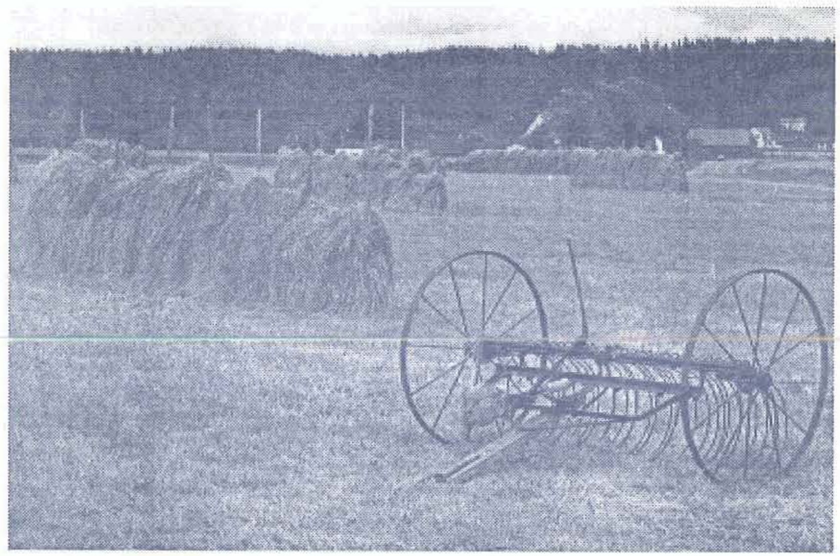
Die Stiftung für liberale Politik

Friedrich-Naumann-Stiftung

Johan Norberg

# Globalisation and the Poor



Occasional Paper

# *Globalisation and the Poor*

*Johan Norberg, November 2003*

The anti-globalisation movement had its coming-out party in Seattle in 1999, when thousands of activists and trade union members protested against a new round of trade negotiations in the World Trade Organisation. Millions were drawn to these protests because of a preceding anti-WTO statement that was circulated on the internet, and signed by about 1500 different groups, from churches to militant communists. Their first accusation against the WTO in the statement was that free trade and globalisation:

> *"has contributed to the concentration of wealth in the hands of the rich few; increasing poverty for the majority of the world's population; and unsustainable patterns of production and consumption."*

Poverty is also the major issue when you read anti-globalist writers and theoreticians. Their view is that globalisation is making the rich richer and the poor poorer. If this is their biggest concern, surely they should change their mind about the globalisation process if they got new information, which not merely shows that globalisation is not increasing poverty, but in fact an efficient way of reducing human poverty. That is what I am going to argue for in this paper, and I will also present the current debate on poverty measurements. What has happened to poverty in the era of globalisation, and why?

## Relative or absolute?

To begin with, we must define what we mean when we discuss poverty. Most often there is a discussion whether absolute or relative poverty is the most relevant measurement. In this debate, I am an absolutist. Relative poverty is not a measure of poverty, but of inequality. Instead of measuring how poor someone is, it says how poor that person is in relation to others. One poverty concept frequently used, e.g. by the UNDP, rates a person as poor if they have less than half the median wage in the country where they live. This means that a person regarded as "loaded" when living in a poor country like Nepal is considered as poor as a church mouse when living in the affluent USA. These relative figures, consequently, cannot be compared internationally.

But the biggest problem with the relative concept is that it completely distorts our view of poverty. Poverty in China has been reduced faster than ever in the last two decades. People have higher wages and better living standards than every before. But at the same time income gaps within China have widened because towns and cities have grown faster than the countryside. Inequality has grown, and therefore, relative poverty has grown, even though everybody is richer than before. Surely there must be something wrong with a measure that says that poverty is increasing when everybody gets richer? Only those who consider wealth a greater problem than poverty can find a problem in some millionaires becoming billionaires while others get out of poverty.

An absolute poverty concept is to be preferred, for example a specific money line. But that view has also been challenged. As Amartya Sen, Indian economist and Nobel laureate, has emphasised, poverty is not just a material problem. Poverty is something wider, it is about powerlessness, about being deprived of basic opportunities and freedom of choice. Small incomes are often symptomatic of the absence of these things, of people being subjected to coercion and marginalization. Human development means leading a reasonably healthy and secure life, with a good standard of living and freedom to shape one's own life.

But even though I accept this criticism to a big extent, the investigation of material development is important. Both because it indicates how these conditions have developed and also because it contributes to development as such. It is material resources, individual and societal, which enable people to feed themselves, be educated, obtain health care and be spared watching their children die. It can and should be combined with other indicators of human welfare, but it is one of the most important ones in itself.

The most common international poverty line is the World Bank's definition of absolute poverty. According to this definition you are poor if your income is less than one dollar a day, to be exact, $1.08. And this is adjusted for purchasing power, so that it corresponds to the same standard in all countries. This definition was chosen because it was the median of the poverty definitions in the ten poorest countries that the World Bank had detailed statistics from. And probably also because it is easy to popularise and remember. Let's use that definition to dig into the historical change in poverty rates.

## The extent of poverty

In 1820, about 85 per cent of the world population lived on the equivalent of a dollar a day, converted to today's purchasing power. The biggest misconception in the debate on globalisation is that poverty is



supposedly something new, and that things are getting worse. It is not. One hundred years ago, every country was a developing country. The new things in our modern world is not poverty, but wealth. The fact that some countries and regions have escaped that poverty.

In the beginning of the 19th century something happened and poverty began to decline. In 1910 only 65 per cent lived in absolute poverty and in 1950 55 percent. Then came another big change. UNDP, the United Nations Development Programme, has observed that, all in all, world poverty has fallen more during the past 50 years than during the preceding 500. In 1970 absolute poverty had shrunk to 35 per cent, in 1980 it was slightly more than 30 per cent, and today it is about 20 per cent. (Often the figure 23 per cent is mentioned, but that is as a proportion of the developing country population.)

Even though the proportion of people in poverty has been shrinking in the last 200 years, the number of poor has increased, because world population has been increasing constantly. The unique with the decline in the last twenty years is that not only the proportion, but also the *absolute number* of absolute poor has declined - for the first time in world history. During these two decades, world population has grown by about 1,8 billion, but yet the number of absolute poor has declined by about 200 million people, according to the World Bank. Material developments in the past half-century have resulted in the world having over three billion more people liberated from poverty.

Even those encouraging findings, however, probably overestimate world poverty, because the World Bank uses survey data as the basis for its assessments on consumption. This data is notoriously unreliable. It suggests that South Koreans are richer than the Swedes and British, for example, and that Ethiopia is richer than India. Furthermore, surveys capture less and less of an individual's income. The average poor person at exactly the same level of poverty in surveys in 1987 and 1998 had in reality seen her income increase by 17 per cent. One of the most basic problems is that people begin to forget what they consumed after just one day, but the surveys are about their consumption a week or a month back. An Indian survey from 2000 showed that questions about the consumption during a shorter period changed the answers dramatically. When they shortened the period to just the last days, the extent of rural poverty in India was "cut" from 43 to 24 per cent.

Former World Bank economist Surjit S. Bhalla recently published his own calculations supplementing survey results with national accounts data (in the book *Imagine there's no country,* Institute for International Economics, 2002). Bhalla found that the United Nations's goal of lowering world poverty to below 15 percent by 2015 has already been achieved and surpassed. Absolute poverty had actually fallen from a level of 44 percent in 1980 to 13 percent in 2000. According to Bhalla's calculations, 800 million people have been lifted out of absolute poverty in 20 years. If this is true, we have just witnessed poverty reduction on such an astonishing scale which we will probably never see again.

## Economic growth

It's extremely difficult to make global calculations about poverty, so it's impossible to say who is right and who is wrong about the true extent. But what we do know is the direction, there is a consensus between the World Bank and Surjit Bhalla that the world has never before seen such a big reduction in human poverty as we have seen in the last 20 years. And such poverty reduction does not happen arbitrarily. It is a natural consequence of economic growth. No country has ever succeeded in reducing poverty without having long-term growth. Nor is there any case of the opposite, i.e. of a country having had long-term sustainable growth which has not been of benefit to the poor population. If we have 3 percent growth per annum, this means that the economy, our capital and our incomes double every 23 years. If growth is twice as fast, these things double about every 12 years. If growth is twice as fast, these things double about every 12 years. This is an unparalleled growth of prosperity, compared with which even vigorous government measures for the redistribution of incomes take on a puny aspect.

This makes growth the best cure for poverty. Some economists have spoken of a "trickle-down" effect, in the sense of some taking the lead and getting rich first, after which parts of this wealth trickle down to the poor, as a result of the rich demanding their labour. This thesis rather reminds one of the image of the poor man getting the crumbs that fall from the rich man's table, but this is a completely mistaken picture of the true effect of growth. On the contrary, what happens is that the poor derive benefit from growth to roughly the same extent and at the same speed as the rich. They benefit immediately from the value of their labour increasing and from the goods they buy becoming cheaper in relation to their income.

Two World Bank economists, David Dollar and Aart Kraay, studied 40 years' income statistics from 80 countries. Their studies show that growth benefits the poor just as much as the rich. With 1 per cent growth the poor increase their income on average by 1 per cent, with 10 per cent growth they raise it, on average, by 10 percent. Not always and not everywhere - there are exceptions and variations - but on average.

This has also made it possible to fight misery and increase living standards generally. During the last 30 years chronic hunger and the extent



of child labour in the developing countries have been cut in half. In the last half century, life expectancy has gone up from 46 to 64 years and infant mortality has been reduced for 18 to 8 per cent. These indicators are better in the developing countries today, than they were in the richest countries a hundred years ago.

It is not a coincidence that the great waves of poverty reduction have also been the periods of two unique growth stories. In its 1997 *Human development report*, the UNDP notes that humanity has seen two "great ascents". The first began in the 19th century, with the industrial revolution in the US and Europe. The second began during the post-war era and is now in full swing, with especially Asia noting ever-greater advances in the war against poverty, hunger, disease and illiteracy. Six Asians in ten were absolutely poor in 175. Today's figure is less than two out of ten.

It is also absolutely essential to understand that this was the two periods in which the West, and later Asia began to globalise in a serious way. Let me pick two examples to show the link between globalisation and poverty reduction. The European example is Sweden in the 19th century, and the Asian example is Taiwan in the 20th century.

## Economic miracle 1 : Sweden

In 1870, Sweden was poorer than Congo is today. People lived twenty years shorter than they do in developing countries today, and infant mortality was twice as high as in the average developing country. My forefathers were literally starving. The lack of trade, markets and communications in one region meant that a crop failure resulted in hunger there. In 1870 Swedes had to make bread from bark, lichen and straw to survive. They minced bones from fish and other animals to meal, on which they made porridge.

If you had levelled out all Swedish property in the middle of the 19th century, it would still have given everybody a life in poverty, of the levels of today's Mozambique. So redistribution was not the solution. Instead Sweden was saved by liberalisation. In a few decades, a couple of classical liberal politicians gave Sweden religious liberty, freedom of speech, and economic liberty, so that people could start their own business and buy and sell freely on the market.

A trade agreement with England and France in 1865 made it possible for Swedes to specialise in what we did best. We couldn't produce food well, but we could produce steel and timber, and sell it abroad. For the money we made, we could buy food. And because we had a free market, people and companies had to think of new and better ideas -

otherwise consumers would turn to someone else. In 1870, the industrial revolution began in Sweden. New companies exported to countries across the world, and production grew rapidly. The competition forced our companies to become more efficient, and old industries were closed so that we could meet new demands, such as better clothes, sanitation, health care and education.

By 1950, before the Swedish welfare state was built, the Swedish economy had quadrupled. Infant mortality had been reduced by 85 per cent and life expectancy had increased by a miraculous 25 years. We were on our way to abolish poverty.

Even more interesting is that Sweden's economy grew at a much faster rate than the developed countries it traded with. The wages in Sweden grew from 33 per cent of the average wage in the US in 1870 to 56 per cent in the early 1900s, even though American wages soared at the same time. This shouldn't surprise anyone. Economic models predict that poor countries should have higher growth rates than affluent ones if there is a free flow of capital, trade and ideas between them. They have more latent resources to harness, and they can benefit from the existence of wealthier nations to which they export goods and from which they import capital and more advanced technology, whereas affluent countries have already captured many of those gains. This is why globalisation is the hope of poor countries.

## Economic miracle 2: Taiwan

The transition that took Sweden 80 years took Taiwan 25 a century later. Because Taiwan began in an even more globalised world, with even richer countries to do business with and borrow ideas from. In 1950 Taiwan was an extremely poor country, with a hungry population. Taiwan was as poor as Kenya and other African countries, today it is 20 times richer. The difference was that Taiwan decided to go global. In contrast to African and Latin American countries, where they produced everything they needed themselves, Taiwan followed the normal East Asian pattern, and specialised in the industries they were best at, exported it to the West, and imported the rest. The factories were dirty, the machines dangerous and the Taiwanese worked long hours.

Taiwan's transition from hunger to South European living standards is personified in an old gentleman I met when I visited the country, Mr. Wang. His parents were poor farmers, who got property rights to their farm in the 60s, so that they could invest and borrow money. So Wange started factory production of toys such as Barbie dolls, sports gear like skateboards, stainless steel scissors with plastic handles.



If the anti-globalisation movement had been around when Taiwan was industrialised, they would have protested against the factories and told us we were exploiting cheap labour. Surely they would have organised a boycott. If enough Americans and Europeans had joined that boycott, Taiwan would still be poor today.

Because these sweatshops were the stepping stones for the Taiwanese. Mr. Wang lost two fingers to a machine, but he also became a millionaire. The decision to go global resulted in the Taiwanese economic miracle. In just ten years, the number of businesses more than tripled, and poverty was cut in half. Until today, Taiwan's foreign trade grew 400-fold, and real wages grew 10-fold. Today it is a country with living standards close to Southern Europe.

## Economic miracle 3: Vietnam

From these historical examples we learn that economic growth is necessary for poverty reduction. And we learn that economic freedom and trade is essential for economic growth. That is why we can see that Sweden's and Taiwan's economic transitions are repeated today, by the globalising nations of our era. Studies show that on average, countries with open markets grow 3 to 5 times quicker than closed economies. Poor, open economies today grow faster than Sweden and Taiwan do.

Let me pick an example. A couple of months ago I visited Vietnam, a communist country that has had second thoughts. When the socialist policies led to starvation in the mid-80's they began to open the economy and liberalise the markets. Since then the country's economy has doubled, and poverty has been halved. The most important reason is Vietnam's surge in exports. And the introduction of foreign multinationals has been an essential element, because it gave Vietnam access to the benefits of globalisation - foreign ideas, capital and technology. Nike is often branded an enemy of the poor. But when I visited Nike's supplier in Saigon the local union leader told me that even the communist party officials use the factories as positive examples of good business, where workers get high wages and a good and healthy work place.

When Nike started there ten years ago, the workers walked for hours to the factories, after three years on Nike wages, they could afford bicycles, another three years later they all drove mopeds to work.

I visited Tsi-Chi, a young Vietnamese woman. Her work at Nike has made it possible for her to leave the heavy and unhealthy work on the family farm, where she had to be outdoors all the day, in burning sun and during the rain period. Now she earns five times what she did, and earns more than her husband - which of course makes independence possible. She now has access to health care, she has bought a television set and built an extension to the house. A generation ago, she would have to put her son to work on the farm from an early age. But Tsi-Chi told me she wants to give him a good education, so that he can become a doctor. She is not an exception. Growth triumphed where prohibition had failed: 2.2 million Vietnamese children have gone from child labour to education in ten years.

If the anti-globalists got as they wanted, and we all boycotted sweatshops and goods produced by cheap labour, Tsi-Chi would lose her job, and have to go back to farming, and put her son to work. If multinationals and better wages is exploitation - then the problem in our world is that the poor countries aren't sufficiently exploited.

## Domestic obstacles

Vietnam is not an isolated success story. A recent World Bank report concluded that 24 developing countries with a total population of 3 billion are integrating into the global economy more quickly than ever. Their growth per capita has also increased from 1 per cent in the 1960s to 5 per cent in the 1990s. At the present rate, the average citizen in these developing countries will see her income doubled in less than 15 years.

Something worth noting is that the industrialised countries during this time only grew by 2 per cent. In other words, big developing countries are growing faster than the rich countries, which means that world inequality is being reduced today. But this doesn't happen everywhere. The biggest problems exist in Africa, where the number of poor continue to climb rapidly. I think there are two common, but false explanations for this fact. The first is that globalisation is to blame. The problem with this explanation is that Africa is the least democratic, least liberal, least capitalist and least globalised part of the world. If globalisation is so horrible, how can it create growth and poverty reduction everywhere, and at the same time be responsible for poverty and misery in the place where it has penetrated the least?

The other false explanation is some variation on cultural or biological traits. Asians are for example supposed to be more hard working or more intelligent than Africans. The problem with this explanation is that there is no clear-cut difference between Asian and African economies like that. We can see that Asian exceptions such as Burma and North Korea, with extremely isolationist and anti-market policies, have not followed the region's success. They are stuck in the deepest misery. And we can also see that African exceptions, that tried a more pro-market, pro-globalisation approach, countries such as Botswana, Uganda and Mauritius, have seen economic growth and poverty reduction.



The difference is not that some poor countries fail because people there are stupid, or not hard working. The difference is that some get the liberty to use their intelligence, and the freedom to work for their own benefit, some don't. Earlier I mentioned that Taiwan was as poor as Kenya 50 years ago, but that it is now 20 times richer. I think two better explanations for the poverty in Kenya and many other developing countries are domestic and external obstacles to globalisation and capitalism.

Recently I visited Kenya, and I saw the people working hard and being innovative - the problem is that they had to devote all that energy - not to production - but to avoid regulations, trade restrictions and corruption. I met Simon, a poor farmer who grew cabbage. His dream was to improve the farm, to get irrigation for the crops, and build a house. But how can he get that, when the government doesn't recognize his property right to his land? In that case he can't borrow the capital to invest. And if he would improve the land, he wouldn't reap the rewards - the government would.

The Peruvian economist Hernando de Soto has explained the problem of this lack of property rights in his innovative work *The Mystery of Capital*. People in the Third World occupy common lands, build simple houses in shanty towns which they are constantly improving, and establish small corner shops, just as poor people in the western world were doing a couple of hundred years ago. The trouble is that in Latin American and African countries today it is practically impossible to register this as property. In fact, the poor of the world are not really poor, but the government does not recognise their wealth, and because of that real estate worth about 9.3 trillion dollars is not officially registered. This is a huge sum, more than the combined value of all companies listed on the stock exchanges of the affluent countries - New York, Nasdaq, Toronto, Tokyo, London, Frankfurt, Paris, Milan - and a dozen more besides.

I also met Pamela in the enormous slums of Kibera in Kenya, who explained to me that she is not allowed to sell her samosa food without a government license. If you don't get a license, the police can demand bribes every time they see you. As someone said about the slums: "It's not safe to carry money around, there's too many policemen". Without a license she can't borrow money or expand. To get a license takes 11 bureaucratic procedures, 61 days and half a year's income. Want to start a business to become rich? Forget it, in Kenya you have to be *rich* to start a business. As a result almost two thirds of all Kenyan jobs are in the informal sector. Production is small scale for the local market, often hidden from potential customers because they have to hide from the authorities.

Once again, this problem is the same in most African and Larin American countries. Starting a business in Argentina takes 15 bureaucratic procedures and 68 days, in Paraguay it takes 18 bureaucratic procedures and 73 days. In Bolivia it costs you almost two year's income to get an official license, in Nicaragua it takes you more than three year's of income. If, as I think, globalisation is an extension of the classical market economy, with its specialisation and competition, then surely countries have to have basic market institutions to be able to participate fully. And therefore, people need more freedom and liberalisation, not less.

## Protectionism

But often, even that is not enough. There are also external obstacles. It was difficult to find success stories in Kenya. No booming sectors, no expanding industries. Except one. Flowers. I met June who was a manager at a rose farm, who explained to me that Kenya is the leading exporter of cut flowers to Europe. When I asked her what was the difference between her sector and others, she replied that the European union had agreed to keep tariffs on Kenya's flowers low. They allowed free trade to work its magic. But this is an isolated Kenyan success, and an isolated example of free trade. Because our guilt, the shame of the Western countries is that we are not practising what we preach. The problem is not that the western world is supposedly trying to trick poor countries into some sort of corporate, neo-liberal globalisation - it is that we are shutting them out from it. The problem is not that we don't have something called "fair trade", the problem is that we do not have *free trade*.

Over the last 50 years, we have liberalised trade, but we made two major exceptions - textiles/garments and agriculture. This happens to be the sort of labour intense goods a poor country is able to produce in the early stages of development. So we give developing countries the right to sell everything that they can't produce. The United Nations Conference on Trade and Development calculates that the developing countries could export for $700 billion more per year if we abolished our protectionism. That is 14 times more than they get in foreign aid.

Someone has said that after the liberalisation of the Chinese economy there are only three centrally planned economies left in the world, Cuba, North Korea and the Common Agricultural Policy of the European Union. This agricultural policy shut poor countries' goods out with quotas and tariffs, but it also subsidises our farmers with billions, and through export subsidies and so called food aid, we dump the surplus in poor countries, so that farmers there are knocked out on their home ground. Sweden makes expensive sugar from sugar beets, instead of



importing them from countries with the climate, the soil and cheaper labour. An average cow in the European Union gets more in subsidies every day than 3 billion people in the developing countries have to live on.

But an end to subsidies and protectionism is not an act of generosity. It is an act of rationality. Because we lose ourselves by these policies, only a tiny special interest profit. The OECD-countries barriers and support for agriculture and horticulture amounts to almost 1 billion dollar a day. It's hard to grasp such a huge sum. 1 billion is a fortune, 300 billion is just a figure. Therefore it's best to put it in perspective. For that sum you could fly all the cows in the OECD, 60 million of them, around the world every year in business class. In addition, the cows could be given almost $2,000 each in pocket money to spend in tax-free shops during their stopovers. The cows could have this sort of trip every year. This much we are forced to pay, tax payers and consumers, to destroy the possibilities for poor countries to compete.

The problem with protectionism is not merely a problem with Western protectionism. An even bigger problem is poor country protectionism. Countries generally need more trade, that means not only exports but also imports. Imports are needed for the consumers and for competition and specialisation in the economy, and to fight monopolies. And low import tariffs are needed for exports as well. Something like 40 per cent of exports from the developing countries go to other developing countries. If, then, poor consumers are forced to pay heavy prices for products from companies in their own country, they are prevented from buying from companies in the neighbouring countries, in which case the producers will also lose by this policy. They may get a monopoly of their own market, but on the other hand they are stopped to sell to other markets. This destroys specialisation, which is an engine for growth. Developing countries' tariffs against other developing countries today are more than two and a half times higher than the industrialised countries' tariffs against developing countries. Thus more than 70 per cent of the customs dues which developing countries are forced to pay are levied by other developing countries. Poor countries would benefit more from poor country liberalisation, than from rich country liberalisation.

## What the poor say

Often in the end of discussions about poverty and globalisation, critiques say that statistics give a superficial view. Economics isn't everything. We should also ask poor people about what they think about globalisation. I agree. But in that case, we can't be content with asking two or three individuals hand-picked by antiglobalists and ask them. We need a broad statistically sound selection of representative individuals. Recently, that was done when the Pew Center surveyed 38,000 people in 44 nations, with coverage of the developing world in all regions. The interesting result was that people hold a positive view of globalisation in all regions, but that views of globalization are much more positive in poor countries than in rich ones. If there is a group which is relatively sympathetic to the anti-globalisation views it is the well-off in rich countries.

This Pew Global Attitude Survey showed that only 28 per cent of people in the US and Western Europe thought growing global trade and business ties was "very good". In developing Asia 37 per cent thought so, and in Sub-Saharan Africa no less than 56 per cent thought it was very good. More than a quarter of Americans and West Europeans thought that globalisation has a bad effect on their country, fewer than 1 in 10 in developing Asia and Sub-Saharan Africa thought the same. Only a little more than half in rich countries thought that multinational corporations has a good effect on their country, but as many as 75 per cent of Africans thought so. More than a third in rich countries think that the anti-globalisation has a positive effect, only a little more than a quarter in Africa thought so.

It seems like Americans and Europeans more than others take freedom, wealth and technology for granted, without examining or understanding the process of markets and internationalisation on which this depends. But people who are deprived of freedoms and opportunities see globalisation as the way to get it.

Even though we have seen history's biggest reduction in poverty, poverty is still with us, and in many places it deepens. According to the World Bank 1, 2 billion live in absolute poverty, and 900 million people live in chronic hunger. History, statistics, theory and the poor themselves all say that the problem is not globalisation, it is that they do not yet have access to the fruits of globalisation. It is worth repeating the words of UN Secretary-general Kofi Annan at the UNCTAD Conference in Bangkok on 12th February 2000, soon after the demonstrations against the WTO:

*"The main losers in today's very unequal world are not those who are too much exposed to globalisation. They are those who have been left out."*

*This paper is based on a contribution of the author to the workshop Campaigning for Free Trade:, organised by the Liberal Institute of the Friedrich Naumann Foundation in November 2003*