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IS GLOBALIZATION MAKING WORLD INCOME DISTRIBUTION MORE EQUAL?

Robert Hunter Wade[1]

Anyone interested in the wealth and poverty of nations must be interested in what is happening to world income distribution, one would suppose. A lot turns on the question. If world income distribution became more equal in the final quarter of the last century, this would be powerful evidence that globalization works to the benefit of all. Not only has it helped to produce a doubling of average world income between 1960 to 1989 (from $2,300 to $4,400 in constant US dollars), it has also helped to distribute the benefits much more equally than when the world was less globalized, contrary to the expectation that such a big jump in the average would destablize income shares as some countries and regions did much better than others.

Lower-income countries should therefore integrate their economies closely into the world economy, as the IMF and the World Bank and their rich country shareholders urge them to do. The "battle of Seattle" and other anti-globalization protests could be seen as blips in the movement towards a fully open world economy delivering benefits to almost all participants, without the need for international redistribution mechanisms. International migration pressures could be expected gradually to abate as world incomes and productivity converge.

At a theoretical level, improving world income equality in the past quarter century supports the growth theory of mainstream or neoclassical economics against other theories. Neoclassical growth theory says that national economies will *converge* in their average productivity levels and average incomes as capital moves from capital-abundant developed countries (experiencing diminishing returns to capital) to capital-scarce developing countries, where each unit of capital, being scarcer, has higher returns.[2] On the other hand, the theory known as "endogenous growth theory" says that the tendency to diminishing returns is often offset in the high-income countries by *increasing* returns due to technological innovation, which has become self-

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[2] Sometimes the expectation is made more plausible by controlling for human skills and the institutional environment of property rights, political stability, and the like that are needed to make capital work; hence called "conditional convergence".

sustaining in the rich world. Endogenous growth theory therefore predicts less convergence than neoclassical theory, and most likely, divergence (growing world income inequality).

A third approach, “dependency theory” and its cousin “world systems theory”, coming out of sociology, also says that convergence is less likely, divergence more likely, because the tendency to diminishing returns in high-income countries is offset by differential benefits from economic integration; core (or high-income) nations benefit disproportionately from trade and investment relations between core and periphery. Indeed, dependency theory says that productivity and income growth in the periphery (lower-income or developing countries) are often hindered by free market relations with the core. These relations can lock developing countries into the production of commodities like rubber, tea, or minerals, the prices for which (except oil) have fallen through the 20th century, reflecting technological innovation in the core that yields more efficient use of the same commodity and substitution of the commodity by synthetics.

A sharp fall in world income inequality in the last quarter of the 20th century would constitute important evidence in favor of neoclassical theory and against both endogenous growth theory and dependency theory.

Despite its importance, world income distribution has received rather little attention within the fields of development studies, international relations, or (until very recently) international economics. Neither the World Bank nor the IMF--the two premier multilateral economic organizations, both with powerful research capacity--have devoted significant resources to studying it.[3] Many analysts take it for granted that world income inequality is falling. According to Paul Omerod, for one, world inequality fell sharply in the

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[3] The World Bank has produced data on national income distributions and sponsored cross-sectional analysis of national distributions. It has not, however, devoted resources to analysing the trends and causes of world income distribution. The World Bank’s *World Development Report 2000*, called *Attacking Poverty*, (World Bank, Washington DC, 2000), has a short discussion of the cross-sectional relationship between national income distribution and national growth rates. It makes a few passing remarks about trends in world income distribution. It admits that “there have been some increases in worldwide inequality between individuals in past decades” (p.51). It puts this trend in optimistic light by adding, “the increases in world-wide inequality in recent years are small relative to the much larger increases that occurred during the 19th century”. This statement runs against the evidence in the two World Bank studies cited later in this paper which show fast widening in 1988-93, and against the report’s own warning that the 19th data are unreliable.

I like to think of the distinction between the analysis of national income distributions (as in “how does national income distribution affect the rate of growth”) and the analysis of world income distribution as akin to the distinction between the analysis of galaxies and the analysis of the macroscopic structure of the universe. Not until the 1980s did astronomers discover that galaxies are not randomly distributed in space; rather, they cluster in “walls” and “filaments” , with vast voids in between. The discovery created a whole new level of questions about macro structure that did not exist before. Similarly, world income distribution raises questions about overall shape, trends, mobility that cannot be reached through cross-sectional World Bank-type work on national income distributions.

second half of the 20th century, "especially in the final quarter".[4] Many other analysts think it is sufficient to focus on poverty, and ignore income inequality as such. Both these views need to be challenged. New evidence suggests that global inequality is worsening, and rapidly. And there are good reasons to be alarmed by that trend, quite apart from what it implies about the extent of global poverty.

The Shape of World Income Distribution

World income distribution deals with income distribution among the planet's 6.2 billion people regardless of country or region. It can be thought of as the combination of (a) the internal income distributions for all the countries, and (b) the distribution of average incomes between countries. Most of the inequality in world income distribution reflects the inequality between the country averages rather than inequality within countries.[5] The world average gap between the average income of the top quintile (20 percent) and the average income of the bottom quintile within each country is about 5:1. The gap between the average income of the top quintile of states and that of the bottom quintile of states is more like 25-30:1. [6]

Chart 1 shows the distribution of the world's population by average income of each country, using compatible data from 1993, the most recent year available. Income is measured in terms of actual purchasing power over comparable bundles of goods and services, or "purchasing power parity", PPP, rather than in terms of actual exchange rates, which reflect purchasing power over the sub-set of goods and services that enter international trade. China and India, almost 40 percent of world population, are divided into

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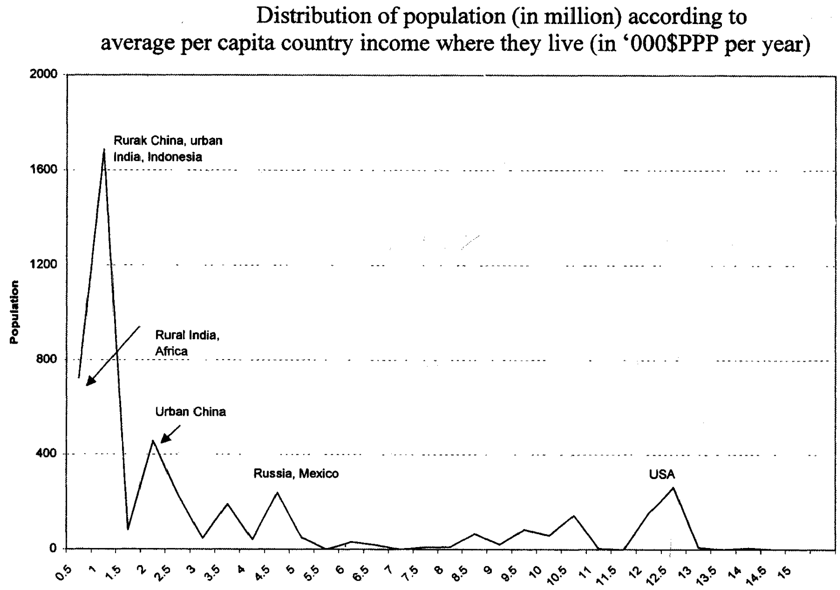
4 Paul Omerod, "Inequality: the long view", *Prospect,* August/September 2000. See also Robert Wright, "Global happiness", *Prospect,* December, 2000. They both make the same strong statement about world income distribution: it has become more equal at the same time as globalization has accelerated. Martin Wolf of the *Financial Times* has championed the idea that globalization improves global income distribution. See for example, "Growth makes the poor richer: reversing the effects of globalization might increase equality as the critics claim, but it would be an equality of destitution", *Financial Times,* 24 January 2001. Ian Castles, former Australian Statistican, claims that "most studies suggest that the past 25 years have seen a reversal in the trend towards widening global inequalities which had been proceeding for two centuries" (letter to *The Economist*, May 26 2001).

5 The evidence on within-country income distribution suggests that income inequality within the developed countries (the composite region of North America, Western Europe and Oceania) has risen only a little on average since 1980, except in the US, the UK, Australia and New Zealand, where it has risen fast. The United States is the most unequal (top household quintile to bottom quintile of 11:1 in 1992), followed by Australia, New Zealand, Switzerland, Canada, Britain, France, Italy, Germany, Holland, Belgium, Sweden, and most equal, Japan (top/bottom quintile of 4.5:1). ("For richer, for poorer", *The Economist*, November 5, 1994) The developed countries are more equal internally, on average, than the countries of any of the other four regions (Africa, Asia, Latin America/Caribbean, and Eastern Europe/Former Soviet Union). In these other regions, internal inequality is generally rising.

6 The quintile ratio of 25-30:1 (1988-93) is for PPP-adjusted (Penn World Table method) real GDP per capita by number of states, not population weighted. Steve Dowrick and Muhammad Akmal, "Explaining contradictory trends in global income inequality: a tale of two biasses", Faculty of Economics and Commerce, Australia National University, 29 March 2001. Available on http://ecocomm.anu.edu.au/economics/staff/dowrick/dowrick.html.

urban and rural sectors and treated as separate countries (rural China then being the most populous "country" in the world).

Chart 1. Distribution of population (in millions) according to the average income of the country where they live, 1993



average country income (US$000)

Source: Branko Milanovic, "True world income distribution, 1988 and 1993", Policy Research Working Paper 2244, Development Research Group, World Bank, November 1999. Available on www.ssrn.com.

Note: Income in PPP dollars.

The distribution has two poles. One is at the bottom end, at an average income level below about $1,500 a year. It contains the populations of most of Africa, India, Indonesia and rural China. The other is at the top end, with average PPP income above about $11,500, made up mostly of the populations of the US, Japan, Germany, France, UK, and Italy. The space between $1,500 and $11,500 is occupied by countries such as urban China, Russia, and Mexico. (Notice the strange "missing middle", the absence of significant numbers of people living in countries with average PPP income between about $5,000 and $11,500, a fact for which there is no explanation.) If income was measured using actual exchange rates the range from poorest to richest would be much larger.

Trends in World Income Distribution

No one disputes that world income distribution became vastly more unequal after the Industrial Revolution. On this time scale divergence dominates, big time. But after 1975?

Having ignored world income distribution for decades, international economics has lately seen a burst of interest. Is it becoming more unequal or less unequal? If more unequal, is this good or bad for growth? How does openness affect income distribution? How does income distribution affect the reduction of (absolute and relative) poverty? But the statistical difficulties are so formidable and the data are such a mine-field that the debate has revolved around questions of econometric technique.

Standing back from the fray we can see that the trend in world income distribution depends heavily on (a) the measure of inequality, (b) the weight given to individuals or countries, and (c) the use of currency market exchange rates or purchasing-power-parity (PPP) exchange rates to compare incomes in different countries.

On (a), the Gini coefficient is a commonly-used measure of inequality. 0 signifies perfect equality, 1 signifies that one person holds all the income. But the Gini coefficient tends to overstate changes close to the average, and understate changes close to the extremes. Comparisons between the top and bottom decile (10 percent) or quintile (20 percent) give a more accurate picture of what is happening at the extremes. The trend based on the Gini coefficient may be different from the trend based on the decile or quintile measures.

The other two issues need more discussion. We shall see how the answer to the question, "What is happening to world income distribution?", depends on which of the four combinations of measures we use. And we shall see that each of the four combinations has its own legitimate uses; which reflects the point that we may be interested in income not only as an indicator of consumption or material welfare but also as an indicator of other things.

Equal Countries Or Equal Individuals

If countries are treated equally (not weighted by population) and average income is measured in PPP terms, most studies find that—whichever measure of inequality is used--world income distribution has become *more unequal* in the past few decades. If countries are weighted by their populations (so China's change in average income counts for many times more than Uganda's), world PPP income distribution over recent decades shows *little change*. [7]

It may seem obvious that one should weight countries by population, giving each individual in the world equal weight. If so, the second conclusion is decisive—little change in world income distribution in recent decades,

[7] In addition to the papers cited elsewhere in this essay, I have drawn on Glen Firebaugh, "Empirics of world income inequality", *American Journal of Sociology*, 104 (6), May 1999; Roberto Koreniewicz and Timothy Moran, "World-economic trends in the distribution of income, 1965-1992", *American Journal of Sociology*, 102 (4), 1997; Giovanni Arrighi and Jessica Drangel, "The stratification of the world-economy: an exploration of the semiperipheral zone", *Review*, X (1), 1986.

neither convergence nor divergence. But we may also be interested in income distribution for the purpose of testing the growth theories mentioned earlier, or assessing the effectiveness of policy advice on how to raise national growth rates; in which case we can treat each country as a laboratory trial--an observation of a set of policies, institutions and resources—and take the average over all the trials, weighing each country equally. Likewise in the context of understanding cooperation and non-cooperation in multilateral organizations such as the UN, where small-population states have more of a voice than their share of world population would warrant, it may make sense to look at world income distribution with countries weighted equally. With countries treated equally, world income distribution has widened.

Market Exchange Rates or Purchasing Power Parity

What about the second measurement issue: exchange rates or PPP? With the market exchange rate method, Ugandan income in shillings is converted into US dollars at the average exchange rate of the past three years; Chinese income in yuan is likewise converted into US dollars; and so on. Then the income distributions in terms of average, total and distribution around the average are mapped onto each other and aggregated to get the world picture.

With the PPP method, Ugandan income, Chinese income, Swiss income and all the others are converted into US dollars using a technique for converting national incomes to purchasing power over comparable bundles of goods and services. This raises the real income of low income countries above the level reached by the exchange rate method. Residents of poor countries are relatively better off than the exchange rate method suggests, because for a given amount of income they can purchase more goods and services (haircuts, for example) that do not enter into international trade and hence do not affect the exchange rate. This matches the experience of international travellers that their US dollars go much further in India or Indonesia than in western Europe. Just how big a difference it makes to use income expressed via exchange rates or PPP can be seen by how it affects the rank order of countries' GDP (table 1).

Table 1. Rank Order of Largest Economies, US$, 1993

Expressed via	1	2	3	4	5	6	7	8
Market exchange rate	US	Japan	Germany	France	UK	Italy	China	Brazil
PPP exchange rate	US	China	Japan	Germany	India	France	Italy	UK

Source: World Bank, World Development Indicators, 1999.

When incomes in different countries are expressed in a common currency using market exchange rates the evidence shows that world income distribution has become *much more unequal* over the past several decades and the inequality accelerated over the 1980s and 1990s, whether countries are treated equally or weighted by population. In other words, when countries' incomes are compared using market exchange rates, globalization has not worked, in the sense that rapidly increasing flows of trade and investment have not yielded the expected neoclassical convergence, have not benefitted the poorer participants by nearly as much as the richer.

On the other hand, when incomes in different countries are compared using PPP exchange rates, the degree of inequality shrinks (the poor are richer, the rich are poorer), and the rate of widening shrinks. Using the standard source of PPP data and weighting individuals equally, world income distribution has shown little change over the past two decades.

It is often said that PPP measures are always superior. Certainly the market exchange rate is a flawed calibrator of purchasing power because it refers to only goods and services traded internationally, a sub-set of total goods and services. It does not reflect the large amount of nonmonetized exchange in developing countries, or money payment for services that are not subject to international competition. It therefore suggests that the income gap between developing countries and developed countries is bigger than the "real" gap in overall purchasing power. Also, market exchange rates are much affected by capital flows and by government policies for the exchange rate and the interest rate; which makes them doubly bad for converting incomes of people living in different countries into a common denominator.

But PPP measures have big drawbacks as well. Comprehensive estimates of PPP incomes for developing countries—based on actual data on prices of comparable goods and services--go back only to the 1970s; for longer run analysis the foreign exchange method has greater consistency. Also, China, eastern Europe and the former Soviet Union constitute big problems, because their PPP figures before the 1990s are of uncertain meaning, and the same remains true for China today. In fact, the problem of making a meaningful estimate of China's PPP income distribution is so severe as to impart considerable uncertainty to all PPP estimates of world income distribution, because China accounts for over a fifth of world population.[8]

But the biggest problem is that different methods of measuring purchasing power parity yield different results. In particular, one common method for comparing real GDP levels across countries uses a fixed price index that introduces a very substantial *downward* bias to international

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[8] Steve Dowrick and Muhammad Akmal (2001) find that, "None of our measures of changing levels of global inequality are robust when we take account of the errors involved in estimating the real income level of China."

inequality (makes inequality look smaller than it actually is). [9] The downward bias arises because the index uses a structure of relative prices that, although described as "average world prices", is actually close to rich country (OECD) prices. So the relative price of services in the index is close to the relative price of services in the OECD countries. People in poor countries consume a lot of services, because they substitute cheap services for more expensive goods. When their consumption of this large quantity of services is valued at OECD-like prices their income appears much larger than it actually is.

Moreover, I suggest later that relative price structures between OECD countries and most developing countries have been *diverging* over the past few decades. If so, then the bias that comes from this method of computing PPP incomes—the bias to understate global inequality—is increasing. Real inequality is greater than and widening faster than the PPP figures suggest.

Steve Dowrick and Muhammad Akmal find that once they adjust the standard PPP price index to reduce or remove the downward bias, the world inequality coefficient rose over the period 1980-93 (world income distribution became more unequal), even when population-weighted PPP incomes are used.[10] Moreover, they find that the main equalizing force in world income distribution has been urban China's rise towards the middle of the distribution. Take out China and the trend towards higher inequality is stronger. They confirm that the top and bottom deciles of the world income distribution have been pulling apart at high speed.

And this is still not the end of the limitations of PPP measures. While comparing incomes in PPP terms gives a better picture of relative welfare, it gives a misleading picture of relative national power and national modernity and of relative class power, matters of more interest to sociologists and political scientists, no doubt, than to economists. If we are interested in class formation and class conflict on a world scale, or in the relative economic or geo-political impact of countries--the relative economic strength of the US compared to China, for example--we should use actual market exchange rates, not PPP dollars (see table 1). Similarly if we are interested in the marginalization of developing countries. The reason why many of the poorest countries are hardly represented in negotiations whose outcomes profoundly affect them is that the cost of hotels, offices, and salaries in New York and Geneva must be paid in US dollars or Swiss francs, not in PPP dollars.

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[9] Studies based on the Penn World Tables (compiled by Bob Summers and Alan Heston) suffer from this weakness. The tables use a fixed price (Geary-Khamis) index for comparing real GDP levels across countries. See Dowrick and Akmal (2001) for the demonstration that this fixed price method introduces a substantial downward bias to measures of international inequality. Ian Castles takes no account of this bias in arguing that world income inequality is falling. See his "'The mismeasure of nations: a review essay on the *Human Development Report 1998*", *Population and Development Review*, December 1998.

[10] Dowrick and Akmal, 2001.

To repeat, world income distribution measured in market exchange rates has become much more unequal since around 1975. This is the starting point for understanding trends in the relative economic power of nations and classes.[11]

The bottom line: The bulk of the evidence on trends in world income distribution runs against the common claim that world income inequality has fallen sharply in the past half century and still faster in the past quarter century. None of the four measurement combinations supports this claim. Table 2 summarizes the evidence on the four measures of world income distribution.

Table 2. Trend in world income distribution over past quarter century, by different measures

		Income measured in	
		Market exchange rates	PPP exchange rates
Countries weighted by population	No	Very much more unequal	More unequal
	Yes	Much more unequal	Little change, using standard Penn World Tables; more unequal, using Dowrick-Akmal adjustment

A New Data Set

Recently a new data base has become available, based solely on household income and expenditure surveys. The earlier studies either used average GDP, ignoring inequality within each country, or used more indirect methods to estimate within-country inequality, including production surveys and revenue surveys, which typically miss important components of household incomes. Branko Milanovic at the World Bank assembled the new data base, using the Bank's formidable statistical organization to obtain household survey data from just about all the Bank's members, covering 85 percent of the world's population, for the years 1988 and 1993. He claims that this constitutes the most reliable data set on world income distribution.[12]

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[11] Notice that the logic of the market says that those non-market or non-internationally-traded goods and services that are captured in PPP but not in market exchange rates should move, with "development", into the same sphere of value as the goods and services that are internationally traded. They are unfortunate hold-overs, and as development proceeds and the sphere of the hold-overs shrinks, market exchange rates should become the only international measure of value. In which case, world income distribution would look even worse than it does with PPP.

[12] Milanovic, note to chart 1.

Critics say, however, that the data excludes important components of total income, including public expenditure on goods and services; and that the five year time span is too short to be meaningful. [13]

Milanovic computes the Gini coefficient for world income distribution, combining within-country inequality and between-country inequality and measuring it in PPP terms.[14] Taken at face value the results are startling. World inequality increased from a Gini coefficient of 62.5 in 1988 to 66.0 in 1993, an increase of just under 6 percent in 5 years.[15] This is a faster rate of increase of inequality than experienced within the US and the UK during the 1980s.[16]

Yuri Dikhanov and Michael Ward apply a different statistical methodology to the same data and come up with much the same results.[17] They confirm that world income distribution became markedly more unequal between 1988 and 1993--the Gini coefficient increased by about 6 percent. In terms of the share of world income going to different income groups, they find that the share going to the poorest 10 percent of the world's population fell by over a *quarter*, while the share of the richest 10 percent rose by 8 percent. The richest 10 percent pulled away from the median, while the poorest 10 percent not only fell away from the median but also fell absolutely by a large amount.

The following table summarizes their results. It shows that world PPP income distribution with countries weighted by population (and China and India split into urban and rural) became "more unequal" between 1988 and 1993.

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[13] Passions about the adequacy of Milanovic's data run high among the cognoscenti. Ian Castles, former Australian Statistician, says that a data set that relies on household surveys "is a massive deficiency. One effect is that such important elements of national product as public spending on goods and services have been left entirely out of account…. These components …can be particularly important in the level and growth of real living standards in the poorest countries" (letter to *The Economist*, 26 May 2001). Catles' point is correct--but implies an impossibly high standard. To link public spending on goods and services to income distribution one needs data on the incidence of the benefits and costs of public goods and services. For a country with a public health system, for example, one needs data on who received what services in a given period of time. Few OECD countries have good data of this kind that can be incorporated into income distribution studies. This is why even OECD countries measure income distribution mainly in terms of disposable income.

[14] Houseold surveys weigh individuals equally, so the issue of weighing country averages by population does not arise.

[15] Critics point out that some of the increase in inequality may reflect data inconsistencies between the two years.

[16] According to Milanovic's calculations, the top 10 percent of the US population has a total income equal to that of 43 percent of the world's population; in other words, the richest 25 million Americans have a total income equal to that of the poorest 2 billion. By 1993 an American on the average income of the poorest 10 percent of the US population was better off in purchasing power terms in 1993 than two thirds of the world's population.

[17] Yuri Dikhanov and Michael Ward, "Measuring the distribution of global income", paper to First Global Conference on Human Development, United Nations, New York, July 1999.

Table 3. World income distribution, 1988 and 1993

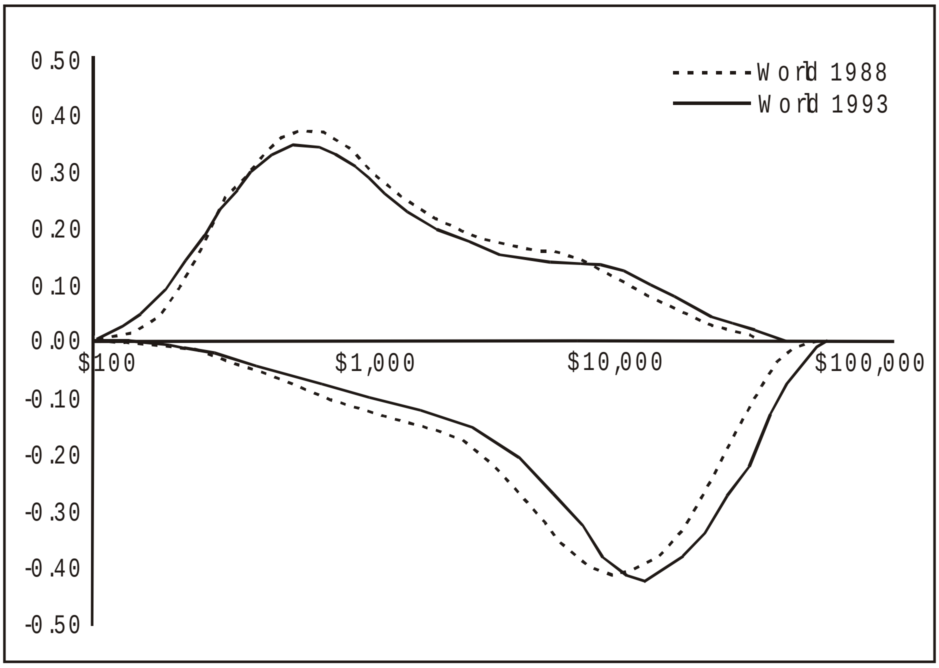
Inequality measure	1988	1993	% change
Gini	63.1	66.9	6.0
Poorest decile (%)	0.88	0.64	-27.3
Richest decile (%)	48.0	52.0	8.3
Median/poorest decile	3.27	3.59	9.8
Richest decile/median	7.28	8.98	23.4

Source: Based on Dikhanov and Ward.

Note: The decile percentages refer to the percentage of world income accruing to in that decile. The upper boundary of the poorest decile fell from $342 in 1988 to $296 in 1993, while the lower boundary of the richest decile rose from $8,153 to $9,547. The median (upper boundary, decile 5) fell from $1,120 to $1,063.

Chart 2 shows the results graphically. The top half refers to the distribution of world population by level of household income, the bottom half refers to the distribution of world income by level of household income. The space between the dotted line and the solid line shows the change between 1988 and 1993. We see from the top half that a larger proportion of the world's population was living at the extreme ends of the income distribution in 1993 as compared to 1988; and that the share of world income accruing to the wealthiest households increased over the same period.

Chart 2. World population by income level, and world income by *income level, 1988, 1993*



Source: Dikhanov and Ward. Note: Income is measured in PPP terms. The vertical axis measures a density function for population (upper half) and income (bottom half). At an income level of, say, $1,000, the area to the left, expressed as a proportion of the total area under the curve, measures (upper half) the share of world population with income of $1,000 per capita or less, and (lower half) the share of world income accruing to people on $1,000 per capita or less.

The Missing Middle

Another study based on the same data helps to describe the phenomenon of the "missing middle", the very small proportion of the world's population living in countries with average PPP incomes in the middle range. The study divides countries, more or less arbitrarily, into three categories by average PPP income: The Third World, from Georgia ($264) to Brazil ($3,470); the Middle World, from Argentina-urban ($3,570) to Greece ($7,840); and the First World, from Italy ($8,020) to Switzerland ($14,070). Table 4 shows the group averages by population share, income share, income, and Gini coefficient (within- plus between-country). The evidence is available only for one year, 1993.

Measurement of overlap between the three categories suggests that the amount of overlap is small, in the sense that few people who live in the Third World have incomes equal to average incomes in the Middle or First Worlds; few people who live in the Middle World have incomes equal to average incomes in the First World; few people who live in the First World have incomes equal to average incomes in the Middle or Third Worlds. In other words, the categories are indeed strata, even though their boundaries are semi-arbitrarily drawn.

As the table shows, the Middle World is tiny. For every person in the Middle World there are two in the First World and ten in the Third World. The typical Third World country probably has a rather similar set of proportions, with a very small middle class, a larger wealthier elite, and a very much bigger and amorphous lower class, in contrast to the more diamond-shaped distribution of First World countries. Which suggests that the world has a whole has a Third World income distribution.

Table 4. Income inequality by country strata, 1993

Country strata	Pop share (%)	Income share (%)	Mean income ($PPP)	Gini
Third World	76	29	1,170	0.49
Middle World	8	12	4,610	0.46
First World	16	58	10,920	0.34
World	100	100	3,030	0.66

Source: Branco Milanovic and Shlomo Yitzhaki, "Decomposing world income distribution: Does the world have a middle class?", typescript, Development Research Center, The World Bank, January 2001.

Note: 1. The overlap measure pertains to the whole distribution. Therefore one cannot make a statement of the kind, "x percent of the population of the Middle World has an income higher than the average of the First World". 2.The threefold breakdown of countries by mean income captures about 70% of the Gini measure of total world inequality. For the three strata, the Gini (between-country + overlapping) is 0.45. For the world (between-country + within-country + overlapping) the Gini is 0.66. 0.45/0.66 = 0.68.

So What Is *Happening to World Income Distribution?*

The short answer to the question, "What is happening to world income distribution?" is, "It depends." It depends especially on whether (1) countries are weighted by population or not, (2) income in different countries is compared using market exchange rates or purchasing power parity (PPP) exchange rates, and (3) inequality is measured with the Gini or other average coefficients, or decile or quintile distributions. There is no single "correct" set of choices, because the choices are sensitive to the purpose at hand.

If we are interested in world income distribution from the point of view of most of the issues that concern the world at large—such as migration flows, the economic and geo-political impact of a country or region on the rest of the world, the marginalization of developing countries, developing countries' capacity to repay foreign debts—we should compare incomes with market exchange rates. Here the conclusion is unambiguous: world income distribution became much more unequal over the past quarter century, whether we use decile distributions or an average coefficient like the Gini and whether we weight individuals or countries equally.

On the other hand, if we are interested in relative material welfare and accordingly use PPP-adjusted data, the conclusions are more complicated. If we weight countries by population and use an average coefficient of

inequality like the Gini, the conclusion seems to be: little change in world income distribution over the past two decades or so. But then come the qualifications. First, the result is heavily affected by just one case, China, because the inequality reducing rise of population-weighted urban China towards the middle of the distribution offsets widening inequality elsewhere, especially if we use the Gini coefficient of inequality which is most sensitive to changes in the middle of the distribution. But the uncertainty in China's income measures is so large, truthfully speaking, that we cannot have a lot of confidence in the "little change" conclusion. With China removed, the trend is clearly towards more inequality in relative material welfare. The second qualification is related to the downwards bias in the standard source of PPP-adjusted incomes. If the bias is eliminated (as in Dowrick and Akmal's paper) the result is a weak trend towards higher inequality over 1980-93.

Two recent studies, using a newly compiled data set based on household surveys, find that even with incomes compared using PPP exchange rates, each individual weighted equally, and China included, world income distribution became sharply more unequal between 1988 and 1993, using both the Gini coefficient of inequality and decile comparisons (with India and China split into rural and urban sectors).

Moreover, the gaps in "real" well-being are probably bigger than the income figures suggest. For one thing, well-being is a function of the security of income as well as the level. Those in the bottom half of the world income distribution have incomes that are not only lower but also more insecure, and they have probably faced rising insecurity over the 1990s (much of the new employment in low income areas is in jobs subject to short-term contracts and immediate dismissal). For another, all the difficulties of international income comparisons aside, the figures on income growth in any one poor country may be biassed upwards (the real figures may be lower), simply because the transfer of activity from the non-market sphere to the market sphere raises measured income by more than the gain in the value of the activity (man marries housekeeper and GDP falls, restaurant meals replace home meals and GDP rises). This effect is likely to be greater in poor countries than in rich, and therefore to overstate poor country income growth.

The Proximate Causes of Rising Inequality

Why has global inequality increased? The proximate answer is in four parts: (1) faster economic growth in developed OECD countries than developing countries as a group; (2) faster population growth in developing countries than in OECD countries; (3) slow growth of output in rural China, rural India, and Africa; and (4) rapidly widening output and income differences between urban China on the one hand, and rural China and rural

India on the other—in other words, rapidly widening income distributions within the biggest countries.

Table 5 shows the extent to which economic growth in the OECD countries has been faster than in the developing countries, both in 1960 to 1979 and in 1980-98, the rise of East Asia notwithstanding. The figures are for countries weighted equally. If developing countries are weighted by population so as to give more weight to faster growing China, India and the rest of East Asia, the developing country median rises only to 0.8 percent in 1980-98.[18]

Table 5. Median per capita income growth rates, OECD and developing countries (%)

	1960-79	1980-98
OECD	3.4	1.8
Developing countries	2.5	0.0

Source: William Easterly, "The lost decades: explaining developing countries' stagnation 1980-98", typescript, World Bank, January 2000.

The income of urban China certainly grew very fast during 1988-93, which reduced the gap between China's average income and that of the middle income and rich countries and so reduced the world Gini coefficient; but the widening gaps between urban China and rural China and between urban China and rural India increased world inequality by even more. [19]

Deeper Causes

These proximate trends have deeper causes. Chart 2 suggests that most of the increase in inequality reflects the increase in the proportion of the world's households located at the extreme rich end and the extreme poor end of the world income distribution. On the one hand, population growth adds disproportionately to numbers at the poor end. On the other hand, technological change results in a disproportionately fast increase in the

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[18] If in the latter period the former Soviet Union countries are excluded (and countries weighted equally) the median per capita growth rises from 0.0 percent to 0.3 percent. The conclusion that developing countries as a group have been growing more slowly than the high-income or OECD countries is not accepted by all analysts. However, even if developing countries have been growing faster, the absolute size of the gap—which is what income distribution measures measure—could still have been increasing, due to the large gap in absolute average incomes. And even if developing countries grew so much faster as to reduce the gap in average incomes, world income distribution may still become more unequal if (because of unequal asset distributions) the rich in developing countries are the primary beneficiaries of the growth and if poor households have faster population growth than rich households.

[19] Over the 1990s the ratio of the average income of China's richest to poorest provinces rose sharply to 11:1. The corresponding US figure is less than 2:1.

number of households at the rich end, without shrinking the distribution at the poor end.

How does technological change have this effect? Perhaps it is through the tendency for knowledge-intensive and high valued-added activities to cluster spatially, even though the technology is available to close great distances. Think of Silicon Valley, a dense concentration of the very companies that are driving the world's communications revolution. But also think of the clustering of the higher value-added activities of multinational corporations in their home countries within the OECD world, despite high congestion costs, while they may outplace the lower value-added activities to less congested and lower cost places in less developed countries. The reason for the continuing clustering of the higher value-added activities in the OECD world has to do with the distinction between information and knowledge.[20] Information can be readily written down, or codified, and so easily posted on a web page, faxed, or e-mailed. Knowledge is more tacit, more difficult to communicate, better conveyed through personal channels or between people who share a similar background. Knowledge in this sense is important for innovation and for niche-market activities, which is where the highest returns lie. This may be a simple explanation of why the OECD countries that already have a stock of innovative companies and a national innovation system continue to be sites for new rounds of high value-added activities--because innovation and many niche market activities depend heavily on knowledge (as well as information), and knowledge-dependence generates locational clustering. This would also explain why they tend to continue to have higher rates of return on both capital and labor; why they tend to have more stable rates of economic growth than poorer countries;[21] and why so few poorer countries have made it into the world club of innovators and the upper stratum of inter-country income distribution—in the period since 1970, only Spain, Taiwan, South Korea, and the Hong Kong and Singapore minnows.

Intermediate Causes

These deep causes yield an important intermediate cause which makes things worse: the prices of the industrial goods and services exported from high-income countries are increasing relatively faster than the prices of goods and services exported by low-income countries and much faster than the prices of goods and services produced in low-income countries that do not enter into international trade. These price trends mean that the majority of the

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[20] G.M.P.Swan, "The Internet and the distribution of economic activity", in S. Macdonald and J. Nightingale (eds.), *Information and Organization*, _______, 1999. D. Audretsch and M. Feldman, "Innovative clusters and the industry life cycle", *Review of Industrial Organization*, April 1996, pp.___.

[21] Lant Pritchett, "Understanding patterns of economic growth: searching for hills among plateaus, mountains, and plains", *The World Bank Economic Review*, 14 (2): 221-50, 2000.

population of poor countries are able to buy fewer and fewer of the goods and services that enter into the consumption patterns of high-income country populations; conversely, that rich country income recipients are able to buy more and more of the goods and services exported by the poorer countries, even with their incomes held constant.

This is the main reason why the market exchange rates give a much bigger income gap between rich and poor countries than PPP-adjusted exchange rates. The other side of poor countries' undervalued market exchange rates is growing demand for foreign exchange in poor countries and net capital outflow from poor countries to rich ones; and consequently a growing investment gap and productivity gap between poor countries and rich countries. Marxists would argue that the net outflows of capital from the poor countries result from the structure of the international political economy, while capitalists would argue that bad policies at the state level are the cause.

Whatever the causes, the upshot is that the poorer countries and the poorer two thirds of the world's population suffer a *double* marginalization: once through slower growing output, again through falling relative prices.[22]

Financial Liberalization and Financial Crises

The financial system carries another mechanism of national and international inequality, though where it fits into a classification of proximate to deep causes is an open question. The argument goes like this. The world economy has been experiencing a "boom in busts", a much higher frequency of financial instability in the 1980s and 1990s than in the post-World War II period up to the end of the Bretton Woods regime in the early 1970s. The instability is a response to the much greater cross-border capital flows relative to GDP compared to the 1950s and 1960s, at least for the OECD countries and the 20 or so developing countries of interest to international investors ("emerging markets").[23]

Large capital inflows and outflows place enormous strains on economies. The strains are especially high in the non-OECD countries, which have relatively weakly institutionalized financial systems. But the emerging market countries do nevertheless tend to rely heavily on capital inflows, because their investment demand is high while their domestic savings are either meager or ineffectively intermediated into investible funds. The capital inflows are predominently in the form of loans, which create fixed-repayment debt obligations in foreign currency.

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[22] On world price trends see Michael Ward and Yari Dikhanov, "What is inflation?", typescript, World Bank, October 27, 1999.

[23] Robert Wade, "The US role in the long Asian crisis of 1990-2000", in F. Batista-Rivera and A. Luukaislas (eds.), *The East Asian Crisis and Its Aftermath*, Edward Elgar, 2001.

The capital inflows tend to occur when economic growth is relatively fast, and the combination of fast growth and capital inflows together tends to boost asset prices, which benefits mainly the rich (asset owners). The benefits to the poor take much longer to accrue through higher employment and government spending on services. So the capital inflows tend to widen national income inequality.

When a shock hits—such as a wave of bankruptcies, a sudden fall in export receipts, or a drain on foreign exchange reserves that pushes the ratio of short term foreign debt to foreign exchange reserves to well over 100 percent--foreign lenders may try to pull back their loans and refuse new lending; which may generate panic as domestic and foreign holders of assets try to shift out of the domestic currency in anticipation of a fall in the value of the currency; which forces the fall. Domestic firms with foreign debt now find that their debt repayment obligations have increased in proportion to the fall of the exchange rate, which may tip them into insolvency. And the government, perhaps pushed by the IMF, may raise domestic interest rates to try to stem the capital outflow and the fall of the exchange rate, which amplifies the pressures towards insolvency. The crisis richochets around the economy, causing layoffs, falls in demand, rises in inventories, bankruptcies, cuts in government services, unrest. While the benefits of the capital inflows are shared "oligarchically", the costs of the crisis are shared "democratically", with immediate impacts on the poor and on the middle class which had taken on lots of debt during the good times.

This is the result of a country having a capital structure—a structure of assets and liabilities, especially the foreign component thereof—which makes the costs of servicing obligations rise just when the ability to repay falls. We could call it an "inversely correlated" capital structure. And the same structure, of course, makes the costs of servicing obligations fall when the ability to repay rises, as during a boom when lenders lend at lower and lower spreads as the good times roll on; which of course only encourages the assumption of more foreign repayment obligations, which then, when the crisis hits, leads to savage contraction. It is a recipe for volatility. [24]

The fact that most developing countries (including the "emerging market" economies) have a strong degree of inverse correlation in their capital structure is at least part of the reason why their growth rates are much more unstable than those of developed countries. Once they go into crisis they

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[24] Michael Pettis, *The Volatility Machine: Emerging Economies and the Threat of Their Financial Collapse,* Oxford University Press, 2001. Wade, "From 'miracle' to 'cronyism': explaining the Great Asian Slump", *Cambridge Journal of Economics*, 22 (6), November, 1998, pp.693-706; "The Asian debt-and-development crisis of 1997-?: causes and consequences", *World Development,* 26 (8), August, 1998, pp.1535-53. Wade and Frank Veneroso, "The gathering world slump and the battle over capital controls", *New Left Review*, 231, September-October, 1998, pp.13-42; "The Asian crisis: the high debt model versus the Wall Street-Treasury-IMF complex", *New Left Review,* 228, March-April, 1998, pp.3-23.

may have negative or only slightly positive growth while the debt resolution process is working itself out, as in Mexico for much of the 1980s and 1990s. The fact that the rich countries continue growing even during their banking-cum-currency crises (which are in any case less frequent), while the poorer countries keep taking two steps forward and two steps back—or keep yo-yoing back and forth between growth episodes that may be faster than the rich countries', followed by contraction--is probably an important contributor to rising global inequality.

The crises cause not only instability of developing country growth rates; they also cause a tendency to lurch towards another set of economic policies—even though there may be no good evidence that the previous policies caused the crisis. The most dramatic case in point is the wholesale revulsion towards "import substitution" in Latin America in the wake of the 1980s debt crisis, and the embrace of neo-liberalism. The crisis was due largely to mismanagement of the capital structure (the debt structure)--the governments borrowed too much and the lending banks, mostly American, lent too much relative to the countries' capacity to repay. But instead of seeing this as the cause of the crisis, the governments, encouraged by the IMF and the World Bank and the US Treasury, abandonned a set of economic policies that had in fact generated high growth in the 1960s and 1970s, and put in place a standard package of neoliberal market opening measures. These have not delivered high growth, and they have resulted in high levels of (corporate, household and sovereign) indebtedness. The neoliberal policies may themselves yet be reversed in a populist backlash if one or more of the Latin American countries is forced to default.

Even *The Economist*, no foe of income inequality, agrees that rapid market liberalization is likely to widen income inequalities. "It is no coincidence that the biggest increases in income inequalities have occurred in economies such as those of America, Britain and New Zealand, where free-market economic policies have been pursued most zealously", it says. [25]

What then are the main causes of growing global inequality? I have suggested several intertwining forces. First, faster population growth at the low income end. Second, slower long-run economic growth at the low income end. Third, continuing concentration of knowledge-intensive, high value-added activity in the already rich OECD countries, reflecting the continuing importance of agglomeration economies of scale in activities of this kind. Fourth, rising prices of the goods and services exported by developed

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[25] "Inequality: for richer, for poorer", *The Economist*, 5 November 1994, 19-21. Explaining why income distribution has become more unequal in the English-speaking countries than in continental Europe, *The Economist* stresses the role of powerful trade unions, centralised wage bargaining and high minimum wages in Europe in propping up the wages of the low-paid; polarization in household structure between two-earner households and jobless single-parent families; and investment income rising faster than wage income as stockmarkets boomed in the 1980s and 1990s.

countries relative to those exported by developing countries. Fifth, more unstable growth rates of developing countries, higher frequency of financial crises among the middle-income countries, and higher costs of financial crises for middle-income countries (compared to crisis-affected rich countries) in terms of lost growth and more unequal internal income distribution.

To this one should add, sixth, the continuing redistribution of income in the OECD countries through the tax system and the welfare state, which in the case of the UK in 1992 reduced the ratio of the income of the top 20 percent of Britons to the poorest 20 percent from 25:1 before taxes and transfers to 7:1 afterwards. This welfare state system prevents anyone living in the OECD countries from falling very far down the world income distribution. And of course it gives a huge incentive for people living elsewhere to try to enter the OECD world by whatever means possible.

George Stigler once said, “There are not 18 good reasons for anything”, and my list of six factors looks suspiciously like the sort of everything-but-the- kitchen-sink list that Stigler was criticising. Clearly arguments of a more analytical kind are needed to weave the factors together. The central facts we need to explain are: (1) the richest 10 percent of the world’s population is pulling up from the median, and the poorest 10 percent is falling away from the median (table 3); and (2) the world middle class, so to speak, remains tiny, while the gulf between the 15 percent of the world’s population living in the richest countries and the three quarters living in the poorest countries remains huge (table 4).

A zone of peace and a zone of turmoil

Income divergence helps to explain another kind of polarization taking place in the world system, between a zone of peace and a zone of turmoil. The regions of the wealthy pole in charts 1 and 2 show a strengthening republican order of economic growth and liberal tolerance (except towards migrants), with technological innovation able to substitute for depleting natural capital. At least for those in the top half of rich country income distributions, this is a blissful time to be alive.[26] On the other hand, the regions of the lower and middle income pole contain many states whose capacity to govern is stagnant or eroding, mainly in Africa, the Middle East, Central Asia, Russia, and parts of East Asia. Here a rising proportion of the people find their access to basic necessities restricted at the same time as they see people driving Mercedes—on television if not outside their own windows.

The result is a lot of unemployed and angry young people, to whom the new information technologies have given the means to threaten the stability of

[26] Yet rates of depression are rising fast. See Robert Lane, “The road not taken: friendship, consumerism, and happiness”, *Critical Review*, 8(4), 1994, 521-554.

the societies they live in and even threaten social stability in countries of the wealthy zone. Economic growth in these countries often depletes natural capital and therefore future growth potential. More and more people see migration to the wealthy zone as their only salvation. The significance of the "missing middle" is partly that the three quarters of the world's people in the Third World must get to the *First* World in order appreciably to raise their incomes. There is not much of a Middle World for them to get to, and in any case average income in the Middle World is only 4 times higher than average income in the Third World, while average income in the First World is over 9 times higher.

The interests of the rich countries

As this suggests, world inequality matters as an indicator of global political strain. But it also matters for more directly economic reasons, as an indicator of the limits of growth of the rich countries. Marginalization of poor country populations robs rich country producers of customers. East Asia currently has excess capacity; Africa has huge shortages; but the two cannot be linked because Africa lacks purchasing power. The US after World War Two realized that its own growth would be imperilled if it did not redistribute massively to Europe, including to the defeated states. The Marshall Plan redistributed around 4 percent of US GDP for several years in order to generate in Europe the purchasing power needed to buy US goods, as well as to keep communist movements from state power. Today, resource transfers from rich countries to poor, and downwards redistribution within poor countries (including via the mechanisms used in the West, such as collective action by the poor and slowly rising legal minimum wages or earned-income tax credits), are in the collective interests of the rich countries as the Marshall Plan was to the United States. Those who respond to evidence of rising world inequality by saying, "pulling up the poor still seems a nobler calling than pulling down the rich"[27], overlook this. Without downwards redistribution, the rich may not remain rich.

Development policies

It might be argued that since the biggest increase in poverty came in Africa, central Asia, rural India and rural China—places not connected to the global economy--this shows that globalization works to reduce poverty. The solution for these areas is fuller integration into the world economy—more globalization rather than less. As Martin Wolf puts it, "One thing, above all,

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[27] "Of rich and poor: elsewhere in this week's issue the economist Robert Wade argues that global inequality is increasing faster than hitherto suspected, and that governments should respond… Is he right?", Economics Focus, *The Economist,* 28 April 2001, p.92.

is quite clear: if the world is to become less unequal through raising the bottom, rather than collapsing the top, and still more if mass poverty is to be eliminated, it can only be via successful integration, not its opposite”. [28] The statement collapses into tautology with the qualifier “successful”; but that aside, it begs the question of the conditions for “successful integration”.

Of course, the populations of these regions would be better off if more densely connected to the world economy—if connected like Europe, say. People in the bottom deciles suffer from the *weakness* of capitalist development in the regions where they live. The question of development policy is whether this weakness can be cured mainly by opening up their markets, investing in infrastructure, removing price distortions, and strengthening the rule of law. Many economists say that the positive correlation between average incomes and countries’ integration into the world economy (high trade to GDP, for example) supports the case for a development strategy based on maximum integration.

But this argument obscures the distinction between the policies that the richer countries followed while they were getting rich and those they follow once rich. The East Asian states achieved great economic success—eliminated poverty, created the capacity to generate self-sustaining improvements in living conditions for the whole population, and closed the gap with average living conditions in the advanced industrial countries--by creating national economic space that was *partially* separate from the world economy, within which resources could be combined and made to produce nationally-marketable products even when those products would not have been able to compete against import substitutes; at the same time as they gave strong incentives for producers to export to world markets. They recognized—as did the World Bank and even the US government in those days--that if they just concentrated on “levelling the playing field” the players might not show up and those who did might include few of their own nationals. Their strategy for creating self-generating development and integrating into the world economy in a strategic way fits neither of the two alternatives—full-scale integration or isolation--that Martin Wolf, among many others, pose. (I spell out the argument in *Governing the Market*.) [29]

In particular, they were careful about the terms on which they allowed foreign capital to enter (whether in the form of direct foreign investment or loans), and about the liberalization and opening of the financial system. In the 1990s Korea abandonned its earlier caution as it came under heavy US pressure to open its financial markets in return for US support of its OECD membership. It was rewarded by being far more adversely affected by the

[28] Martin Wolf, “Growth makes the poor richer”, *Financial Times*, 24 January 2001.

[29] Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization*, Princeton University Press, 1990.

Asian crisis of 1997-98 than nearby Taiwan, which remained more cautious about financial liberalization and opening.

In African conditions today, what possibility is there of national populations which are 50 percent functionally illiterate and innumerate getting access to the productivity gains of new technologies? In open competition with labor forces and infrastructures elsewhere, they will always lose, however low the exchange rate (except where high transport costs give natural protection). They should put up partial barriers as the East Asians did, behind which partly different rules apply, so as to balance (a) the benefits of comparative advantage and competitive discipline, against (b) the benefits of putting resources to work that could not be profitably put to work in a fully open economy. They should have a partly closed capital account, and should take care to minimize the "inverse correlation" in their capital structure (minimize the extent to which repayment obligations are lower when capacity to repay is higher and higher when capacity to repay is lower). Hence they should pay more for foreign loans during goods times, by hedging or by indexing them to the price of their main exports or by denominating them in *domestic* currency; and they should also hedge the price of their main commodity exports.[30] They should follow Friedrich List as much as Adam Smith.

All developing countries need to be cautious about financial liberalization and opening. We now have many examples of how the monetary policies of the US, Japan and Europe (G3) have "externalities" in the form of costs that are shifted onto others—which could have been shifted onto them nearly as easily had the countries maintained limits on capital inflows and outflows. The messy Mexican crisis of 1994-95 and the crises of East Asia and Russia in 1997-98 were due in large part to aggressive monetary easing by the US Federal Reserve after the 1990-91 recession and by the Japanese central bank after the bubble burst in 1990. But nervous consumers and shaky banks were slow to respond, and the abundant low-yielding dollars and yen ended up, via "carry trades", invested in high-yielding emerging market currencies—which could happen because the governments had removed most of the restrictions on capital inflows. The volume of foreign currency obligations built up to such a point in Mexico and then in East Asia that quite small shocks were sufficient to precipitate sharp falls in currencies and other assets, at great cost to economic growth. Remarkably, the prevailing explanation for these crises—prevailing not only in the G3 but also in the crisis-affected countries themselves—says that the governments of the crisis-affected countries are to blame because of their "crony capitalism", lack of transparency, and insufficient commitment to

[30] Pettis, *The Volatility Machine.*

"reform".[31] This is like saying that fire is caused by the presence of inflammable material and the only way to prevent fire is to remove inflammable material. It is true but trivial. It directs attention away from the question of the contingent causes of fire, such as the behavior of cigarette smokers and arsonists.[32]

China is in the midst of perhaps the fastest and most far-reaching transformations seen anywhere in the past two hundred years—but doing so in a "gradualist" way in line with the broadly *dirigiste* strategy of pre-1970 Japan and pre-1990 South Korea and Taiwan; and thereby violating many current World Bank precepts about how countries should to develop. Russia and most of the former Soviet empire have followed a Big Bang strategy of full-scale integration and privatization (with Harvard-based American advisors and the World Bank playing the leading role in devising and implementing the Big Bang). The result? Large parts of the former Soviet Union are more impoverished than they were in 1989, and the most profitable assets have fallen into the hands of economic gangsters. In the comparison, China easily wins. [33]

The great danger of the state governing the market is wholesale corruption and incompetence—the danger that the state does not establish rules and organizations that build development capacity but instead rips off the population to the benefit of state incumbants and allied "businessmen" and thereby discourages productive investment. Where governmental gangsterism reigns, as in much of Africa and the former Soviet Union, then in the shorter run (which in development terms means at least a decade) a development strategy focused on building up the institutional infrastructure of markets, investing in infrastructure of roads, schools, health systems, and promoting the rule of law, may be about the best that can be hoped for.

In the longer run, building up organizational capacity outside the state is important. "Non-governmental organizations" can constitute a form of social mobilization through which governments can be made more accountable, and provide training grounds for organizational competence generally, whether in business or the state. But NGOs tend to be single-interest and therefore politically divisive. They have to be balanced by political parties and by the state itself, organizations where different interests can be aggregated, brought to a point of convergence, compromises struck, priorities established. [34]

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[31] See my earlier cited papers on the Asian crisis. Also Wade, "Wheels within wheels: rethinking the Asian crisis and the Asian model", *Annual Review of Political Science 2000*, (ed.) N. Polsby, 3: 85-115.

[32] Arun Motianey, letter, *Financial Times*, 1 November 2000.

[33] Paul Starobin, "What went wrong?", *National Journal*, Dec 4, 1999.

[34] The East Asian cases, in contrast, had relatively weak "civil societies" and intense social mobilization through state-controlled channels. (Wade, *Irrigation and Agricultural Politics in South Korea*, Westview

By and large, stronger markets need stronger states, and stronger states need both stronger markets and stronger civil societies. Need, and also tend to foster. The complementarities are strong. The Marshall Plan's programs in post-war Europe recognized that redistributive flows had to be accompanied by measures to build state capacity to manage the national economy and regulate markets, financial markets especially. [to CHECK]

The World Bank has attracted criticism from its borrowing governments for entering the "political" terrain of governance. Through Structural Adjustment Loans (SALs) it has required Uganda, for example, to privatize many of its loss-making state-owned enterprises, cut the number of civil servants on the payroll, raise salaries of those who remain, institute meritocratic recruitment, and raise the tax revenue from 4 percent of GDP to more like 18 percent of GDP; while at the same time the Bank has been fostering the growth of NGOs operating in Uganda. In the eyes of some this is derided as an anti-statist, neoliberal agenda, and in the eyes of others, as an infringement of sovereignty. By my lights it is the only sensible way forward. What the Bank should also be doing but is not—here its neoliberal bias is damaging—is to encourage the Ugandan government to begin on a small scale to take the sorts of direct productive-capacity-enhancing interventions that the East Asian governments deployed in a national economic space partially insulated from the world economy.

Concerted strategies to strengthen states, industries, and civil societies in the low income parts of the world have to be complemented by more open markets in Europe, North America and Japan for exports from these areas[35] ; and by increases in the flows of cheap, low cost resources from rich countries to poor, to be invested in the many sectors (like water treatment, universities) where private financiers have no interest. Without a big push, we can expect world income distribution to continue widening, especially between Subsaharan Africa and parts of South Asia, on the one hand, and the rest of the world. This will generate more global political turbulence and more economic crises--not only in the low income world but in the rich world as well.

The multilateral organizations

Press, 1982) The states remained relatively disciplined in their use of economic power thanks in part to looming threats from hostile neighbors—hardly a prescribable source of state discipline.

[35] Western markets have much higher barriers against imports from the 50 or so poorest countries than they do against imports from each other. Opening western markets has to be complemented with adjustment assistance for displaced western workers.

It is remarkable how unconcerned are the World Bank, the IMF, and other agenda-setting global organizations about world income inequality.[36] The Bank's *World Development Report* for 2000 even said that rising income inequality "should not be seen as negative" provided that the incomes at the bottom do not fall and the number of people in poverty falls.[37] Indeed, they neglect not only matters of world income distribution, but also world inflation, world exchange rates, and world interest rates; and in the case of the World Bank, the world environmental issues of the oceans, the atmosphere, and nuclear waste.[38] When the Bank's governors (finance ministers of member countries) issued a set of priorities for the World Bank's new "global" work in September 2000 (the Prague Communique), what was the number 1 priority problem for the Bank to work on, ahead of: mitigating conflict and disease, protecting the environment, and sharing knowelege about development? "Facilitating international movement of goods, services, and factors of production". The very lack of priority given to properly global problems by these organizations shows why it is misleading to call them "world organizations". They are world bodies in the sense that almost all states are members, but they think in state-centric rather than global ways.

It is striking that most of the organized opposition, as well as much of the support, for more globalization comes from North America, Western Europe and Oceania.[39] Why have elites from developing countries for the most part subscribed to the globalization agenda that western states, businesses, and multilateral organizations have been promoting, if a plausible case can be made that the gains of free markets for goods and capital tend to be concentrated in the top levels of the income distributions of their countries? Why are they doing rather little to integrate their economies into

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[36] Milanovic, Dikhanov and Ward are at the World Bank; but they are virtually the only Bank staff to have worked on world income distribution for years, and they have pushed their work forward with little encouragement from management.

[37] Bank publications tend to give a misleadingly optimistic spin to the relationship between "growth" and the incomes of the poor. A typical formulation goes as follows: "By stimulating higher growth, [trade] integration [as measured by an increase in the ratio of trade to GDP] can have a strong positive impact on poverty reduction. There is now robust cross-country empirical evidence that growth is on average associated one-for-one with higher incomes of the poor" (Amar Bhattachariya, "Poverty in an age of globalization", The World Bank, October 2000. In plain English this says that a 5 percent increase in the average national income tends to be associated with a 5 percent increase in the average income of "the poor", a 1 percent increase in the average with a 1 percent increase in the income of the poor, and so on. What the Bank consistently does not point out is that this implies a *widening* of the gap. By arithmetical necessity, an x percent increase in a higher number and an x percent increase in a lower number implies an x percent increase in the gap between them. The Bank's favorite phrase, "one-for-one", as in the above, suggests the metaphor of "a rising tide lifts all boats (equally)".

[38] The World Bank's co-sponsorship of the Global Environmental Facility represents a small qualification.

[39] However, Mark Ellis-Jones of the World Development Movement reports that in the year between the 1999 World Trade Organization meeting in Seattle and the 2000 International Monetary Fund/World Bank annual meeting in Prague there were at least 50 outbreaks of civil unrest in 13 different countries directed at IMF policies alone. Half of them ended in violent clashes with the police or military, and ten people were killed (letter, *Financial Times*, 4 May 2001.)

the world economy in a strategic way rather than open-endedly? Part of the reason may be that elites in developing countries, like their counterparts in the rich world, are content to believe either that world inequality is falling, or that inequality is good because it is the source of incentives. They, like the intergovernmental economic organizations (and the reformers of Victorian England), worry about *poverty*. But they see no link between widening world income distribution and poverty; and they think that poverty can be fixed by providing the poor with welfare and opportunities without changing income and asset distributions or mounting an active state industrial policy. Academic analysts have a responsibility to counter the current neglect by analysing the relationship between world income distribution trends and poverty trends as a way of getting distribution issues onto the world agenda.

The growing inequality in world income distribution is like global warming. Its effects are diffuse and long term, and there is always something more pressing to deal with. We don't seem to be able to rely on leadership and appeals to humanity to generate action. (Consider how much mobilization and lobbying effort was necessary just to get the rich countries to agree to the small amount of debt relief for the poorest countries under the Highly Indebted Poor Countries initiative.) The question is how much more unequal world income distribution can become before the resulting political instabilities, migration flows and social disruption reach the point of harming the rich world enough to move it to action. Afterall, the last great surge of global integration and inequality--in the second half of the 19th century and the first decade of the twentieth--produced such unequalization and disruption that governments constrained and then reversed global integration, producing on the way some of the worst catastrophes of the millenium. If today's inequalities continue to increase, if social policy continues to move in the direction of "risk is an opportunity for individuals to profit from" and away from "society has a responsibility to protect individuals from certain kinds of risks", if the operational norm of world elites continues to shift towards "grab what you can and the devil take the hindmost as quickly as he can", opposition to the things called "globalization" will continue to spread. We in the rich world should mobilize our governments, the multilateral organizations, and international NGOs—the actors who have the power to change the norms and rules of the world economy--to establish as an overarching priority a more equal world income distribution, and not just, as now, fewer people in poverty.