

SPREADING THE BENEFITS OF GLOBALISATION: 'SELLING' THE COMPOUNDING BENEFITS OF REFORMS

Dinner address by Dr Ken Henry
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to the
Sydney G-20 Workshop on
Globalisation, Living Standards and Inequality: Recent Progress and
Continuing Challenges

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Welcome to the official dinner of the G-20 workshop on *Globalisation, Living Standards and Inequality: Recent progress and continuing challenges*.

GLOBALISATION AT DINNER

Some might think that the only appropriate dinner for a globalisation meeting would be a McDonald's with Coke, followed later by a coffee from Starbucks.

Economic globalisation, we are told frequently, means a narrowing of cultural diversity, including culinary diversity. McDonald's, MTV, and CNN stand among the pet hates of the anti-globalisation movement.

Illustrative of those worries is the fear that the globalising trends symbolised by McDonald's will enervate or overwhelm local cuisines.

That fear seems to me to underestimate the robust diversity of human tastes, and the potential for rising incomes to enable fuller expression of those tastes. We hope tonight's exposure to an example of 'modern Australian' cuisine provides you with an enjoyable illustration of other possibilities for tomorrow's world.

Contemporary Australian cuisine is often Asian influenced, but usually founded in classical French cuisine. It uses distinctive local produce and is created by chefs who often have either worked abroad and learnt from the world's great cuisines, or are themselves among the almost 1 in 4 Australians born overseas, or more than 1 in 10 born in other G-20 economies. In 2000, prominent G-20 sources of emigration to Australia were (in descending order of migrant numbers) the UK, Italy, China, Germany, India, South Africa, Indonesia and the US.

Australians enjoy considerable culinary diversity: we have just over 700 McDonald's outlets, but over 4000 Chinese restaurants, over 2000 other Asian restaurants, and over 2500 Italian restaurants.¹ Surprisingly, only about six hundred Australian restaurants identify themselves as French, but I suspect that is simply because so many restaurants with preponderantly French culinary foundations are among the more than 10,600 who today style themselves 'modern Australian'.

Are these culinary examples an economically trivial case of diversity in the face of globalisation? Well, you may be surprised to hear that the accommodation, café and restaurant industries employ more people in Australia than our agriculture, forestry and fishing industries; more than transport and storage; more than finance and insurance; more than government administration and defence; and many, many more than the mining industry.²

Over a broader canvass than just cuisine, I suspect that wealth creation and international integration will support the widening of cultural choices, as Bollywood prospers alongside Hollywood, as Tokyo's fashions turn heads as well as Paris's fashions, as Korean industrial design in whitegoods and electronics begins to rival Japan's and Europe's, and Al-Jazeera is as readily available as CNN.³ The citizens of all our countries enjoy more options and greater freedom to shape their own cultures as a result.

Dynamic, confident and prosperous people seem more likely to integrate wider choices from all other cultures, than to narrow their choices to a single dominant culture. The contribution good economic policy can make to cultural diversity is to defeat impoverishment, and thereby increase the means, and the self-confidence, by which our peoples can express their diversity of tastes.

WELCOME TO INDIA AS G-20 CHAIR

This Workshop is the first G-20 event for 2002, and the first under India's Chairmanship of the G-20.

By way of welcoming India to that role, let me say a little about international economic governance, which can be pictured in part as a quest for balance between representativeness, and workable size.

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- 1 These estimates apply a BIS Shrapnel categorisation of restaurants by style of cuisine to an Australian Taxation Office count of the total number of restaurants registered for the purposes of the Goods and Services Tax. See <http://www.restaurantcater.asn.au/facts.asp>. On McDonald's numbers, see <http://www.mcdonalds.com.au>.
 - 2 Australian Bureau of Statistics data Wage and Salary Earners December 1999, 6248.0.
 - 3 See, for example, Vijay Mishra, *Bollywood Cinema: Temples of Desire*, Routledge 2002; Douglas McGray, 'Japan's Gross National Cool', *Foreign Policy*, May-June 2002; and broadcast details of Al-Jazeera at <http://www.almajaz.com/qatar/aljazeera/>.

Since the United Nations was founded in 1945, its membership has expanded from 51 to 189 countries. It and all other universal organisations grapple with a total membership far too large for informal discussion or prompt responses to rapid change. But on the other hand, smaller groupings generally lose the representation of the range of global experience as they gain the practicality of smaller size.

The G-20 arose from a 1999 decision by the G-7 Finance ministers to create a remarkably different and uniquely representative informal economic grouping.

The G-20's members account for almost 65 per cent of the world's population, around 70 per cent of the world's poor, and over 75 per cent of the world's economy at purchasing power parities.⁴ But perhaps as interesting as these levels of representativeness are the trends:⁵

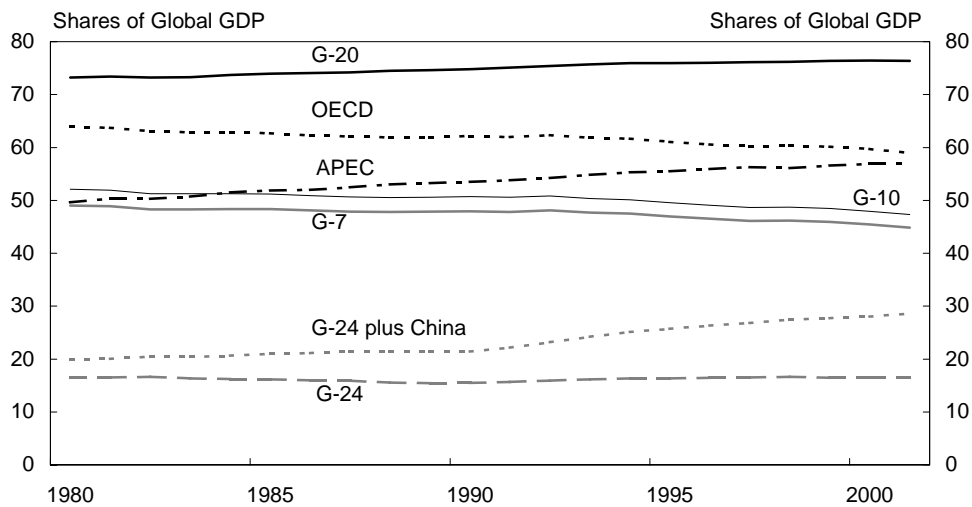
- From 1980 to 2001, the G-7's share of world GDP fell by about 4 percentage points, to just under 45 per cent.
- In the developing world, the G-24's share of world GDP has been constant over the last 20 years at almost 17 per cent, while adding China's GDP to the G-24's produces a 2001 share of world GDP of around 29 per cent.⁶
- In contrast, the G-20's share of world GDP rose about 3 percentage points from 1980 to over 75 per cent today.

4 Population figures from World Bank Atlas 2001 (data for 1999); GDP share from IMF's World Economic Outlook database, 2002; poverty headcount of those currently living on less than US\$2 per day, from the World Bank Atlas 2001 and the World Development Report 2002.

5 IMF's World Economic Outlook database, 2002, data for China do not include Hong Kong SAR.

6 The Intergovernmental Group of Twenty-Four on International Monetary Affairs is a twice-yearly meeting of Finance Ministers and Central Bank Governors on the eve of the Annual and Spring meetings of the IMF and the World Bank. Its members are Algeria, Cote d'Ivoire, Egypt, Ethiopia, Gabon, Ghana, Nigeria, South Africa, Democratic Republic of Congo, Argentina, Brazil, Colombia, Guatemala, Mexico, Peru, Trinidad and Tobago, Venezuela, India, Iran, Lebanon, Pakistan, Philippines, Sri Lanka, and Syria. China is a special invitee that can address plenary sessions.

Chart 1: International groupings' shares of world income



Source: World Economic Outlook (WEO) Database April 2002; IMF.
 Note: Data for China do not include Hong Kong SAR.

The G-20's close relationships with the IMF and World Bank help inject an influential mix of developed and emerging market experience into the operations of the international financial institutions, and ensure that finance ministers, central bank governors and their senior officials have informal opportunities to reflect on developments between the twice-yearly meetings of the Fund and Bank.

The hand-over from March 2002 of G-20 chairmanship from Canada, the inaugural Chair, to India is a step of great practical and symbolic importance for the G-20, and for the evolution of global economic governance.

For the first time, one of the world's great emerging economies is leading a globally representative grouping of significant economies, transcending traditional 'North-South' boundaries of the developed and developing world, and linking Eastern and Western hemispheres, and all the continents bar Antarctica.

The Australian government welcomes India's chairmanship and I am sure I speak for us all tonight when I say that as officials, we look forward to working with India to develop further the role of the G-20.

'SELLING' THE POVERTY-REDUCING BENEFITS OF APPARENTLY SMALL REFORMS

In the remainder of my time tonight, I would like to examine the changing economic outlines of the world we might be able to achieve with continued policy reforms and closer international economic integration, and explore some of the challenges that we, as policy advisers and researchers, confront in explaining the case for those changes.

Our fundamental challenge is a very simple one, at least in concept — little more than a bit of basic arithmetic. It is to show that economic and policy reforms which lift productivity and income growth by apparently rather small amounts quickly compound to produce significant change in real income levels, and much wider human opportunities.

As the evidence mounts of the last few decades' remarkable progress against poverty, and the associated narrowing of the inter-country and global income distributions, it is interesting to note two qualifying or dissenting observations that I suspect we will hear more of in years to come.

- First, many observe that the progress against poverty has not been uniform. While some formerly poor countries have made great strides, others have not, or have even suffered absolute declines in per capita GDP. In an extreme form, this observation is sometimes expressed as if progress has been essentially confined to China and, more recently, India.
- Second, it is often claimed that inequality is really still widening, because the absolute (dollar) income increases in rich countries (or at the top of a national income distribution, for that matter) are still larger than the increases accruing to the poor. Related to this claim, it is sometimes argued that progress is too slow, even if relative income convergence across many countries is now under way. (By relative income convergence, I mean a situation in which poorer countries have faster GDP per capita growth rates than richer countries.) Incomes in successful developing countries would not converge to rich country levels for over a century.⁷ On this view, growth alone cannot be the answer to poverty, and significant redistribution is required.⁸

Progress against poverty is patchy: the Africanisation of poverty

Clearly, progress has been patchy.

We are witnessing, in effect, the 'Africanisation' of extreme poverty. Xavier Sala-i-Martin, in some recent work, estimates that while the global numbers living below a US 1 dollar-a-day poverty line have fallen by over 200 million between 1970 and 1998, the numbers in Africa have risen by over 175 million. Africa was home to only about one in ten of the world's extremely poor in 1960, but two in three of them in

7 The Australian Treasury illustrated this arithmetic in *Global Poverty and Inequality in the 20th Century: Turning the Corner?*, Economic Roundup Centenary Edition, 2001, pp 42-44.

8 For one example of this view, see Michael Haynes and Romy Husan, *National Inequality and the Catch-up Period: Some 'Growth Alone' Scenarios*, *Journal of Economic Issues*, Vol XXXIV No 3 September 2000, pp 693-705.

1998, such has been the progress against poverty outside of Africa, and such the lack of progress in Africa.⁹

Since China is home to about 20 per cent of the world's population, and India another 16 per cent, it is inescapable that the poverty-busting successes of those two countries will statistically dominate the world's progress.¹⁰

But progress against poverty has been much broader than just China and India. The World Bank has identified 22 other success stories (subsequent to the original globalisation successes of Korea, Taiwan, Hong Kong (SAR) and the like) that have enjoyed strong real income gains in the post-1980 wave of globalisation, mainly through successfully entering the booming global trade in manufactures.

Unlike China and India, many of them are not sufficiently populous for their success to make a notable statistical impact on the global measures.

Sala-i-Martin singles out Indonesia's performance for special mention, noting that in 1970 almost half the population fell below the US 1 dollar-a-day poverty line. But by 1998, less than 1 per cent fell below that line, while the income distribution had narrowed as well.¹¹

Sala-i-Martin also stresses an interesting characteristic of recent and prospective changes in the global income distribution. The narrowing of the inter-country and world income distributions over the last 20 to 30 years is essentially because of 'convergence to the rich' by formerly poor but now rapidly globalising economies — most notably (because of their population size) China and India.

But if those formerly poor countries continue to grow over the next 50 years at recent rates, while African economic growth remains weak, recent 'convergence to the rich' will be followed by future 'divergence from the poor'. Rather than the middle catching up with the top of the income distribution, both middle and top would leave the poor

9 Xavier Sala-i-Martin, *The World Distribution of Income (Estimated from Individual Country Distributions)*, 21 April 2002 (unpublished) see: <http://www.columbia.edu/~xs23/home.html>

10 This is especially true for statistical measures such as global Lorenz curves or Gini coefficients, which are moved most by countries with large populations, or initially at the low or high extremes of the distribution. These statistical issues are well treated in A. Melchior, K. Telle and H. Wiig, *Globalisation and Inequality: World Income Distribution and Living Standards*, Royal Norwegian Ministry of Foreign Affairs, Studies on Foreign Policy Issues, Report 6B, 2000. Available at http://odin.dep.no/archive/udvedlegg/01/01/rev__016.pdf

11 Xavier Sala-i-Martin, *The World Distribution of Income (Estimated From Individual Country Distributions)*, op. cit., p 10.

behind, and global income inequality measures would, under these assumptions, start to rise again from about 2010 or 2020¹².

Relative and absolute convergence

Turning now to the second claim, I think we ought dispute the argument that whatever the statistics say, real inequality is still widening because absolute income increases for the poor remain smaller than the absolute increases for the rich. That claim fails to understand the feasible economic growth paths that link initial relative catch-up to ultimate absolute catch-up from widely diverse starting points.

Since the early 20th century, economists who have studied inequality and devised the analytical tools we now use to measure it, have argued that any desirable measure of inequality should be independent of the scale with which income is measured. For example, if all incomes in a distribution double, the measure of inequality should stay the same, even though the absolute income increase of the rich will have been larger than that of the poor.¹³

In accord with this principle, if poorer people in an income distribution enjoy faster income growth than richer people, standard measures of inequality such as the Gini coefficient, the Atkinson index and the Theil index would all diminish. The income distribution would correctly be shown to be narrowing, even though it is quite conceivable that poorer people enjoying faster (percentage) rates of income growth might initially receive smaller absolute income increases than the rich.

The claim that relative catch-up can only be counted a success if, from the outset, there is also absolute catch-up, implicitly sets a test for narrowing inequality that is practically impossible to meet. Given that the inter-country income distribution has grown so wide over the last 200 years, there is no feasible rate of growth in poor countries that would give them annual absolute (dollar) per capita income increases that were larger from the outset than annual increases in those countries that are already rich.

Consider, for example, the US, with per capita GDP in 1998 of about USD 27,300 in PPP terms, growing (on average in the decade to 1998) at 2.0 per cent per annum; and China, with per capita GDP in 1998 of USD 3,117 at PPP, growing (on average in the decade to 1998) at 5.6 per cent per annum.

12 Xavier Sala-i-Martin, The Disturbing 'Rise' of Global Income Inequality, NBER Working Paper No 8904, April 2002.

13 That is why researchers do not use the variance of income as a summary indicator of inequality. If all incomes double, the variance of the distribution quadruples.

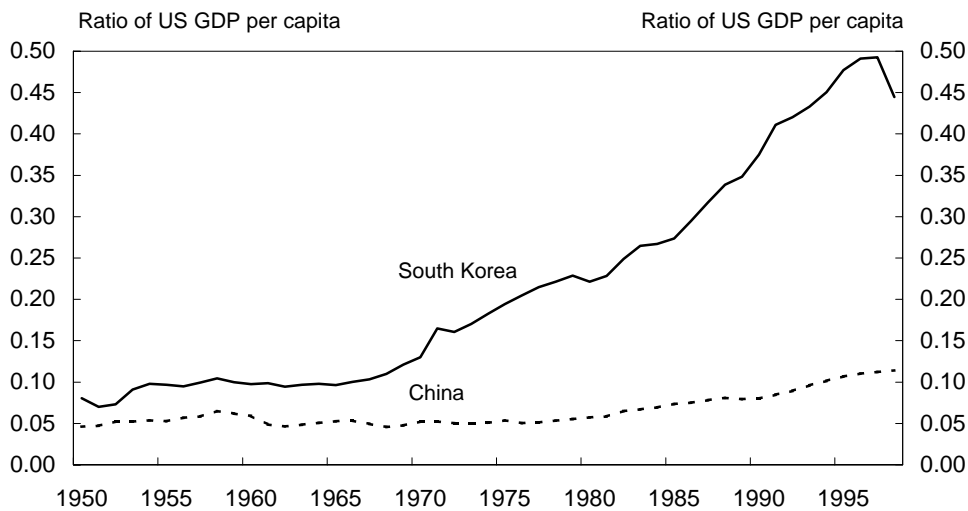
Chinese growth performance since the late 1970s is unprecedented in history. Never before have so many people been lifted out of poverty so quickly by such sustained high growth.¹⁴

But using these average numbers for illustration, the increase in Chinese per capita GDP in 1998 would have been only about \$174, while the increase in US per capita GDP in 1998 was \$546. For the Chinese growth rate to generate a larger per capita increment than in America, would require an annual growth rate in Chinese per capita GDP of over 17 per cent — eight and a half times the US growth rate!

The practical conclusion is simply that relative catch-up — that is, faster per capita income growth in poor countries than in rich — is the most that will be observed for many years to come. Yet even relative catch up means striking real improvements in living standards along the way, which quickly compound to phenomenal progress.

For example, South Korea has converged over fifty years from under 10 per cent of US per capita GDP levels at purchasing power parities to about 45 per cent, and China has converged from about one-twentieth to about one-tenth US levels.

Chart 2: GDP per capita (PPP) relative to the United States 1950-1998

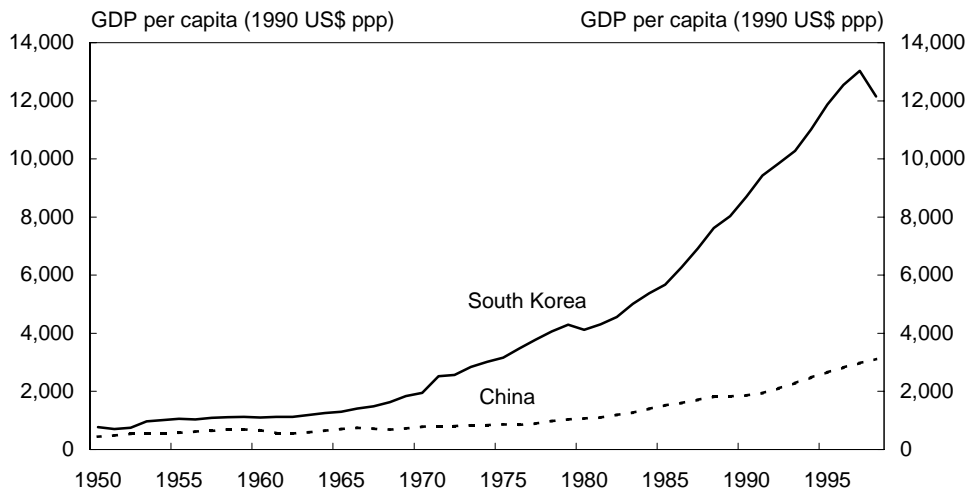


Data source: estimates published by Angus Maddison; *The World Economy: A Millennial Perspective*, OECD Development Centre Studies, Paris 2001.

14 These comparisons use real per capita GDP levels at PPPs estimated by Angus Maddison in *The World Economy: A Millennial Perspective*, OECD Development Centre Studies, Paris 2001. In order to gain the advantage of longer periods of PPP comparisons (back to the dawn of the 20th century and indeed earlier), Maddison uses an approach which produces slightly different PPP estimates over the last 30 years than those compiled by the IMF for the World Economic Outlook Database, and cited earlier in Chart 1.

But over those fifty years, South Koreans have become over 15 times richer, and over six times richer than they were in 1970. Chinese are over seven times richer than fifty years ago, and over four times richer than in 1970.

Chart 3: GDP per capita 1950-1998



Data source: estimates published by Angus Maddison; *The World Economy: A Millennial Perspective*, OECD Development Centre Studies, Paris 2001.

THE INDIAN EXAMPLE

The experience of the current chair of the G-20 teaches how powerfully policy reforms can compound to huge advances in living standards from apparently small starting point productivity increases, while along the way making some illustrious critics look very silly.

Just thirty-five years ago, in an article in *New Scientist*, Stanford University biologist Paul Ehrlich argued that the United States should '... announce that it will no longer ship food to countries such as India where dispassionate analysis indicates that the imbalance between food and population is hopeless. ... our insufficient aid should be reserved for those whom it may save.' Ehrlich argued that it was a 'fantasy' to believe India would be able to feed the additional 120 million people that it was then estimated would be born by 1975.¹⁵

¹⁵ Ehrlich, P.R., 1967, *Paying the Piper*, *New Scientist*, 14 December 1967, p 655.

In fact, India's actual population growth over that period turned out to be 104 million rather than 120 million, and India had produced enough additional food for 144 million, so nutrition improved.¹⁶

India's formerly highly controlled and closed economy has been progressively opened to the world, in fits and starts, since 1985. Notwithstanding severe fiscal and balance of payments problems in the early 1990s, reforms have broadened and accelerated in the last decade. Trade as a percentage of GDP has risen from under 10 per cent in the 1960s to almost 20 per cent in the 1990s, which I note is still less than half China's exploitation of trade as an engine of specialisation, productivity enhancement and growth.

From 1950 to 1979, India's GDP per capita was growing at about 1.3 per cent. By the 1990s, per capita income growth had risen to about 3.7 per cent — not such a big difference, one might think.¹⁷ But that growth has cut the Indian poverty rate from 55 per cent in 1974 to 26 per cent in 2000.¹⁸

Bradford DeLong has pointed out that at India's per capita GDP growth rates before the 1980s, today's per capita income would double every 50 years and India would reach current US per capita income levels around 2250. But the increased growth rate achieved in the 1990s through accelerated reforms means per capita income is now doubling every 16 years. If that growth can be sustained, India would reach current US income levels by 2066.¹⁹

SPREADING PROGRESS TO AFRICA

Regardless of how we read the evidence of recent progress against poverty, there can be no doubt that governments have much further to go, both in broadening progress to those countries that have not yet benefited from globalisation's opportunities for raising productivity, and deepening progress in countries that are already making headway.

Spreading progress to the 2 billion residents of countries not yet benefiting from closer international economic integration will require sustained peace, the enforcement of property rights, the rule of law, better national economic institutions, and better

16 FAOstat database numbers, cited in Bjorn Lomborg, *The Skeptical Environmentalist: Measuring the Real State of the World*, Cambridge University Press, p.60.

17 Maddison, op cit.

18 Stanley Fischer, *Breaking Out of the Third World: India's Economic Imperative*, India Today Conclave, New Delhi, 22 January 2002, available at <http://www.imf.org/external/np/speeches/2002/012202.htm> .

19 J. Bradford DeLong, *Preliminary Thoughts on India's Economic Growth*, April 2001, pp 4-5, available at <http://www.j-bradford-delong.net/TotW/India.html> . Using the 1990s growth rate calculated from the Maddison data, we calculate that GDP per capita would double in 21 years, with India reaching current US income levels by 2080. These conclusions are sufficiently consistent with DeLong's statement to further illustrate the point.

economic policies. And as the third wave of globalisation has shown, access to global markets in trade and investment is vital to rapid progress in raising productivity. When we better understand the successes of the last twenty years by China, India, Indonesia, Mexico and others, we will be better placed to spread those successes. But I think we can say already that the role of greater economic openness in driving productivity-enhancing structural change is a powerful beneficial force, though of course it also requires other necessary conditions for growth to be put in place.

Initiating progress in Africa will be a particular challenge, but it is clearly feasible with the right institutions and policies, such as articulated in the New Partnership for African Development.

Let me offer Burkina Faso as an example, which I choose simply because its circumstances have been so difficult. It is one of the poorest countries on earth, and one of only nine to have been continuously in the ranks of the poorest twenty countries on earth for all the last quarter-century.²⁰

It embodies all the difficulties that are likely to make strong future growth in sub-Saharan Africa more difficult than it has been for the earlier globalisers of the last 50 years.

Burkina Faso is tropical and landlocked;²¹ it has a high population density and a 2.7 per cent population growth rate (notwithstanding the recent scourge of AIDS, enumerated below); it is mostly dependent on agriculture, but has fragile soils and has suffered desertification; it endured over twenty years of civil unrest from the late 1960s to the early 1990s, with repeated coups; its neighbours are all similarly poor, and some have also been racked by unrest, further complicating effective transport links to local and world markets; adult male literacy is 28 per cent; adult female literacy only 9 per cent.

From a population of just under 11 million, about ¼ million had died of HIV/AIDS by mid-2001, and some ½ million live with the disease; life expectancy is only 44 years, having fallen by about 10 years because of AIDS. And finally, it is heavily indebted, with a peak net present value of debt-to-exports of over 300 per cent before recent decisions for relief through the Heavily Indebted Poor Countries initiative.

20 Australian Treasury, *Global Poverty and Inequality in the 20th Century: Turning the Corner?*, *ibid*, p 36 table 2.

21 Economic analysis suggests that tropical location carries particular development difficulties because of health and agricultural problems that are more severe than in temperate zones, and less well addressed by the stock of temperate zone technologies. See Jeffrey Sachs, *Tropical Underdevelopment*, NBER Working Paper 8119, February 2001. Moreover, being landlocked raises transport costs of trade, especially if neighbours are poor and political unstable. Burkina Faso's neighbours are Mali, Niger, Togo, Cote d'Ivoire, Ghana and Benin.

Yet in the face of all these disadvantages, Burkina Faso has enjoyed stable government for over a decade, and macroeconomic policy has been steadily improved over recent years. The Burkinabe Government has defined and implemented a Poverty Reduction Strategy with the World Bank and IMF, and has adhered to the terms of funding under the IMF Poverty Reduction and Growth Facility. It has initiated an anti-corruption strategy, and begun to reform the inefficient state enterprises that dominate much of the economy, including the marketing of cotton which constitutes almost 60 per cent of export receipts and provides income to more than 2 million people. Aided by these reforms and several good seasons, GDP growth has been over 5 per cent in each of the last two years.²²

But recent international developments have not been helpful. The recent US Farm Bill votes US farmers subsidies of US \$180 billion over 10 years. Such subsidies provide about 1/3 of the annual income of US cotton farmers. The IMF and World Bank estimate that without the depression of world cotton prices from this and similar production-distorting subsidies, the numbers of Burkinabe in extreme poverty could be halved in six years.²³

Unfortunately, the problem is more general than the US Farm Bill. The need to negotiate limits to domestic agricultural support in rich countries was recognised as long ago as the conclusion in 1967 of the Kennedy Round of GATT negotiations, but the Tokyo and Uruguay Rounds made little substantive progress.²⁴

Limiting agricultural subsidies remains a central priority for the Doha Round. For Burkina Faso and other small, poor countries, the only international instrument they have for limiting market-corrupting subsidies and lowering other barriers to their exports is the WTO and the Doha Round. The enemies of the WTO are no friends of Burkina Faso.

Developing countries will not enjoy higher productivity, a prerequisite to achieving catch-up, without structural change. That is the point of trade and investment liberalisation — it drives structural change. It is ironic, then, to observe rich countries being so resistant to structural adjustment in their own economies. But it is far more serious than irony: the very policy interventions that are preventing structural adjustment in the rich countries are simultaneously undermining the prospects of much needed structural change in the poor.

22 Information is from the Burkinabe Letter of Intent to the IMF of 14 March 2002, the IMF country report No 02/93 of April 2002, and the Enhanced HIPC Initiative Completion Point Document, all available on the IMF web site.

23 See IMF Issues Brief, *Improving Market Access: Toward Greater Coherence Between Trade and Aid*, March 2002, <http://www.imf.org/external/np/exr/ib/2002/032102.htm#iii>, and forthcoming World Bank & IMF report, cited in World Bank Press Clips of 6 May 2002.

24 See Corbett, Hugh; *US not interested — Cairns has to lead*. Australian Financial Review, 13 May 2002.

If the world's governments were prepared to lower trade barriers and production-distorting subsidies in agriculture, and broaden the application of the economic institutions and policies that have been shown to produce wealth, there is no doubt that we could complete the conquest of food scarcity for the first time in human history, and leave our children a much fairer world than we inherited.

