

The IFS Deaton Review: Inequalities in the 21st Century

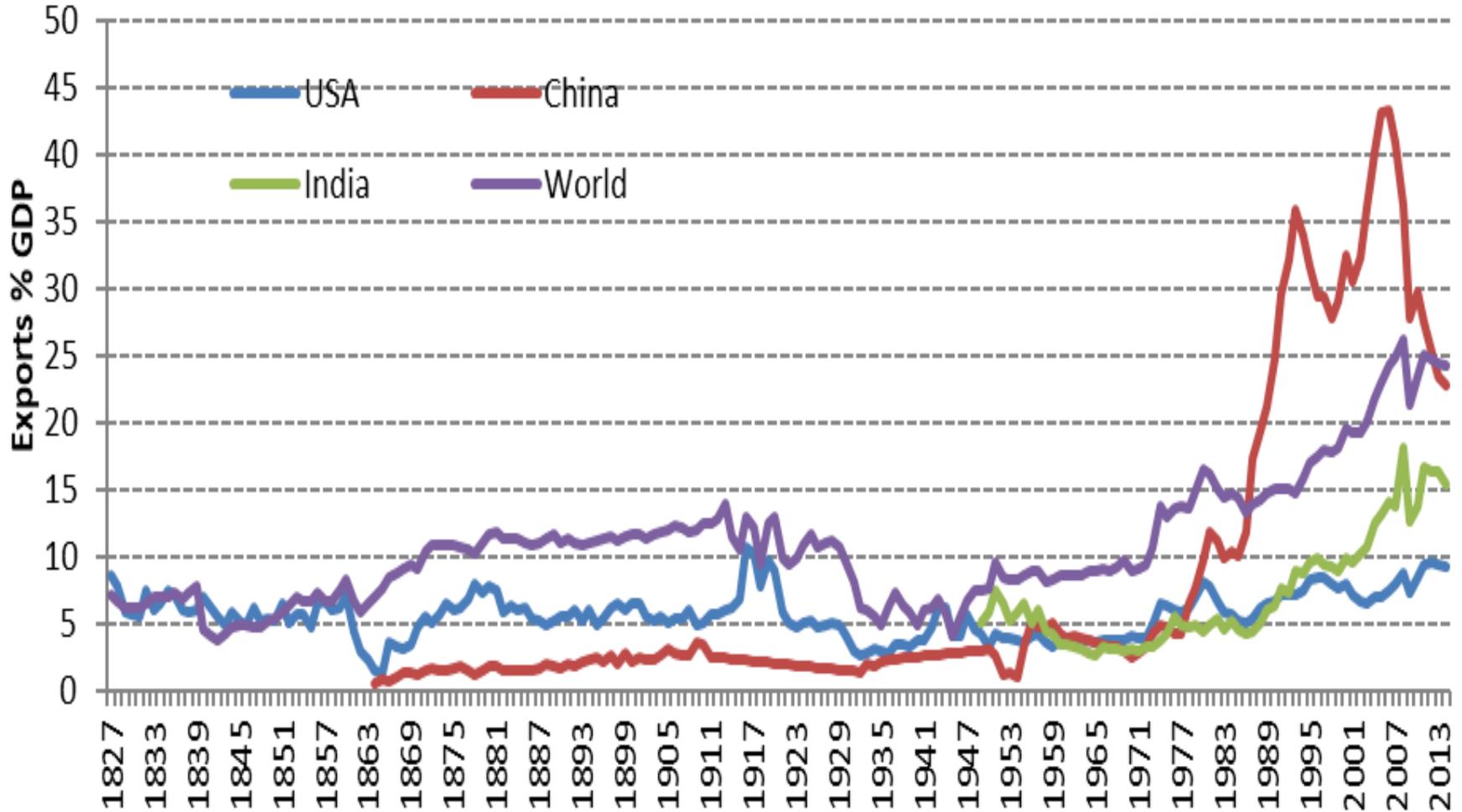
Thoughts on Globalization and Inequality

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The Age of Globalization

Exports as % of GDP, 1827-2013



Source: Fouquin and Hugot; CEPII 2016; National data

The Backlash

- Revolt of the public in many (developed) countries against free trade and immigration
- Not specific to a particular country
- US: Return to Protectionism; UK: Brexit
- Paralyzed WTO

The Puzzle

- Backlash started at a time of global prosperity
- Public attitudes towards trade positive
- Academia: Emphasis on aggregate gains from Trade

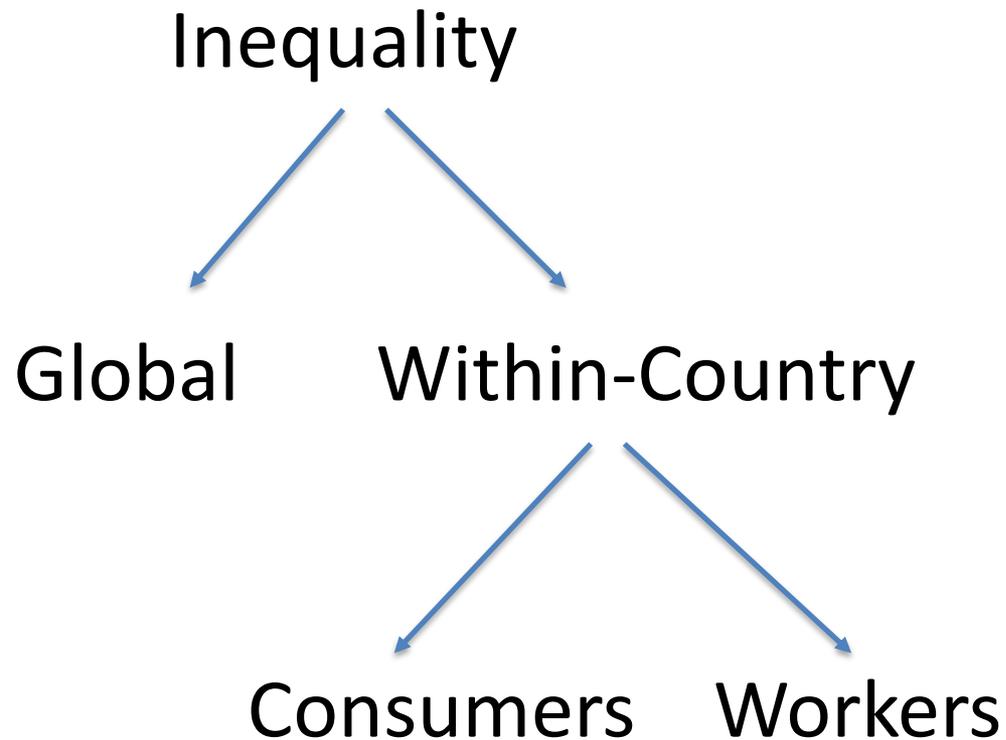
On the Aggregate Gains from Trade

- In static models, gains shown to be small, especially for large countries.
- ACR formula:
 - Aggregate gains depend only on **share of domestic expenditure and trade elasticity** in a large class of models
- More recently, Fajgelbaum, Goldberg, Kennedy and Khandelwal: “The Return to Protectionism”
 - Aggregate effects of current trade war: very small
- BUT: Distributional effects considerable

Role of Rising Inequality?

Globalization and Inequality

- Inequality: What inequality?



Global Inequality

- Has been reduced dramatically post-World War II
- Deaton (“The Great Escape”); World Bank (WDR 2006); Branko Milanovic (“Global Inequality....”)
- Globalization, and in particular the integration of China and East Asian economies into the world trading system played an important role
- Tradeoff between global and within-country inequality?

Within-Country Inequality

People as Workers

→ Labor Market Effects of Globalization

Labor Market (US and Europe)

- Increase in Skill Premium in the 70s, 80s and 90s.
- Polarization starting in the late 90s
- Decline in Manufacturing Employment in the last 15 years

→ Role of Globalization?

What we know so far

- Workhorse model of international trade (Heckscher-Ohlin) provides a natural way to link trade to the increase in skill premium
- BUT: Consensus that trade played only a secondary role in the increase of the skill premium
- Trade only important in interaction with technology

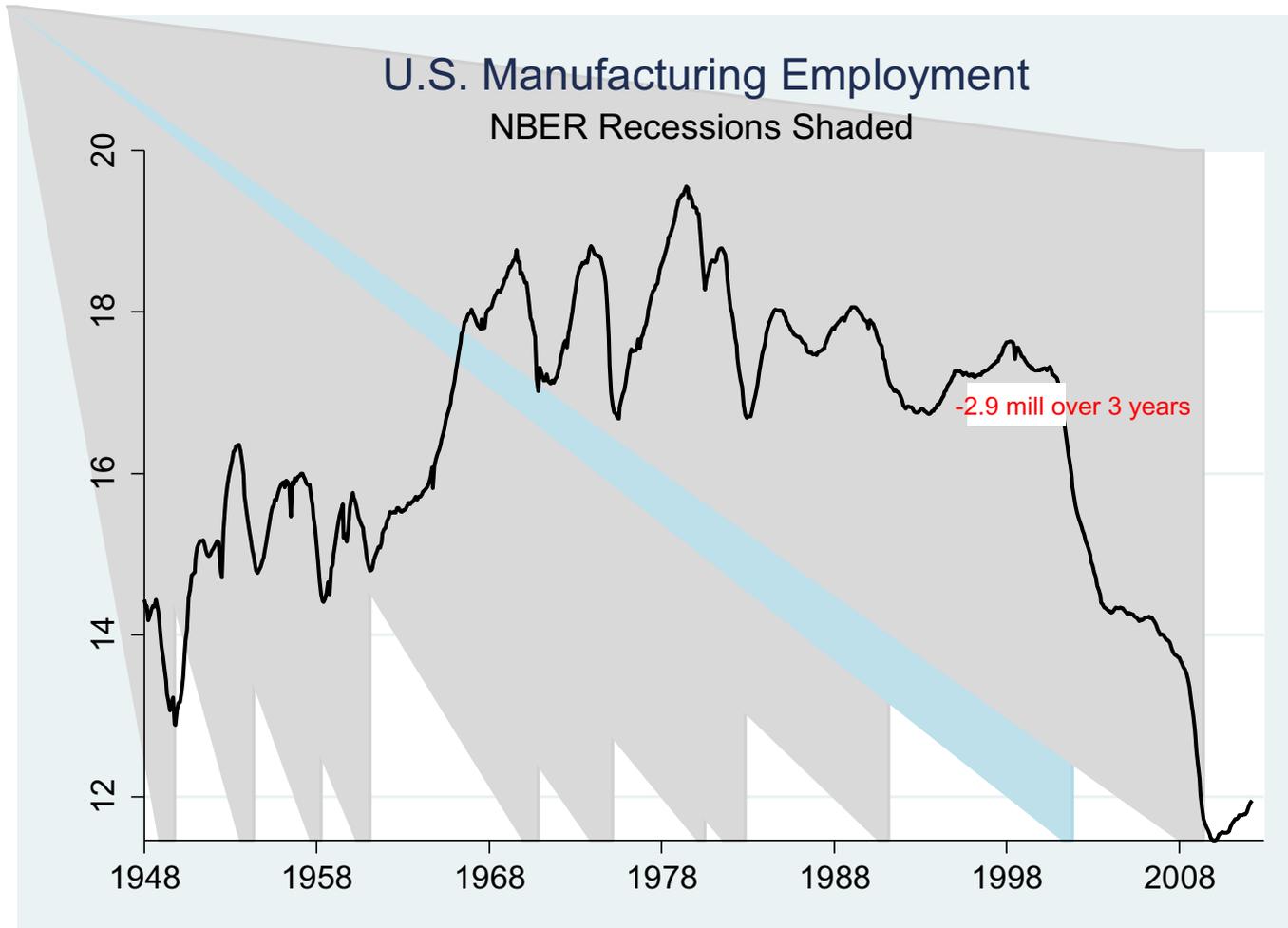
Shifting Consensus in the 2000s

- Trade is a potentially important driver of inequality
- Why? (→ still open question)
 - China
 - Shift of focus from Skill Premium to Regional Inequality

On the Role of China

- ADH, Pierce and Schott (AER papers):
→ The “China Shock”
- China responsible for dramatic decline of US manufacturing employment and rising regional disparities
- How about Europe?
- Deaton Review will provide additional evidence on European countries
- Was the experience there different, and if so, why?
- Policy Implications

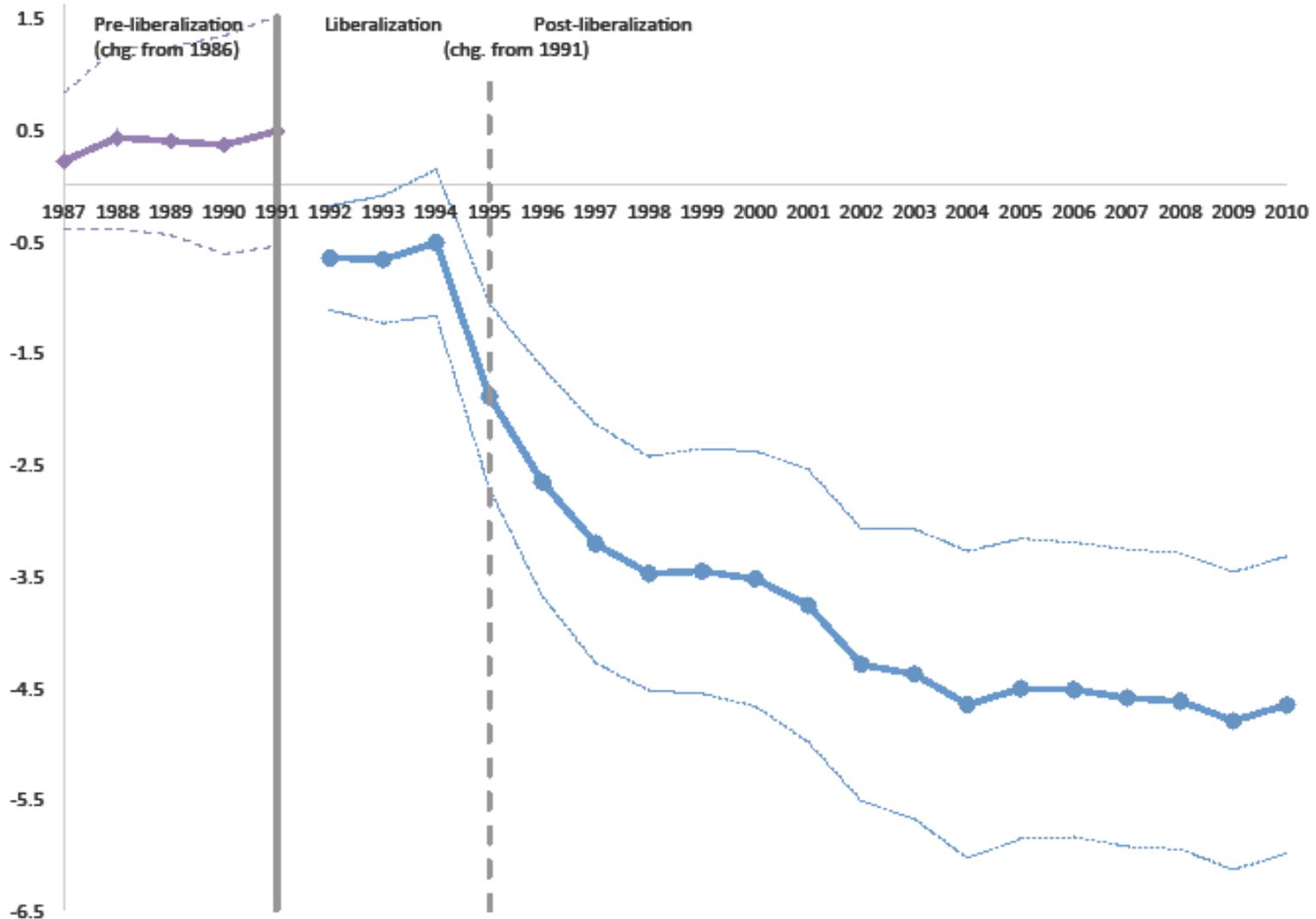
Post-War U.S. Manufacturing Employment



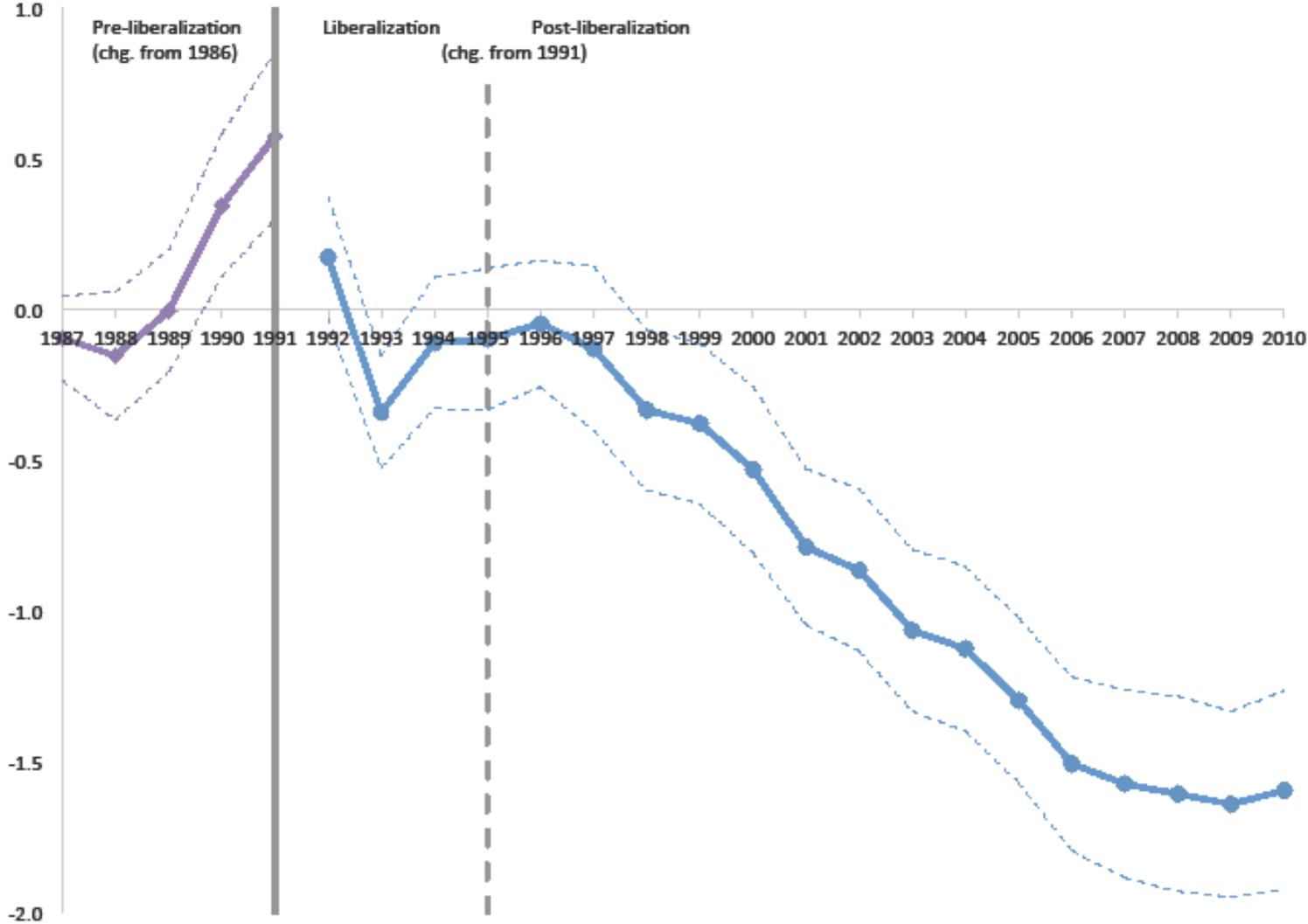
Alternative Interpretation: Shift of focus to Regional Inequality

- Supported by evidence from developing countries (Topalova, Dix-Carneiro and Kovak)
- ADH focuses on inequality across commuting zones
- Suggests limited mobility of labor across space

Effects of Brazilian Trade Liberalization on Employment (Dix-Carneiro and Kovak, 2015)



Effects of Brazilian Trade Liberalization on Earnings (Dix-Carneiro and Kovak, 2015)



Open Questions for the Deaton Review

- Experience in European countries?
- What is the role of country size in inter-regional mobility?
- How long is the long-run?
(ADH and Dix-Carneiro/Kovak suggest very long)
- What is the role of policy?

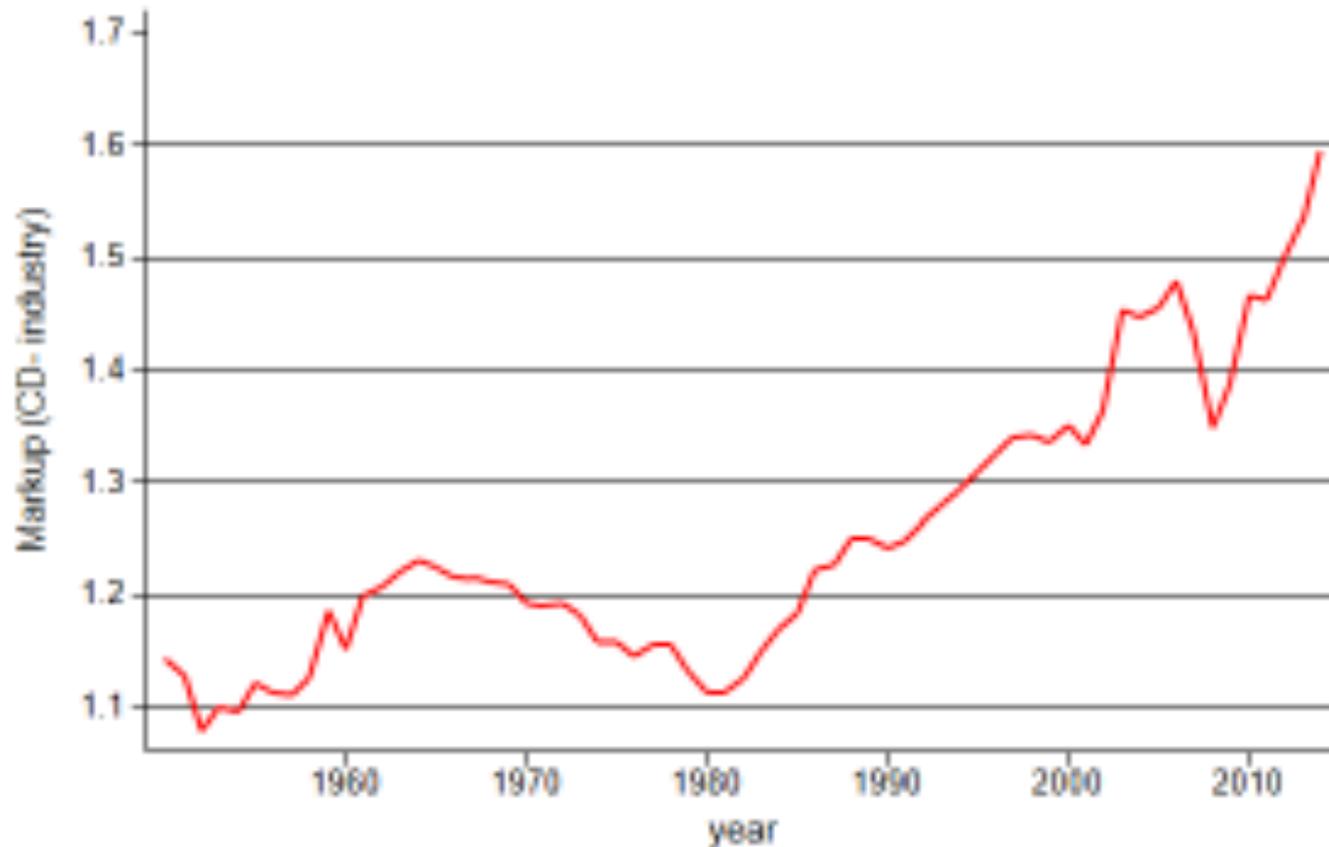
Within-Country Inequality

People as Consumers

- Models tell us that trade leads to lower prices, higher quality, more variety
- But what do the data tell us?
- Work on prices very limited.
- Deaton Review: Provide more evidence on price and quality effects of trade in European countries.

Some Open Questions

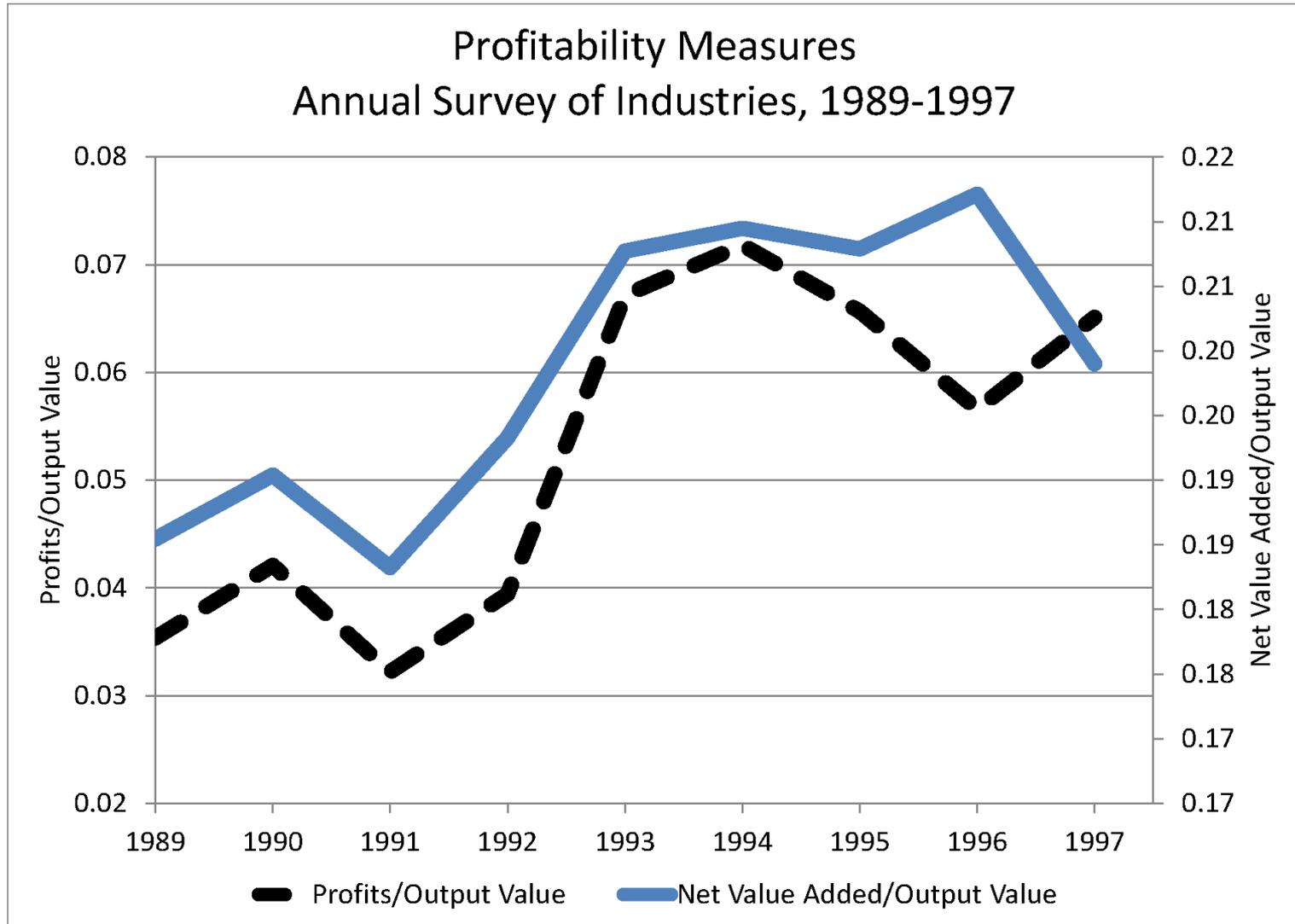
- Increase in Firm Profits (De Loecker and Eeckhout)
- Role of Globalization?



Evidence from Developing Countries

- DeLoecker, Goldberg, Khandelwal and Pavcnik (ECA 2016):
 - Trade Liberalization reduced prices
 - It increased quality
 - Led to greater product variety
 - But increased firm profits
 - Benefits to consumers in the form of lower prices smaller than predicted by models of perfect competition or constant markups

Evolution of Markups in India



- Did globalization contribute to the rise of markups worldwide?
- Did it contribute to the declining labor share?

Thank you!