

## **II.D.2. INSTITUTIONS AND POLICIES**

In this section we review proposals for governing institutions and policies that would allow the elements of Scenario 3 to be achieved under conditions of continued globalization. We address three topics. The first concerns global economic management, that is, our ability to ensure that global economic fluctuations are kept within acceptable levels. The second concerns ecological integrity: what institutions and policies will allow ecological problems to be successfully addressed under conditions of globalization? The third concerns distributive equity: what institutions and policies will ensure that economic inequality within countries will not exceed the levels seen in the mature industrial countries of the present time?<sup>1</sup>

### ***II.D.2.a. Global Economic Management***

The destabilizing potential of large, unregulated global currency and financial markets is widely acknowledged. Many authorities recognize the need for collective institutions and policies to ensure adherence to sound standards and practices on the part of firms and countries alike, and to provide assistance in times of emergency.<sup>2</sup> During any given episode of instability national leaders blame greedy speculators, who in turn blame deficit-prone national leaders. But there is a strong mutual self-interest in reaching agreements about policies and institutions that can ensure global financial stability. Some propose a return to fixed or semi-fixed exchange rates, perhaps modeled on the European Monetary System (EMS). Greider (1997) proposes “tighter terms of credit, tighter requirements for purchasing bonds and other financial instruments on borrowed money, restriction of the use of derivatives to the genuine market hedging needs of multinational commerce, and ceilings on some interest rates to curb reckless borrowing.”

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<sup>1</sup> A fourth topic of concern is the governance of technologies of profound consequence. For convenience this is discussed in Section II.E.

<sup>2</sup> See Soros (1998), Kapstein (1996) and Simai (1994).

An increasingly noted proposal for reducing foreign exchange fluctuations due to speculation is that a tax be levied on short-term currency transactions. Known as the “Tobin tax” (see **IID-11**), this tax would be set at very low levels so that it would be negligible for transactions used to make long-term investments or finance conventional commercial transactions, but its burden would rise steeply as the cycling periods became increasingly smaller.<sup>3</sup> (The Tobin tax is also a potential major revenue source, as described in IID-11 and discussed in Section IID.4.a below.)

Beyond currency and financial controls, the long-term stability of a growing, globalizing market economy requires regulation of trade, investment and other macroeconomic flows. The conclusion of the Uruguay Round of GATT and the creation of the WTO demonstrates the practicability of such regimes with respect to trade. In 1998 the OECD attempted to secure approval of the Multilateral Agreement on Investment described in **IID-12**. This effort stalled after protest from NGO’s and others, but corporations, governments and multi-lateral institutions remain committed to the goals of the MAI. The WTO, in particular, has begun preparations for negotiations over global standards and policies concerning investment. Hirst and Thompson list a full roster of policies and institutions that they suggest can practicably be employed to ensure global economic stability, as shown in **IID-13**.

I cite the IMF, WTO and MAI as examples of our ability to construct governance regimes of the scope and scale needed to successfully ensure global economic stability, not to suggest that the current programs of these institutions will do so, or to defend their programs in other regards.

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<sup>3</sup> The Tobin tax is named after Nobel-laureate economist James Tobin, who first proposed it in 1972.

**BOX IID-11. THE TOBIN TAX**

The Tobin tax is a percentage levy on foreign exchange transactions. If set at low rates it would have a negligible effect on currency transactions used for trade and investment, but could strongly penalize the short term exchanges that characterize speculative strategies, and thus reduce exchange rate volatility. The high volume of foreign exchange transactions means that even low taxes would generate large revenues.

**volatility reduction** Let the domestic rate of return per year =  $i$ , the foreign rate =  $i^*$ , the Tobin tax =  $t$ , and the duration of the investment, in years or portions of a year, =  $y$ . Returns on domestic and foreign investments are equalized when:

$$(1) \quad (1 + i^*y) (1-t) - t = 1 + iy, \quad \text{or}$$

$$(2) \quad i^* = (i + 2t/y) / (1-t)$$

Plugging in, we see that with a domestic rate of return of 10% and a Tobin tax of 0.10% , the return would need to be 10.1% on a foreign investment of 2 years, 11.2% on an investment of 2 months, 15.2% on an investment of 2 weeks, and 46.5% on an investment of 2 days.

By increasing the cost of short round-trip transactions, the Tobin tax reduces the proportion of “speculators”, i.e., those who expect exchange rates to diverge from their long-run equilibrium. Frankel (1996:41) shows that if the proportion of speculators declines with respect to the proportion of “investors” --those who expect exchange rates to regress *towards* their long-run equilibrium--then the volatility of exchange rates can be expected to decrease.

**bases, rates and revenues** Foreign currency exchanges totaled \$1.3 trillion per day in 1995. Of this amount 80% involved round-trips of 7 days or less. After accounting for possible changes in the volume of transactions due to the tax, Felix and Sau (1996: 223) give these revenue estimates:

<u>Tobin tax rate</u>	<u>total revenues</u>
0.05%	\$ 90 billion
0.10%	\$ 148 billion
0.25%	\$ 290 billion

**tax evasion** Traders may seek to evade a Tobin tax by moving their trading sites to countries that have not agreed to abide by the provisions of the tax. The best way to prevent this is to push for as near a universal agreement to participate as possible. If this is not possible participating states can agree to impose a stiff surtax on any trades made in a non-participating jurisdiction.

Traders may also seek to replace currency transactions with near-substitutes, such as currency futures, forwards, swaps and options. Most analysts assume that some of these instruments would need to be taxed but have different opinions about how difficult this would be.

The tax rate chosen has an important bearing on the amount of evasion. Some authors estimate that if the tax is 0.10% or lower, evasion will not be worth the effort.

[more...]

BOX IID-11. The Tobin tax (cont.)

**major devaluations** The Tobin tax should dampen general volatility but will not be able to stop speculation if traders suspect that a country has so mismanaged its finances that a major devaluation, say of 15% or more, is in store. The Tobin tax dampens a speculative “build up” and gives a country time to adjust its policies to forestall a major devaluation.

**administration** Banks, which provide most foreign exchange, could either add the amount of the tax to each customer bill or absorb it. Most authors suggest that the tax be collected at the site of the transaction by each national government. The government would keep an agreed upon portion and forward the balance to an international agency for use or redistribution.

After the basics of a Tobin tax have been agreed to by treaty, an international body would be needed to 1) draft a tax code; 2) interpret and amend the code thereafter; and 3) collect and administer revenues earmarked for international purposes. Some authors suggest the IMF but others prefer a new, independent agency. A weighted voting rule would be needed to gain the support of countries with large foreign exchange markets.

**distribution of the proceeds** Kaul and Lagmore (1996:257) estimate that a 0.10% Tobin tax levied in 1995 would have generated \$148 billion in revenues, from the UK (29.5% of total revenues, or \$44 billion), USA (15.5%), Japan (10.2%), Singapore (7%), Hong Kong (6%), and some other European countries. Industrial countries would have generated 85% of total revenues and developing countries (including Singapore and Hong Kong), about 14%.

However, we saw that to be effective the Tobin tax would need to be universal. Developing countries would be able to bargain for a larger share of the proceeds in return for their support. Kaul and Lagmore suggest a distribution formula in which:

- \* low and middle level income developing countries would retain 100% of proceeds
- \* higher-middle-income developing countries could retain 90% of proceeds
- \* high-income countries could retain 80% of the proceeds
- \* remaining proceeds are used for “global commons” purposes

Kaul and Lagmore estimate that under this formula the Tobin tax would have generated \$27 billion per year for global commons purposes in 1995.

**reservations about the Tobin tax** Analysts skeptical about the Tobin say that:

- \* “Rocket engineers” could devise sophisticated market derivative instruments to evade the Tobin tax, reduce the tax base and decrease its effectiveness.
- \* The political challenge of getting all nations to agree on a program for levying, collecting and administering such huge amounts of money could be prohibitively difficult.
- \* Exchange rate volatility would not be a problem if governments simply followed prudent fiscal and monetary policies.
- \* Global commons needs can be adequately provided for from conventional funding sources.

**BOX IID-12. OECD Multilateral Agreement on Investment (MAI)**

[source: Preamble Center for Public Policy (1997) ]

The purpose of the MAI is to remove obstacles to the further integration of the global economy. The agreement limits the ability of national and subnational governments to restrict foreign investment, and to otherwise regulate both foreign and domestic firms within its boundaries. Key provisions include:

\* **National Treatment** Countries cannot take actions that have the effect of putting foreign investments at a disadvantage relative to domestic ones. For example, countries could not require that foreign firms hire a certain percentage of managers locally.

\* **Most Favored Nation (MFN)** Countries are required to treat all foreign countries and investors the same with respect to regulatory laws. This provision would prohibit, for example, national boycotts of goods produced by a country charged with human rights violations

\* **Performance Requirements** Laws that require investors to meet certain conditions if they want to establish an enterprise in a particular locale or if they want to be eligible for tax incentives or other government aid would be prohibited. This would include, for example, state laws that require local financial firms to invest a percentage of their assets in the community.

\* **Compensation for Expropriated Assets** Countries would be required to compensate foreign firms for expropriated assets. This is not controversial. However, the provision may be interpreted to include as “expropriation” any policy that reduces a firm’s profits from what they might otherwise have been, e.g., anti-pollution laws.

\* **Repatriation of Profits** Countries would not be able to prohibit or restrict an investor from moving profits from the operation or sale of a local enterprise, or any other assets, to the investor’s home country.

\* **Investor-to-state Dispute Resolution** International investors and firms would have the right to sue national governments, and to seek monetary compensation, in the event that they believe a law or policy violates investor rights. They would have the option to have the case heard by an international tribunal rather than in the countries’ domestic courts.

\* **“Roll-back” and “Standstill” Provisions** Countries would be required to eliminate any federal, state or local laws that might violate MAI provisions, and to refrain from passing such laws in the future. Country-specific exemptions may be provided for in the final MAI treaty.

\* The MAI does not currently contain provisions concerning the responsibilities of firms regarding fair compensation, treatment of employees, environmental protection, and other concerns.

**BOX IID-13. GLOBAL ECONOMIC GOVERNANCE**

Hirst and Thompson (1996) review the prospects for economic governance under conditions of globalization and conclude that "...there are good economic grounds for believing that the international economy is by no means ungovernable..." They offer this menu of practicable governance mechanisms:

1. Governance through agreement between the major advanced states, and particularly the G3 (Europe, Japan and North America), to stabilize exchange rates, to coordinate fiscal and monetary policies, and to cooperate in limiting speculative short-term financial transactions.
2. Governance through a substantial number of states creating international regulatory agencies for some specific dimension of economic activity, such as the WTO to police the GATT settlement, or possible authorities to police foreign direct investment and common environmental standards.
3. Governance of large economic areas by trade and investment blocs such as the EU or NAFTA. Both are large enough to pursue social and environmental objectives in a way that medium-sized nation-states may not be able to do independently, enforcing high standards in labor market policies or forms of social protection. The blocs are big enough markets in themselves to stand against global pressures if they so choose.
4. Governance through national-level policies that balance cooperation and competition between firms and the major social interests, producing quasi-voluntary economic coordination and assistance in providing key inputs such as R&D, the regulation of industrial finance, international marketing, information and export guarantees and training, thereby enhancing national economic performance and promoting industries located in the national territory.
5. Governance through regional-level policies of providing collective services to industrial districts, augmenting their international competitiveness and providing a measure of protection against external shocks.

### ***II.D.2.b. Ecological Integrity***

We saw in Section II.A that the rates and patterns of economic growth shown in Scenario 3 can likely be achieved without necessarily triggering global ecological collapse or so degrading the resource base that further growth is impaired.<sup>4</sup> However this achievement would require significant collective action on a global scale over an extended period of time. If there is reason to believe that such collective action would be difficult then our initially optimistic analysis is challenged.

Since 1970 nearly 20 major international treaties have been negotiated addressing such concerns as ocean pollution, endangered species, ozone depletion, transboundary hazardous waste movement, biological diversity, climate change, and other critical issues (see **IID-14**). Several hundred more have been negotiated addressing more narrow issues, many on a regional or bilateral basis. The effectiveness of these treaties has been mixed, but they are evidence that the simple mechanics of constructing policy regimes of global environmental governance is within the capacity of nation-states.<sup>5</sup>

In recent years new concerns have been raised about the compatibility of continued global economic growth and environmental protection. One concern is that increased economic integration and trade puts pressure on developed countries with high environmental standards to reduce them, and on developing countries to maintain low standards. Another is that environmentalists in both developed and developing countries are increasingly denied access to the processes by which policy concerning trade and the environment is decided. A third is that

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<sup>4</sup> The critical provisos are that either solar hydrogen or nuclear fusion become practicable sources of energy by about 2050, or that some other means of preventing atmospheric warming from exceeding 3.6° C be found.

<sup>5</sup> See IIASA (1995), Haas et al. (1993), and Bernauer (1995) for extended discussions of global environmental governance.

**BOX IID-14. MAJOR ENVIRONMENTAL TREATIES AND CONVENTIONS SINCE 1970**

<u>Treaty or convention</u>	<u>Date formulated</u>	<u>Number of signatories and ratifiers</u>
Wetlands of International Importance	1971	84
Prohibition of Biological and Toxic Weapons	1972	122
World Cultural and Natural Heritage	1972	120
Prevention of Marine Pollution by Dumping	1972	73
International Trade in Endangered Species	1973	111
Prevention of Pollution from Ships	1978	65
Transboundary Air Pollution (Europe)	1979	47
Conservation of Migratory Species	1979	47
Conservation of Antarctic Marine Life	1980	27
UN Law of the Sea	1982	126
Vienna Convention on the Ozone Layer	1985	103
Early Notification of Nuclear Accident	1986	80
Assistance for a Nuclear Accident	1986	82
Montreal Protocol on the Ozone Layer	1987	96
Transboundary Hazardous Waste Movement	1989	58
Convention on Biological Diversity	1992	140
Convention on Climate Change	1993	143
Kyoto Protocols on Climate Change	1997	

[*source*: World Resources Institute (1992, 1994); compiled by Sandler (1997) ]

the accelerated economic growth that greater integration and trade allows threatens to destroy important ecological resources before steps to protect them can be taken.

Berlin and Lang (1996) divide trade and environmental conflicts into five categories and offer solutions that they believe should be able meet the demands of environmentalists while enabling trade and economic growth to continue, as outlined in **IID-15**. They urge that existing and future trade regimes allow a greater responsiveness to the legitimate environmental concerns of the developed nations, and that a major financial commitment be made to assist developing nations in accelerating their acquisition of environmental protection infrastructure. They urge that a new international body be formed to provide the ongoing coordination that these efforts demand. Such a “WTO for the environment” would allow rules to be negotiated, compliance monitored, violations punished, cooperation rewarded, and more.

Like Berlin and Lang and others, Esty (1994) acknowledges that developing nations would find it costly to move rapidly towards stronger environmental protection at the same time that they desire to secure high and stable rates of conventional economic growth. He cites Maurice Strong’s estimate that developing countries will need \$625 billion per year to devote to environmental protection, restoration, and industrial ecology. Strong suggests that \$120 billion of this annual amount should be provided by the developed world.

Esty proposes as a first step that the developed countries set up a fund to enable developing countries to remedy those environmentally harmful practices that have major impacts upon the *developed* countries, either directly or indirectly. Esty suggests an initial goal of \$10 to \$20 billion annually, provided by a tax or import duty of perhaps 1/100 of 1% on global trade and capital flows.<sup>6</sup> Such a Green Tax, which is an extension of the Tobin tax discussed earlier, would be progressive (because rich countries have higher trade and capital flows), neutral in its

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<sup>6</sup> This suggestion is similar to that proposed by European Community GATT Ambassador Tran Van Think, who calls for “creation of a Solidarity Fund for the global environment, financed by a 0.25 percent levy on all imports except those of the least-developed countries.” (Esty 1994).

**BOX IID-15. TRADE AND THE ENVIRONMENT: CONFLICTS AND SOLUTIONS**

Berlin and Lang (1996) divide trade and environment conflicts into five categories and suggest ways that critical environmental concerns can be addressed without unduly restricting continued economic growth, as outlined below.

**1. Application of product standards to goods sold within a nation's borders**

*Problem:* Traders want to harmonize acceptable standards to facilitate trade. Greens, knowing that traders are less concerned about environmental protection, fear harmonization at lowest common standards.

*Proposed Solution:* So long as product standards do not discriminate in favor of domestic producers, trade law should recognize the right of nations to impose them on imports as they desire. Berlin and Lang say that Chapter 9 of NAFTA recognizes this right, but that GATT, which requires standards based on “sound science”, does not, and will generate continued conflict.

**2. The application of import restrictions on industrial goods because production processes in the exporting nation do not met the importing nation's standards**

*Problem:* Historically traders oppose letting one country restrict imports from another that has lower production standards because, they argue, countries at different stages of development put different values on the various trade-offs involved. Greens argue that citizens of developing countries are willing to allow more pollution in their production processes because market and governance failures don't allow the true price of environmental degradation to be internalized.

*Proposed Solution:* Global agreement on minimum process standards is a reasonable goal, if due allowance is made for phasing-in over time. Further, individual nations should be allowed to restrict imports whose production they feel is harmful to the global commons, so long as the country imposing the condition pays for the action with offsetting trade concessions elsewhere. Finally, nations should be allowed to require that any domestic firms relocating or developing production facilities in another country abide by process standards of the *home* country. Berlin and Lang suggest that negotiations to tighten process standards begin as existing international agreements are periodically revisited. After progress has been made on these, negotiations could begin on a case-by-case basis concerning additional practices of high global concern. Berlin and Lang state: “As this process proceeds, we believe that it will become apparent that there is a need for the creation of a counterpart of the GATT for the environment.”

**3. The role of government subsidies for pollution control equipment**

*Problem:* Governments have long used subsidies as a way to give their industries a trade advantage without having to impose tariffs, and traders have long sought to prohibit this. But in many developing countries local industries are unable to afford effective pollution-reduction technology, and if any pollution control is to happen at all it requires government

[more...]

BOX IID-15. Trade and the Environment (cont.)

subsidy. Under current GATT rules, if a government wishes to subsidize the installation of pollution-control equipment, other nations can challenge that action as an unfair practice.

*Proposed Solution:* GATT should be amended to allow subsidies for installation of pollution control and similar facilities, with the allowance graded by level of development. As industries in developing countries improve their ability to finance pollution-reduction facilities, the amount of allowable subsidy should be reduced.

**4. The special case of wildlife, forest and other renewable resources**

*Problem:* Many persons, especially though not exclusively in the US and Europe, consider wildlife, forest and other renewable resources to be “part of a common heritage,” even when the resource in question might be located wholly within one country, and thus legitimate objects of trade discrimination. Traders tend to treat products based on such resources no differently than they do industrial products.

*Proposed Solution:* Traders should agree that “wildlife, fish and plants are subject to different standards from those for industrial goods, and that bans on importation of fish and wildlife should be accepted so long as they are applied equally to domestic and foreign products.” Berlin and Lang say that article 104 of NAFTA includes such provisions, and that GATT should be amended to do so as well.

**5. The impact of trade on patterns of development and thus the environment.**

*Problem:* Even if trade agreements require environmentally sound practices for particular commodities, the impact of increased trade and the resulting economic growth will result in many second- and third-order stresses on the environment, which developing countries in particular are not yet affluent enough to prevent or mitigate.

*Proposed Solution:* A very small (e.g., ½ of 1%) duty on all imports by all countries should be agreed upon, with the revenues used to help developing countries “leapfrog” to a higher level of environmentally sound infrastructure, even as economic development proceeds at an otherwise conventional pace. If such a duty were levied on the current \$5.2 trillion of annual world trade it would generate a fund of \$26 billion

distortionary effects among countries, and too small to have any noticeable impact on trade or capital flows themselves.

Esty follows Berlin and Lang and advocates formation of a Global Environmental Organization (GEO). In order to ensure its political legitimacy among global and national publics, the GEO should employ a governance structure similar to that of the WTO, which operates on a consensus basis with an implicit understanding that the positions of the larger countries are given more weight. In addition the GEO might follow the example of the International Labor Organization (ILO) and include structured roles for business, environmental and governmental organizations.

The policy and administrative challenges facing a GEO would be great, but with agreement on substantive goals they would not be insurmountable. The creation of a GEO would indeed represent an incursion on nation-state sovereignty, but not to any extent greater than is currently the case with countries that are members of the IMF, the World Bank, or the WTO.

Some authors are not convinced that the global environmental governance regimes described by Berlin and Lang, and Esty, would be successful. They say that although such proposals are mechanically plausible, the costs that such elaborate processes impose on environmental activists, indigenous peoples, rural communities, and others who are not part of the global professional class, are prohibitive, while the multinational corporations that are primary agents of the problems at hand have effectively immediate access.<sup>7</sup>

Perhaps the most frequently offered response to this concern is to suggest that the growth of the “NGO community” or, more generally, “global civil society” will provide the necessary vehicles of participation. However, understandings of the nature and significance of “civil society” are as diverse as the understandings of “globalization.” For some authors civil society stands in opposition to governmental authoritarianism, and in fact includes and embraces the

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<sup>7</sup> See Mander and Goldsmith (1996).

institutions of neoliberal capitalism. For other authors civil society stands as a loyal opposition that keeps neoliberal capitalism from destroying itself through excess. Still others see civil society as the seed-bed of a new order that might someday succeed neoliberal capitalism.

We discuss global civil society further in Section II.D.5 below. For now we note that it is not difficult to imagine a global regime that could successfully address those environmental issues of most concern to the world's professional classes. How that regime might be made truly accountable to other constituencies is not clear. However, while this inequity is unsatisfactory from the standpoint of democratic governance, it is not obvious that this would prevent such a regime from successfully avoiding ecological catastrophe or growth-impairing resource degradation.

### **II.D.2.c. Distributional Equity – What the Data Show**

After making their case for the practicability of global economic governance under conditions of globalization (see IID-13) Hirst and Thompson go on to say,

“Such governance cannot alter the extreme inequality between [the advanced developed nations] and the rest, in terms of trade and investment, income and wealth. Unfortunately, that is not really the problem raised by the concept of globalization. The issue is not whether the world's economy is governable towards ambitious goals like promoting social justice, equality between countries and greater democratic control for the bulk of the world's people, but whether it is governable *at all*.” (p 189)

This is an amazing and telling statement. It suggests that the function of governance under globalization is reduced to the single important but limited task of maintaining the rate of growth of per capita GDP at some positive value. One may hope that this growth is equitably distributed and that desires for public goods are minimal; but if not, there is little that can be done.

Taken as it stands, the statement by Hirst and Thompson is incorrect. The issues raised by globalization are precisely those of social justice, equality, and democratic control. If increasing globalization generates social injustice and economic inequality, and undercuts the prospects for democratic governance, it is not sustainable.

### **Recent Trends and Findings**<sup>8</sup>

Economic inequality among countries declines when per capita GDP growth rates of low-income countries exceed those of high-income countries. To the extent that globalization allows developing countries greater opportunities for trade and investment, and for the acquisition of technology and human and social capital, globalization should help reduce income inequality among countries.

The table in **IID-16** shows that 48% of the world's people currently live in developing countries that are growing faster than the high-income countries. If we suppose that over the next several years the countries of the Former Soviet Union and Eastern Europe are able to attain annual rates of growth higher than the 1.9% of the high-income countries, then 70% of the world's people would be living in either high-income countries or countries that are narrowing the income gap. That leaves, however, some 30% of the world's people living in countries whose growth rates are not keeping up with those of the high-income countries. Put differently, of the people living in the developing world, 65% live in countries that are becoming more equal to the industrial North and 35% live in countries that are becoming less equal.

The situation regarding distribution of income within countries is equally mixed. As we saw in Section II.B, there is much uncertainty regarding the causes of changes in economic inequality within countries. Historically the single greatest cause of reductions in economic inequality has been the transition from an agricultural to an industrial economy. If globalization helps developing nations make this transition it should contribute to greater economic equality within countries. However, the 150-year agricultural-industrial transition made by today's developed countries was accompanied by massive expansion of a national public sector that

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<sup>8</sup> This section extends to the international arena the discussion of economic inequality in Section II.B that focused largely on the domestic United States.

provided health care, education, infrastructure, social insurance and other collective and redistributive goods. It is possible that the circumstances of 20<sup>th</sup> - 21<sup>st</sup> century globalization may

**BOX IID-16. GROWTH RATES OF COUNTRIES**  
 source: United Nations Development Program, 1997

countries	number of countries	annual per capita GDP growth rate, 1985-95	population (millions)	% of world population
High-income countries	26	1.9	902	15.9
countries w/ less than 1.9% pc GNP growth, 1985-95	54	-1.1	1208	21.3
countries w/ 1.9% pc GNP growth or greater, 1985-95	25	3.7	2754	48.5
Former Soviet Union + Eastern Europe	17	-6.9	351	6.2
figures not available	11	0.8	458	8.1
<b>totals</b>	<b>133</b>	<b>0.8</b>	<b>5673</b>	<b>100.0</b>

make the provision of such services more difficult for today's developing countries.

Alternatively, the market efficiencies and availability of advanced technologies that globalization fosters could allow persons in developing countries to acquire the human capital necessary for income growth more rapidly than in previous eras.

The economic position of the working classes of the developed nations appears to be more unambiguously threatened by globalization. However, the magnitude of this challenge is highly uncertain. Perhaps the most comprehensive recent analysis of the impact of increased economic integration on income inequality is that prepared by Cline (1997). The structure and results of his TIDE ("trade and income distribution") model are outlined in **IID-17** through **IID-20**. Cline finds that over the past twenty years increased economic integration has accounted for about 9% of the pressure that has widened the gap between skilled and unskilled wages in the United States<sup>9</sup>. In the future the disequalizing impact of integration is expected to be even less, largely due to rising skill levels in the developing countries that will reduce the comparative advantage that skilled workers in the developed countries currently hold. Further, Cline finds that because trade liberalization has already proceeded quite far, further liberalization will not have as great an impact on inequality as it has had over the past decades.<sup>10</sup> Finally, Cline's analysis reconfirms that while economic integration has worked to the disadvantage of low-skilled workers in the developed countries, it has worked to the advantage of low-skilled workers in the less developed countries.

This comparatively mild assessment of the impact of globalization on income inequality is tempered, however, by the fact that Cline's model is unable to explain nearly 60% of the increased disparity between skilled and unskilled wages in the US over the past 20 years (see IID-

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<sup>9</sup> Cline considers "economic integration" to include the effects of trade liberalization, lower transportation and communication costs, outsourcing and immigration.

<sup>10</sup> By the same token, of course, further liberalization will not provide the same gains in output growth that it has in the past.

**BOX IID-17. The TIDE [“Trade and Income Distribution Equilibrium”] Model**  
[Cline, 1997]

Equations of the model

$$(1) \quad Q_{ij} = \tau_{ij} [S_{ij}^{\gamma S_j} U_{ij}^{\gamma U_j} K_{ij}^{\gamma K_j}]$$

$$(2) \quad \tau_i = ce^{a_i + b_i t}$$

$$(3) \quad C_{ij} = Q_{ij} + M_{ij}^* - X_{ij}, \quad j = (1,3)$$

$$= Q_{ij}, \quad j = (4,5)$$

$$(4) \quad M_{ij}^* = \sum_{p=1}^n X_{pij} (1 - \lambda_{pij} - \beta_{pij}), \quad j = (1,3)$$

$$= 0, \quad j = (4,5)$$

$$(5) \quad M_{ij} = \sum_{p=1}^n X_{pij}$$

$$(6) \quad Max W = \sum_{i=1}^n W_i$$

$$(7) \quad W_i = \prod_{j=1}^5 C_{ij}^{\phi_j}$$

subject to:

$$(8a) \quad \sum_{j=1}^5 S_{ij} \leq S_i$$

$$(8b) \quad \sum_{j=1}^5 U_{ij} \leq U_i$$

$$(8c) \quad \sum_{j=1}^5 K_{ij} \leq K_i$$

$$(9) \quad -0.01Q_i \leq X_i - M_i \leq 0.01Q_i$$

$$(10a) \quad X_{ij} < 0.5Q_{ij}$$

$$(10b) \quad M_{ij}^* < 0.5C_{ij}$$

where:

Q = output (GDP)

$\tau$  = parameter of technological productivity

S = skilled labor

U = unskilled labor

K = capital

C = consumption

M = gross imports

X = exports

M\* = effective imports

B = costs of trade protection

W = well-being

i = country (1,13)

j = product sector (1,5)

p = trading partner country

a,b,c = technological productivity parameters

$\lambda$  = transportation costs

$\gamma$  = output elasticity

$\phi$  = welfare elasticity

t = year (1973 = 1, 1993=21)

**BOX IID-18. DESCRIPTION OF THE TIDE MODEL**

The TIDE model divides the world into 13 “countries” or regions: United States, Canada, European Union, Japan, rest of OECD, Mexico, rest of Latin America, China, G4 (Hong Kong, South Korea, Singapore, and Taiwan) India, rest of Asia, Eastern Europe including Russia, and rest of world.

There are five product sectors: 1. skill-intensive manufactures, 2. unskilled-intensive manufactures, 3. capital-intensive manufactures, 4. skill-intensive nontradables, and 5. unskilled-intensive nontradables.

Equation (1) shows output (GDP) as a function of skilled labor (S), unskilled labor (U), capital (K), and technological productivity ( $\tau$ ).

Equation (2) shows that technological productivity grows at constant rates that can vary for each country  $i$ , but which do not vary by type of product  $j$  within each country.

Equation (3) shows that consumption (C) of tradable goods is equal to the value of those produced domestically (Q) plus effective imports ( $M^*$ ) less exports (X). Consumption of non-tradable goods is equal to the total produced.

Equation (4) shows that for country  $i$ , the value of effective imports of a product  $j$  equals the sum of exports of that product from all other countries, less transportation costs (fraction  $\lambda$ ) and trade barrier costs (fraction  $\beta$ ). Imports of nontradable goods are zero.

Equation (5) shows that for country  $i$ , gross imports (i.e., what must be paid to acquire effective imports) of product  $j$  are equal to the sum of exports of product  $j$  from all other countries.

Equation (6) is the objective equation. In the TIDE model global well-being is maximized if each country maximizes its own well-being.

Equation (7) defines well-being as a decreasing function of consumption in which goods in all five product sectors are substitutable among one another.

Equations 8, 9 and 10 impose boundary conditions on the optimization problem.

TIDE is a static general equilibrium model. When it is run to optimize well-being it generates the optimal pattern of production and trade, i.e., levels of these such that no country could increase its well-being by increasing or decreasing them, given available factors. In addition it shows the marginal products of the factors of production, i.e., their wages and rents, under these circumstances. Cline runs the model using estimated and projected factor endowments (i.e., levels of labor, capital and technological productivity) for 1973, 1984, 1993, 2003 and 2013. He is thus able to calculate relative changes in skilled and unskilled wage levels over this period. By varying the values of the trade parameters  $\lambda$  and  $\beta$  he can estimate the impact of trade policies on the wage ratio of skilled and unskilled workers.

**BOX IID-19. Sources of the Increase in Wage Disparity in the United States**  
[percentages]<sup>1</sup>

[from Cline 1997; table 5.1]

I. 1973-93

A. Equalizing forces		
Increase of stock of skilled relative to unskilled labor		- 40
B. Unequalizing forces		97
Trade: Stolper-Samuelson effects <sup>2</sup> [3-10]	6	
lower transportation and communication costs	3	
trade liberalization	3	
Trade: outsourcing, Hicksian convergence <sup>3</sup>	1 ?	
Immigration	2	
Falling minimum wage	5	
Deunionization	3	
Skill-Biased Technological Change <sup>4</sup>	29	
Other unexplained	29	
C. Net Effect		18

II. 1993-2013

Trade: Stolper-Samuelson effects	4
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notes

1) percentages for each potential force must be chained, not simply added, to equal total unequalizing impact. Similarly, "A" and "B" must be chained to calculate "C." [i.e.  $(1 - .40) * (1 + .97) = (1.18)$  ].

2) These are the "classic" effects of trade whereby producers and consumers adjust their economic behavior based on comparative advantage.

3) Hicksian convergence refers to the theorem suggesting that as lower income countries become more productive the terms of trade will change in ways that decrease wages in high-income countries.

4) Cline's model leaves 58% of the increase in inequality unexplained. He arbitrarily divides this residual equally between "skill-biased technological change" and "other unexplained".

**BOX IID-20. SUMMARY OF CLINE'S CONCLUSIONS**

[Cline, 1997]

After a survey of the literature on trade and income distribution, and his own analysis using the TIDE model, Cline offers these conclusions:

1. The contribution of trade and immigration to rising US wage inequality has been somewhat larger than previously estimated in most of the literature<sup>1</sup>.
2. Nonetheless, the bulk of increased inequality probably arose from skill-based technological change, with additional significant contributions from the falling real minimum wage and the decline in unionization.<sup>2</sup>
3. A doubling in the ratio of US skilled (some college or more) to unskilled (high school or less) labor supply over the past two decades should have caused the skilled wage to fall sharply relative to the unskilled wage, in the absence of other factors.
4. As a result, whereas the impact of trade and immigration may have been as much as about half of the net increase in US unskilled wage inequality, these external-sector influences only contributed about one-tenth of the gross unequalizing forces on US wages<sup>3</sup>.
5. Trade liberalization in the past has probably caused little if any reduction in the absolute level of US unskilled wages, although by raising skilled wages it has contributed part of the rise in wage inequality associated with trade.
6. At least an equal part of the impact of trade was attributable to falling transportation and communications costs rather than changes in trade policy.
7. For the future, free trade under Asia-Pacific Economic Council (APEC) and the Free Trade Area of the Americas (FTAA) should not cause much change in wage inequality and is unlikely to cause absolute reduction in unskilled wages.
8. A policy of new, high protection against developing countries would cause serious losses to US skilled labor and either some loss or minimal gain to unskilled labor.

notes:

1) Cline's review of the results of past studies suggests that trade contributed about 20-30% of the recent increase in the skilled/unskilled wage ratio, while the TIDE model suggests it was near 50%. Box IID-19 shows the total of trade and immigration impacts to be  $(1.06) \times (1.01) \times (1.02) = 1.09$ , i.e., 9%, which is 50% of the overall increase of 18% (but see 3 below).

2) IID-19 shows the total impact of these three sources to be  $(1.29) \times (1.29) \times (1.05) \times (1.03) = 1.799$ . i.e., 80%.

3) That is, 9% is only about 10% of the 97% total of unequalizing forces shown in IID-19.

19). Economists have taken to attributing this unexplained portion to “skill-biased technological change.” However, as Cline notes, the evidence for this and in fact the concept itself are ambiguous. If we were to suppose that an important portion of the growth of “skill-biased technological change” was in some sense caused or encouraged by increased economic integration, or perhaps by “globalization” in its broadest senses, then the relation between globalization and increased economic inequality may be of more significance than Cline’s analysis suggests.<sup>11</sup>

In any event, Cline recognizes that even an apparently small increase in economic inequality can have large social and political consequences. He concludes his study by emphasizing that “a commitment to open trade needs to go hand in hand with a commitment to a whole array of domestic policies that help ensure that the society evolves in an equitable rather than an inequitable direction.” (p 275)

#### ***II.D.2.d. Distributional Equity – What Is To Be Done?***

Scenario 3 calls for equality of per capita GDP among countries by 2150. This is achieved through high, steady growth rates in the lower-income countries and slower growth rates in the high-income countries. Scenario 3 also calls for a stable 80:20 ratio no greater than 6.5 within all countries by 2150. What mechanisms and policies are available that would allow these goals to be achieved, under conditions of globalization?

Below we offer some comments on the challenges that these goals present. Then we summarize proposals for addressing one or more of the elements of Scenario 3. We close with comments on the proposals.

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<sup>11</sup> This is, in fact, the contention of Rodrik (1997), but he offers no further justification for it.

**i. Comments on the Equity Goals of Scenario 3**

1. Scenario 3 requires that low-income countries grow faster than high-income countries, but 35% of the developing world population lives in countries that are not even matching the high-income growth rates. A high priority needs to be given to policies and assistance that will enable these countries to achieve strong, steady economic growth.

2. In order for economic inequality between the high- and low-income countries to be eliminated within the next 150 years, Scenario 3 requires that per capita GDP annual growth rates in the high-income countries decline to and stabilize at 0.5% by 2050. Many people believe that it is unrealistic to expect this to happen. We discussed this concern in Section II.C.4 and will discuss it further in Section III, but in order to make headway with the other elements of Scenario 3 we won't address it in this section.

3. The policies needed to maintain an 80:20 ratio of 6.5 to 1 are particularly uncertain because, as noted, we are not sure what the forces of disequalization truly are and how strong they might be. Cline's analysis indicates that the disequalizing effects of trade liberalization can be expected to decrease with time, and we can see that the impact of several other sources of inequality—the lagging minimum wage and de-unionization in particular—can be significantly reduced by policy. Rough calculations using Cline's figures suggest that conventional policy tools, along with the major “natural” equalizing impact of rising skill levels in developing nations (which decreases the comparative advantage, and thus the premium, of skilled workers in developed countries) might be able to reduce the percentage increase of skilled over unskilled workers over the coming two decades to 7%, which is a marked improvement over the 18% increase of 1973-1993.<sup>12</sup> But confidence in this exercise is unwarranted because of the large

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<sup>12</sup> If we assume that the minimum wage is regularly adjusted for inflation, and that stronger labor legislation and organizing halts the disequalizing impact of deunionization, and that Stolper-Samuelson effects decline from 6% to 4%, but that all other forces remain as shown in Box IID-19, then the net unequalizing effect over the period 1993-2013 is  $(1-.40) \times (1.04) \times (1.01) \times (1.02) \times (1.29) \times (1.29) = 1.069 = 7\%$ .

uncertainty concerning the future of “skill-biased technological change” and other unknowns. Cline’s figures suggest that small changes in these factors could lead to either much greater disequalizing pressures or much greater equalizing pressures.<sup>13</sup>

In order to make at least some progress towards addressing our topic question, we posit this minimal condition, namely, that nation-states, or some other collective structures, must be able to provide public goods capable of having a distributive impact comparable to that provided by the public goods of today’s social democracies: education, health care, progressive taxation, social security, collective bargaining, a minimum wage, and the like. We don’t have to specify, at this point, the types or levels of such goods that might be required over any period of future decades. But we need to know that public goods with an equivalent distributive impact could be provided if needed—either autonomously by national governments, by national governments as part of multilateral agreements, by supranational institutions, or by other means. If it turns out that the impacts of globalization on economic inequality are mild then we won’t need to use these capabilities to a great extent. But we need to know that they would in fact be available if we are to proceed confidently to support continued globalization while holding to the goals of Scenario 3.

## **ii. Summaries of Proposals**

1. In preparation for the 1995 World Summit on Social Development, **the United Nations Development Program (UNDP)** offered an ambitious program to enhance the human and social capital of the world’s poorest populations, so as to enable them to participate thereafter in the benefits of the expanding global economy. This program is outlined in **IID-21**. Such a

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<sup>13</sup> If we make the same assumptions as in the immediately preceding exercise, but assume also that “skill-biased technological change” and “other unexplained” are each 22% more unequalizing (i.e., their impact increases from 29% to 35%), then the net unequalizing effect for 1993-2013 returns to its 1973-1993 value of 18%. If the two uncertain factors each *decrease* by 22%, (from 29% to 22.6%) then the equalizing and unequalizing forces balance and the skilled/unskilled wage ratio is unchanged from 1993 to 2013.

program, if successful, would go a long way towards allowing the among-countries equity goal of Scenario 3 to be achieved. The UNDP program increases the flow of development aid, trade, and

**BOX IID-21. UNDP PROPOSAL FOR GLOBAL SOCIAL DEVELOPMENT**

[source: UNDP 1994 Human Development Report]

1. A **new world social charter**, prepared by the United Nations, in which “We the people of the world solemnly pledge... (to) take all necessary actions, nationally and globally, to reverse the present trend of widening disparities with and between nations... (and to) overcome the worst aspects of poverty in our lifetime through collective effort.” The charter would include priorities, time tables and enforcement provisions.

2. A **human development social compact**, in which all countries pledge to ensure the minimal human development requirements for their own people, and to assist the very poorest nations that are not able to do so on their own. Targets for 2005 are:

- \* universal primary education, for both girls and boys
- \* cut adult illiteracy rates in half
- \* primary health care for all, with focus on immunization of children
- \* eliminate severe malnutrition, and halve moderate malnutrition
- \* universally available family planning
- \* safe drinking water and sanitation for all.
- \* credit for all, to ensure self-employment opportunities

UNDP estimated that the cost of accomplishing these goals before 2005 would be about \$100/billion per year, an increase of \$40 billion over current spending of \$60 billion. \$32 billion would be come from developing countries (by increasing the share of current GDP going to these programs from 13% to 20%) and \$8 billion from donor countries (by increasing the proportion of all aid they give for the above human priority concerns from 7% to 20%).

3. **Mobilization of the peace dividend.** Although military spending in the industrial countries has declined by 3.6% since 1987, it has remained constant or increased in poor countries. Resolving local conflict should be made a global priority so that financial, human and social capital and resources can be freed up for peaceful development.

4. A **global human security fund.** Economic growth, globalization and uneven development have resulted in a number of major problems that impose costs on all nations, particularly on poor nations, and that can only be addressed on a global level. Treaties need to be negotiated to address:

- \* nuclear proliferation
- \* ethnic conflicts
- \* natural disasters
- \* refugee flows
- \* transmittable diseases
- \* natural resource depletion
- \* environmental pollution

Implementation of such treaties would require financial support, especially to ensure compliance by developing nations not yet able to contribute their share. UNDP estimated global human security funding needs of \$250 billion annually. They suggested three revenue sources:

[more...]

**BOX IID-21 UNEP Proposal (cont.)**

1. Peace Dividend: The 3% annual decline in military spending in the rich countries since 1987 has generated a peace dividend of \$385 billion. If the developing countries could begin a similar 3% decline they could realize a dividend of \$75 billion by 2005. If the rich countries contributed 20% of their dividend to the global human security fund, and the developing countries contributed 10%, an average of **\$14 billion/year** would be available.

2. Fees on globally important transactions or polluting emissions:

a) a Tobin tax of .05% could raise **\$150 billion/year** [see IID-11].

b) a global energy tax of \$1/barrel of oil or coal equivalent could raise **\$66 billion/year**.

3. Official Development Assistance: Donor countries currently contribute about 0.35% of their GDP to ODA, one-half of their .7% pledged amount. If they “restructured existing ODA and committed some new funds”, they could provide around **\$20 billion/year** to the global fund.

6. A **UN economic security council** would be created to oversee these efforts. It would have 11 permanent members from the industrial countries and 11 rotating members. All decisions would require majorities of both the industrial and the developing country members.

7. A **World Central Bank** would be created to help stabilize global economic activity, act as lender of last resort to financial institutions, calm financial markets, regulate financial institutions, and create and regulate new international liquidity. UNDP says the IMF was supposed to play this role but the industrial countries have not cooperated, and are not likely to “until a crisis forces the issue”. In the meantime UNDP believes the IMF should:

\* be allowed to issue special drawing rights, in the range of \$30-50 billion, to “help fuel world recovery at a time when... most of the world is in the grip of deflationary policies”;

\* be given more power to impose conditionality, but re-focused on promoting economic growth, employment and human development, rather than on short-run demand management;

\* acquire regulatory control over international banking activities.

9. The **World Trade Organization** rules should be modified to address environmental concerns and to liberalize exchange of labor services. Eventually the WTO should become the World Trade and Production Organization, with power to negotiate and enforce rules concerning production and technology as well.

10. A **World Anti-Monopoly Authority** should be created to ensure that TNC’s, which control 70% of world trade and dominate production, do not resort to monopolistic and restrictive practices, but rather use their considerable power for human social and economic development.

foreign direct investment going to developing countries, refocuses these flows in ways that benefit the poorest within these countries, and calls for the strengthening of the international regimes that would guide this effort. If successful, the UNEP program would reduce world poverty by 50% within a decade of its inception.

2. **Ian Robinson** (1995) acknowledges the benefits of increased trade, investment, and communications but wants to ensure their distributive equity. He notes that a “social democratic globalization” would have to:

1) neutralize social dumping pressures associated with the high levels of capital mobility that will exist in any global market economy; and

2) create new mechanisms for redistributing a substantial portion of the economic gains from globalization to those individuals and nations most in need. These would require: 1) a *social and environmental charter*, which “would set out basic worker rights and labor and environmental standards that all members of GATT, the IMF, and other international organizations would have to meet;” and 2) *structural funds*, which “would help pay for the upgrading of standards and infrastructure, and the promotion of economic development in depressed regions.”

Robinson suggests that a minimal social charter would protect just four basic worker rights:

- 1) the right to organize unions that members control democratically;
- 2) the right to engage in collective bargaining and to strike;
- 3) freedom from forced labor for prisoners and children; and
- 4) freedom from discrimination in hiring, promotion or remuneration.

To provide structural funds Robinson proposes a Tobin tax of 0.5 percent, which would yield about \$1.5 trillion in annual revenues.<sup>14</sup> For a decade or so these funds would be used to

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<sup>14</sup> Note that this rate and yield is very much higher than the levels considered practical by the authors cited in Box IID-11.

eliminate developing country debt. After that time funds would be disbursed on a per capita basis to all qualifying countries for restricted uses, such as universal public education and health care.

To qualify for their share of structural funds governments would have to:

- 1) respect and protect the four basic labor rights of social charter; and
- 2) be democracies.

Robinson sees little support at this time among national governments for his package of social democratic reforms, although he notes some interest from France and the EU. Therefore, he believes, the task at hand is less to advance this package programmatically than it is to:

“[D]emonstrate to democratic publics that the neoliberal form of globalization is not natural, inevitable, or desirable. Success in this regard will undercut the hegemony that neoliberal economic ideas currently enjoy. Putting a simple yet radical alternative form of globalization on the political agenda weakens their standard argument: ‘There is no alternative’.” (p 379)

3. **Hirst and Thompson** (1996) consider the mechanisms necessary to address distributional equity concerns both among and within countries. Regarding the former they focus on the small levels of foreign direct investment that finds its way to the poorest countries. They note that much of the Uruguay Round of the GATT dealt less with trade per se than it did with FDI, including TRIMS (trade-related investment measures) and TRIPS (trade-related aspects of intellectual property rights), thus confirming the legitimacy of investment regulations as a multilateral concern. They propose a general agreement on international investment (GAI) which would:

- 1) define, codify and guarantee property rights of multinational corporations regarding FDI;
- 2) protect the rights of labor and conditions of work;
- 3) recognize the rights of governments to defend certain of their legitimate national economic functions, including support for R&D, defense considerations, and balance of payments issues;
- 4) establish binding protocols on taxation of multinational corporations;
- 5) establish a disputes mechanism that would be written into international law;
- 6) strengthen existing protocols on the environment.

They see little active support for such a comprehensive agreement at this time, and suggest two more modest initiatives as interim efforts:

1) The Triad (US, EU and Japan), which accounts for 75% of FDI, could agree on the treatment of FDI within their own borders, and of FDI in developing countries by companies over which they have influence.

2) Separate agreements on key topics, such as taxation and transnational corporation property rights, could be negotiated among a larger number of countries.

In order for nation-states to address equity concerns within their own borders, Hirst and Thompson identify three requirements:

- 1) the state must construct a *distributional coalition* that agrees upon a sustainable program of national income and expenditure, the major provisions of which would specify:
  - i) the division of national income between consumption and investment;
  - ii) the level of taxation necessary to sustain state investment in infrastructure;
  - iii) training and other collective services for industry;
  - iv) a framework for controlling wage settlements, the growth of credit, and levels of dividends such that inflation is kept within internationally tolerable limits;
- 2) the state must support a *political culture* that balances collaboration and competition and in which the major interests are accustomed to bargaining over national economic goals; and
- 3) the state must negotiate a workable *distribution of fiscal resources and regulatory authority* among its national, regional and municipal levels of government.

4. **Luard** (1990) states that “politics is basically about disparities of income, wealth, influence and power” and thus “the inequality of nations drives global politics.” However, he’s skeptical of the practicability of the more ambitious proposals to address distributional equity. He offers a set of more moderate trade policy reforms that, he believes, “could simultaneously work to increase growth in low-income countries, and work to benefit lower income sectors in those countries” (pp 133-135). He proposes that:

a. Changes be made in the GATT to reduce protection of agricultural products. These provisions hurt rural populations in developing countries, whereas the current emphasis on

reducing protection of manufactured goods benefits mostly the better-off urban populations in those countries.

b. Declines in commodity prices be compensated for at higher levels than are currently provided by the IMF and EEC. Luard says that this is far more efficient than assistance to producers through “commodity schemes.”

c. When quantitative trade restrictions are imposed, larger quotas be allowed to the 40 or so poorest developing nations.

d. More attention be given to activities of those development agencies, such as Tradecraft and OXFAM, that specialize in buying handicrafts and other products from the rural poor in developing countries.

e. The IMF, and creditor countries in general, extend conditionality to include a “...commitment to policies aiming at a better distribution of income.” This reassurance to the poorest, including the urban poor, would help gain acceptance of other, necessary but painful, conditionality requirements.

f. UNESCO programs be reformed to benefit the poorest in the poor countries. For example, “assistance for irrigation works can be of a kind which brings benefits to poor peasants rather than wealthy landlords.”

g. Technical assistance focus on raising the skills of rural agricultural workers rather than of urban industrial workers.

h. Medical assistance focus on basic care in rural areas rather than expensive hospitals in the capital city.

i. Priority should be given to assisting landless peasants to organize to protect their interests, rather than, say, to assisting urban workers in the formation of western-style trade unions.

Luard sees little active support for most of these reforms at this time. He suggests that in future years the most disadvantaged in the poorest countries will constitute a large percentage of

migrating populations. This will motivate concern within the developed nations, and will establish transnational capabilities that poor countries will be able to use to exert pressure for reforms.

5. Earlier we noted the critique of globalization offered by **Rodrik** (1997). What does he suggest be done to avoid the “solidifying of a new set of class divisions”? His proposals fall into two categories. The first are income generation and distribution measures. These include recommendations that a global tax on “foot-loose factors” (i.e., portfolio and investment capital) be considered, with the proceeds shared among countries; that national governments explore ways to enhance social insurance within existing levels of spending, so as to avoid budget deficits;<sup>15</sup> and that an international convention to restrict the ability of firms to avoid taxes through foreign investment be negotiated.

Rodrik’s second set of proposals are trade and “social tension” measures. On the one hand, he says, “we need international institutions that must encourage greater convergence of policy and standards (‘deep integration’) among willing countries, in order to help reduce tensions arising from differences in national practices.” On the other, he says room must be made “for selective disengagement from multilateral disciplines, under well-specified contingencies, for countries that need breathing room to satisfy domestic requirements that are in conflict with liberalizing trends.”

6. **Greider** (1997) argues for a global commitment to “shift returns from capital to labor, reversing the maldistribution of incomes generated by the marketplace under the *rentier* system.”

He says the key features of such a new world order would include:

1. *taxation of capital* rather than labor;
2. *reforming the terms of trade* to ensure more balanced flows of commerce, compelling exporting nations to become larger consumers of global production. Nations that run large trade surpluses would be punished with temporary trade barriers.

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<sup>15</sup> He suggests shifting the composition of income transfers from “old-age insurance” and other entitlements to labor-market risk insurance (i.e., unemployment compensation, trade adjustment assistance, and training).

3. **raising wages** on the low end as rapidly as possible, by requiring trading nations to honor labor rights.
  4. a general **write-off of the bad debts** of the poor nations.
  5. reforming the objectives of **the central banks** to support a pro-growth regime that will allow a reflation of wage incomes. “Central banks must learn to take some risks on the upside, instead of worrying about inflation.”
  6. refocusing national economic **policy on raising wages**: raising minimum wages, strengthening labor laws, reducing tax breaks and subsidies for corporations, and underwriting high-speed rail systems, urban housing rehabilitation and childcare.
7. **Bello** (1998), arguing from the perspective of the Global South offers a critique of the “failed Asian model” and calls for a new developmental agenda characterized by “negotiated and selective integration” with the global economy. Its themes include:

1. A **Tobin tax** to control disruptive speculative capital flows;
2. **Progressive income taxes** to support national investment, and democratic management of this investment to avoid speculative gambles by corrupt, nepotistic politicians and financial elites;
3. Completion of “the unfinished social justice agenda of the progressive movement in Asia,” notably **land and asset reform**, to bring the still very large marginalized populations of the region into the market, with the wherewithal to compete successfully;
4. A fundamental economic mechanism that is “more rational than the invisible hand of the market”, yet avoids the failings of both “the heavy hand of socialism” and “the interventionist hand of the Asian model”. Bello believes the new mechanism “must be **democratic decision-making** by communities, civic organizations and people’s movements. The challenge is how to operationalize such institutions of economic democracy.”
5. A commitment to **ecological sustainability**. Bello says, “Instead of 8 to 10 percent [growth] rates, many environmentalists speak of rates of 3 to 4 percent.” He says that slower growth rates would simultaneously lessen ecological damage and force attention to the imbalances of wealth and power in Asian society. Higher growth rates, Bello says, allow the elites to take the greatest share while permitting the incomes of the masses to grow just enough to avoid political unrest.

Bello concludes, “These ideas and others remain to be welded into a coherent strategy, and that strategy in turn awaits a mass movement to carry it.”(pp 16-21)

8. Analysts who are skeptical of the desirability or political practicality of the sorts of structural reforms or redistributive measures outlined above have only a few credible options available with which to address problems of distributional equity under globalization. The most

widely embraced of these is education and training. **Mandle** (1997), arguing from the social-democratic left, says that for all their obvious flaws, globalization and technology, if guided properly and made inclusive, have the potential to make dramatic inroads against poverty, malnutrition, illness and ignorance. He says that the “anti-trade left” is “silent on the question of how, in the absence of trade, wages in poor countries could be increased over the long-run.” Mandle acknowledges that some US workers will be disadvantaged by more open trade and globalization, but replies that the answer is not to stop trade but to shift those workers to industries where the US has the comparative advantage. He is forthright in acknowledging that this will require more and better education, training, retraining, and other support. He goes on to say that,

“The real danger lurking in the liberal anti-trade position is that it concedes precisely what we have to fight for: a supportive government committed to advancing the productive skills of the labor force and offering an adequate safety net for those who confront difficulty in the highly competitive world economy. Aside from the impossibly high price tag associated with such a strategy, this strategy turns its back on the legitimate interests of the poor in other, less-developed nations. ... Rather than pitting the poor of the developed world against the poor of the third world, as protectionism does, we should be prepared to continue to fight for economic justice everywhere.” (p 12)

Mandle supports limits on trade in goods produced with child labor, goods produced under demonstrably unsafe working conditions, and goods produced in violation of internationally negotiated environmental protections. But he believes that the only ultimately effective path is to “...make certain our workers can compete at the highest levels of productivity.”

9. In a similar vein **Reich** (1991) presents a set of policies designed to bolster the earnings power of workers in the developed countries without resorting to across-the-board trade barriers. He stresses the important point that it is in the long run interest of workers in the developed countries to help enhance, not retard, the economic development of poor countries. His program of “positive economic nationalism” calls for developed countries to:

1) *eschew governmental barriers to trade*, money, and ideas, but allow focused governmental intervention designed to *enhance training, skills, and education*.

2) consider *public subsidies to firms that undertake high-valued production* within the nation's borders. To prevent unproductive competition among nations in this regard, a "GATT for investment" would need to be negotiated. Its provisions would include appropriate levels and targets for focused subsidies, rules defining fair tactics, and a prohibition on threats to close domestic markets, unless compensating investments are made. Reich suggests that "the amount of a permissible subsidy might be directly proportional to the size of a nation's work force but inversely proportional to its average skills. Nations with large and relatively unskilled work forces would be allowed greater leeway in bidding for global investment than nations with smaller and more highly skilled work forces." (p. 313)

4) support the *pooling and allocation of subsidies to sectors where they could do the most good*, as the European Community has begun to do regionally for major R&D efforts.

5) *ease the transition of workers out of old industries* and technologies, using "severance payments, relocation assistance, extra training grants, extra unemployment insurance, regional economic aid, and funds for retooling or upgrading machinery. Since every nation benefits when overcapacity anywhere is reduced, these subsidies might come from a common fund established jointly by all nations."

6) seek to *develop the capacities of the work forces of the Third World*, "as a means of promoting indigenous development and thereby enhancing global wealth. To this end, the shift of high-volume, standardized production to Third World nations would be welcomed, and markets in advanced nations would be open to them."

### iii. Comments on the Proposals

1. The UNDP proposal is the most ambitious of the proposals surveyed. If implemented it would mean a 67% increase in annual bilateral aid (from \$60 billion to \$100 billion) and a nearly 5000% increase in the funds administered by the development agencies of the UN (from \$5 billion to \$250 billion.) The numbers invite skepticism, and indeed, the 1995 UN World Summit on Social Development, for which the UNDP proposals were prepared, passed with little notice. But it is difficult to deny that the conditions described in the human development social compact (item #2 in IID-21) will in fact need to be achieved if the poorest 30% of the world's people are to become part of the global economy. Further, these conditions—better education, health care and sanitation—are precisely the sort that have been addressed by the public sector, rather than the market, in the history of economic development in the West. The burden appears to rest on skeptics to show how the needed results can be achieved in ways that don't require focused collective attention and support.

Skeptics might dismiss the \$250 billion “human security fund” proposed by UNDP (item #4 in IID-21) as a thinly-veiled subsidy program for inefficient developing country bureaucracies. But careful consideration of the major problems listed in item #4 suggests that at least the premises of UNDP’s proposal are sound. The problems listed appear in the most immediate instance to be caused by underdevelopment and poverty, yet they impose hardships on both the developed and the developing world. The poorest nations, especially, simply do not have the resources needed to address these problems. Thus if the North wants to see real results, it is going to have to make more of a commitment to assisting the developing countries.

The stated intent of the UNDP proposal is to encourage the vitality of market economies in the developing world and their integration into the larger global market economy. This stands in contrast to similar ambitious UN proposals of two decades ago, notably those intended to establish the New International Economic Order (NIEO), which were intended as challenges to market capitalism.

2. Ian Robinson highlights the two measures most often called for in the proposals reviewed. One is the inclusion of labor rights and standards in international economic agreements. The other is a source of funds to provide assistance that markets cannot be expected to provide.

The real impact of labor rights and standards on incomes, growth and equity depends on many more factors than we can review in these notes. For now I’m going to assume that there exists a regime of such rights and standards that will be acceptable to labor and capital in both the developed and the developing world, and that will not significantly impede continued economic growth and integration. The existence of such rights and standards can have an important impact on particular sectors of the labor force, but, as our review in Part II-E suggested, does not have a large direct impact on aggregate levels of inequality. However, rights and standards can be of indirect benefit by helping empower a labor constituency that can influence other policies that might reduce inequality.

The real impact of the Tobin tax is likewise difficult to assess. If we take the high-middle estimate of \$150 billion in annual revenues suggested by Felix and Sau, and re-distribute it on a per capita basis as suggested by Robinson, we find that the Tobin tax generates revenues of about \$25/year per person. For the 75% of the world's population who live in the 49 poorest of the world's countries, and whose mean per capita income is \$430, this amount would represent an annual income increase just under 6% (i.e., \$430 to \$455). On the other hand, Tobin tax revenues would represent a very large supplement to the national budgets of most developing countries. For example, Kenya and Nicaragua would receive per capita Tobin revenues totaling \$640 million and \$94 million, respectively, which in both cases is nearly 25% of their current national budgets. Alternatively, if the Tobin tax were used to support global commons initiatives, its real impact on poverty, growth, and equity would depend on many complex factors.

3. Rodrik warns that globalization may cause “the solidifying of a new set of class divisions, but his proposals to prevent this seem inadequate. Regarding trade he recommends only that greater efforts be made to achieve convergence of standards, and that more allowance be made for “selective disengagement” where national differences appear particularly acute. These policies would allow the advocates of global economic integration to placate the minimum number of aggrieved constituencies necessary in order to prevent the formation of a broad-based anti-trade coalition. The two tax measures Rodrik recommends are worthy but he does not provide details on rates and estimated potential yields.

4. Greider's package of reforms largely derive from two, somewhat contradictory, understandings of the nature of the global economic problem. On the one hand Greider asserts that economic growth is too slow. This is because bankers have a self-interest in ensuring that high demand does not generate inflationary pressures that decrease the value of their outstanding loans. Thus they unduly restrict credit that could otherwise support growth, new jobs and higher wages. On the other hand Greider asserts that economic growth is, in a sense, too fast. This is because technology and liberalized trade are allowing more and more goods to be produced by

lower and lower paid workers. This will generate a glut, which will lead to a global depression. In order to address the first problem Greider calls for inflationary monetary policies (item #5). In order to address the second problem he calls for constraints on trade, and on other measures that raise the wages of lower income workers.

Both Rodrik (1997) and Krugman (1997) have criticized Greider's analysis. Bankers are as pro-growth as any capitalists; inflation feeds on itself and high inflation is no friend of the working classes. The "global glut" argument is valid only if the real marginal propensity to consume declines as income increases, but despite the intuitive reasonableness of this assumption the evidence for it is thin.

Greider's six proposed measures, if implemented very cautiously, could—separately and together—move the levels and distributions of income in a more equitable direction, but not by great magnitudes. On the other hand if they were implemented aggressively enough to have a more appreciable equity impact, they would likely be seriously destabilizing.

5. Bello's call for progressive taxes and land and asset reform is central to any program of growth and equity in developing countries, and of proven efficacy. But Bello is also looking for something more, for a "fourth way" beyond neoliberal capitalism, state capitalism and state socialism. He calls for the development of economic democracy rooted in local communities, and for slower, more ecologically sensitive economic growth in the South. Skeptics can dismiss this orientation as pastoralist or escapist, and as we saw in Section II.C.1, often with good reason. But the growth and equity goals of Scenario 3 can in fact be achieved with per capita GDP growth rates in the developing countries of as "low" as 4%-5%, provided these are maintained over several decades.

6. Mandle and Reich distinguish themselves from the other authors reviewed in arguing that greater trade liberalization and economic integration can work to the benefit of workers in the developed world, if accompanied by a commitment to training and education. This stance is attractive because it holds out the prospect that the interests of workers in the developed and the

developing world need not, in fact, be at odds. We saw in Section II.B.3 that Reich's proposals for training and education did not hold great promise of significantly reducing aggregate economic inequality in the United States. However, Scenario 3 only seeks to guarantee that inequality *becomes no worse*, in which case training and education may be able to play a more critical role. The remaining uncertainty, of course, concerns the extent to which skill-biased technological change is encouraged by the process of globalization.

### ***II.D.2.e. Assessment and Next Steps***

In this section we reviewed proposals for governing institutions and policies that might allow us to achieve the goals of Scenario 3 under conditions of globalization. Proposals exist for practicable institutions and policies that could allow a growing, globalizing, market economy to be managed in a way that keeps financial, trade and investment fluctuations within some safe range. Proposals also exist for institutions and policies that could address environmental concerns in a way that allows economic output to grow at the rates and to the levels desired in Scenario 3.

There also appear to be institutions and policies that could enable those developing countries whose growth rates are below those of the high-income countries to grow faster. But the magnitude of this challenge needs to be acknowledged.

Our assessment concerning institutions and policies by which we might keep economic inequality from increasing is more ambiguous.<sup>16</sup> On the positive side we note that the direct contribution that economic integration makes to inequality appears to be moderate, and is expected to decrease. On the negative side we note that the single largest suspected cause of increased economic inequality--"skill-biased technological change"--is in fact not well understood, and it is not impossible that some aspects of globalization may contribute to it. Our

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<sup>16</sup> These comments draw on material covered in Sections II.B and II.C as well as in this section.

review identified many governing institutions and policies that are mechanically practicable and could be expected to encourage greater economic equality. If the disequalizing forces of globalization turn out to be mild, we might be cautiously optimistic about the ability of the programs described above to offset these. If disequalizing forces turn out to be strong they will pose a major challenge to continued economic globalization, and to our chances for realizing Scenario 3.

*Next steps*

The existence of reasonable institutional and policy blueprints is a necessary but not a sufficient condition for Scenario 3 to be credible. The financial, environmental and distributive policies just reviewed presume the existence of healthy nation-states, or other structures of governance in some manner accountable to nation-states, that are able to successfully craft and administer complex global public good regimes. They also presume the existence and continuity over time of a majority socio-political ethos that affirms the humanitarian and solidaristic values of Scenario 3.

What impact might globalization have on the viability of the nation-state? Does globalization encourage or discourage solidaristic social norms and values? These critical questions are addressed in the next section.