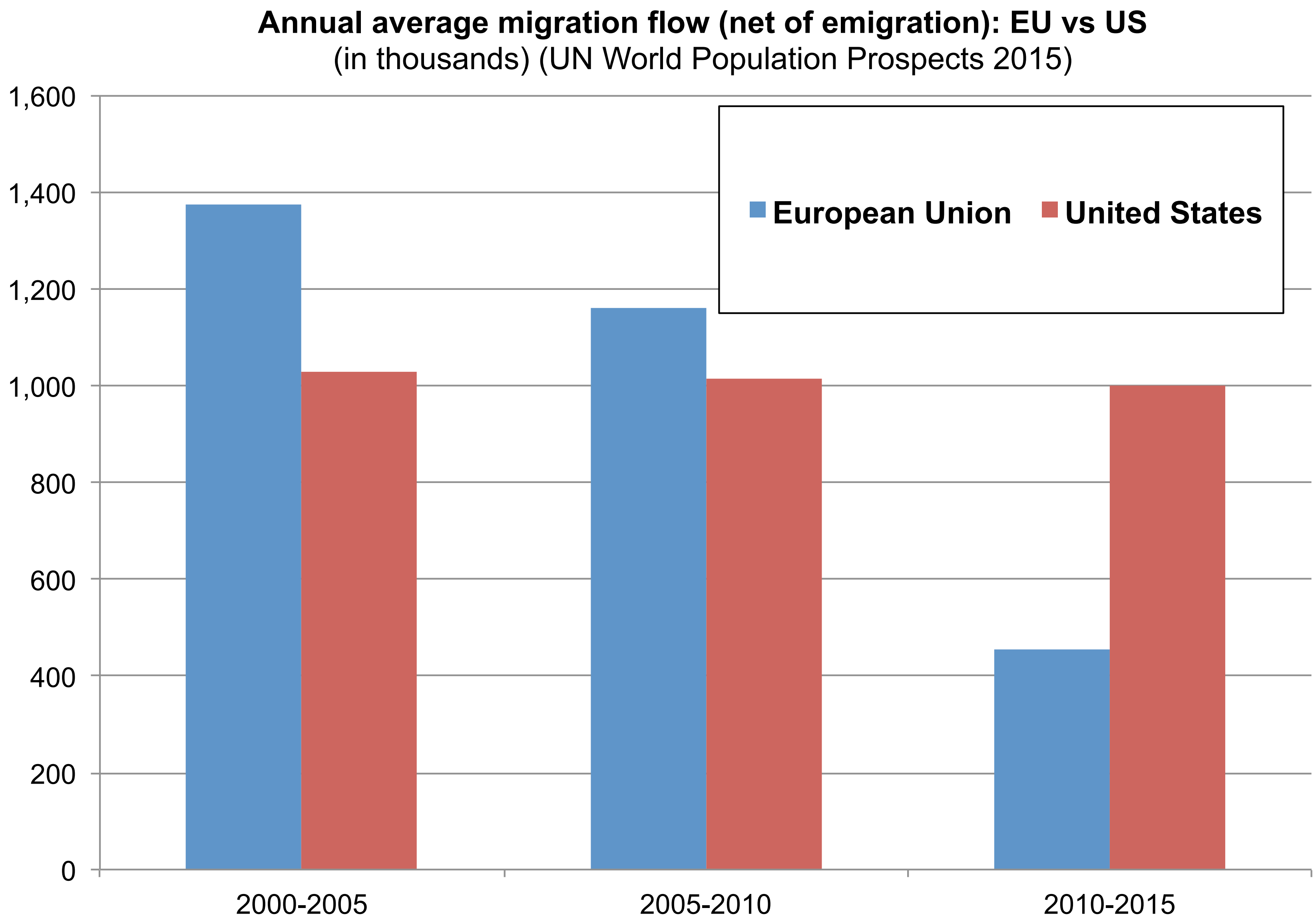
- High school dropouts are perfect substitutes for workers with high school education

  $\rightarrow$ impact of low-skilled immigration diffused across wide segment of labor market

- By educ. groups, immigrant & natives are imperfect substitutes

  $\rightarrow$ Effects of additional immigrant concentrated among immigrants themselves

- Immigration could increase inequality nonetheless:
  - Immigrants concentrated in the tails of the skill distribution
  - Higher inequality among immigrants than natives
- But quantitatively, effect of immigration on US inequality is small:
  - Card: accounts for 5% of 1980-2000 $\nearrow$ in US wage inequality
  - Before 2008 crisis, immigration was higher in EU than in US


Annual average migration flow (net of emigration): EU vs US
(in thousands) (UN World Population Prospects 2015)
1,600
1,400
1,200
1,000
800
600
400
200
0
European Union
United States
2000-2005
2005-2010
2010-2015

1.2 The effect of emigration in source countries

Effect of emigration in developing countries is ambiguous:

- Makes low-skill workers more relatively abundant $\rightarrow$ negative impact on wages of the poorest

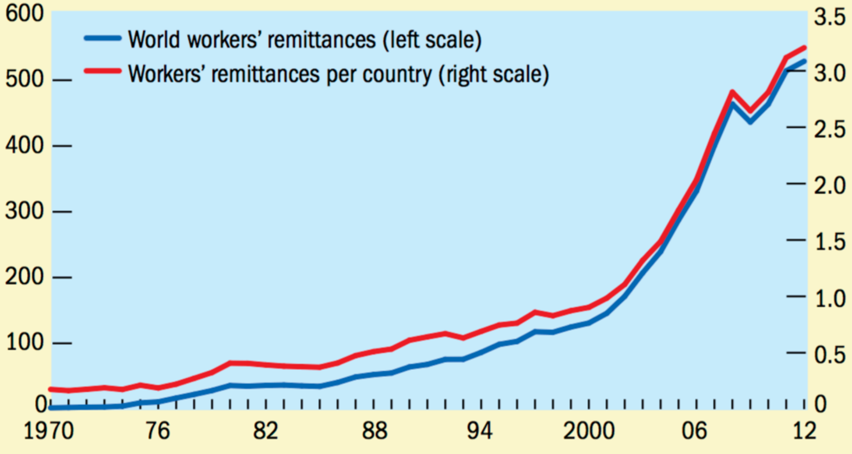
- But remittances from highly-skilled emigrants can be an important source of income for developing countries and contribute to the accumulation of human capital locally

Chart 1

Funds from abroad

Remittances have grown over the four past decades, increasing sharply from 2002 to 2008.

(billions of dollars)



Source: World Bank, 2013.

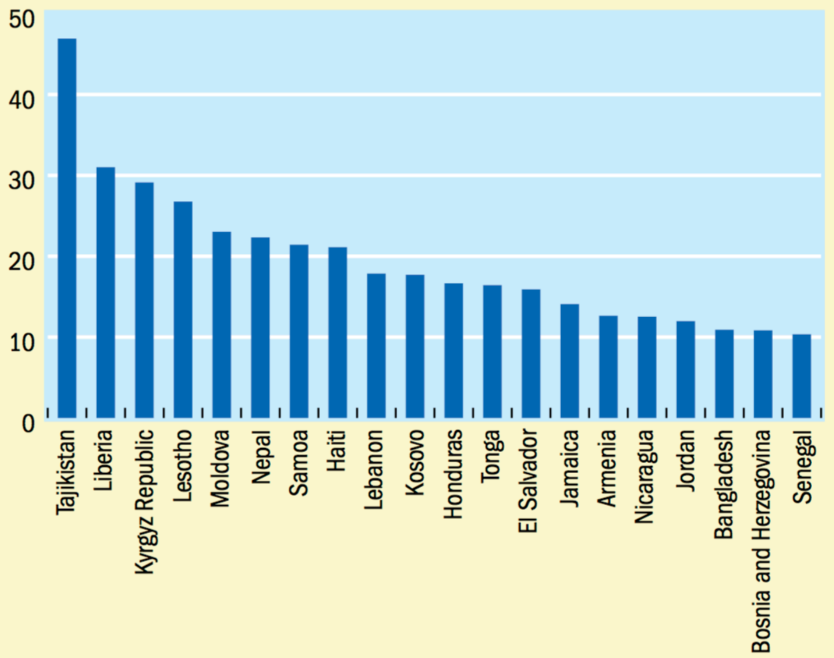
Note: World workers' remittances adds up workers' remittances across all countries for which data are available for the year specified. Per country figures divide this amount by the number of countries reporting data in that year. Most of the growth in remittances in this period was due to increased migration, but some is due to an increase in easier-to-measure transmission of remittances through formal channels such as banks.

Chart 2

Remittance dependent

For a number of countries, remittances account for 15 percent or more of GDP.

(remittances, percent of GDP)



Source: World Bank, 2013.

2 Global inequality and capital mobility

- Global capital mobility has increased much more than global labor mobility

- Actively promoted by policy makers, IMF, etc.

- One way to quantify capital mobility: $\frac{FA_t + FL_t}{GDP_t}$

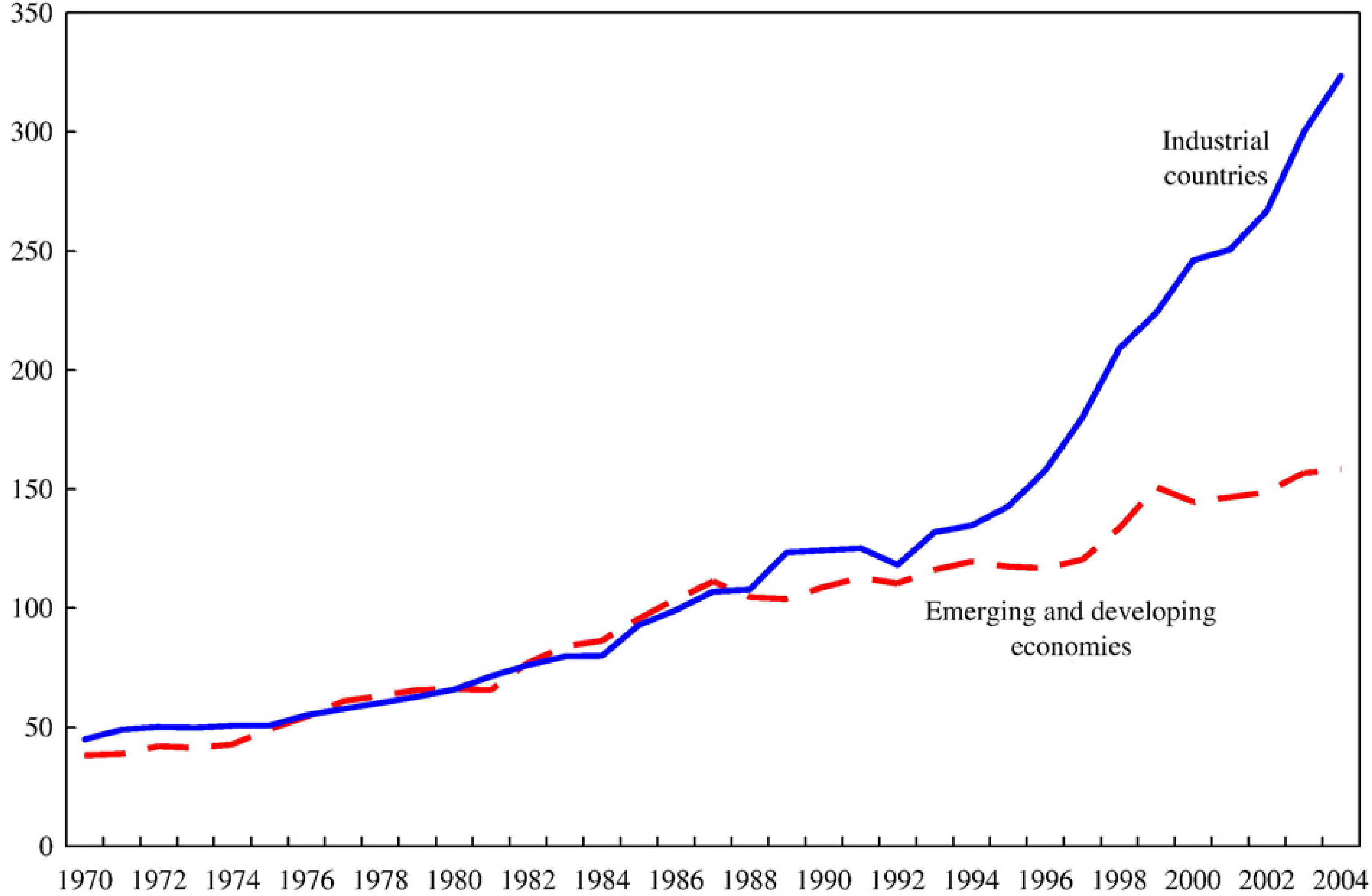


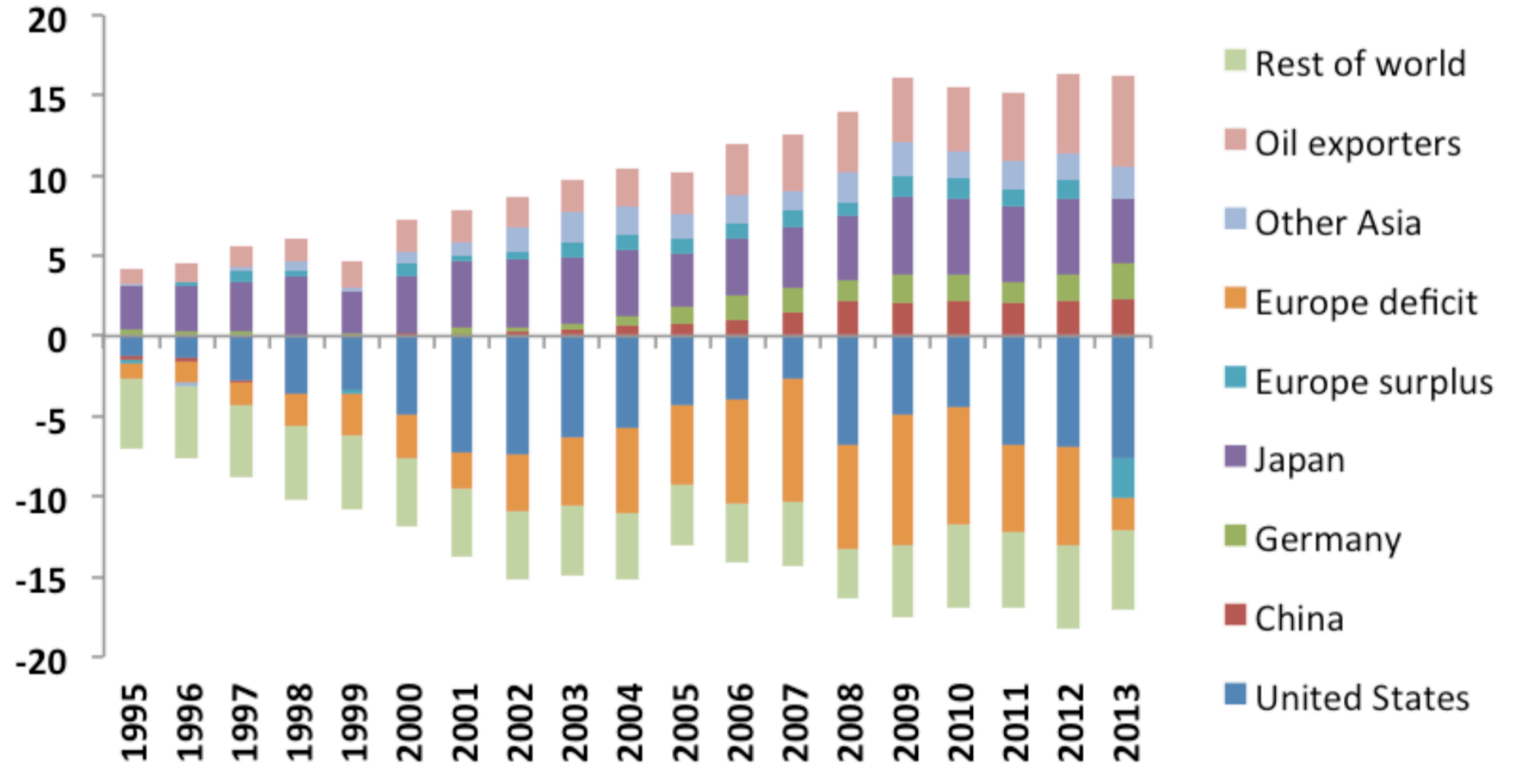
Fig. 3. International financial integration, 1970–2004. Note: Ratio of sum of foreign assets and liabilities to GDP, 1970–2004.

Economic logic and evidence does not suggest big positive impact of capital mobility on average income of poor countries:

- Theory: gain from switching from financial autarky to perfect capital mobility equivalent to a 1% increase in domestic consumption for non-OECD country (Gourinchas and Jeanne 2006)

- History: most growth success stories financed by domestic, not foreign, investment

- Developing countries receive relatively foreign capital on net



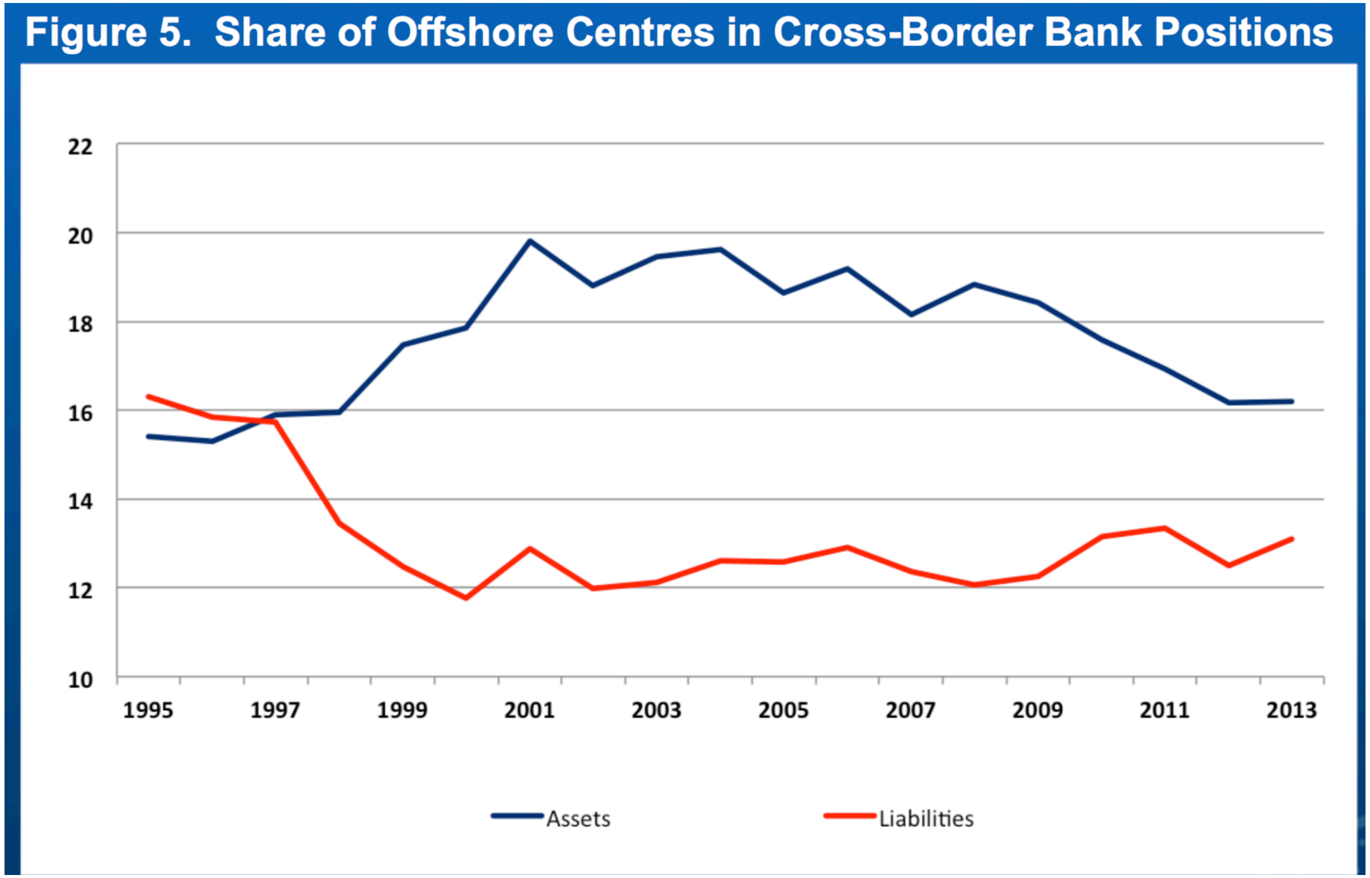
Net foreign asset positions / world GDP. Source: IMF World Economic Outlook

Capital mobility may exacerbate inequality within countries:

- Makes it easier for wealthy taxpayers to avoid / evade taxes

- High return investments may mostly benefit the wealthy $\rightarrow$ increases wealth inequality

- Financial fragility in recipient countries



Source: Bank for International Settlements

3 Summary

- There is a high degree of international capital mobility, much less labor mobility

- International migration reduces inequality across countries and has ambiguous effects on inequality within countries

- Capital mobility has small effects on inequality across countries and is likely to increase inequality within countries

References

Card, David, "Immigration and Inequality", *American Economic Review*, 2009 (web)

Gourinchas, Pierre-Olivier and Olivier Jeann, "The elusive gains from international financial integration", *Review of Economic Studies*, 2007 (web)

Lane, Philip and Gian Maria Milesi-Ferretti, "The external wealth of nations mark II: Revised and extended estimates of foreign assets and liabilities, 1970?2004", *Journal of International Economics*, 2007 (web)