Global inequality: What to address?*

Young-Mok Kim(KOICA President)

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I. Piketty and rising inequality

We normally would not expect a seven-hundred-page scholarly tomb full of numbers and figures written by an academic to become an international bestseller. The success of *Capital in the Twenty-First Century* by Thomas Piketty indicates that the public discontent caused by the rising inequality in the modern capitalist societies may have reached a boiling point. The debate surrounding *Capital* has been intensely polarizing, inciting passionate responses from the intelligentsia of both the Left and the Right.

* [본 원고는 'Huffington Post'(2014.08.14) 기고문을 재구성하여 작성되었음을 알려드립니다]

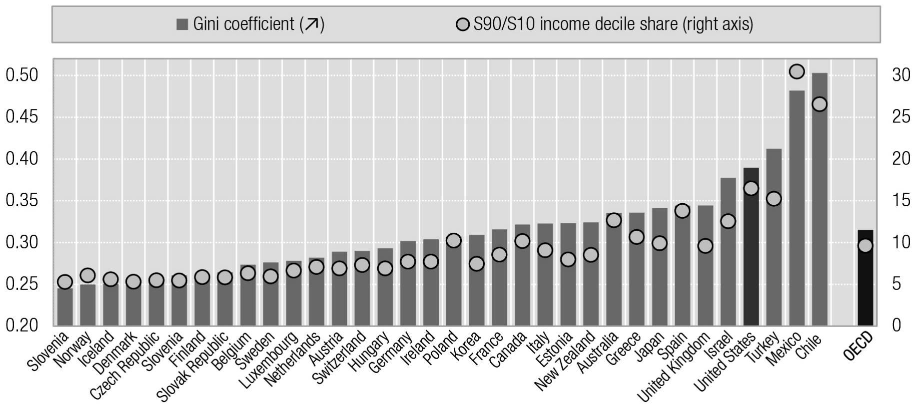
Inequality is a serious topic, and prominent economists including Paul Krugman and Joseph Stiglitz have also been voicing their concerns for years. Professor Stiglitz warned the world of the great magnitude of the damages caused by widening inequality, particularly in the aftermath of the global financial crisis.

The major point of the argument was that inequality is self-enforcing: the rich use their political influence to cut taxes and government spending, which leads to underinvestment in infrastructure, education and technology, which disproportionately affects the people at the bottom of the economic spectrum, further contributing to rise in inequality.

Inequality looks to be doomed to ever increase.

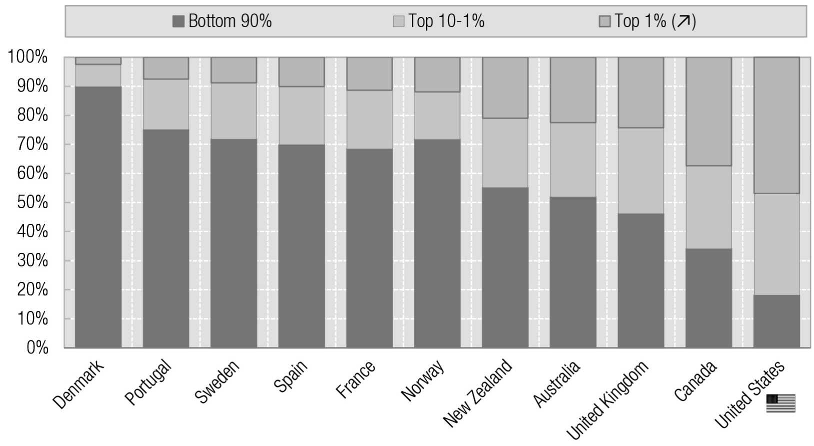
Many studies show that there is compelling evidence for rise in inequality in most advanced economies. In 2010, an estimated 18% of the world's wealth belonged to the top 1 percent, compared to 1980, when it was only 8%. Regardless of whether Piketty's diagnosis is right or misleading, rising inequality deserves attention and remedy searching.

<Graph 1> Gini coefficient and gap between richest and poorest 10%, 2010



Source: United States Tackling High Inequalities: Creating Opportunities for All (OECD, 2014)

<Graph 2> Share of total income growth captured by income groups from 1976 to 2007



Source: United States Tackling High Inequalities: Creating Opportunities for All (OECD, 2014)

II. Triumph and challenges facing global development

While Piketty and other prominent Western economists have been mainly analyzing major advanced economies, there still remains the question of how inequality appertains to the context of global development, particularly in relation to eradicating poverty and sustaining growth in developing countries.

In fact, the global landscape of inequality has been remarkably improved over the past few decades. Inequality between rich nations and poorer nations has been narrowed thanks to the economic surges of China, India, Brazil and other developing nations. A number of economists opposing the “doomed inequality of Piketty” have pointed out that income inequality for the world as a whole has been falling.

It would be fair to note that globalization in trade, investment, technology and human resources greatly contributed to making the world more equal while increasing inequalities in individual countries.

The population under *extreme poverty* living on $1.25 per day has been reduced by half over the past two decades. In 1999, nearly half the population in developing regions lived on less than $1.25 per day; by 2010, the rate dropped to 22%.

The income of hundreds of millions of people in emerging economies or developing countries could, to some extent, catch up to that of rich nations, particularly when we compare the urban median incomes of these nations.

Yet, inequality has risen within most of these developing countries, as is the case with advanced countries, making social stability and sustainable growth more difficult than in the previous decades. Furthermore, a large population still lives on the poverty line, if not under extreme poverty.

According to the World Bank Group, the population living on $2 per day is an estimated 2.4 billion, which is only a slight decline from 2.6 billion in 1981.

III. Middle-income trap and inequality trap

China, Brazil and India, champions of economic development, can be proud of great achievements in reducing poverty of large population. Yet it is astonishing that 70 percent of people living under extreme poverty still live in these emerging "middle-income" countries where we often are overwhelmed by the wealth of the new super rich.

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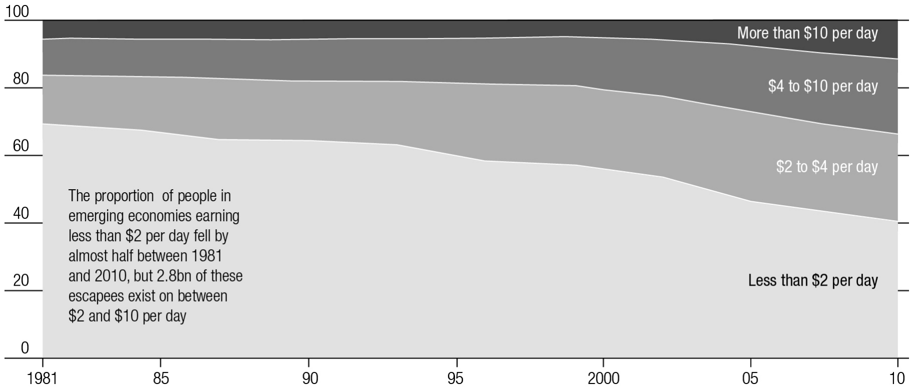
<Graph 3> Income distribution in emerging economies by income group, 1981-2010, percentage



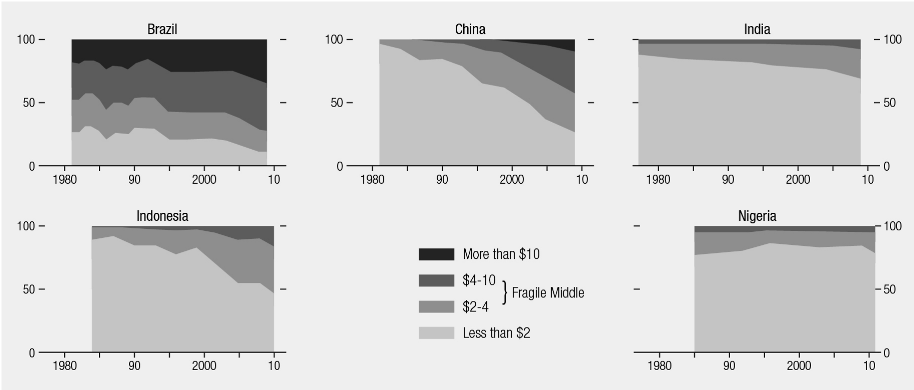
Source: A slippery ladder (Financial Times, April 13, 2014)

Noting this fact, Erik Solheim, chair of the Development Assistance Committee of the OECD, wrote earlier this year that inequality should be tackled first as a new goal in the global development efforts to end poverty.

The world's economic and development organizations, including such prominent private ones like the World Economic Forum, have become more concerned with inequality across countries in different stages of development. These concerns come from the practical analysis that economic growth would not be sustainable without addressing the poverty of the vast population at the lower layer of the income pyramid.

A recent OECD report titled "Perspectives on Global Development 2014," expressed concern on fragility of the lower bottom. "Rapid economic growth in non-OECD countries has lifted whole swathes of the population out of extreme poverty in recent decades and led to the creation of 'middle-classes'… However, the concept of 'middle-class' covers a wide spectrum of strata, some of which remain fragile."

<Graph 4> Daily wages in Brazil, China, India, Indonesia, and Nigeria, 1981-2010, Percentage



Source: The Fragile Middle: millions face poverty as emerging economies slow (Financial Times, April 13, 2014)

In one word, many emerging economies are caught in a "middle-income trap." The Financial Times recently raised concern that a vast majority of people ("escapees from extreme poverty") still live on $2 to $4 per day, and that they are only "fragile middle-class."

Since this "fragile middle-class" can easily regress into poverty depending on external situations, dealing effectively with the trap is becoming important.

IV. New goal setting: Inclusion of the bottom

What causes further concern is fear that the worldwide trend may worsen in the coming decades. In a separate report titled "Policy challenges for the next 50 years," the OECD warns that the world economy will face challenges such as slower growth worldwide, *rising inequality*, threats to climate change and fiscal pressure on governments. Among others, sustaining growth while addressing rising inequality will be a major policy challenge, the study says. Today, not only "*middle-income trap*," but worldwide "*inequality trap*" matter.

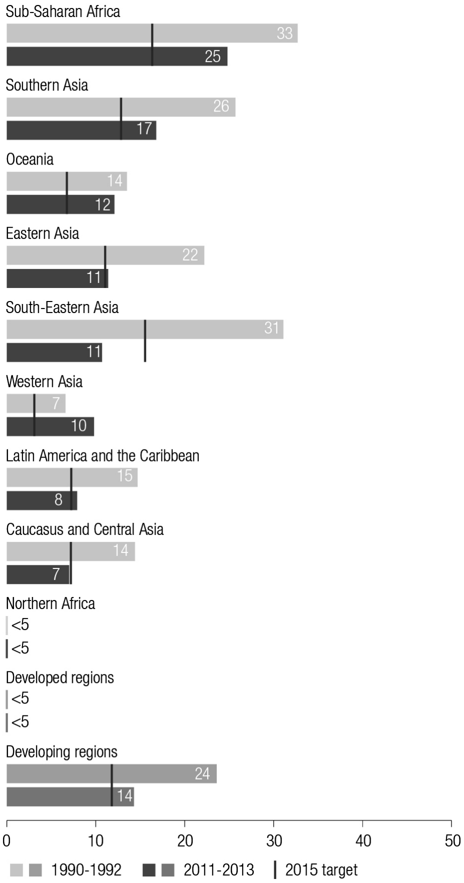
The World Bank Group, for its part, had set last year an ambitious goal to achieve "*shared prosperity*." The Bank announced it would seek faster income growth among "the bottom 40 percent" of a country's population. This new goal setting must have been driven by concerns that the "new middle-class" remains fragile and that a growing GDP did not necessarily trickle down to the poor-well over the course of growth.

True, shared prosperity is not achievable if we are not able to include those people at the larger bottom in the process of growth. From the perspective of the world development community, proportion of inequality may matter less than inclusion of the people left behind.

In most under-developed countries or regions, inequality does not stop at income. High inequality exists in terms of access to most critical services and public goods, such as clean drinking water, proper sanitation, basic health care, adequate education, running electricity, protection from natural disasters, etc. There are also inequalities related to civil rights and good governance with efficient institution.

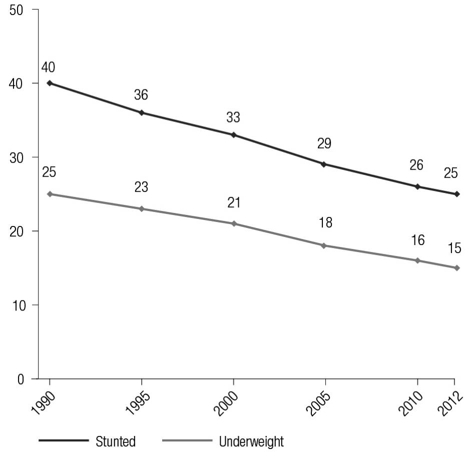
Children are usually the first victims of the plight of extreme poverty. Although the proportion of undernourished people living in developing regions decreased from 24 to 14 percent in two decades, still an estimated quarter of all children under the age of five are said to be stunted. Additionally, 162 million young children are still suffering from chronic under-nutrition. 51 in every 1000 children in developing regions die before the age of five, despite the improvements made in the past decades.

<Graph 5> Proportion of undernourished people, 1990-1992 and 2011-2013, percentage



Source: The Millennium Development Goals Report 2014 (UN, 2014)

<Graph 6> Proportion of children under age five moderately or severely stunted, and moderately or severely underweight, 1990-2012, Percentage



Source: The Millennium Development Goals Report 2014 (UN, 2014)

Today, war and conflict continue, even proliferate. We witness on-going human tragedy in many places, and more than 33 million people are being forcibly displaced from their homes as a result. Civil wars all too easily destroy what has been achieved over decades. The costs for providing care to refugees and wounded are immense, let alone the costs for their rehabilitation.

Shared prosperity, therefore, needs to include as many of these people as possible in the growth. That would be the meaning of "*inclusive growth*."

V. Inclusive growth: Ownership at the bottom

How can we bring those at the bottom up and effectively include them in shared prosperity? One part of this strategy is for them to have a clear sense of ownership.

It is not too difficult to imagine the lives of people living under extreme poverty or the plight of war. Desperation can make these people feel isolated and abandoned, thus posing a threat to an inclusive growth which requires a sense of ownership of those to be included.

Of course, inclusion needs a firm social contract from the top to the bottom and from the public to a broad spectrum of private sectors. To make the new goal of inclusive growth take root, empowering people and having them motivated for an inclusion is the first step.

From the Korean experience, transforming desperation into hope was the key to inclusion. Without the self-motivation of those who should rise up from poverty and desperation, smart policy and investment will have little effect.

Modernization and industrialization of Korea, once one of the poorest countries in the world and devastated by war, owed much to the rapid development of the rural areas. Inspiring people with a "*can-do spirit*" through creating a sense of ownership, was one of the key factors for Korea's fast growth with inclusion.

VI. Inclusive partnership with innovation

The other part of the strategy for inclusive growth is financial resources and engagement of committed stakeholders. Under this worldwide economic slump, pooling tangible and intangible resources from a wider spectrum of players becomes increasingly critical.

"*Inclusive partnership*," one of the key concepts framing the Post-2015 agenda, is already drawing the interest and participation of many new players in global development. It is both a coalition and a strategy that makes the coalition work.

A smartly designed inclusive partnership could make sustainable growth easier since this partnership can bring in additional assets enabling poorly equipped developing communities to be lifted up to the level of "*value chain*." Creating and expanding the social value chain requires, therefore, innovative approaches which can maximize the benefit of coalition, both in terms of securing needed capacity and bigger financial resources.

Bringing in management skills and sharing know-how and even intellectual property are some additional benefits of this partnership compared to monolithic assistance.

"Impact investment" is another benefit of innovative approach that a smart partnership can produce. Leveraging private sectors both in funding and expertise would greatly help people and countries at the bottom to join the global value chain, thus making sustainable, inclusive growth easier.

Even though many advanced governments would face increasing fiscal pressure in coming years due to rising expenditure, including costs for dealing with demographic change, there remains a huge financial resource available, yet underused in the global capital market.

According to a new report "*Private Capital, Public Good,*" recently released by the U.S. National Advisory Board, impact investment is to seek measurable, socially or environmentally beneficial impact while earning financial returns. For now, the total amount mobilized in impact investment accounts for only 0.02 percent of the $210 trillion in the global financial market.

Now, working to eradicate poverty while reducing inequality, is not a job only for social workers, governments or charity organizations. Corporations, financial investors and fund managers are also invited to join in these efforts.

Nelson Mendela said, “As long as poverty, injustice and gross inequality persist, we cannot rest.”

Participating in a broad, inclusive partnership is what we can do right now to get to sustainable growth and shared prosperity. Inequality will become much more acceptable when the bottom is lifted upward by being given better opportunities and access to value chains.