Shaping the Social Dimension of Globalisation

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I. Introduction

- ***Ministers and distinguished guests,*** I would like to thank you for this invitation to address you today. It is an honor to be here.

- ***I have been asked to speak about the social dimensions of globalization in the developing world and in particular about its implications for social protection.*** To effectively address this issue I would like to place it within the broader context of the opportunities and risks that globalization presents developing countries and their related need to manage it quite closely.

- ***Following a brief overview*** of the main opportunities and risks globalization poses for developing countries, I will highlight the main priorities facing developing countries in managing globalization, and then turn to what we each can do to help developing countries take full advantage of globalization and avoid its downside risks.

- ***Globalization is good for prosperity.*** Globalization is a positive sum game in the aggregate for both developed and developing countries, but it produces both winners and losers. It is strongly associated with successful developers as seen in the experiences of China, Bangladesh and Vietnam, which have achieved 7% plus growth for a decade or more.[1][2]

- ***But to understand what drives the globalization debate is to be aware of who benefits and loses both across countries and within countries.*** Globalization and skill biased technological change have been linked to rising inequality in the developing world. In China, the bottom 10% of the income distribution has seen

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[1] Evidence from Chinese provinces, Indian states, and the countries of Bangladesh and Vietnam shows conclude that the 'new globalizers' have experienced large-scale poverty reduction: during the 1990s the number of their people who were poor declined by 120 million. World Bank. 2002. Globalization, Growth, and Poverty. Building an inclusive world economy.

[2] India's opening up to foreign investment has been associated with a fall in poverty. In Zambia, poor consumers benefit from lower prices of the goods they buy, while poor producers benefit from trade reform through the higher prices they receive for their goods. Colombia's increased export activities are associated with better compliance with labor legislation, as well as a fall in poverty. In Mexico, the poor in the most globalized regions have managed macroeconomic crisis better then their more isolated neighbors. Ann Harrison. 2006.Draft October 2005. *Globalization and Poverty* NBER Working Paper 12347.

its income rise by 42% in the past 10 years. The middle has grown by 115% and the top ten percent by 168%. These are large numbers. So is the fact that 96m Chinese have moved across the poverty line in the last decade.

- Returns to skilled labor, relative to unskilled labor, have risen dramatically and are a key factor behind this rising inequality. In Sub-Saharan Africa, returns to skilled labor were 5 times greater than for unskilled labor in 2001, a trend that can only be expected to increase.[3]

II. Four lines of action for managing globalization

- ***Governments need to manage globalization.*** Avoiding globalization is not an option for developing countries, it is inevitable and the upside benefits are too great. Managing it, however, is crucial. <u>The dual challenge is to ensure that the benefits of globalization are broadly shared and the risks properly managed.</u>

- ***Managing globalization in developing countries involves four broad and overlapping lines of action:*** (1) creating more "good" jobs; (2) helping countries to manage risks; (3) expanding opportunities for excluded groups; and (4) promoting macrostability and growth.

  - *First, the foremost problem in developing country labor markets is not unemployment, but rather the scarcity of decent jobs.* With globalization comes the expectation of more and better jobs. Expanding access to good jobs for poor workers involves labor market policies, but also complementary actions to improve the quality of the investment climate and to raise education and productivity.

    - In many countries the <u>rigidities of the formal labor markets</u> militate against new job creation. For instance, tight regulations of the formal labor market in Latin America restrict access of rural workers and the urban poor to formal income-earning jobs.[4] Some countries, like China have found pragmatic ways around the problem by sanctioning a secondary labor market that is still formal but with fewer benefits. In many parts of the world, however, very few new jobs are created each year. While policy solutions are of course context specific, the goal ought to be *sufficiently flexible labor markets* to provide incentives to firms to hire new (formal sector) workers.

    - A poor <u>investment climate</u> dissuades firms from expansion and job creation and pushes down wages because investors need a higher rate of return to enter risky markets. African countries have taken steps to improve their business climate. Senegal has become one of the most reliable suppliers of electricity in Sub-Saharan Africa, and this has been

[3] GEP 2007
[4] Kaufmann, Mastruzzi and Zavaleta, 2003 "Sustained Macroeconomic Reforms, Tepid Growth: A Governance Puzzle in Bolivia?" World Bank Policy Research Working Paper.

linked to strong employment performance in the past decade.[5] Countries need to continue their progress towards favorable investment climates that support firm expansion and job creation through lower and more predictable costs of doing business.

  - Education is strongly linked to poverty reduction through its impact on wages. In Mozambique an extra year of education raises wages by 3 percent in agricultural areas and between 5 and 15 percent in non-farm activities.[6] Governments increasingly recognize the importance of a *high quality education system* to increasing productivity, job creation and poverty reduction.

- *Second, turning to the problem of risk management, globalization has exposed developing countries to more risks* at the same time as they are coping with increased climatic and disease risks. Here, I would like to highlight the different context for social protection in developing countries, which makes it difficult for them to copy "western style" programs.

  - Developing countries tend to have a much broader concept of risk management, which exists largely outside formal social protection programs. Indeed, the most effective and realistic form of social protection in developing countries may be ex ante risk mitigation efforts, such as microfinance programs that help households diversify economic activities or flood infrastructure programs to better cope with climatic risks, or basic education programs that help individuals make employment transitions.

  - Due to the prevalence of the informal sector, social protection in developing countries should strive to transcend job categories to provide equitable benefits for all workers. As seen in Mexico and other Latin American countries, a social protection system which relies on contributions from formal sector workers incentivizes firms to remain small and informal. Social protection needs to be de-linked from employment status if it is to meet the urgent needs of the majority of the working poor.

  - The affordability of formal social protection is undoubtedly a key constraint in developing countries. It is of course unrealistic to expect most developing countries to provide a social protection system which encompasses welfare, unemployment, disability, maternity and pensions benefits, to name just a few of the common elements in most developed countries. While contribution based systems should be encouraged, their impact on incentives for formal sector employment need to be considered,

[5] Sekkel M and L Fox. 2006. "Work in progress: job creation and the quality of growth in Africa" World Bank, Working Paper.
[6] Mozambique, 2005 – Country Economic Memorandum: sustaining growth and reducing poverty

especially should there be uncertainty about the future benefit stream these programs may offer.

- *Third, I would like to emphasize again the importance of sustained high growth* for helping countries to manage globalization. East Asia benefited from phenomenal growth and poverty reduction with average per capita GDP/growth rates of almost 7% since 1990 leading to dollar a day poverty to drop dramatically from 30% in 1990 to 9% in 2004. In Africa, despite higher growth since 2000, long-term growth remains very modest over the last 15 years, with GDP/capita rising by only 0.6% per year and dollar a day poverty falling from 47 percent to 41 percent. A*s Professor Robert Solow is fond of saying, it is easier to steer a bicycle that is moving faster than one moving slowly.* Higher growth trajectories will enable developing countries to proactively deal with shocks or negative effects of globalization on the poor.

- *Fourth, an important objective in managing globalization ought to be to extend its benefits to more households, especially those which are typically excluded.* Even though globalization can be expected to expand the "global middle class" some social groups are likely to be left behind in the growth process. Nobel Laureate, Mike Spence, who is leading the Commission on Growth and Development (an independent group of policy makers organized by the Bank) has expressed the view that in all countries (developed and developing), domestic policies must and can deal with those left behind as long as the size of the pie is growing sufficiently and there are resources that can be captured to deal with economic dislocations. With strong growth rates, developing countries will be well-placed to invest in market connectivity and essential public goods so as to expand the benefits of globalization to lagging regions, depressed areas, or to previously excluded minorities.

III. What can the Bank and OECD countries do?

- **When thinking about globalization we ought to perceive it as more of an opportunity than a threat**. The growth of Chinese, Indian and other emerging markets offers enormous opportunities for developing and developed countries to increase their exports. China's imports have increased by almost 500% over the past decade and will continue to rise, with 79% of imports sourced from developing countries.[7]

    - *Growing South-South trade offers developing countries a growing market, in contrast to the relatively stagnant demand from rich countries*. Demand in Asia, and primarily China and India, has been the main source of the acceleration in African exports since 1990. Asia also has been a key source of recent export growth for Latin America. Overall, China's share of the world's non-oil imports grew from 1.8% in 1990 to 6.5% in 2004, implying

[7] Chinese imports increased 477% in value terms in the past 10 years; 79% of imports are sourced from developing countries (GEP, 2007).

substantial opportunities for its trading partners to expand exports and create jobs.

- **What can the Bank do?**
    - *Provide country specific advice on how to create more "good" jobs and how to protect workers and not jobs.* The ILO estimates that even without taking into account the growing labor force, around 1.6 billion 'good jobs' are needed for those who are currently unemployed or in bad jobs.[8]
    - *Improve knowledge and statistics on women's economic empowerment to better understand who benefits from government interventions.* Through the Gender Action Plan we plan to increase the productivity and earnings of women producers and their access to markets.
    - *Help increase the benefits of migration* for both sending and receiving countries by improving the understanding of the benefits and risks of migration, so that well-managed and well-coordinated migration policies can be put in place.
    - *Provide advice on growth strategies both with respect to maintaining macroeconomic stability and putting into place the micro foundations of growth.* Social protection is an important element of this as detailed in the background note that was distributed on "Social Protection for the Poorest: The Position and Experience of the World Bank Details."

- **What can G8 / Developed countries do?**
    - *Open markets to developing countries so that poor countries can raise their incomes and create local employment.* Negotiate preferential trade agreements for products produced predominantly in developing countries.[9]
        - Trade preferences can work if they have liberal rules of origin and are flexible. For example, AGOA's special rule for apparel led to a strong export response, with apparel exports from Kenya, Madagascar, Lesotho, and other areas of Southern Africa soaring from around \$300mn to \$1,500mn pa.
    - *Be careful in disentangling the motives for social protection.*
        - It is important to acknowledge that the promotion of workers' rights in developing countries may not always originate from concern for the workers in developing countries, but rather out of fear for 'unfair' competition from these poor workers.
        - An expansive formal social protection system increases labor costs, and is likely to maintain a large informal sector with vast

[8] The ILO estimates that in 2006, the number of unemployed worldwide was at an all time high of 195.2 million, or a global rate of 6.3 per cent. The number of people living on \$2 a day or less reached almost 1.4 billion.

[9] As is well-known, trade reform in agriculture would yield the largest welfare gains, as it is so much more distorted than other sectors and as roughly 70% of the poor in developing countries live in rural areas. At present, support to agricultural producers (including trade-distorting subsidies and market access barriers) in developed countries adds up to about \$280 billion, more than three times the level of 2005 global overseas aid.

differences between 'insiders' and 'outsiders' within particular countries.[10]

- *Scale up and improve the quality of development assistance to help countries deliver on their shared growth strategies*. In 2006, overall levels of official development assistance were down by 5.1% from 2005, a far cry from the scaling up required to meet the commitments made by the G8 in Gleneagles. But more aid is not the only issue. Improving aid coordination among the numerous donors, and the predictability of aid flows are also essential to helping developing countries make the necessary investments for sustained growth and successfully managing globalization.
- *Promote circular migration and facilitate the efficient flows of remittances to sending countries.* Circular migration maximizes the benefits and acceptance of migration for migrants, receiving countries and sending countries alike. Remittances to developing countries exceeded $160 billion in 2004, far surpassing development aid and representing the largest source of foreign exchange for some countries. And this official figure is believed to capture only part of the actual funds that migrants send home. More efficient ways to send remittances to sending countries could increase the amount of remittances sent, and the share of this amount that actually arrives at its final destination.

- ***In closing, I would like to highlight a stark contrast.*** Almost 50% of the world lives on less than 2 dollars a day – the amount we spent on our morning croissant (at least if bought it at the World Bank cafeteria). This contrast clearly highlights the global inequities of our world, but it does more than that. It also points to the tremendous potential for more trade and integration that could benefit the populations of both rich and poor countries, as well as the potential for OECD countries to support sound policies and good investments in developing countries contributing to global prosperity and a reduction in global poverty.

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[10] Together with trade clauses on environmental safeguards, social protection and labor clauses can be seen as 'disguised protectionism' originating from developed countries.