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Global Inequality: The Current Debate, It's Importance and Policy Recommendations

Selim Erdem Aytaç*

ABSTRACT

Despite the recent popularity of the subject of global inequality in the literature, most studies focus only on the debate about the direction and magnitude of change of global inequality during the last few decades, without deliberating about the different policy recommendations needed to address it. This article aims to fill this gap in the literature by reviewing the contemporary research on global inequality with an emphasis on different policy recommendations. In order to introduce the bigger picture, the study also presents a discussion on the latest findings on the level of global inequality and why it should be considered as a significant problem for humanity.

Keywords: Global Inequality, Pro-poor Growth, Globalization, Poverty.

Küresel Eşitsizlik: Güncel Tartışma, Önemi ve Politika Önerileri

ÖZET

Literatürde küresel eşitsizlik konusu son zamanlarda geniş bir yer bulmasına rağmen var olan çalışmaların büyük kısmı küresel eşitsizlik düzeyinin geçtiğimiz yıllarda hangi yönde ve ne kadar değiştiğine odaklanmakta, bu eşitsizliği giderecek politika önerilerine yeterince yer vermemektedir. Mevcut makale literatürdeki bu boşluğu küresel eşitsizlik konusunda önde gelen çalışmaları inceleyip ortaya çıkan bulguları sunarak ve özellikle değişik politika önerileri üzerinde durarak doldurmayı amaçlamaktadır. Ayrıca küresel eşitsizlik konusundaki büyük resmi daha iyi görebilmek için çalışmada eşitsizlik seviyesi hakkındaki en son bulgulara ve küresel eşitsizliğin insanlık için neden önemli bir problem olarak görülmesi gerektiğine dair değişik görüşlere de yer verilmiştir.

Anahtar Kelimeler: Küresel Eşitsizlik, Fakir-lehine Büyüme, Küreselleşme, Fakirlik.

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Introduction

Anand and Segal note that the last few years have witnessed a surge in the number of studies analyzing global income inequality[1] and attribute this increase partly to an effort to make sense of the effects of globalization, i.e. whether global inequality has increased or decreased in recent years. [2] In addition to this controversy which has significant policy implications, it can be argued that by increasing people's awareness about others' living standards, globalization has also a further effect of magnifying public interest in global inequality. As early as 1970s, Hirsch suggested that economic growth alone may not be sufficient to bring satisfaction to individuals due to the increasingly social nature of consumption[3], and we can safely assert that globalization has both confirmed and added another dimension to Hirsch's argument by taking the social aspect of consumption to unprecedented levels.

Despite the significance of the issue, however, we observe that the focus of the bulk of recent research on global income inequality has been on determining its direction and magnitude of change (i.e. whether it is increasing or decreasing, and by how much) in the era of neoliberal globalization.[4] I believe that this situation is unfortunate for two reasons. First, determining the direction of inequality turned out to be a very arduous task due to several methodological and data problems as well as the difficulty of establishing a clear causal linkage between globalization and inequality so that much of the effort in this area did not give satisfactory results. Second and more importantly, even if we cannot agree about the direction of inequality, there is one observation in the literature that has been long established and agreed upon: The current level of global income inequality is very high.[5] Therefore, I argue that instead of spending valuable resources on a futile globalization vs. inequality debate, the scholarship

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1 Throughout the paper the terms "global income inequality" and "global inequality" will be used interchangeably since the focus of the paper is on material income inequality between the individuals and although very important, issues such as social exclusion, social disintegration and subjective poverty are left out in order to have a clear focus. For an introduction to such concepts, see Fred Hirsch, *Social Limits to Growth*, London, Routledge, 1997; Alastair Greig, David Hulme and Mark Turner, *Challenging Global Inequality: Development Theory and Practice in the 21st Century*, Hampshire, Palgrave Macmillan, 2007; Ronaldo Munck, *Globalization and Social Exclusion: A Transformationalist Perspective*, Bloomfield, Kumarian Press, 2005.

2 Sudhir Anand and Paul Segal, "What Do We Know about Global Income Inequality", *Journal of Economic Literature*, Volume 46, No 1, 2008, p. 57-94.

3 Hirsch, *Social Limits to Growth*.

4 Anand and Segal, "What do We Know", p.57.

5 Robert H. Wade, "Is Globalization Reducing Poverty and Inequality", *World Development*, Volume 32, No 4, 2004, p. 567-589; Branko Milanovic, "Global Income Inequality: A Review", *World Economics*, Volume 7, No 1, 2006, p. 131-156.

should expend more effort in pursuing the question of how to solve (or at least alleviate) the problem of global inequality.

In the light of this observation, the primary purpose of this paper is to review the existing policy recommendations on addressing global income inequality. Analyzing the relevant literature, we see that whereas the mainstream liberal paradigm emphasizes the importance of economic growth leading to recommendations centered on policy reform, fighting corruption and effective international aid, there are also more poverty-focused approaches embodied in the concept of "pro-poor growth" that stresses the importance of the agricultural and labor-intensive manufacturing sectors. Lastly, one can also discern more unorthodox propositions in the literature such as giving workers claims to a certain share of corporate equity income or establishing an international agency that can levy taxes on the rich in the developed world. Before reviewing these policy recommendations, however, in order to introduce the bigger picture of global inequality the paper will also present a brief discussion on where we currently stand in terms of global inequality and why it should be considered a significant problem for humanity at large.

Inequality in the Era of Neoliberal Globalization

The latest research points to three conclusions about the nature of global inequality over the last few decades that can be relatively safely asserted: (i) Population-weighted between-country inequality has decreased primarily due to the fast-growing economies of China and India, (ii) within-country inequalities have increased in most parts of the world, and (iii) global inequality is high but its direction of change is unclear.[6] The questions of how these conclusions are derived and exactly what they mean require us to discuss briefly the different types of inequalities developed by Milanovic and which are used widely in the literature.[7]

Milanovic describes three types of measures of inequality which are differentiated according to data requirements and estimation methodology. First, Concept 1 inequality refers to unweighted inter-national inequality that mean income levels of countries as the benchmark for measuring inequality. Accordingly, each country is taken as a unit of observation without being weighted by its population and a comparison is made between the levels of average per capita income. Obviously, this type of inequality is not helpful for understanding the level of global inequality, since countries are of unequal population size, implying that Concept 1 inequality provides us with a distorted

6 Wade, "Is Globalization Reducing Poverty and Inequality", p. 575-579; Milanovic, "Global Income Inequality", p. 140-144, Anand and Segal, "What do We Know".

7 Milanovic, "Global Income Inequality", p. 131-134.

picture of reality.[8] In order to remedy this deficiency, Concept 2 inequality, namely the weighted inter-national inequality, weighs each country by its population so that each individual is assigned the average per capita income of his country. Except for this significant difference, Concept 1 and Concept 2 inequalities are identical both in terms of data requirements and methodology.

The problem with Concept 2 inequality is, however, that it does not take within-country inequalities into account. This measure is inadequate if we want to determine true global inequality, i.e. inequality between individuals, since Concept 2 inequality rests on the implicit assumption that each individual within a country has the same income, which is obviously not true. Addressing this issue takes us to the third and last type of inequality, Concept 3 or global inequality, which is quite different from the previous types both in terms of data requirements and methodology. Concept 3 inequality directly takes individuals as the unit of observation through household surveys and measures the per capita disposable household income as the welfare indicator (instead of national accounts and GDI per capita, respectively). In this way, it takes into account the important within-country income inequalities as well and provides us with the most realistic measure of global inequality.

Although we would logically expect Concept 3 inequality to be the most widespread measure of global inequality due to its desirable properties, this is not the case and Concept 2 inequality is the most popular measure in the literature.[9] Milanovic argues that there are principally two reasons for this tendency.[10] First, compared to the data requirements of Concept 3 inequality, Concept 2 inequality measure requires a relatively small amount of data: Whereas for Concept 3 inequality we need representative household surveys from a large number of countries, the only data needed for Concept 2 inequality are GDI per capita and population information of countries. Second, estimates indicate that between-country inequalities are responsible for two-thirds to three-quarters of overall global inequality and therefore Concept 2 inequality is considered to be the largest component of inequality between world citizens. [11] This observation leads policy makers to assume that the movements of Concept 2 inequality can adequately reflect changes in global inequality which is itself very difficult to measure, and since the debates on the effects of globalization on global inequality are focused on trends of inequality rather than its absolute level, the popularity of Concept 2 inequality is further reinforced.

Given this background of different types of inequalities, what do the empirical studies suggest regarding their level and trend? First, Concept 1

8 Ibid., p. 132.
9 Anand and Segal, "What do We Know", p. 59-60.
10 Milanovic, "Global Income Inequality", p. 132.
11 Ibid., p. 132.

inequality seems to have been increasing in the last few decades,[12] but it is difficult to understand what this suggests regarding global inequality. What is more interesting for our purposes is the trend of Concept 2 inequality which is considered to be decreasing over the same period, meaning that the population-weighted, between-country inequality diminished over time. Wade, however, urge us that this type of "…falling income inequality is not a general feature of the world economy" since if we exclude China and India then this measure shows a widening, indicating that the reduction in Concept 2 inequality is confined to only a specific region of the world.[13] Moreover, even if we accept that Concept 2 inequality shows a decreasing trend in general, this does not mean that inequality between world's people are decreasing since, as stated, this measure does not take within-country inequalities into account. This point is particularly important because within-country inequalities have been rapidly increasing in most parts of the world recently.[14] We do not know whether this increase in within-country inequalities offsets the decrease in between-country inequalities and therefore the information about Concept 2 inequality does not permit us to be certain about the direction of global inequality.

Third and most importantly, studies about Concept 3 inequality are also inconclusive about the direction of global inequality, due to a lack of adequate data. Household surveys needed to measure Concept 3 inequality were not available in countries like China, Soviet Union and large parts of Africa before the mid-1980's and the total span of studies focusing on this type of inequality is only ten years, which is insufficient to reach any reliable conclusion about the trend.[15] What is more certain, however, is that the current level of global inequality, estimated by the Concept 3 measure, is very high (significantly higher than the estimations by the other types of inequalities) with a Gini coefficient between 0.63 and 0.68.[16] This level of inequality is equivalent to an income distribution where the top 5 percent of individuals receive about one-third of the total income whereas the bottom 5 percent's share is just 0.2 percent. Thus, although the Concept 3 inequality does not tell us much about the recent direction of global inequality, it shows that it is very high which should be equally important as the direction itself.

12 Wade, "Is Globalization Reducing Poverty and Inequality", p. 576.

13 Ibid., p. 576.

14 James K. Galbraith, "Global Inequality and Global Macro Economics", David Held and Ayse Kaya (eds.), *Global Inequality*, Cambridge, Polity Press, 2007, p. 148-175; Ranja Sengupta and Jayati Ghosh, "Understanding the Extent and Evolution of Inequalities in China", Jomo K. S. and Jacques Baudot (eds.), *Flat World, Big Gaps: Economic Liberalization, Globalization, Poverty and Inequality*, New York, Zed Books, 2007, p. 376-403.

15 Wade, "Is Globalization Reducing Poverty and Inequality", p. 577; Milanovic, "Global Income Inequality".

16 Milanovic, "Global Income Inequality: A Review", p. 140-144; Anand and Segal, "What do We Know", p. 61-65.

Now, one may ask where this picture leads us. Overall, as Anand and Segal indicate "…it is not possible to reach a definitive conclusion regarding the direction of change in global inequality over the last three decades of the twentieth century".[17] Nevertheless, regardless of the direction of change we know that the current inter-personal inequality in the world is very high, more than the inequality levels found in countries like South Africa or Brazil which are notorious for their large income disparities. [18] So, the next logical question would be whether this high income inequality is important enough for society to take specific action to reduce it. The next section will present different perspectives about this question.

Importance of Global Inequality

The preceding discussion illustrates that the current level of global income inequality is quite high, suggesting that there should be ways to decrease it to more acceptable levels, at least in theory. In order to contemplate possible policy options for this purpose and put them into practice, however, first both the public and policy makers should be convinced that global inequality is an important problem for society. In the following, I will briefly discuss some prominent perspectives on the importance of global inequality, ranging from a pragmatic view to an ethical one. This brief overview illustrates that concerns about global inequality are now more pronounced than before[19] and it is widely considered as a serious problem worth allocating resources to fight.

The pragmatic perspective arguing that income inequality is harmful for society is based upon the increasing challenges to neoliberal arguments that there are desirable incentive effects of income inequality. Wade points to considerable evidence indicating that desirable effects from inequality on incentives and competitiveness apply only at moderate, Scandinavian-type levels of inequality.[20] Higher levels of inequality, which are much more prevalent throughout the world from the U.S. to Brazil, however, cause these desirable

17 Anand and Segal, "What do We Know", p. 90.

18 Milanovic, "Global Income Inequality", p. 142.

19 It has been noted in the literature that the problem of global inequality began to receive considerable attention only since the late 1990s because throughout the 1980s and early 1990s, the prevalent neoliberal view regarded income inequality as a secondary issue in comparison to economic efficiency. For a detailed discussion on why this was the case, see: Robert H. Wade, "Should We Worry about Income Inequality?", Held ve Kaya (eds.), *Global Inequality*, p. 104-131; Greig et al., *Challenging Global Inequality*; Edward Miliband, "Does Inequality Matter?", Anthony Giddens and Patrick Diamond (eds.), *The New Egalitarianism*, Cambridge, Polity Press, 2005, p. 39-51; Eddie J. Girdner, "A Spectre Haunting Europe: The European Constitution, the Budget Crisis, and the Limits of Neoliberal Integration", *Uluslararası İlişkiler*, Volume 2, No 7, 2005, p. 63-85.

20 Wade, "Should We Worry about Income Inequality", p. 115.

effects to be cancelled by social costs. A more than moderate level of inequality results in an undersupply of collective goods (e.g. personal security and human capital formation) which are essential for the proper functioning of the economy and society. Wade further asserts that there is ample evidence suggesting that higher income inequality within countries is associated with a lower contribution of economic growth to poverty reduction, higher unemployment, higher crime, lower average health, lower standards of public services and more fragile democracies. [21] Milanovic also notes some pragmatic reasons why global inequality matters, the prevention of possible political tensions between the poor and rich being the most important one.[22] Relying on an argument made by Simon Kuznets a long time ago, Milanovic asserts that the growing interaction among the people of the world due to globalization may increase one's awareness of the others' income and therefore fuel the perception of inequality among the poor and rich. In this situation, even if the real income of poor people increases as much as other segments of the society, it may not be enough to abate the feelings of deprivation among the poor which would result in continuous tensions.

In addition to these practical concerns about global inequality, Pogge asserts that economically developed societies have also a moral obligation to make a serious effort toward poverty and inequality reduction in the developing world.[23] In order to make his point, Pogge offers three morally significant connections between people in the advanced countries and the global poor. First, part of the reason why today's wealthy societies are wealthy and poor societies are poor is the historical wrongdoings of today's wealthy societies against today's poor societies, such as colonialism, slavery and genocide. Second, Pogge argues that the affluent countries together with the rich of the developing states, have divided and appropriated the world's resources for their mutual benefit without caring for the majority, excluding them from the benefits of common resources with no compensation. Third, the current global economic order largely devised by wealthy societies, has a strong tendency to perpetuate and exacerbate global inequality. Besides these morally significant connections, Pogge strongly emphasizes that "For the first time in human history it is quite feasible, economically, to wipe out hunger and preventable diseases worldwide without real inconvenience to anyone".[24] Thus, Pogge concludes that implementing policies aimed at reduction of global poverty and inequality should be one of the moral priorities of the developed world.

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[21] Ibid., p. 115.

[22] Milanovic, "Global Income Inequality", p. 148-149.

[23] Thomas W. Pogge, "Priorities of Global Justice", Thomas W. Pogge (ed.), *Global Justice*, Oxford, Blackwell Publishing, 2001, p. 6-23.

[24] Ibid., p. 13.

Lastly, Sachs evaluates the importance of global inequality from a very different angle, i.e. its strategic significance for the developed world and especially the U.S. [25] The primary focus of Sachs is the occurrence of state failure, the probability of which is found to substantially increase with economic failure and poverty. State failure is important both for the country that experiences it and for the world in general, because if it happens and governments fail to provide the most basic public goods for their people, then it is quite likely that there would be spill-over effects to the rest of the world. According to Sachs, these problems include, but are not limited to, terrorism, international criminal groups, mass migration, drug trafficking, and diseases. Also empirically, comparing the dates of U.S. military intervention with the timing of state failures reveals that "…virtually every case of U.S. military intervention abroad since 1960 has taken place in a developing country that had previously experienced a case of state failure".[26] Besides these security-related concerns, it has also been argued that the economic success or failure of a developing country also determines gains from trade and investment the developed states obtain from that particular country, and given that low-to-moderate rates of inequality and poverty are related with better growth performance, policies that help developing countries to keep their inequality levels low have also economic benefits for the developed world. In short, Sachs concludes that global income inequality has a strategic significance for the developed nations and particularly the U.S.

What Can We Do About Global Inequality?

Having established the contemporary status of global income inequality and its significance, this section will present some notable policy proposals for addressing this issue. First, I will review some papers that demonstrate mainstream views of global institutions like the World Bank and the IMF, and argue that they primarily focus on promoting economic growth, fighting with corruption, realizing market-oriented policy reforms and designing effective aid mechanisms. Although all of these policy recommendations have some merit, in practice it has been increasingly acknowledged that they might not be sufficient to overcome inequality. This observation has led some policy makers to look for additional measures that are embodied in the term "pro-poor growth"[27] which will be discussed in the second subsection. In essence, the advocates of pro-poor growth emphasize the importance of agriculture and argue that policies that target specifically the agricultural sector would be the most effective measure to eradicate poverty and inequality. The last subsection will touch upon some more

[25] Jeffrey D. Sachs, "The Strategic Significance of Global Inequality", *The Washington Quarterly*, Volume 24, No 3, 2001, p. 187-198.

[26] Ibid., p. 191.

[27] Growth policies favoring the poor segments of the society disproportionately positive.

unconventional views on the subject, such as giving workers claims to a certain share of corporate equity income or establishing an international organization that can levy taxes on the rich of the developed world and distribute directly to the poor in developing countries.

The Mainstream Liberal View on How to Fight Global Inequality

One of the best examples of studies representing the mainstream liberal view emphasizing economic growth is the work by Dollar and Kraay.[28] The main argument of the paper is quite straightforward: "We simply emphasize that growth on average does benefit the poor as much as anyone else in society, and so standard growth-enhancing policies should be at the center of any effective poverty reduction strategy".[29] Thus the study presents a strong case for governments which want to fight inequality by reducing poverty, i.e. they should simply pursue growth-maximizing policies while maintaining fiscal discipline and avoiding high inflation.[30] According to the authors, the article was written due to the lack of adequate systemic cross-country empirical evidence on the extent to which the poorest segment in the society benefits from overall economic growth.[31] In order fill this gap, the study empirically examines the relationship between growth in average incomes of the poor and growth in overall incomes. Without going into the details of research design and methodology, we can state that the main finding of the study is that within countries, incomes of the poor (those in the bottom fifth of the income distribution of a country) on average rise equiproportionately with average incomes. Moreover, the study also reports little evidence for the idea that greater economic integration across countries is associated with increases in inequality within countries and measures such as international openness and the presence of capital controls do not have any systematic effects on the share of income accruing to the poorest in society.

Another important empirical test of the study for our purposes is the investigation of four factors that are widely thought to benefit the poor more than the rest of the society: primary educational attainment, public spending on health and education, labor productivity in the agricultural sector relative to the rest of the economy, and formal democratic institutions. Surprisingly, the study does not produce any evidence that these factors systematically raise the share of

28 David Dollar and Aart Kraay, "Growth is Good for the Poor", *Journal of Economic Growth*, Volume 7, 2002, p. 195-225.

29 Ibid., p. 219.

30 Although the authors state that their findings "...do not imply that growth is all that is needed to improve the lives of the poor...and the potential distributional effects of growth...can or should be ignored" (p. 219), a clear implication of the paper is that there is no solid reason for governments to follow pro-poor growth policies to reduce inequality.

31 Ibid., p. 195.

income of the poorest in society within the large cross-country sample considered. Given this result, the authors conclude that "…policies that raise average incomes are likely to be central to successful poverty reduction strategies, and that existing cross-country evidence provides disappointingly little guidance as to what mix of growth-oriented policies might especially benefit the poorest in society".[32] Therefore, in order to tackle both poverty and global inequality, a basic policy package that will promote the overall growth of the economy (such as private property rights, fiscal discipline, macroeconomic stability and openness to trade) should be the primary focus of governments. As expected, this study has received considerable attention in the literature, sparking a controversy around the idea of focusing predominantly on economic growth for reducing poverty and inequality. Kakwani, Prakash and Son[33], for example, discuss some of the methodological problems of Dollar and Kraay. One of the problems they point to is the usage of the unweighted method of estimation for the regression equations which gives equal weight to every country irrespective of its population. Obviously, such an approach is flawed since it does reflect an accurate picture of reality. Similarly, Foster and Szekely illustrate that using different methodologies for characterizing the well-being of the poor can lead to different results about the relationship between economic growth and poverty: Measuring the impact of economic growth on the poor by placing greater weight on the income growth of people with lower incomes instead of defining a cutting point as Dollar and Kraay does, the authors conclude that although overall growth is beneficial for the poor, it is not necessarily as good as that of the other segments of the population, contrary to the argument of Dollar and Kraay.[34] Thus, we can conclude at least that the arguments of Dollar and Kraay are not as powerful as they claim to be.

Policy makers from institutions such as the World Bank or IMF also emphasize the importance of addressing corruption in developing countries as a policy tool to fight income inequality. In this regard, the work of Gupta, Davoodi and Alonso-Terme claim to be the first study presenting cross-country empirical evidence regarding the relationship between corruption, income distribution and poverty.[35] Examining cross-country data over the period of 1980-1997, the results of their study indicate that high and rising corruption levels increase income inequality and poverty; specifically, an increase of one standard deviation

32 Ibid., p. 198.

33 Nanak Kakwani et al., "Growth, Inequality, and Poverty: An Introduction", *Asian Development Review*, Volume 18, No 2, 2000, p. 1-21. This study criticizes the working paper version of Dollar and Kraay (2002) - David Dollar and Aart Kraay, "Growth is Good for the Poor", Working Paper, World Bank, Washington, D. C., 2000 - but the points still apply for the published version.

34 James Foster and Miguel Szekely, "How Good is Growth", *Asian Development Review,* Volume 18, No 2, 2000, p. 59-73.

35 Sanjeev Gupta et al., "Does Corruption Affect Income Inequality and Poverty?", *Economics of Governance,* Volume 3, 2002, p. 23-45.

in corruption increases the Gini coefficient by about 0.11 points. The basic argument for this result is that the benefits from corruption are most likely to accrue to the better-connected individuals with the government who mostly belong to high-income groups. [36] From this argument it follows that corruption would not only negatively affect investment and growth but also the income distribution of a society. Other arguments on how corruption may affect income inequality and poverty include (i) reduction in the level of social services available to the poor as well as improper targeting of such services to the truly needy, (ii) creation of incentives for higher investment in capital-intensive projects as opposed to labor-intensive projects which deprive the poor of income-generating jobs, (iii) reduction of overall growth, (iv) creation of tax exemptions that disproportionately favor the wealthy population groups, and (v) increase in the operating cost of government which in turn reduces the resources available for education or health spending that disproportionately hurts the poor.[37] In short, the authors conclude that policies aimed at reducing corruption will likely contribute also to decreasing income inequality and poverty.

Lastly, another mainstream liberal point of view regarding income inequality and poverty reduction is the importance of sound economic institutions and policies. [38] Collier and Dollar, for example, argue that differences in economic institutions and policies are extremely significant in explaining differences in productivity and income across countries, and suggest that "Rapid poverty reduction in low-income countries depends primarily on these countries improving their own policies and institutions".[39] Effective foreign aid can also make a contribution to greater poverty reduction in poor countries especially if good policies exist in the recipient country. Collier and Dollar's argument is built precisely on these two observations and proposes a model of efficient aid in which more emphasis is given to countries with better policies. Specifically, Collier and Dollar design an aid allocation rule in which for countries with similar levels of poverty the received aid increases as the quality of policies[40] improves, whereas for countries with similar policies the aid increases with the severity and prevalence of poverty within a country. The authors argue that compared to the actual allocation of aid their proposal "(i) has the same relationship with population, (ii) is more sharply targeted to low-income

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36 Ibid., p. 23.

37 Ibid., p. 25-27.

38 Paul Collier and David Dollar, "Can the World Cut Poverty in Half? How Policy Reform and Effective Aid Can Meet International Development Goals", *World Development,* Volume 29, No 11, 2001, p. 1787-1802.

39 Ibid., p. 1787.

40 By "good policies" the authors refer to the extent to which a country has a good institutional and policy environment (macroeconomic stability, public sector management, etc.) for long-term growth and poverty reduction. The measurement of such policies is based on the World Bank's Country Policy and Institutional Assessment (CPIA) data.

countries, and (iii) has a stronger relationship with policy".[41] After calculating optimal aid allocations for each country according to their proposed algorithm, they find that more efficient aid alone could double poverty reduction in Africa by 2015 compared to the baseline scenario which assumes that policy in developing countries and the level and efficiency of aid will remain the same. Moreover, if Africa improves its policies (by attaining the policy level currently observed in South Asia) together with the presence of efficient aid then the poverty reduction further doubles compared to the case of optimal aid allocations alone. It has been argued that such a positive outlook would also provide the recipient countries with a solid incentive to improve their policies in order to attract more aid. The authors conclude that the combination of economic reform and efficient aid can substantially reduce poverty in developing countries and contribute to overcoming global inequality.

Advocates of Pro-Poor Growth

As we have seen in the preceding discussion, the emphasis of the mainstream liberal views on how to address inequality is recommending policies that would ensure growth. It is clear that economic growth is important and any significant step towards overcoming inequality would necessarily require achieving sustainable growth rates, yet it is also widely agreed that economic growth *per se* is not sufficient for diminishing inequality.[42] Although sustainable economic growth tends to reduce poverty on average and in the long term, there are several examples of short-term growth episodes in various countries that had a negative impact on poverty.[43] Eastwood and Lipton describe some situations where growth might be anti-poor:[44] First, growth can be detrimental for poverty reduction if it shifts demand away from products made by immobile poor workers. Second, growth may not benefit the poor if there is a technical progress that is either labor-saving or relatively slow in sectors in which the poor are working. Lastly, growth may shift resources away from sectors that make products poor people demand, so their relative prices rise. As these cases illustrate, growth may not be sufficient to fight poverty and inequality.

As a response to these observations about the relationship between growth and inequality, we see an identification of a new type of economic growth in the

41 Ibid., p. 1794.

42 Martin Ravallion and Gaurav Datt, "Why Has Economic Growth Been More Pro-Poor in Some States of India than Others?", *Journal of Development Economics,* Volume 68, 2002, p. 381-400.

43 Stephan Klasen, *In Search of the Holy Grail: How to Achieve Pro-Poor Growth?* Mimeo, University of Munich, 2004.

44 Robert Eastwood and Michael Lipton, "Pro-Poor Growth and Pro-Poor Poverty Reduction: Meaning, Evidence, and Policy Implications", *Asian Development Review*, Volume 18, No 2, 2000, p. 22-58.

literature, the pro-poor growth.[45] At the most basic level, pro-poor growth implies a disproportionate, i.e. higher than average, growth of incomes of the poor in a society. The amount of pro-poor growth could be measured by a poverty-weighted growth rate which puts greater weight on the income growth rate of the poorest quintiles and declining weights on the rates of the remaining richer quintiles, and one can identify a pro-poor growth if this measure exceeds the average income growth rate of the country.[46] If such a pro-poor growth could be achieved, i.e. the income growth rate of the poor could exceed the growth rate of the non-poor, then we would observe a significant reduction in poverty which would also abate income inequality. In this regard, Klasen argues that economic growth can be pro-poor in two ways. [47] The first way is to develop a growth pattern that favors those regions and sectors where poor people live and work, and utilizes the factors of production they possess. Second, pro-poor economic growth can be achieved with the help of public redistributive policies such as progressive taxation implemented together with targeted government spending on the poor. Although the first way is preferable for sustainable poverty reduction, it inevitably has the disadvantage of being vulnerable to economic crises so that it should be complemented by second way measures in order to provide some sort of safety net for poor segments of society. In the following, each of these pro-poor growth ways will be examined in more detail.

The basic policy recommendation of the first way of pro-poor growth is that economic growth should be realized in those sectors where the poor work and are able to utilize the factors of production they possess. In this regard, Eastwood and Lipton report that a large majority of the poor live in rural areas depending upon agriculture for their livelihoods and labor is the factor of production they most possess and use.[48] The significant implication of this observation is that pro-poor growth aiming at poverty reduction must place an emphasis on improving agricultural productivity and raising incomes in rural occupations. [49] Empirically, Ravallion and Datt analyze the sectoral growth rates of different states of India and find that while urban growth had some positive impact on urban poverty only, rural growth has reduced poverty in both rural and urban areas. [50] This effect has also been reported in cross-country analyses where improvements in agricultural labor productivity have been found to be more pro-poor than improvements in other sectors. [51] In terms of factors of production, the policy recommendation is also validated empirically whereby the

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45 Eastwood ve Lipton, "Pro-Poor Growth", Ravallion and Datt, "Why Has Economic Growth" Been More Pro-Poor in Some States of India than Others?"; Klasen, "In Search of the Holy Grail: How to Achieve Pro-Poor Growth?".

46 Klasen, "In Search of the Holy Grail", p. 65.

47 Ibid., p. 67-71.

48 Eastwood and Lipton, "Pro-Poor Growth and Pro-Poor Poverty Reduction: Meaning, Evidence, and Policy Implications", p. 51.

49 Klasen, "In Search of the Holy Grail", p. 68.

50 Ravallion ve Datt, "Why Has Economic Growth".

51 Eastwood ve Lipton, "Pro-Poor Growth".

analysis of countries such as, India and China suggest that poverty reduction was largest when growth utilized the assets poor people possess, such as unskilled labor and land.[52]

The importance of agricultural development in fighting poverty is especially emphasized in Eastwood and Lipton.[53] The authors note that the poor spend some 70 percent of their income on food and about half their income on food staples. Moreover, they also earn over half their income from growing such food staples, or working for those who do: Some 75 percent of the poor are mainly engaged in agriculture and many of the rest in rural non-farm activities whose income depends mainly on growing demand from farm-based producers and consumers. Therefore, for reducing poverty and inequality especially in the developing countries implementing policies that increase the poor people's command over food via more labor income and less food cost could be the primary approach of policy makers. In this regard, Eastwood and Lipton develop three specific policy recommendations: (i) emphasizing labor-intensive growth in food staples production, (ii) stimulating smaller-scale farms via land distribution in order to enhance the impact of cheaper food and higher demand for rural labor, and (iii) developing incentives to reduce fertility especially of the poor.[54] The authors assert that there is ample evidence that a high rate of growth in agriculture is associated with poverty reduction, land redistribution increases the income share of the poor, and declining fertility results in faster growth of GDP per capita and a more equal income distribution.

The second way of promoting pro-poor growth involves government action in establishing social funds and providing some targeted cash transfers to the poor in order to enhance their economic self-reliance for pursuing income-earning opportunities. [55] For the pro-poor growth in the long run, on the other hand, the government can also allocate resources to improve the human capital of the poor by raising the standards and prevalence of education and health services. Such an approach would provide valuable safety nets for the poor in the short run while reducing their reliance on such redistributive programs in the long run as their capacities develop. Galbraith notes that part of this approach is also favored by institutions like the World Bank where it has been argued that a significant factor for the success of the East Asian nations in eradicating poverty was early redistribution of land and primary schooling.[56]

Some Other Policy Proposals for Ameliorating Global Inequality

Lastly, we will have a brief look at some other policy proposals on how to abate global inequality that may be considered to involve more unconventional

52 Klasen, "In Search of the Holy Grail", p. 70.
53 Eastwood ve Lipton, "Pro-Poor Growth", p. 51-52.
54 Ibid., p. 52.
55 Klasen, "In Search of the Holy Grail", p. 68.
56 James K. Galbraith, "A Perfect Crime: Inequality in the Age of Globalization", *Daedalus*, Volume 131, No 1, 2002, p. 11-25.

elements than the previously discussed ideas. An obvious policy to address income inequality within a society would be to utilize government funds for income transfers in forms of retirement pensions or unemployment benefits. It has been noted that such policies to offset rising inequality in a country has been successfully employed by the developed countries for many years[57], yet an immediate question at this point is whether developing countries are capable of pursuing similar policies: Developing countries may lack both the financial resources and technical-organizational capabilities required for extensive redistribution schemes. Moreover, as globalization progresses, the competition between countries in international trade intensifies and given the increased factor mobility, it is getting increasingly difficult for states to pursue independent national policies. [58] At this point, Basu emphasizes the need for the coordination of policies across countries and proposes a rather radical step of establishing a new international organization for coordinating equitable development and inter-country anti-poverty policies. [59] He correctly points out that any unilateral effort by a country to decrease inequality (such as levying a new tax) is likely to cause the flight of capital and skilled labor from the country and damage those who stay behind. Thus, even if every country would like to take steps to decrease inequality they may not be able to do so due to a Prisoner's Dilemma type of situation. Noting that the existence of coordination problems has been acknowledged by the international community in areas like trade and environment, and accordingly appropriate institutions to address these problems have been established (WTO, UNEP), Basu asserts that there is nothing comparable to these for anti-poverty and anti-inequality policies. Being aware that his recommendation is a very complex task to realize, however, Basu provides no details in this regard and claims that his aim "…was to float the idea and place it in the public domain".[60]

Related to the recommendation of a new international organization, Basu also proposes a specific action focused on the workers who have lost their jobs because of globalization (e.g. due to outsourcing or low-cost imports).[61] The idea is based on giving workers claims to a fraction of corporate equity income. Rather than just involving profit sharing in the firm where the worker is employed, the proposal requires a fraction of equity earnings from all firms to be given to workers in all firms and even to laborers who are currently unemployed. Basu argues that such a scheme can be accomplished if a small amount of equity in firms is owned by some governmental organization on behalf of people in the

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57 For a discussion and examples of such government redistribution schemes, see Anthony B. Atkinson, "Is Rising Inequality Inevitable? A Critique of the Transatlantic Consensus" *WIDER Annual Lecture 3*, Helsinki, UNU-WIDER, 1999.

58 Kaushik Basu, "Globalization, Poverty, and Inequality: What is the Relationship? What Can Be Done?" *World Development*, Volume 34, No 8, 2006, p. 1361-1373.

59 Ibid., p. 1370.

60 Ibid., p. 1371.

61 Ibid., p. 1370.

poorest category which would also include workers. So when some workers lose their job as a result of outsourcing then part of the extra profit generated by this process should be earned by the disadvantaged workers. Such a policy is related to the proposal of a new international organization above because at least in the long run it will also entail developing some rules for inter-country transfers of equity income. Although the ideas of Basu are quite interesting, their implementation would demand extensive and radical changes in several national as well as international policy domains.

Also Milanovic points to the need for designing some mechanism for global redistribution in order to abate global inequality.[62] He acknowledges that the sustainable growth of the mean incomes of developing countries is an important goal for reducing global inequality since large income differences among individuals are mostly due to the large differences in countries' mean incomes; yet he also emphasizes that given that this is a long and difficult task to accomplish, we still need a global redistribution scheme to facilitate the reduction of both between and within country inequalities. In turn, to maximize the effectiveness of this global redistribution mechanism in fighting inequality Milanovic develops a "globally progressive" transfer scheme which will be briefly discussed below.[63]

The first and obvious requirement of such a scheme is that redistribution funds should flow from a resource-rich (high mean income) to a resource-poor (low mean income) country. Milanovic notes that this requirement is straightforward and easily satisfied in the current aid allocation. Second, in terms of the actual payer and beneficiary of the transfer, the payer should be richer than the beneficiary. At this point, we may consider a hypothetical transfer from a relatively poor individual in a rich country to a relatively rich individual in a poor country, Milanovic points out that such a transfer would satisfy the preceding two requirements. However, this transfer would be quite problematic for global inequality in the sense that although it would reduce between-country inequality, it would exacerbate within-country inequality in both countries. This follows because the relatively poor payer in the rich country would be poorer whereas the relatively rich recipient in the poor country would be richer. In order to account for this problem, Milanovic envisages a third requirement according to which global transfers should be allocated such that inequality decreases in both the payer and the recipient country. This requirement can be satisfied if the payer is relatively rich both in the payer and the recipient country whereas the beneficiary is relatively poor in both. In order to maximize the inequality-reducing effects of global transfers, the most crucial rule to follow is this third one.

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62 Milanovic, "Global Income Inequality".

63 Ibid., p. 149-152.

These three requirements for an effective global redistribution scheme would be relatively easily satisfied if the income distributions of every country involved in the transfer did not overlap at all. Since this is far from being the case in reality, Milanovic offers the creation of a new global agency with the responsibility of making sure that the requirements are satisfied. According to this idea, the agency "…would be financed by a tax raised from the rich in rich countries and…would transfer these funds to poor *individuals* in poor countries".[64] Moreover, he pushes his idea further by suggesting that the new agency should operate directly with the national NGOs and individual citizens in both the poor and rich countries since such an arrangement would both prevent the waste of aid due to corruption or inefficiency of the government and help poor people in developing countries directly without the authorization from governments. Obviously, Milanovic is aware that such a proposal is quite radical since it directly infringes the sovereignty of states by levying taxes; however, pointing to the general trend of globalization in the recent era, he is optimistic that such an agency could be institutionalized in the near future. Admittedly, if realized and allowed to function properly, this arrangement would significantly benefit the reduction of both within and between country inequalities.

Lastly, Pogge makes a call to affluent societies for taking action towards eradicating global poverty and hence improving inequality.[65] He basically argues that the developed countries should allocate financial and technical resources for implementing projects aimed at enabling poor people to afford foodstuffs and shelter, financing schools and basic health services, and improving the local infrastructure in the world's poorest regions. Specifically, Pogge recommends that the most developed nations of the world should be willing to spend at least 1 percent of their GNP, even 2 percent if possible, for the specific purpose of poverty eradication in the developing world via implementing the projects mentioned. Although these numbers may seem quite low in terms of percentages, in absolute terms they are very substantial (roughly $229 billion annually).

Concluding Remarks

This paper has presented a comprehensive review of the latest research on the direction and level of global inequality, its importance, and different policy recommendations, with a focus on the latter. In terms of the direction and level of global inequality, we have seen that there is inadequate evidence to confidently assert whether global inequality has been increasing or decreasing over the past few decades. Having said that, however, the relevant literature presents considerable evidence indicating that within-country inequalities have increased for many countries, and the latest methods on measuring global inequality (the Concept 3 inequality) suggest that the contemporary level of

[64] Ibid., p. 151.
[65] Pogge, "Priorities of Global Justice".

global inequality is considerably more than the previously estimated figures. Such a picture is a source of concern for humanity at large for pragmatic, ethical and strategic reasons: While the pragmatic perspective emphasizes the social costs of high levels of inequality, the ethical view posits that developed countries have a moral obligation to fight rising inequality throughout the globe. The strategic perspective, on the other hand, considers efforts to address global inequality imperative in order to minimize the likelihood of state failure and prevent the associated risks.

Regarding the different policy recommendations on how to decrease global inequality at least to acceptable levels, three distinct approaches can be identified in the literature. First, the liberal paradigm argues that achieving a high economic growth rate should be the primary objective of any government or international organization in fighting poverty and inequality. Accordingly, policy reforms to boost efficiency, minimizing corruption, and designing an effective aid mechanism to poor countries are the main tools recommended by this view. There should be no doubt that achieving sustainable growth is important, however, at the same time we have also seen that economic growth alone may fail to deliver satisfactory results in terms of reduction of poverty and inequality. The second approach that is centered on the concept of "pro-poor growth", on the other hand, focuses on the rural, agricultural and labor-intensive sectors with a prospect of reducing inequality both in rural and urban regions. [66] Given that the recent evidence on global inequality points out that within-country inequalities are rapidly increasing and the most significant source of income inequality in the developing countries is the growing rural-urban disparities[67], the pro-poor growth approach is quite promising in reversing this trend. Lastly, we have also reviewed some unorthodox policy recommendations involving major redistributive schemes at the international level. Ultimately, the decision about which policy recommendation should be employed to fight global inequality would be primarily a political one; yet the latest evidence on the nature of global inequality and past experiences can shed considerable light on this crucial task and should not be ignored.

66 Ravallion ve Datt, "Why Has Economic Growth".
67 Sengupta and Ghosh, "Understanding the Extent and Evolution of Inequalities in China".

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