Econ 133 – Global Inequality and Growth

Global inequality and trade

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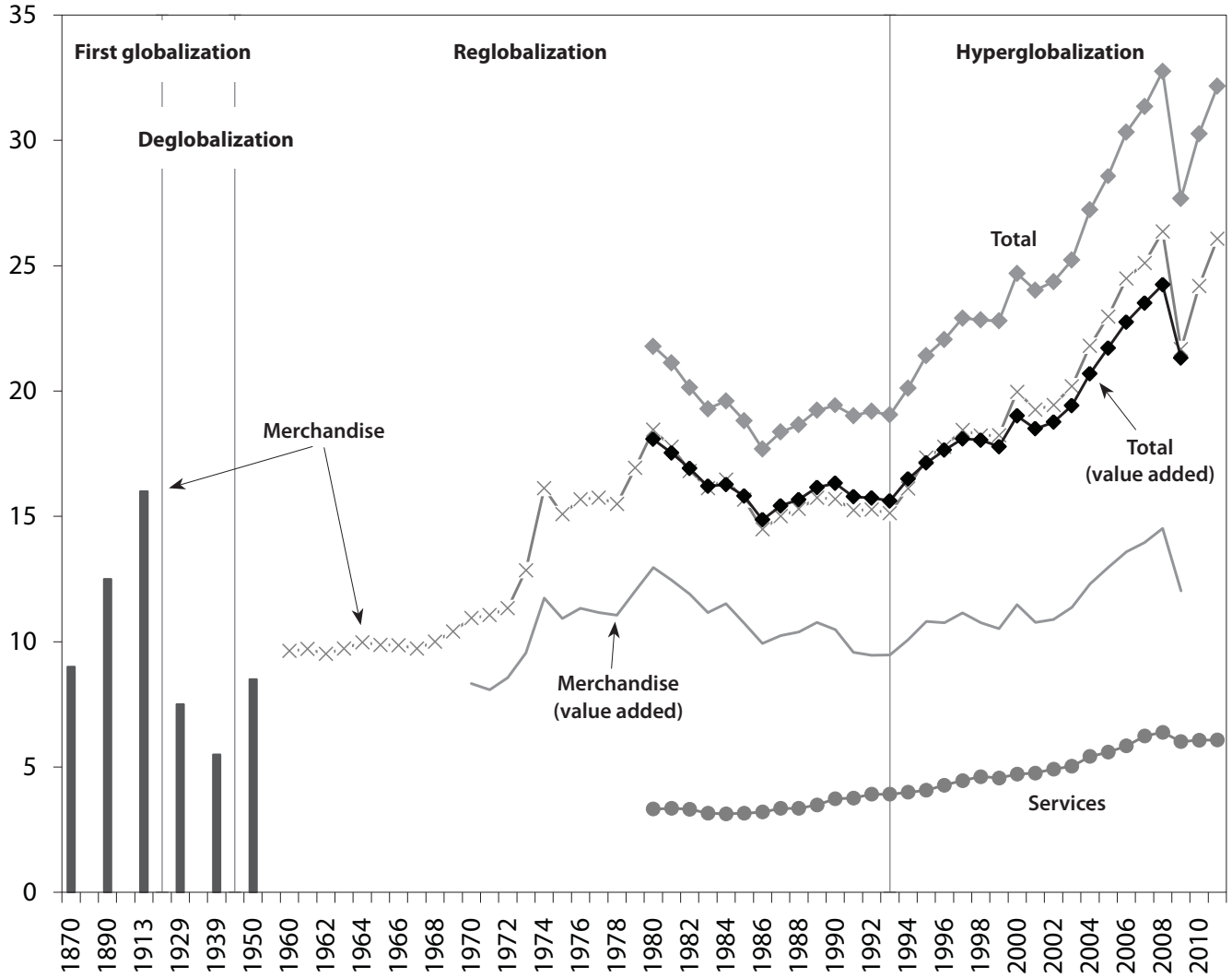
Roadmap

- Does trade help poor countries growth?
- How does trade affect inequality in the US?
- The economic effect of trade agreements: patent regulations and Investor-State Dispute Settlement (ISDS)

Figure 2.1 World exports, in current dollars, 1870–2011



Sources: Authors, based on Klasing and Milionis (2012) for historical estimates (1870–50), World Trade Organization for 1951–2011, and Johnson and Noguera (2012) for value-added exports estimates.

1 Trade and growth

Trade is a powerful force of convergence in average income across countries in the long run

- Channels: diffusion of knowledge and know-how
- Raises efficiency and productivity
- Important when country far beyond technological frontier and initially closed; less so for already open or frontier economies

Empirical evidence on effect of trade on growth:

- Challenge: hard to establish causality
- Best evidence: Frankel and Romer (1999)
- Use geographic characteristics as instrument for trade
- "Trade has a quantitatively large and robust positive effect on income"

2 Trade and within country income inequality

- Is rising trade responsible for rise of the skill premium in the US?
- Most of North-South is between relatively skill-endowed economies and relatively skill-scare economies
- Developing countries mostly export unskilled-intensive products; developed countries mostly export skill-intensive products
- So opening to trade analogous to rich countries exporting skilled

workers & developing countries exporting low-skilled workers

$\rightarrow$ increase in the supply of low-skilled workers in the North $\rightarrow$ rise of the skill premium

- Too small to matter?

Autor et al. 2014: large effect of exposure to international trade on employment and earnings of US workers

- Look at industry shocks to import competition stemming from China's spectacular rise as a manufacturing exporter
- Follow individuals who in 1991 worked in manufacturing industries that experienced high subsequent import growth
- Results: they have lower cumulative earnings, face elevated risk of obtaining public disability benefits, spend less time working for

their initial employers

- Earnings losses are larger for individuals with low initial wages, low initial tenure, and low attachment to the labor force

- Low-wage workers churn primarily among manufacturing sectors, where they are repeatedly exposed to subsequent trade shocks.

- High-wage workers are better able to move across employers with small earnings losses & are more likely to move out of manuf.

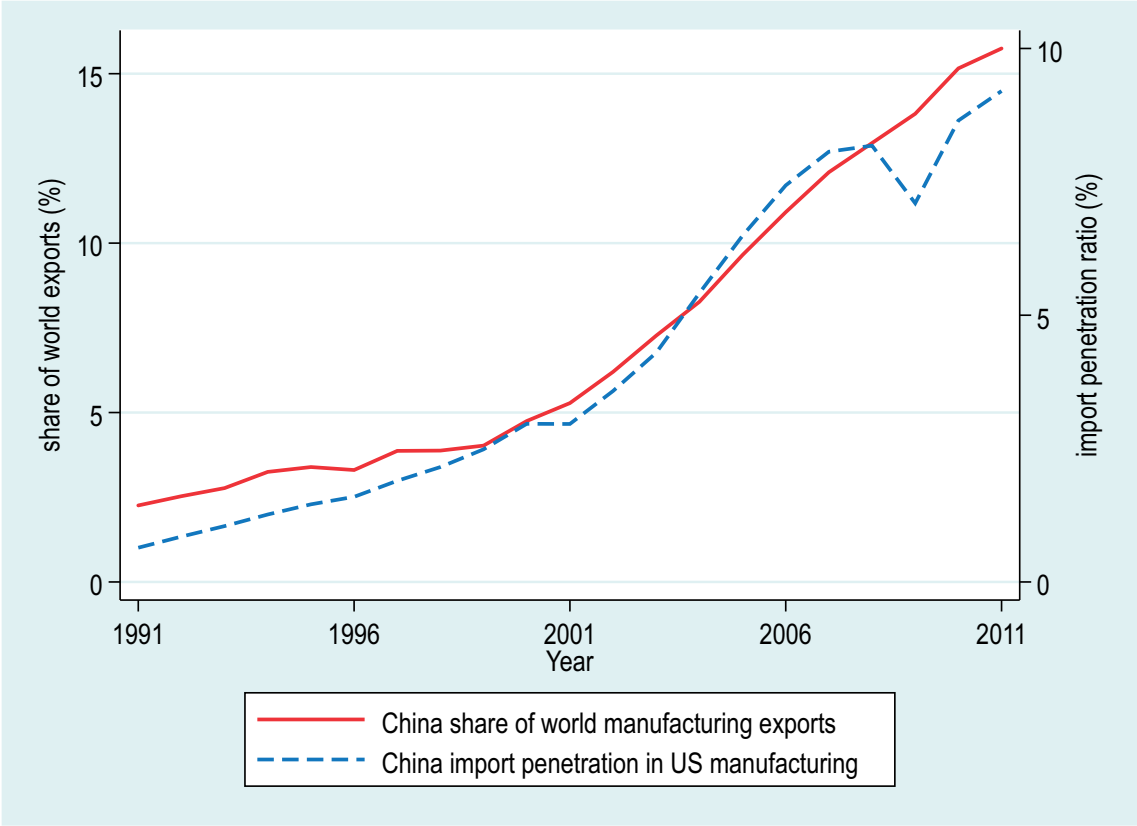


FIGURE I

China Share of World Manufacturing Exports and China Import Penetration in U.S. Manufacturing, 1991–2011

The China share of world manufacturing exports is the ratio of China's total manufacturing exports to world total manufacturing exports as reported in World Development Indicators (http://data.worldbank.org/). The China import penetration ratio is U.S. manufacturing imports from China divided by U.S. domestic absorption in manufacturing (shipments plus imports minus exports).

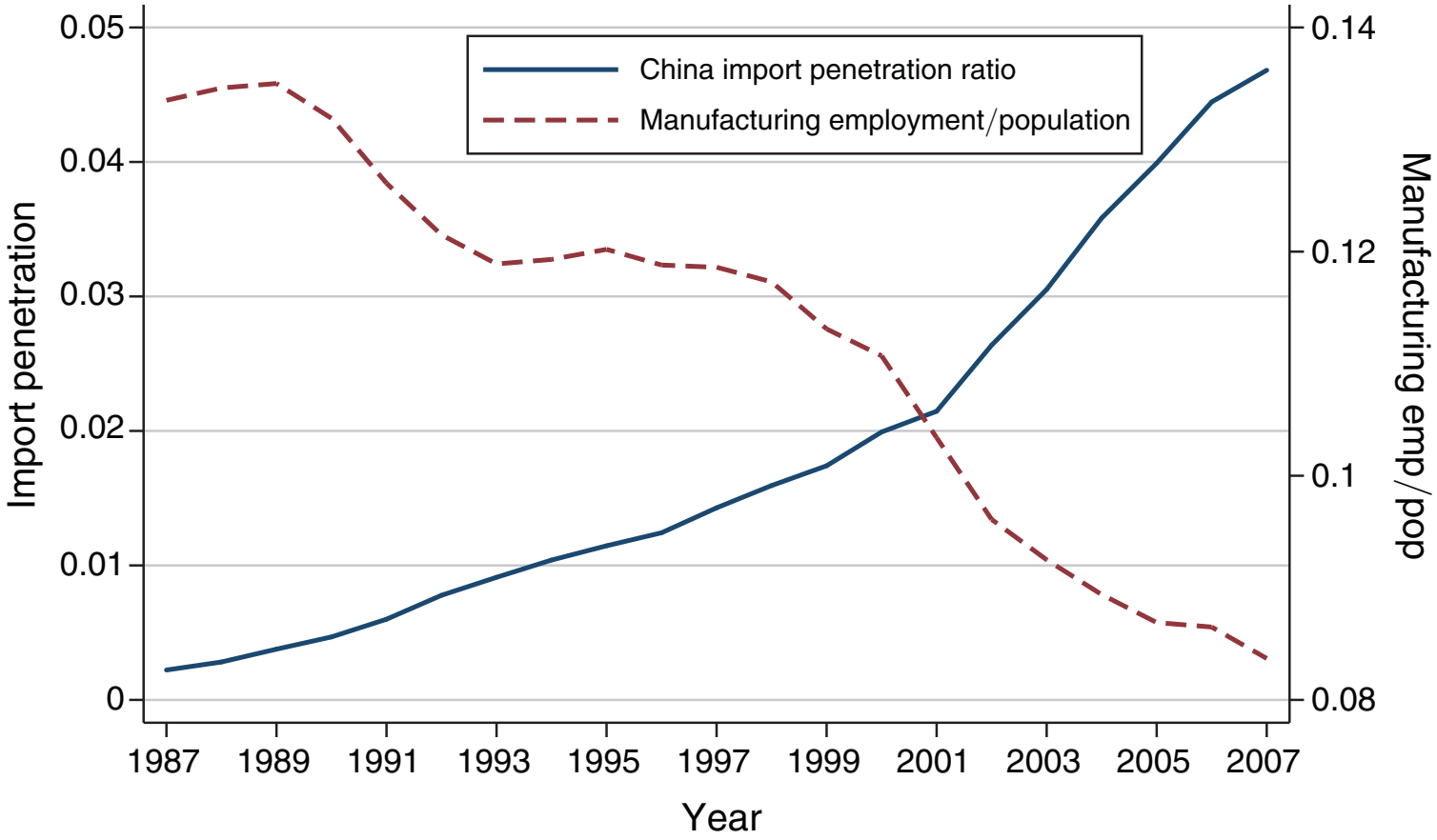
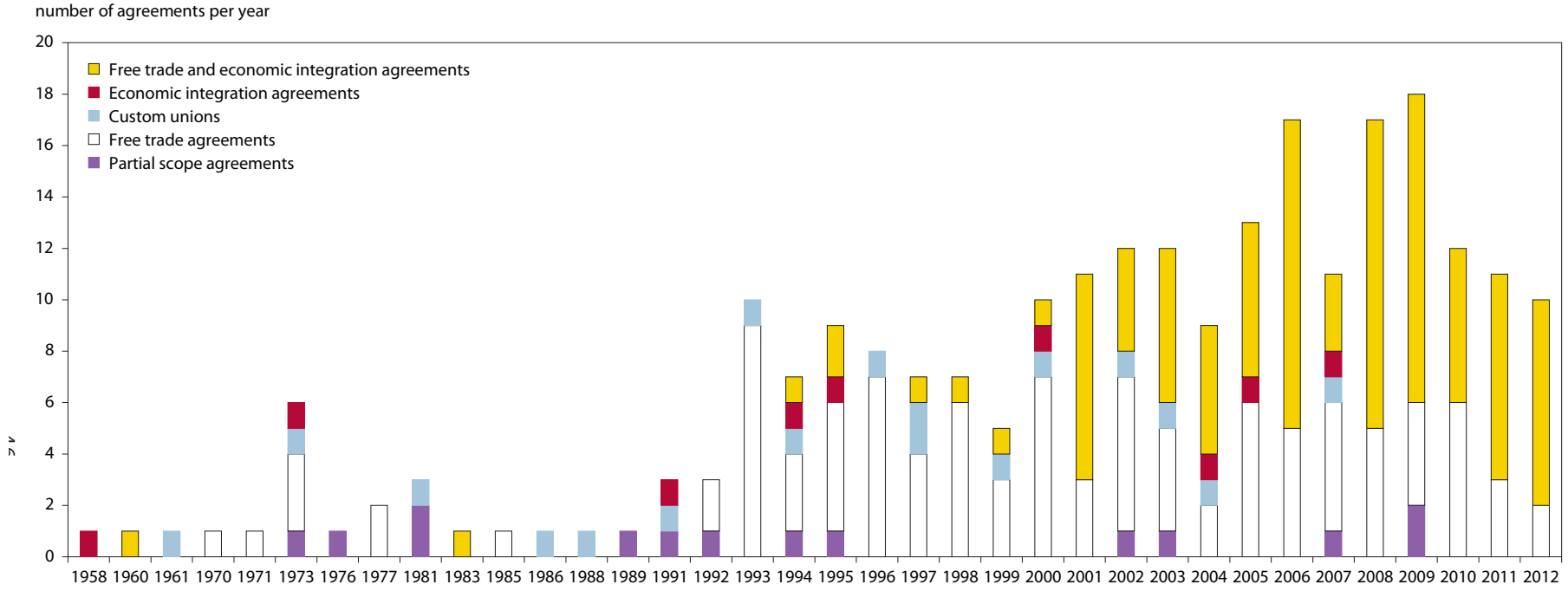


FIGURE 1. IMPORT PENETRATION RATIO FOR US IMPORTS FROM CHINA (*left scale*), AND SHARE OF US WORKING-AGE POPULATION EMPLOYED IN MANUFACTURING (*right scale*)

3 How trade agreements affect inequality

- For a long time, trade agreements = mostly about reducing tariffs
- Now increasingly about non-tariff barriers; intellectual property; dispute settlement
- Intellectual property rights provisions and dispute settlement = main provisions of currently discussed TTIP and TPP agreements
- Economic effects of these types of agreements?

Figure 2.6 Number of new signed preferential trade agreements, 1958–2012



Note: The year of the count is the year the World Trade Organization (WTO) was notified of the agreement. To simplify the classification of agreements, all agreements that are both economic integration agreements and customs unions or partial scope agreements are included in the "economic integration agreement" category.

Source: WTO 2011.

3.1 Patent regulations

- Large literature on economic effects of IP rights
- Boldrin and Levine (2013): "There is no empirical evidence that they serve to increase innovation and productivity"
- Very high profitability of US pharmaceuticals
- Main effect of further protection could be to deny life-saving drugs to poor people

3.2 Investor-State Dispute Settlement

- Rise of international arbitration procedure
- Various forms of ISDS are now a part of over 3,000 agreements worldwide
- Can help thwart expropriation and unfair treatment, bypass corrupt, incompetent or biased national courts
- But also restrict ability of governments to regulate; opaque

functioning; arbitrary and potentially large payment

- Main problem: used a lot by tax havens to deprive developing countries of government revenue

Table 1: Countries with the most arbitration clauses in tax treaties

Country	No. arbitration clauses
Netherlands	41
Switzerland	40
United Kingdom	22
Canada	21
Italy	18
Mexico	15
Belgium	12
United States	12
Liechtenstein	12
Luxembourg	12

Source: Martin Hearson and Todd Tucker (2015)

4 Summary

- Trade is a powerful force of convergence in average income across countries

- But its distributional consequences within countries are major

- Recent trade agreements are mostly about IP and ISDS which are unlikely to contribute to reducing global inequality

References

Autor, David, David Dorn, Gordon Hanson, and Jae Song "Trade adjustment: worker-level evidence", *Quarterly Journal of Economics* 2014 (web)

Boldrin, Michele and David K. Levine "The case against patents", *Journal of Economic Perspectives* 2013 (web)

Frankel, Jeffrey A. and David Romer, "Does trade cause growth?', *American Economic Review*, 1999 (web)