

**Linking Economic Growth to Poverty Reduction under Globalisation:  
A Case for Harnessing Globalisation for the Poor in Sub-Saharan Africa**

**Machiko Nissanke**

School of Oriental and African Studies  
University of London

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## 1. Introduction

As the process of global economic integration has intensified since the early 1990s, the question of how globalization affects the world's poor has become one of the central issues in international political economy and international relations. Many of the current issues and problems facing the global community is increasingly related to the question over how the international economic and political system is perceived to be fair and just *vis-à-vis* the poor in developing countries. Indeed, the contemporary debate on globalisation is often overwhelmed by the fears and anxieties that the poor could be actually hurt in the globalisation process.

The risks and costs brought about by globalization can be significant for fragile developing economies and the world's poor. The downside of globalization is most vividly illuminated at times of periodical global financial and economic crises. Until the current global financial crisis was broken out in 2007, the costs of repeated financial crises fuelled by the globalization process have been borne largely by the developing world, and often disproportionately so by the poor in these countries who are the most vulnerable. On the other hand, the benefits from globalization during boom times are seen not shared widely and equally in the global community. It is not surprising, therefore, that besides the issues related to the huge costs and risks stemming from globally synchronised economic cycles, such as the global recession as we are currently going through, a question is also raised as to whether the actual distribution of gains from globalization is fair and, in particular, whether the poor benefit proportionately less from globalization.

Despite the potential of globalisation in accelerating economic growth and development through greater economic integration, in particular, through the spread and transfer of technology and the transmission of knowledge and information, the impact of the on-going process of globalisation on poverty reduction has been uneven and often marginal.

According to the most recent estimate (Chen and Ravallion (2008), the share of the population of the developing countries living below US\$1 per day declined from 42 per cent to 16 per cent between 1981 and 2005, but this was mainly achieved by the substantial reduction of the poor in Asia, in particular in China. Chen and Ravallion (2007: 2) show that 'when China is excluded, the number of people living on less than US\$1 a day is fairly static with no clear trend'. Furthermore, the total number of people living under US\$2 per day actually has increased worldwide over the period 1981–2005 by about 56 million to 2.6 billion in 2005, while the share of the world's population receiving less than US\$2 per day fell from 69 per cent in 1981 to 48 per cent in 2005.

There is a clear disparity in the regional trends in poverty reduction. As discussed in Section 3 below, while East Asia and the Pacific experienced the sharpest reduction in the number of poor living below US\$1 per day, poverty has increased significantly in rural areas of sub-Saharan Africa in terms of poverty incidence as well as the depth of poverty. In much of sub-Saharan

Africa (SSA), in particular in rural areas both the prevalence and depth of poverty remains unacceptably high.<sup>1</sup>

The fear that the poor have been bypassed, or actually hurt, by globalization is also highlighted by the findings from a number of empirical studies, which point towards a continuing prevalence of high inequality in world income distribution and the sharply skewed pattern of income convergence among participating national economies and across region.<sup>2</sup> Though any trend in poverty and income inequality observed cannot be exclusively or even mainly attributed to the 'globalisation' effect as such, numerous empirical evidences pointing to the increasing inequality under globalisation reviewed below cannot dismiss the concerns raised that the globalisation process, as it has proceeded so far, may have had adverse effects on poverty and income distribution. Indeed, globalisation has created winners and losers at numerous levels throughout the modern history.<sup>3</sup> The losers include many of the poor who have actively participated in the process of globalisation.<sup>4</sup> These concerns have generated a passionate debate worldwide as well as a powerful anti-globalisation movement.

The extent of controversy surrounding this debate reflects the fact that globalization is not a process proceeding neutrally in a policy vacuum, but it is a policy induced condition.<sup>5</sup> Globalization is not purely driven by new technological innovations and progress or by 'neutral' market forces and other inescapable sociopolitical forces, as often depicted in popular writings.<sup>6</sup> In particular, the current phase of globalization is, to a certain extent, an outcome emerging from the global consolidation and diffusion of the economic policy paradigm, which emphasises benefits and positive features of the liberalised policy regime. Therefore, it is not surprising that the globalisation debate takes place from the two opposing positions, as Kozul-Write and Rayment (2007) summarise:

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<sup>1</sup> See Wade (2002) and Deaton (2001, 2002) for critical discussions of the World Bank's estimates of global poverty and inequality used in these studies. Kanbur (2008) also discuss a number of drawbacks in official statistics on poverty trends.

<sup>2</sup> See Nissanke and Thorbecke (2006b) for a review of literature and more detailed discussion on the concepts used for analysing the trends in world inequality and empirical evidence, since the trends in world (global) income inequality depend on which concept of inequality is used. According to the estimates by Milanovic (2005a), the 'between country' inequality weighted by population but ignoring 'within-country' inequality shows a declining trend largely driven by the China factor, while all other estimates show that the world inequality has been increasing.

<sup>3</sup> See Williamson (2002), among others, for winners and losers from globalisation in modern history

<sup>4</sup> See Aggrawal (2008) for the case cotton farmers in India.

<sup>5</sup> See Kozul-Wright and Rayment (2004 and 2007) for an extensive discussion on this policy-induced condition.

<sup>6</sup> Helleiner (2001) emphasises the need to distinguish two different phenomena associated with the term 'globalisation': the technology driven aspects and that is associated with policy choices for external liberalisation. For discussion on the effects of technological progress on the shrinkage in space and time, see Cairncross (1997), Bairoch and Kozul-Wright (1996).

“On the one hand, many proponents and supporters of globalisation insist that their agenda for liberalization on a global scale is the only way to eliminate poverty and ensure a prosperous economic future for rich and poor alike - identifying globalisation as a “win-win” process. At the other end of the scale are various groups from both developed and developing countries who see globalisation as a western corporate conspiracy against the poor and who see market-friendly policies simply as a means of perpetuating privilege—identifying globalisation as “winner takes all” process ( Kozul-Wright and Rayment, 2007: x)”.

These polarised positions are often expressed frequently without much rigorous analyses or solid empirical evidences. In reality, as discussed in Nissanke and Thorbecke 2006a&b), the globalisation-poverty relationship is much more complex and heterogeneous, involving multifaceted channels. It is non-linear in many aspects with several thresholds effects. Because these multifaceted channels interact dynamically over space and time, the net effects of globalisation on the poor can only be judged and asserted on the basis of ‘context-specific’ empirical studies. Cross-country regression studies, requiring precise measurements and definition of the two key multi-faceted concepts—globalisation and poverty—in a composite index, tend to fail to give robust insight into this critical nexus.

With this background and built on the recent UNU/WIDER study co-directed by Erik Thorbecke and myself, <sup>7</sup> the primary objectives of this paper are threefold: i) to examine the experiences of the SSA region with the globalisation-growth-poverty relationships in a comparative perspective with other developing regions, in particular, with countries in East Asia; ii) to discuss some specific conditions prevailed internationally and domestically that could explain the disappointing experiences of the SSA region in harnessing the benefits of globalisation for the poor; and iii) to produce pertinent research questions for detailed country case studies.

The paper is structured as follows: Section 2 presents a brief summary of channels and transmission mechanisms through which the process of globalisation affects poverty dynamics in the developing world. Section 3 discusses in a comparative perspective with other developing regions, salient features of the globalisation-growth-inequality-poverty nexus in Sub-Saharan Africa over the recent decades. Section 4 discusses salient international and domestic conditions that could explain Africa’s disappointing experiences with globalisation. Section 5 offers first concluding remarks on the way forwards for the region in linking economic growth to poverty reduction under globalisation. It then lists research questions generated from this particular framework paper for country-case studies that can be conducted under the AERC research project, “Understanding links between growth and poverty reduction”. We shall suggest possible country studies where empirical results from case-studies could be particularly illuminating for understanding the effects of globalisation on the growth-inequality-poverty nexus in SSA.

## **2. The Transmission Mechanisms in the Globalisation-Growth-Poverty nexus**

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<sup>7</sup> The UNU/WIDER study focused on the predominantly economic manifestations of globalization, hence, it did not attempt to provide a fully comprehensive and multidisciplinary treatment of the impact of globalization on poverty.

Economic manifestation of globalisation filters through greater integration via numerous transmission mechanisms such as trade and investment liberalization; movements of capital, labour migration across borders and within countries; the nature of technological change and diffusion of knowledge and technology; the worldwide information flows; and institutional environments. As explored in detail in Nissanke and Thorbecke (2006 a & b and forthcoming), various transmission mechanisms are in operation to form the *globalisation (openness)-growth-income distribution-poverty nexus*, as globalisation affect poverty through two different paths: first, through their contributions to the growth channel and, secondly, through their impact on distribution since globalisation is also known to affect vertical and horizontal inequalities and produce winners and losers. Thus, globalisation works through: from openness to growth; from openness to income distribution (inequality); from growth to income distribution and vice versa; from growth to poverty, and from income distribution to poverty, respectively. In short, the two main channels of globalization- the “growth” and “distribution” channels - further interact dynamically over time to produce a growth-inequality-poverty triangular relationship.

At an analytical level, each subset of links embedded in the *globalisation (openness)-growth-income distribution-poverty nexus* can be contentious and controversial. For example, the direction of causality in the first link, i.e. the openness-growth link is still being debated as well as how trade and capital flows could be interlinked into a virtuous circle. In this context, we suggested that the positive openness-growth link is neither automatically guaranteed nor universally observable, as the growth-enhancing effects of trade openness depend critically on the way and extent to which a country is integrated into the global economy, as discussed in Section 3. Furthermore, a greater integration/openness does not necessarily ensure uninterrupted growth spells. For example, the on-going global financial crisis originated in the US sub-prime mortgage debacle has spread and engulfed all economies in the developing world (even those who have not opened up capital markets and hence had limited financial market linkages). Clearly in this case, globalisation, or precisely the way globalisation has been proceeded so far, is responsible for the scale and depth of the current recession hitting all developing countries hard through financial and trade linkages. Thus, the greater integration does also entail accepting great downside risks of contagion effects of crises (Nissanke 2009b).

The second link in the causal chain from openness to poverty through the growth effect is the interrelationship between growth and inequality. First, relating the causal chain from income- and wealth-inequality to growth (the ‘inequality-growth’ link) in the interrelationship between growth and inequality, there are two conflicting theoretical strands: the traditional (classical) approach and the ‘new’ political economy of development theories (modern). Whilst the former emphasizes the growth-enhancing effects of income and wealth inequality, the latter links greater inequality to reduced growth through various conditions such as the diffusion of political and social instability leading to greater uncertainty and lower investment; unproductive rent-seeking activities, high transaction costs, and increased insecurity of property rights<sup>8</sup>.

The Kuznets hypothesis of the inverted U-shaped relationship between growth and inequality that examines the opposite causal flow in the link, i.e. the ‘growth-inequality’ link is also examined and challenged by a number of recent theoretical and empirical studies. Many earlier

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<sup>8</sup> See Thorbecke and Charumilind (2002).

development economists note that economic growth, if left to market forces alone, tends to be accompanied by more inequality. Growth is inherently inequalising.<sup>9</sup> In this regards, the new political economy of development approach suggests that with two causal chains combined, growth patterns yielding more inequality would, in turn, engender lower future growth paths resulting in less of a growth-induced poverty reduction.

Thus, a critical question in understanding *the growth-inequality-poverty interrelationship* is whether or not inequality is an impediment to poverty-reducing growth, or in other words, whether high inequality attenuates the growth elasticity of poverty. Several empirical studies confirm that the elasticity of poverty with respect to growth is found to decline with the extent of inequality.<sup>10</sup>

We argue that while globalisation-induced growth may benefit the poor, the ultimate poverty-reduction effects will depend also on how the growth pattern under globalisation affects income distribution, since inequality is the *filter* between growth and poverty reduction. If growth leads to an increase in income inequality the poor may benefit less or, in some instances, actually be hurt by the globalization-induced economic growth. Thus, the *pattern* of economic growth and development, not just the rate of growth *per se*, have significant effects on a country's income distribution and poverty profile, as growth can be pro-poor, distribution neutral or even poverty-increasing. Indeed, the recent debate on the meaning of *pro-poor growth* is related to the complex triangular relationships among poverty, growth and inequality. Clearly, poverty reduction would require some combination of higher growth and a more pro-poor distribution of the gains from growth. In our view, growth is considered truly pro-poor if in addition to reducing poverty, it also decreases inequality.

In this context, it can be argued that the distribution effects directly stemming from globalisation require separate discussion from the growth effects, since several specific features associated with the current phase of globalization have contributed to producing amplified adverse effects on the poor through the combined effects of the growth and distribution channels. These include: a) the nature of technical changes, the asymmetrical access to new technology and knowledge, and the uneven process of technology diffusion; b) the differential treatment of international migration between skilled and unskilled workers, which produces a greater migration of skilled labor from developing countries to developed countries, while unskilled labor migration tends to be strictly controlled; c) the perverse movement of capital in the form of capital flight from developing or emerging market economies or *diversification* finance characterizing portfolio capital flows conducted through asset swapping for risk hedging and shedding, which results in global macro imbalances and periodical financial crises; d) uneven, skewed FDI flows, which have not necessarily guaranteed host developing countries access to potential benefits of management and knowledge transfer.<sup>11</sup>

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<sup>9</sup> For example, Myrdal (1957), Rosenstein-Rodan (1943) or Hirschman (1958) as noted in Milanovic (2005b).

<sup>10</sup> For example, see Ravalion (2002)

<sup>11</sup> . See Nissanke and Thorbecke (2006a and b) for detailed discussion on these mechanisms.

These features have affected the functional income distribution between labor and capital decisively against the former, which has led the anti-globalization movement observed worldwide to regard globalization as driven by the interests of big Transnational Corporations (TNCs) or large financial institutions. Under corporate-led globalization as known by many, globalisation has resulted in the erosion of the capacity of governments to raise revenues for redistributive purposes or to enact regulations to protect and enhance labor rights or protect local environments, in fear of driving away TNCs or capital flight and asset mobility. Further, the poor and unskilled are most adversely affected by asymmetries in market power and access to information, technology and marketing as well as TNCs activities and the dominance of TNCs in commodity value chain.

Further, in discussing the impact of globalisation on the poor, concerns are particularly strong about the increased vulnerability of the poor to globalization forces that generate greater fluctuations in income and expenditure caused by global shocks, such as the various financial crises that have hit many emerging economies in Latin America and Asia in the last two decades or the on-going global financial crisis or food crisis hurting disproportionately the poor.

In addition to a substantial predicted increase in the number of unemployment worldwide as a direct consequence of the global financial crisis, the recent ILO Report (ILO, 2009) predicts that the proportion of those in “vulnerable employment” (own-account workers or contributing family workers in small concerns) in total employment could rise globally to 56 % in 2009 from 50 % in 2007. Further it predicts that the share of those in extreme working poverty (those working but fall below a poverty line of \$1,25 per day) would rise from 21 % in 2007 to 27 % in 2009, while that of those in working poverty (those working but fall below a poverty line of \$ 2 per day) would increase from 41 % in 2007 to over 50 % in 2009. Many of “vulnerable employment” and the majority of extreme working poverty and working poverty are found in the developing world. The World Bank also issued a stark warning on February 12, 2009 that the current global recession triggered by the financial turmoil and meltdown in the US and European financial centres could trap 53 million more people into extreme poverty.<sup>12</sup>

All in all, while globalization can be a major engine for growth in aggregate, it is critical to put in place strong institutions that mediate the various channels and mechanisms through which the globalization process influences poverty. Indeed, institutions act as a filter intensifying or hindering the positive and negative pass-through between globalization and poverty and can help explain the diversity, heterogeneity, and non-linearity of outcomes.<sup>13</sup>

### **3. The Globalisation-Growth-Inequality-Poverty nexus in Sub-Saharan Africa in a comparative perspective**

#### ***3.1 Income Divergence in the South***

Because of the complex and heterogeneous relationships in the globalisation-poverty nexus discussed so far, it is not straightforward to establish, in the absence of a counterfactual scenario,

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<sup>12</sup> . See <http://go.worldbank.org/1FWPZ7KCJ0>

<sup>13</sup> . See, for example, Sindzingre (2006).

systematic hard empirical evidences to substantiate the claim that globalisation has given rise to an increase in poverty globally or otherwise. However, as discussed above, it is possible to point to the transmission mechanisms whereby the forces shaping the current process of globalization may be at least partially responsible for the recent enormous increases in world income disparity between the rich and the poor.

At minimum, the observed ‘big time divergence’ in inter-country income levels (when each country is weighted equally) brings into question the validity of the openness induced income *convergence* thesis, advanced by Sachs and Warner (1995a) and others. Whilst Pritchett (1997) documents the historical trends towards income divergence, Quah (1996) discusses the twin peaks in world distribution dynamics, which are characterized by the tendency for stratification and polarisation. Basu (2006) points to the staggering degree of global inequality today and how rapidly the inequality has risen in recent times. In his recent empirical studies, Milanovic (2005a and b) also demonstrates how ‘global’ income inequality has been all the time increasing to an acceptably high level.

Yet, economic theories are often bluntly used as a most powerful intellectual case for free, liberal trade and investment regimes, which are supposed to be capable of *trickling-down* of benefits from economic growth to the poor under globalisation. The reality is that the mere adoption of open trade and investment regimes does not guarantee, or promote, developing countries’ entry into the “income convergence club”. Indeed, many poor countries in Africa that have opened their economies since the 1980s have fallen behind, not having succeeded in reaching the take-off point, necessary for benefiting from positive forces of globalization.<sup>14</sup> Many more countries that have seen a substantial increase in their trade/GDP ratios have experienced a rapid increase in income- and asset-inequality.

Indeed, the conundrum of the persistent ‘non-convergence’ of world per capita income should be explicitly addressed in terms of structural features of the global economic relationships as they evolved over time and institutional and socio-political conditions found in participating countries. The income convergence trend among nation states, to the extent that it has been observed historically, is likely to be explained more effectively by the specific nature of the integration and specialization process followed by sub-groups of countries, rather than by the degree of openness of the trade and investment regimes *per se*, as often claimed.

Clearly, countries need to have reached the take-off point before they can take advantage of the potential benefits of openness and globalisation. One of the critical reasons why globalisation may not be working for low-income developing countries lies in the fact that the effects of international trade on growth are critically dependent on the pattern of specialisation and integration. By treating two sectors symmetrically, the conventional Heckscher-Ohlin trade model (consisting of two countries, two sectors and two factors) shows that two countries equally reap aggregate gains from trade through efficiency gains.<sup>15</sup> In reality, however, the

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<sup>14</sup> For example, Dowrick and DeLong (2001) suggest that many poor countries after adopting liberalisation measures have fallen behind, not just relatively but absolutely in terms of both income levels and structural development.

<sup>15</sup> This two-sector model of international trade can be easily extended to N-sector models (for example, see Dornbusch, Fisher and Samuelson 1977).

pattern of specialisation does matter for welfare implications of a trade-induced growth path on at least two accounts.

Two sectors need not be symmetrical, first, through the well-known immiserizing effect of trade *à la* Bhagwati, i.e. the terms-of-trade (TOT) effects. Though many dismiss the likelihood of such an effect in a small economy, low-income countries dependent on the exports of a limited range of primary commodities face a deterioration of TOT through the ‘fallacy composition effect’. In the 1980s and 1990s, many primary commodity exporting countries in sub-Saharan Africa, which implemented structural adjustment programmes, underwent simultaneous export drives, leading to depressed prices in many export commodities.<sup>16</sup>

Furthermore, two sectors are not necessarily symmetrical because of the possible differential impact of dynamic scale economies- that is dynamic externalities through technological spill-overs and the accumulation of knowledge capital. As the endogenous growth theory emphasizes, it is the difference in the scope for scale economies that largely accounts for diverging growth rates among countries in the current phase of globalisation. A country specialising in an industry endowed with a larger positive externality would experience a faster growth rate compared with the trading partner that specialises in an industry with a weaker externality. Thus, the growth rates of the two trading countries could differ considerably, depending on the pattern of specialization.

If a country follows the Rybczinski line dictated by static comparative advantage with given relative resource endowments, the country with an initial comparative advantage in ‘non-dynamic’ sectors may end up in a low equilibrium trap through the evolving patterns of production and trade. Similarly, the effects of FDI on host economies diverge enormously, depending on the sectors into which TNCs are attracted to move in and invest. Low-income developing countries tend to attract natural resource based FDI in extracting mineral resources or FDI geared towards the lower end of TNCs’ vertical integrated global operations ( their global value chain) such as simple assembly line operations. These sectors and activities are characterised by very little dynamic externalities and knowledge and skill spill-overs.

Seen from this perspective, openness *per se* is not sufficient to ensure that development will follow. Referring to as one of the fundamental differences between the two waves of globalisation, Baldwin and Martin (1999) note that in contrast to the experiences under the late 19<sup>th</sup>-century globalisation wave, when an enormous North-South income divergence was produced as result of industrialisation of the North at the expense of deindustrialisation of the South, the current wave of globalisation has industrialised the South whilst the North experiencing deindustrialisation.

In reality, however, the globalization experiences in the South tend to be very heterogeneous as sharp divergences have emerged in the development paths followed by different countries in the

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<sup>16</sup> See Maizels (1992). In this context, Birdsall (2002) also draws attention to the fact that measured by the trade-GDP ratio or tariff rates, most commodity-dependent countries have not been more reticent than less commodity-dependent countries about participating in international trade, but the former group has failed to grow (especially after 1980), as they have remained dependent on exports of primary commodities.

South over the recent decades. As shown in Table 1, all developing regions have accelerated the pace of integration into the global economy, as measured by their trade intensity ratios (exports + imports divided by GDP) since 1980s.<sup>17</sup>

**Table 1: Trade Intensity Ratios of Major Developing Regions, 1980-2006**

	1980-84	1985-89	1990-94	1995-99	2000-4	2005-06
<i>Trade openness</i> <sup>1</sup> : (X+M)/GDP						
East Asia	40.4	43.0	60.1	60.7	69.6	82.7
South Asia	18.5	17.3	22.7	27.5	32.8	45.5
<b>Sub-Saharan Africa</b>	<b>52.5</b>	<b>49.7</b>	<b>52.3</b>	<b>59.4</b>	<b>66.3</b>	<b>73.5</b>
Latin America and Caribbean	28.2	28.1	30.3	35.1	45.7	49.0
E Europe and Central Asia	..	..	57.9	62.7	76.3	77.0
Middle East and North Africa	68.3	48.2	67.7	59.0	67.8	84.6 <sup>2</sup>
<i>World total</i>	<i>40.57</i>	<i>37.7</i>	<i>40.3</i>	<i>45.1</i>	<i>51.0</i>	<i>57.52</i>

( .. not available)

Sources: World Development Indicators 2008

Notes: 1. World Bank *World Development Indicators*, 2008 (calculated from current US\$ estimates)  
Only 2005

Yet, Tables 2 shows that growth rates diverge widely across developing regions. Some countries in the South were able to benefit from *virtuous* cycles of globalization- induced growth, while others were left behind in *vicious* cycles of globalization- induced decline.

<sup>17</sup> . While an increase in trade intensity ration (TIR) is usually interpreted as an indicator of globalisation in economic literature, the trade intensity ratio is by no means a perfect measure to reflect the degree of economic globalisation. It reflects a degree of integration only through trade, though the concept of globalisation embraces a much wider set of integration indicators. Besides, it has a number of technical drawbacks as indicator, such as not corrected for the size of an economy or for the endogeneity problem (Round 2009 and Thorbecke and Nissanke 2009). Though these shortcomings are duly acknowledged, the trade intensity ratio is used here for its simplicity for obtaining a broad picture across the regions. See Round, (2009) for discussion on various composite indices constructed so far for measuring globalisation.

**Table 2: Growth of GDP per Capita of Major Developing Regions, 1980-2006**

	1980-84	1985-89	1990-94	1995-99	2000-4	2005-06
<i>Growth of GDP per capita (average annual)<sup>1</sup></i>						
East Asia	5.8	6.3	7.9	5.7	7.1	8.4
South Asia	3.1	3.4	2.6	4.0	3.9	7.0
<b>Sub-Saharan Africa</b>	<b>-1.3</b>	<b>-0.3</b>	<b>-2.0</b>	<b>0.7</b>	<b>1.5</b>	<b>3.2</b>
Latin America and Caribbean	-0.9	0.3	1.6	0.9	1.0	3.7
E Europe and Central Asia	..	..	-6.0	1.8	5.4	6.4
Middle East and North Africa	0.3	-1.6	1.6	2.3	1.9	3.0
<i>World total</i>	<i>0.5</i>	<i>2.0</i>	<i>0.7</i>	<i>1.7</i>	<i>1.6</i>	<i>2.4</i>

(...) not available

Source: World Bank *World Development Indicators*, 2008 (average annual %)

Further, there appears to have emerged a marked difference in the extent to which and ways benefits of economic growth trickled down to the poor as these developing economies were integrating into the global economy. The income poverty trends, as indicated by head-count ratios for \$1 a day and \$2 a day in Table 3a & b respectively show the regional differences on this account.

**Table 3a: Global Comparisons of Income Poverty Trends for US \$1 a day: Major Developing Regions, 1981-2004**

	1981	1987	1993	1996	1999	2002	2004
<i>Income poverty<sup>1</sup> (headcount ratios)</i>							
<b>Sub-Saharan Africa</b>	<b>42.3</b>	<b>47.2</b>	<b>45.5</b>	<b>47.7</b>	<b>45.8</b>	<b>42.6</b>	<b>41.1</b>
Latin America and Caribbean	10.8	12.1	8.4	8.9	9.7	9.1	8.6
South Asia	49.6	45.1	36.9	36.1	34.9	33.6	30.8
East Asia and Pacific	57.7	28.2	25.2	16.1	15.5	12.3	9.1
Of which China	63.8	28.6	28.4	17.4	17.8	13.8	9.9
E Europe and Central Asia	0.7	0.4	3.6	4.4	3.8	1.3	0.9
Middle East and North	5.1	3.1	1.9	1.7	2.1	1.7	1.5

Africa							
World total	40.1	28.7	25.6	22.7	22.1	20.1	18.1
<i>Ratio: SSA/World</i>	1.05	1.64	1.78	2.11	2.07	2.12	2.27
<i>Income poverty<sup>2</sup></i>							
<i>(numbers million)</i>							
<b>Sub-Saharan Africa</b>	<b>167.5</b>	<b>222.8</b>	<b>252.6</b>	<b>286.2</b>	<b>296.1</b>	<b>296.1</b>	<b>298.3</b>
Latin America and Caribbean	39.4	50.0	38.8	43.0	49.0	48.1	47.0
South Asia	455.2	471.1	436.7	452.9	463.4	469.6	446.2
East Asia and Pacific	796.4	428.8	420.2	279.1	276.5	226.8	169.1
Of which China	633.7	310.4	334.2	211.4	222.8	176.6	128.4
E Europe and Central Asia	3.0	1.6	16.9	20.9	17.9	6.0	4.4
Middle East and North Africa	8.8	6.4	4.5	5.4	5.7	4.9	4.4
World total	1470.28	1180.7	1170.17	1087.8	1108.6	1051.5	969.5
<i>Ratio: SSA/World</i>	0.11	0.19	0.22	0.26	0.27	0.28	0.31

Sources: Ferreira and Ravallion (2008): Table 2; based on international poverty line (\$1.08 1993 PPP)

**Table 3b: Global Comparisons of Income Poverty Trends for US \$2 a day: Major Developing Regions, 1981-2004**

	1981	1987	1993	1996	1999	2002	2004
<i>Income poverty<sup>1</sup></i>							
<i>(headcount ratios)</i>							
<b>Sub-Saharan Africa</b>	<b>74.5</b>	<b>77.4</b>	<b>76.1</b>	<b>76.4</b>	<b>75.9</b>	<b>73.8</b>	<b>72.0</b>
Latin America and Caribbean	28.5	29.6	24.1.4	25.2	25.3	24.8	22.2
South Asia	88.5	86.6	82.2	82.1	80.4	79.7	77.1
East Asia and Pacific	84.8	68.5	65.0	52.5	49.3	41.7	36.6
Of which China	88.1	68.6	68.1	53.3	50.1	40.9	34.9
E Europe and Central Asia	4.6	3.1	16.5	18.0	18.6	12.9	9.8
Middle East and North Africa	29.2	24.2	21.4	21.4	23.6	21.1	19.7
World total	67.0	60.7	59.4	55.5	54.2	50.7	47.6

<i>Ratio: SSA/World</i>	1.11	1.28	1.28	1.38	1.40	1.46	1.51
<i>Income poverty<sup>2</sup> (numbers million)</i>							
<b>Sub-Saharan Africa</b>	<b>295.5</b>	<b>365.0</b>	<b>422.1</b>	<b>458.4</b>	<b>490.6</b>	<b>512.6</b>	<b>522.3</b>
Latin America and Caribbean	103.9	122.3	111.1	122.3	128.4	131.1	120.6
South Asia	813.0	904.2	974.0	1031.5	1067.2	1115.5	1115.8
East Asia and Pacific	1169.7	1040.7	1083.2	907.8	882.7	776.3	683.8
Of which China	875.8	744.1	802.9	649.5	627.6	524.2	452.3
E Europe and Central Asia	19.8	14.0	77.8	84.9	87.9	60.8	46.3
Middle East and North Africa	50.6	50.2	51.8	55.4	64.5	60.9	59.1
World total	2452.5	2496.5	2721.7	2665.7	2721.3	2647.2	2547.9
<i>Ratio: SSA/World</i>	0.12	0.15	0.16	0.17	0.18	0.19	0.20

Sources: Ferreira and Ravallion (2008), Table 3

In our view, these divergences can be explained by the distinct internal patterns of economic growth and the forms of integration adopted. In order to discern and highlight the differential impact of the forces of globalisation on the poor in the developing world, in the next sub-section we present salient features and key differences in the globalisation-poverty relationships found in Sub-Saharan Africa and Asia, which will be followed by a brief synthesis of our comparative analysis of the integration experiences in SSA, Asia and Latin America.<sup>18</sup>

### ***3. 2. Comparative analysis of the experiences in the Globalisation-Growth-Inequality-Poverty nexus***

#### ***Integration Experiences in Sub-Saharan Africa***

Following largely an inward oriented development strategy in the early decades of the post independence period, the majority of SSA countries failed to take advantage of the potential provided by the dynamic growth spurt through integration. The region was largely marginalized and experienced slow growth and stagnation. With growing recognition of their disadvantageous position, most SSA countries over the past two decades have searched for ways to accelerate their participation in the global economy. Indeed, most economies in SSA significantly liberalized their trade and investment policy regimes as part of SAPs since the mid 1980s.

<sup>18</sup> With the space constraints, we omit here discussion on the Latin American experiences. The detailed discussion on the Latin American cases, see Nissanke and Thorbecke (2009) and Thorbecke and Nissanke (2009).

Today, SSA is not behind other developing regions in terms of their trade intensity ratios (Table 1). In spite of the increase in trade intensity, however, Africa's share of total world trade has fallen over the last two decades. Similarly, many countries in SSA have intensified their efforts to attract FDI with the help of various fiscal and other incentive measures. Yet, FDI flows to the region so far have been largely limited to extraction of oil and other natural resources.<sup>19</sup> More recently, a rapid increase in FDI to Sub-Saharan Africa from China, India and other emerging economies has been observed. While a large proportion of these FDI is known to be in extractive sectors, services and some manufacturing sectors have started attracting investment from these Asian drivers.<sup>20</sup> However, it is still too early to detect discernable effects of these South-South flows on growth and poverty in the region's aggregate statistics. Further, though there has also been FDI into low-skill manufacturing sectors in response to some preferential trade agreements such as AGOA (Africa Growth Opportunity Act), many of these investments are foot-loose and fragile in their nature with little long-term commitment. They are mostly in the garment industry with little potential of marked knowledge and technology transfer.<sup>21</sup>

Hence, so far, SSA presents a clear example in support of the argument that the shift to an open policy regime alone is not sufficient to bring about economic growth and consequent poverty reduction. After two decades of reforms dominated by liberalization, privatization and deregulation, the economies of SSA have not yet been able to escape from the 'growth tragedy' syndrome—the term popularly used in characterizing the region's dismal economic performance in the comparative growth literature.<sup>22</sup>

The recent upturn in economic growth in 2005-6 recorded in many natural resource-rich economies in SSA, as shown in Table 2 is closely associated with the price hike of oil and mineral commodities in world markets since 2003. The sustainability of these high growth rates is very much dependent on a continuation of favourable exogenous factors unless the windfalls from commodity booms are used purposely to help diversify and transform the existing economic and trade structures. Highly competent macroeconomic management over the commodity price cycle is required to avoid the 'Dutch disease' often associated with commodity booms.<sup>23</sup> Otherwise, the foundation for long term economic development of these natural resource-rich economies would remain fragile. Indeed, the total collapse of many commodity prices in the second half of 2008 associated with the sharp global economic slow down triggered by the deepening of the financial crisis since the mid September 2008 demonstrates the high vulnerability and fragility of these commodity dependent economies. The commodity market linkage is one of most powerful transmission mechanisms through which Africa's growth prospect has worsened as result of the on-going global financial and economic crisis.

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<sup>19</sup> See Round (2009) for data in FDI flows to Sub-Saharan Africa compared to other developing regions.

<sup>20</sup> See, for example, Broadman (2007)

<sup>21</sup> See Fukunishi (2009).

<sup>22</sup> See O'Connell and Ndulu (2000) and Ndulu (2006) for an updated literature review and their analysis on Africa's growth tragedy.

<sup>23</sup> See Nissanke (2003 and 2009c&d).

The failure of SSA economies to diversify and undergo structural transformation, and hence, to benefit from the technology driven, highly dynamic aspects of the on-going globalization process has led to major drawbacks in terms of low economic growth and persistent poverty (see Table 3a and b)<sup>24</sup> The ratio of headcount ratio for US\$1 a day in SSA to the average in the developing world increased from 1.05 to 2.27 over the period of 1981-2004. As Ali and Thorbecke (2000) notes, poverty in SSA is both most prevalent and severe in rural areas.

Furthermore, as Milanovic (2003) notes, countries in SSA display a high intra-country inequality. This can be seen as a puzzle as Africa should be a low inequality continent according to the Kuznets hypothesis because ‘African countries are poor and agriculture based, and also because the main productive asset—agricultural land—is relatively evenly distributed in most of SSA (except the region of Southern Africa) in part thanks to the tradition of communal land holding’. (Milanovic 2003: 2). The degree of income inequality in Africa has increased sharply between the 1980s and the 1990s.<sup>25</sup> In this context, it can be argued that Africa’s growth has been distinctly against the poor not only in terms of its ability to deliver the required growth rate to ensure that the poor could benefit from economic growth, but also in terms of its ‘inequality-increasing’ pattern. Little progress in poverty reduction in SSA is the outcome resulting from the combined effects of low growth and rising inequality. Economic growth in SSA, where it has occurred, has not been translated into significant poverty reduction. Critically, the nature and pattern of integration of the SSA economies into the global economy, the slow rate of structural transformation and the neglect of the agricultural sector all combined have not been conducive to generating *virtuous* cycles of globalization- induced growth and poverty reduction.

### Integration Experiences in Asia

Asia is the region widely regarded as having benefited most from the dynamic *growth* effect of the recent wave of globalization, which has also resulted in a very substantial reduction of abject poverty in many economies. Income poverty based on the headcount ratio of US\$1 a day in the East Asia and Pacific region and in China fell from 58 per cent and 64 per cent in 1981 to 9 per cent and 10 per cent in 2004 respectively (Table 3a). Though the poverty trend in the region is dominated by the two populous countries of China and India, it is clear that extreme poverty has been steadily declining over the last three decades across most of Asian countries.

There is very little disagreement over the powerful growth-enhancing effects of openness through trade and FDI in the case of most Asian countries. Following aggressively an ‘outward oriented development strategy’, most *East* Asian economies had not only managed the process of integration into the world economy much earlier than other developing countries but also upgraded their form of linkages to the global economy in the years of their rapid economic growth. A number of earlier studies (World Bank 1993; Ahuja et al. 1997; Campos and Root 1996) described the growth pattern of *East* Asian countries in the 1960s and 1970s as highly inclusive and viewed as a model of ‘shared growth’. These studies attributed this successful

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<sup>24</sup> . According to the recently revised estimates on poverty (Chen and Ravallion, 2008), the number of poor below the US\$1.25 a day increased from about 212 million in 1981 to 388 million in 2005 in SSA. The poverty incidence fell marginally during this same period from about 53 per cent to 51 per cent.

<sup>25</sup> See Round (2009).

growth performance to an appropriate set of economic policies and institutions well suited to the conditions prevailing in East Asia during that period. The relatively quick turnaround of many emerging economies in East Asia in the years following the severe crisis of 1997–98 is often attributed to their strong export performance and renewed adaptability and flexibility in responding swiftly to new opportunities offered by globalisation.

Critically, the structural transformation of most economies in East Asia has been facilitated considerably by the integration/globalization process. The catch-up process and associated growth dynamism in Asia, as a whole, has been popularly examined in terms of the ‘Flying Geese Paradigm’, wherein a sequence of staggered catch-up growth has successively taken place in the region since the end of the Second World War.<sup>26</sup> Importantly, as Ozawa (2009) observes, poverty alleviation has been occurring, in flying-geese style (i.e., in tandem with growth) among these rapidly catching-up Asian economies as well. Hence, Ozawa argues that the growth performance—accompanied by a substantial reduction of abject poverty—in East Asia can be explained in terms of the region wide *comparative advantage recycling* in production and export of labour intensive goods.

The process involves a strong demand for unskilled and semi-skilled labour, driven by exporting labour intensive goods and attracting pro-trade FDI, bringing about effective technology, knowledge and skill transfer. In short, most of the East and South-East Asian economies have successfully gone through the structural transformation of their production and trade structures with continuous upgrading of their human skill endowments and technology/knowledge base. By relying on their fast evolving dynamic comparative advantages these countries were able to maximize the benefits from dynamic externalities. Their increasing specialization in sectors with large spill-overs and dynamic externalities was conducive to engendering a pattern of equalizing growth.

However, Asia is no exception to the rapid increase in ‘within country’ income inequality observed globally over the recent decades under globalization, (Milanovic 2005a). While the growth pattern of many East Asian economies in the early decade was equated with that of *shared* growth, the growing inequality in East Asia was already evident before the financial crisis of 1997–98, and the rising spatial disparity in growth performance was seen as a characteristic phenomenon (Ahuja et al. 1997). The financial crisis of 1997-8 did exacerbate this trend in the region.

In both China and India, income inequality among provinces and states as well as interpersonal inequality has been rising in both countries in recent decades particularly after a decisive step was taken towards opening the respective economies (Nissanke and Thorbecke 2008a). There is growing evidence that ‘within country’ inequality has been rising at an accelerated pace across most developing economies in Asia in the 1990s.<sup>27</sup>

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<sup>26</sup> See Ozawa (2009) for the detailed analysis of this process and further references on the Flying-Geese Hypothesis.

<sup>27</sup> See Cook (2006).

However, the rising inequality could put a brake on economic growth as it tears apart social cohesion required for economic development in the region. The poor in Asia, as elsewhere, have been particularly subject to increased vulnerability from globalized market forces.<sup>28</sup>

Thus, it can be argued that economic growth over the recent decades in Asia has so far produced a marked reduction in poverty *despite* the adverse distributional changes against the poor.<sup>29</sup> That is, growth produced the adverse distribution effect, but the former was so vigorous that it more than compensated for the latter (ADB 2004): the process of integration of many Asian economies into the global economy has generated such a strong growth impact that the poor were not left out from its beneficiary effects.<sup>30</sup>

However, poverty still remains high in many developing countries in Asia, if it is measured on the basis of the US\$2 a day poverty line (Table 3b). In East Asia and Pacific Region, the headcount ratio for \$2 dollar per day is 37 % in 2004, a fall from 85 % in 1981, while that in South Asia is still 77 % in 2004, a decline from 88 % in 1981. Though these are dominated by China and India in each sub-region, poverty is widespread in Asia as a whole, and the challenge facing policymakers in the region in attacking poverty of this magnitude is non-trivial.

#### *Synthesis of comparative analysis of the integration experiences by the developing regions*

In Nissanke and Thorbecke (2006 a& b and 2009) we argued that the effects of globalization on poverty are diverse and context specific<sup>31</sup>, conforming to the view that ‘the forces of globalization as such are not *inherently* beneficial or deleterious for development prospects’ (Sanchez 2003: 1978). At the same time, we showed, through our comparative analysis of the globalization experiences across the three developing regions, globalization works best for the poor through the ‘growth’ channel when globalization induced economic growth generates secure employment opportunities continuously at a steady rate for a growing population and labour force. On the whole, the employment creating effect of growth is pronounced in East Asia, where globalization has brought about a substantial poverty reduction due to vigorous growth despite the increasing inequality.

The process of poverty reduction in the Asia and Pacific region has closely followed the waves of employment creations for unskilled labour and the poor in tandem with the evolution and shifts of comparative advantages within the region in the ever accelerating integration process. In contrast, such a poverty reduction process through globalization could not be achieved in SSA and ECLAC regions, where liberalization of trade and investment regimes failed to produce

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<sup>28</sup> Aggarwal (2008).

<sup>29</sup> Kanbur (2008) also notes “in countries where there has been high growth it has been accompanied by inequality increase, but the growth effect has been sufficiently strong that poverty has fallen”(2008:2).

<sup>30</sup> See Nissanke and Thorbecke (2008a) for detailed case studies that examine the effects of different aspects of globalization on inequality and poverty in Asia.

<sup>31</sup> See also Ravallion (2006) and Bardhan (2006) for the detailed discussion on the tenuous but complex nature of the openness-poverty relationships. Winters et al. (2004) also present a careful examination of multiple mechanisms found in the link between trade liberalization and poverty.

either strong or significant employment creating growth. Instead it has resulted in ‘jobless’ growth, casualization of employment and informalization of their economies, as Latin American case studies most vividly illustrated.<sup>32</sup> This observation leads us to argue that the employment creation effect achieved through globalization-induced economic growth is a most direct and powerful channel through which globalization can make a noticeable dent on poverty.<sup>33</sup>

However, even in East Asia where the employment creating effects of globalisation-induced growth has been most pronounced, there is mounting evidence that the distribution effect engendered by the globalization process is generally not in favour of the poor, and that growth has been increasingly disequalizing over time. The pattern of growth in Asia has been pro-poor only according to the weak definition but not according to the strong definition of pro-poor growth (that is the poor benefit proportionately more than the non-poor). Hence we argued (Nissanke and Thorbecke 2008 a), the ‘inequality increasing’ effect of globalization should be attenuated by public policy measures to ensure that benefits from globalization-induced growth are shared more equally and equitably. Sustaining the shared growth process is hence critical for ensuring economic growth to continue under globalization, as growing inequalities could easily weaken social cohesion and risk reducing the momentum for economic growth and integration everywhere, including countries in Asia.

#### **4. International and domestic Environments for explaining the disappointing integration experiences of Sub-Saharan Africa**

##### *International Poverty Trap: Commodity Dependence, Debt and Aid*

Today, several decades after gaining political independence, the high primary commodity dependence remains one of the most conspicuous characteristics of the trade linkage of countries in SSA with the rest of the world under globalisation. According to UNCTAD (2007, 2008a), in Africa, 34 countries are dependent on three or less primary commodities, and 23 countries are dependent on a single commodity for more than 50 % of total export earnings. Most of African countries, classified as LDCs and HICPs, have higher dependency ratio of 80 % for their export earnings. As UNCTAD (2002) suggests, any low income countries dependent on primary commodity exports and natural resource based structures could be locked in an *international poverty trap* through integration into the global economy. Ocampo and Parra (2006) also attribute the cycles of growth spurts and collapses of many developing economies depended on primary commodity exports since 1950s to their susceptibility to external shocks originating from the global economy, and accordingly identify a ‘global development cycle’ that

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<sup>32</sup> .Countries in the ECLAC region have experienced weak growth and rising inequality since 1980s, where globalization had produced an essentially “jobless” pattern of growth with little impact on poverty reduction (Nissanke and Thorbecke, 2009 and Thorbecke and Nissanke, 2009).

<sup>33</sup> Making a clear conceptual distinction between ‘non-globalizers’ and ‘unsuccessful globalizers’, Jenkins (2006) also emphasize the role of employment creation of labour-intensive exports of manufactures and agricultural products as an important differentiating factor between the successful globalizers in Asia and the unsuccessful ones in Africa.

circumscribes the growth possibilities of these economies on a sustainable basis. The ‘commodity dependence’ is naturally more severe for low income countries in sub-Saharan Africa or small countries in the Central America than for natural-resource based middle-income countries in Latin America.

Indeed, it is not a mere historical accident that the beginning of the debt crisis of low-income economies in SSA in the late 1970s coincided exactly with that of the conveniently forgotten ‘commodity crisis’ (Maizels, 1992). All debt relief mechanisms employed since the outbreak of the debt crisis, including the HIPC initiatives, failed to pay sufficient attention to the plight of many commodity-dependent low-income developing countries in the face of the huge loss of their purchasing power in international economic transactions as well as the dwindling of the fiscal capacity to implement development-oriented policies domestically.

In particular, in the resolution of the debt crisis, the effective and flexible facility of *contingency financing* to deal with external shocks on an *ex-ante* basis has been absent. Yet, it is critically important to establish genuinely flexible, *state-contingent* debt relief mechanisms in order to avoid the recurrence of debt crises and the debt overhang conditions developing, which has stalled economic development of low-income countries for so long. The state-contingent schemes could make a distinction between the consequence of a debtor’s own efforts and events outside its control.<sup>34</sup> Hence, in state-contingent aid or debt contracts, incentive structures for contract parties are better aligned. Now, drawing an efficient, state contingent debt contract is technically possible. However, the political will and commitment to realise this possibility is absent. Instead, official creditors have kept applying *ex-post* debt relief mechanisms with policy conditionality attached in response to recurrent liquidity crises and the ensued ‘debt overhang’ condition.

It had to wait for an eventual cancellation of most of official debt, embedded in the MDRG in 2005, to shake-off the overhang of the prolonged debt crisis of these countries.

All these are indeed a reflection of the failure on the part of the international development community, in particular, the International Financial Institutions, to acknowledge and deal with the commodity-related issues effectively and in a timely fashion. This has entailed a huge cost to these low-income countries, mostly in Sub-Saharan Africa in their forgone development opportunities. Economic policies recommended by International Financial Institutions, in the semblance of both Washington and Post-Washington consensuses, have not succeeded in facilitating the process of structural transformation and diversification of their economies through rigorous productive and social investment. At the macroeconomic stabilization front, the demand management of commodity-dependent economies governed by external shocks should be *counter-cyclical* to the commodity price movements. Yet, at times of an externally induced balance-of payment crisis accompanied by a sharp drop in domestic demand, these countries have been forced, in the absence of alternative financial facilities, to adopt the IMF sponsored *pro-cyclical* stabilization programme that aims at a further contraction in aggregate domestic demand.<sup>35</sup>

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<sup>34</sup> Krugman (1988).

<sup>35</sup> See Nissanke (1993 and 2009d) for a critical review of macroeconomic adjustment policies over the commodity price cycles in mineral-based developing countries.

The position and development experiences of highly commodity –dependent economies in the globalising world economy since the early 1980s are in a sharp contrast to those of newly industrialising developing economies in the South. With the debt crisis more or less stalled the development progress over the full two decades, many low-income countries dependent on primary commodity exports and natural-resource based structure have failed to diversify their production and trade structures so far. The disappointed globalisation experiences by countries in the ECLAC region can also be explained, at least partly, by their commodity dependence. Thus, Ocampo and Parra (2006) note that over the last three decades, the course of macroeconomic adjustments necessitated from, and the institutional effects of, the massive shocks coming from global financial and commodity markets have considerably exacerbated the distributional conflicts inherent to the economies in the ECLAC region..

In contrast, as discussed above, many countries in East Asia have managed to integrate into the global economy through diversifying their exports into manufactured goods with potential of exploiting economies of scale, and experienced a dynamic growth process through gradually climbing technology-and skill- ladders in their integration process. It is these dynamic emerging economies that account largely for a rapidly increased share of developing countries in global GDP and world trade in goods and services.<sup>36</sup> What countries export does really matter to the development process with globalisation (Hausmann et.al, 2005). These contrasting experiences point to the importance of reaching the *takeoff stage* before countries can benefit from dynamic forces associated with the on-going process of globalization (Nissanke and Thorbecke 2006 and 2008).

While the commodity issues were not featured in the early debate on the debt crisis that have inflicted low income countries, there is now almost unanimous agreement, including the World Bank and IMF, that vulnerability to external shocks represents a major factor behind their debt crisis and the renewed accumulation of unsustainable external debt stocks. Yet, the donor community has persistently shown reluctance to grapple effectively with commodity issues - one of the critical factors shaping debt dynamics of these economies. The performance-based aid allocation rule, evaluated in the ‘Country Policy and Institutional Assessment (CPIA)’ rating, and the debt-sustainability framework embedded in the IDA allocation procedure adopted as a part of the ‘new aid architecture’ does not satisfy the conditions required for making aid really effective and debt truly sustainable as well as for improving donor-recipient relationships.

As discussed in Nissanke (2009a), aid effectiveness rests critically on the nature of the recipient-donor relationships among other conditions. The donor-recipient relationships had been severely impaired by the two-decade long experiences with policy conditionality attached to Structural Adjustment Programmes, whereby a series of restrictive policy conditionality was imposed as a universally applicable basis for reforms in return for debt relief and foreign aid. While the blame for the low effectiveness has been placed too readily on recipient governments and institutions in terms of poor policy environments and their incapacity, the donor community has to take a fair

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<sup>36</sup> UNCTAD (2007) reports that in 2005, developing countries’ share of global GDP at purchasing power parity surpassed that of developed countries for the first time, climbing rapidly from 44 % to 53 % just over the decade from 1995 to 2007.

share of responsibility for the poor relationships evolved. By generating a sharp configuration of winners and losers in the domestic political economy context, these reform packages were often so contentious, that donor governments themselves would have found hard to implement or to sell to their own domestic constituencies.

The new aid architecture emerged as result of the recent aid effectiveness debate is supposed to address these issues. Despite the claim that greater ownership and partnership has been achieved under the new aid architecture, the donor-recipient relationships are still built on a shaky ground, where recipient governments and donors tend to position themselves in an ‘aid power’ game, which could result in an inferior non-cooperative equilibrium. Unfortunately, donors tend to police over whether recipient governments adopt, and adhere to, economic policies and institutional governance structures recommended by donors. The true sense of ownership and partnership is hard to emerge under such a condition. For the latter, the donors should take a much less intrusive position, and should focus on providing aid for enhancing recipients’ efforts in building an institutional foundation with the necessary technical capacity for developing their own ‘home-grown’ strategies, policies and institutions. It can be argued that the unhealthy aid relationships have dominated and shaped the way many low-income countries in Sub-Saharan Africa have integrated into the global economy for far too long.

After all, the donor community has not necessarily had a credible track record in diagnosing accurately binding constraints for economic development in Sub-Saharan Africa. For example, it is only recently after the newly emerging literature on Africa’s ‘growth tragedy’ identified the region’s geographical disadvantages as one of the most binding growth constraints that the need for massive infrastructure investment is officially recognized as critical for accelerating economic and productivity growth as well as the progress in poverty reduction. As discussed in detail in Nissanke (2007), the donor community had steadily reduced aid to economic infrastructure projects in relative to overall aid as well as to social infrastructures in SSA in the 1980sand 1990s..

It is rather both surprising and disturbing that it has taken so long to reinstate the critical importance of infrastructure investment for African development. This reflects largely the unhealthy situation evolved since the early 1980s, wherein the priority of the development agenda for Africa is predominantly set by the donor community, in particular by IFIs. They themselves have to climb a rather steep learning curve over time to realize that the simple adoption of liberalisation and deregulation measures would not be sufficient to address Africa’s development challenge. Along this learning curve, the aid relationship between the donor community and African countries evolved, as Adam and O’Connell (1997) note, from the “capital shortage” diagnosis in the 1960s and 1970s, to the “policy failures” diagnosis in the 1980s, and finally to the “institutional failures” diagnosis in the 1990s. Now, eventually, the ‘infrastructure’ failure has got a due attention in the 2000s.

The belated official recognition of Africa’s disadvantages in infrastructure development has entailed a heavy cost in terms of forgone economic growth and poverty reduction. This is because both economic and social infrastructures are known to be ‘public goods’, where public financing through governments and external agencies are supposed to have an active role in their provisions at least at the early stage of economic development.

With this mind, we shall now turn to the domestic policy environments that have influenced the integration experiences by countries in SSA.

### *Domestic Policy Environments under Globalisation*

In the early decades after gaining political independence, many politicians in SSA are known to have used more expensively divisive fiscal instruments such as subsidies or preferential credits than other regions as the favoured mechanisms to buy political support or to appease various interest groups.<sup>37</sup> Furthermore, having often a narrow political support base in urban areas, governments have had a tendency to ignore their agricultural sectors and often failed to undertake pro-poor public investment in rural areas. Through these early experiences, the majority in rural areas were de facto disenfranchised from the developing process. Private agents and rural farmers were likely to have refrained from making forward looking productive investments.<sup>38</sup>

This is in a sharp contrast to the earlier experiences in East Asia, where the observed poverty-reducing effect of globalisation and integration was not purely a manifestation of market driven growth effects. As Ozawa (2009) suggests, in most of East Asia, the pro-poor pattern of public expenditure in favour of the rural poor at early stages of development produced and sustained the 'shared' growth process for some time. There were concerted efforts on the part of governments to facilitate building primary assets of the poor through such measures as an equitable distribution of land (through appropriate land reforms); extensive public provision of free and universal primary education; promotion of small scale enterprises and development of rural infrastructure—roads, irrigation, schools, agricultural support outposts, health stations, and irrigation systems.

With the advent of the debt crisis in the 1980s, fiscal retrenchment (hence reduced spending on rural infrastructure) has been consistently pursued as part of the stabilization-cum-adjustment policies. Governments were generally left with little capacity and resources to undertake public investment on a sustained basis. Typically, it is large-scale infrastructure projects that get first axed in fiscal expenditure allocations at the times of crises. In reality, the fiscal retrenchment at the height of the debt crisis in the 1980s was so deep that essential public goods provision in social infrastructure such as basic education and health expenditures were also axed and it was assumed that these services could be provided on a fee-paying basis. This has also resulted in a fragile state with a seriously depleted and impaired institutional capability to deliver social services and to build physical and social infrastructure. Under these conditions, the scope and quality of public social services and infrastructure provision has progressively deteriorated.

In the absence of reliable public goods provisions, economic transactions in SSA remain to be conducted in highly uncertain and risky environments, which engender eminently more volatile returns to investment and income streams than in other parts of the world. The high degree of uncertainty and instability is also known to have a powerful deterrent effect not only on the rate of

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<sup>37</sup> This line of characterization of African states is found in Bates (1981, 1983). See also Teranishi (1996)

<sup>38</sup> See Nissanke and Aryeetey (2003) for detailed discussion on the relationships between private agents and governments in SSA in a comparative perspective with those found in East Asia.

private investment and economic growth but also the *composition* of investment in Africa in favour of reversible and safe investments that have a self-insurance character. Thus, it is argued that safe and liquid assets are systematically chosen over less liquid but high-yielding assets. While wealthy segments of population chose to invest abroad, resulting in increased capital flights, other private investors chose to put their capital in short-term assets in sectors with relatively lower sunk costs and shorter turnover periods, such as trading, rather than in long-term physical investments (Aryeetey 1994).

Indeed, the political and economic environments in SSA have kept the economic activities of a significant proportion of private agents away from the "official" economy. The so-called *informal* economy has become an important source of employment and income for many households. In the absence of functioning formal institutions, economic exchange tended to be restricted to small-scale production and local trade, to obviate the contract enforcement problem through repeated dealing and cultural and social homogeneity. While there was an increase in the aggregate rate of growth and investment over the recent years, the majority of the poor, particularly the rural poor have been left behind. Today, many parts of SSA remain isolated from urban centres, global markets and the global community. The most recent improvement in growth performances has not been translated into structural transformation of these economies yet.

At this juncture, it is also important to note, however, that the intensified process of globalisation has not left commodity dependent low income economies in SSA untouched. The landscape of world commodity markets and production - through which many of the economies in SSA are linked to the global economy - has undergone substantial structural changes over the recent decades at both the global and national levels.<sup>39</sup>

At the global level, the heightened price volatility over time has led to a rapid expansion of derivative markets across commodities, as demand for risk hedging instruments has intensified. The rapid growth of derivative markets has subsequently attracted new players to the trading floors, resulting in a radical change in the structures of trading on commodity markets. In particular, the period of 2002 -2008 saw a huge increase in trading in commodity derivatives associated with the launch of numerous new commodity hedge funds and increasing interest from global institutional and private investors, who have increasingly sought to hold a number of primary commodities as part of their asset portfolio holdings.

The rise in trading activities on derivatives markets by private agents, not engaged in the trade of physical commodities, has resulted in a loosening of the relationship between derivatives and physical markets. The growing interlinked activities between commodity and financial markets by portfolio investors manifested itself in important changes in commodity price dynamics over short-run or even the medium-term. At least over the short-term, prices have become less reflective of actual supply and demand dynamics of physical commodities, and exhibited greater volatilities.<sup>40</sup>

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<sup>39</sup> See Nissanke (2009d) for a more detailed discussion on the new landscape of commodity markets and production under globalisation.

<sup>40</sup> Further the fundamental demand-supply relationships in commodity markets have experienced significant changes due to intensifying demand for commodities (e.g. oil and metals as well as agricultural commodities) from fast growing

In addition, the process of market consolidation has been intensifying along commodity supply chains over the recent decades. Today, Transnational Corporations (TNCs) can dictate significantly the patterns of international trade through intra-firm trade under their globally integrated production and marketing strategy. TNCs' activities are strategically organised and integrated either horizontally or vertically. This is reflected in their dominance in commodity value chains.

In agricultural commodity production and marketing, there are considerable asymmetries in market power and access to information, technology and marketing know-how between TNCs, on the one hand, and local entrepreneurs, farmers and traders in developing countries, on the other. Ironically, for small-scale producers and their governments, commodity markets have become fragmented, as TNCs' have hastened the integration process of their operation globally. This parallel process of fragmentation and integration has often resulted in a hugely skewed distribution of gains from commodity trade. Under the prevailing market structures, the potential benefits of productivity improvements can be largely appropriated by the TNCs and global supermarket chains, instead of going to fragmented producers and farmers. The governance structures of primary commodity value chains have become increasingly buyer-driven with a shift in the distribution of value skewed in favour of consuming countries.

In mineral commodities, many mineral concerns in the regions were privatized in the 1990s under auspices of World Bank and International Monetary Fund (e.g. copper mines in Zambia). Depending on how privatization was negotiated and implemented, a large part of mineral rents from the recent commodity boom may not be guaranteed to be used for economic development of producer countries.

At the national level, there have been significant changes in institutional environments facing producers and farmers engaged in Africa's main tradable goods - primary commodity sectors. For example, the waves of domestic market and trade liberalisation/deregulation transformed arrangements in production and marketing of agricultural commodities, including cash crops such as cotton and coffee. Most of state-run marketing boards were dismantled or downsized and price stabilisation funds or mechanisms ceased to exist. Domestic commodity traders and producers are now exposed to greater price risks as highly volatile prices are transmitted from the downstream commodity chain through the international marketing system to small traders and producers operating in upstream chain.

While the use of hedging instruments such as futures and options has been encouraged as an effective price risk management instruments for traders and farmers in producing countries by international financial institutions, these market-based instruments are not perfect in reducing and hedging price risks. In addition, issues such as the prohibitive financial cost and skewed access to information and high technical barriers for small actors as well as creating an adequate

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emerging economies such as China and India as well as changes in the relative composition between cash and food crops under the effects of climate changes. This has led to the recent world-wide increases in prices of staple foods, which has given rise to increasing fear over food security for the poor (Nissanke 2009c&d).

regulatory oversight agency required for liquid, functioning markets would make it hard to popularize these risk hedging mechanisms as universally applicable instruments.

Further, with the withdrawal of institutional support from governments, stable and guaranteed access to provision of necessary inputs such as seeds or fertiliser and new technology are no longer available to farmers. The institutional vacuum thus created is supposed to be filled by private agents and traders. This has often resulted in geographical fragmentation of marketing activities, and placed small-holders in a weaker position in relation to private traders in both inputs provisions and marketing of their produce in upstream commodity chains. For example, in Tanzania, many poor cotton and coffee growers are left with very little institutional support in all vital areas of service provisions, including marketing and processing arrangements; input provisions; information and extension services and access to new technology and dissemination of R&D activities by local institutions. Producers have become spatially fragmented and isolated both between and within villages. Therefore, it is no surprise that production of both cotton and coffee had declined considerably in Tanzania. While producers have been increasingly exposed to vagaries of the international market (i.e. price volatility transmitted from international markets), they are not adequately equipped to deal with price risks and other marketing risks.

Similarly, we tend to observe a considerably weakening position of governments after privatisation programmes of mineral concerns were implemented in a number of sub-Saharan African economies. Under the prevailing ownership structure of mineral concerns dominated by TNCs, the policy space for autonomous fiscal and monetary management economies in bringing about short-run stabilisation as well as long-run economic development is substantially reduced in these countries. Due to the differences in the privatisation programmes negotiated with TNC conglomerates, for example, Zambia found itself, compared to Chile, in a much less favourable position in distribution of mineral rents as well as in use of rents for macroeconomic management and the long-term prospect of economic development.

There is no doubt that an eventual transformation into more diversified economic structures is the real solution to the problems associated with the “commodity- dependence trap”. Thus, developmental problems of these countries could be overcome only through rigorous investments in production capacity and physical and social infrastructures, leading to transformation of their trade and production structures. In the transition period, however, countries are required to develop a strong capacity in managing the commodity sector, where the process of active learning-by-doing experiences and accumulation can be facilitated. Yet, the new landscape of commodity marketing and production under globalisation tend to discourage the process of learning and accumulation of critical importance for economic development in SSA. On the contrary, the institutional environments facing commodity producers both at the global and domestic levels have considerably weakened the capacity and resiliency of small holders and mining industries. As countries in SSA have failed to take a required strategic position to these fundamental changes, they have been losing their market shares in a number of world commodity markets and trade since the 1980s.

## **5. Concluding Remarks and Research Questions**

### **5.1 Concluding Remarks**

Our comparative analysis, in particular, the dynamic integration experiences in Asia point to the need for policies of *strategic integration*, not policy of *passive integration or de-linking* from the global economy.<sup>41</sup> Such a strategic position should, first of all, aim at facilitating the transformation of production and trade structures from the narrowly based commodity dependence that is bound to expose economies to external shocks. In terms of sustained economic growth, developing countries that have successfully diversified their exports structures into manufactured goods, in particular, increasingly into medium and high technology sectors, have systematically outperformed those dependent on primary commodities, and natural resource based processing goods.<sup>42</sup> Thus, whether global market forces establish a virtuous circle or vicious circle depend not only on the initial conditions at the time of exposure but also importantly on the effective design and implementation of policies to manage the integration process. As Kaplinsky (2000) notes, ‘the issue confronting policymakers is not *whether* to integrate into the global economy but *how* to integrate so as to have a stable foundation for sustainable and equitable growth’.

A strategic position towards globalization cannot be equated with a mere adoption of liberal policy regimes, or a simple fine-tuning of the pace and sequence of liberalization measures. Rather, national integration strategy should be designed in the light of the skewed nature of the on-going process of globalization. First, dynamic externalities and rent-rich activities are increasingly concentrated in high skill, knowledge intensive sectors. In short, the skill and technology related divide has become wider over recent decades. This trend is clearly reflected in the continuously declining terms of trade of less skill intensive manufactured goods relative to high skill and technology intensive goods over recent decades. The markets for many labour intensive products have come to resemble those for primary products.<sup>43</sup> The entry of China and India into global markets for these products has depressed and will continue to depress real wages and returns in these low technology and low skill sectors. On the other hand, it is difficult to sustain economic growth that is capable of creating job opportunities for growing labour force, exclusively on the basis of the primary commodity boom, as commodity prices are inherently highly volatile. Broad based development of these economies would require a strategy of using resource rents and windfalls for economic diversification.<sup>44</sup>

Second, intra-firm trade in parts, components and other intermediate goods and intra-industry trade with highly differentiated products command a predominant share of contemporary global trade. In particular, international trade is less and less conducted in arm’s length relationships between firms. Rather a growing share of world trade is accounted for by intra-firm trade undertaken by TNCs, which command a lion share of global production and marketing networks. Under globalisation, there has been a tremendous growth in offshore outsourcing and global

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<sup>41</sup> Generally, not integrating into the global economy is not a viable or attractive development option. Deardorff and Stern (2006) show that ‘outsiders’ are likely to be harmed, through the terms-of-trade- effects, by multilateral MFN tariff reductions as well as preferential trading arrangements (PTAs) between ‘insiders’.

<sup>42</sup> Ocampo and Perra (2006: tables 2 and 3, and figure 9).

<sup>43</sup> Maizels (1998).

<sup>44</sup> See Nissanke (2009c&d).

division of labour, dictated by TNCs' globally integrated production and marketing strategy. TNCs' activities are strategically organized and integrated either horizontally or vertically. In particular, with a sharp decline in transport and communication cost over the recent decades, TNCs have been aggressively organizing their operations vertically by slicing up the production process finely into numerous separate operations and locating them in different parts of the world according to cost advantages of each location.<sup>45</sup> Consequently, intra-firm trade within TNCs and intra-industry trade with highly differentiated products command a predominant share of global trade.

Generally, in the light of these specific features of contemporary globalisation, developing countries need a long term vision for upgrading their comparative advantages towards high value added activities by climbing the technology ladder step-by-step through learning and adaptation.<sup>46</sup> To succeed, developing country governments should consciously engage in building institutional capacities for integration, including a capable nation state that is ready to take on the enormous challenges posed by globalization. The positive benefits from globalization are neither automatic nor guaranteed, whilst passive liberalization would risk perpetual marginalization.

Furthermore, since openness could potentially benefit the poor in countries which have already reached the take-off stage, it is very critical that in addition to a long term vision for strategic integration, low income countries should embark on the path towards *structural transformation* of their agrarian economies, as a necessary condition for successful integration. The importance of this critical step in relation to the globalization–poverty nexus is underscored by the fact that there are critical *thresholds* that need to be reached before the positive effects of globalization on poverty reduction can be realized as discussed above. The non-linear Laffer-type relationship between globalization and poverty shows that openness helps those with basic and higher education, but reduces the income share of those with no or little education and it is only when basic education becomes the norm for the poor that openness may exert an income equalizing effect.<sup>47</sup>

Hence, sizable public investment in skill upgrading, as a specific pro-poor measure, is the key for ensuring positive benefits from globalisation for the poor. In conjunction with building assets of the poor in their human capital base, there is a need to invest in rural physical and social infrastructures, so that the poor can be connected and networked beyond isolated communities and villages. In terms of inter-sectoral flows, a continuing *gross* flow of resources should be provided to agriculture – irrigation, inputs, research and credit – to increase this sector's productivity and potential capacity of contributing an even larger flow to the rest of the economy and hence a *net* surplus to finance the subsequent development of the rest of the economy.

Finally, there is a clear need for instituting safety nets and appropriate regulations to protect the poor from large downside risks associated with globalization. Globalization has significantly

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<sup>45</sup> Krugman (1995) and Kaplinsky (2000).

<sup>46</sup> See Venables (2008) for examples of strategic thoughts on integration through an economic geography lens.

<sup>47</sup> Milanovic (2002), and Agenor (2002)

increased the vulnerability of the poor through channels such as: (i) the increased scale and frequency of macroeconomic shocks; (ii) larger exposure to changes in the ecosystem or new unknown technology with often uncertain pay-offs; and (iii) their deteriorating working conditions and weakening bargaining powers in global value chains.<sup>48</sup> Thus, governments should take a pro-active and pro-poor stance in enhancing access to information, technology and knowledge, standing firm for negotiating good deals and protecting workers' rights as well as instituting various schemes of public transfers and safety nets to shelter the poor from these adverse conditions.<sup>49</sup> Mitigating the negative effects of globalization on inequality and the poor is of particular importance in developing countries, where there is today widespread dissatisfaction with the social injustice associated with high poverty and rising inequality, which is widely viewed as a result of globalisation.

Indeed, there is not much disagreement over the need for instituting a programme of safety nets to protect the poor at times of financial crisis. However, it should be recognised that financial resources required for such a programme through a fiscal transfer mechanism is generally scarce at the national level when fragile economies are in a crisis situation. Indeed, the current global economic crisis has placed globalisation at a crossroad. The nature and course of the contemporary globalisation is now seriously challenged. We have now an overwhelming case for initiating fundamental changes into the way the globalisation process is governed at the global level.<sup>50</sup>

Meanwhile, governments of developing countries need to pursue both strategic integration and an active domestic development agenda to ensure that the poor benefit from globalization, while they are adequately protected from negative impacts. Bardhan (2006) notes that globalization should not be allowed to be used, either by its critics or by its proponents, as an excuse for inaction on the domestic as well as the international front. What is *at minimum* called for is liberalization to be accompanied by a comprehensive policy package for enhancing the capability of the poor and instituting a safety net for people who lose from the globalization process. In order to achieve this goal, the capacity of the nation states should be strengthened rather than weakened.

## 5.2 Research Questions for Country Case Studies

We emphasized in this paper the importance of examining the globalisation-growth poverty nexus in a country specific context. There are several avenues to deepen our understanding how globalisation has affected poverty through country case studies.

At the macro level, it is interesting to undertake an in-depth analysis of *whether* and *how* globalisation/integration has generated specific distribution dynamics that could affect in turn the pattern of growth and poverty. However, it should be recognized at the outset that it is hard or

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<sup>48</sup> See various case studies included in Nissanke and Thorbecke (2006d, 2006e, 2008b, 2008d).

<sup>49</sup> See Kakwani and Son (2008) and Kakwani et al. (2008), among other project case studies.

<sup>50</sup> See Nissanke and Thorbecke (2006), Nissanke (2006, 2009b) for discussion on how to make globalisation pro-poor.

even not necessarily fruitful to conduct a time-series regression analysis of the globalisation (openness)- growth-inequality-poverty relationships in a single-country context.

Therefore, I recommend that after documenting distributional consequences of globalisation, including identifying winners and losers from globalisation, a country case-study can proceed to more detailed case studies at microeconomic levels on a location-specific or sectoral specific basis. Specific questions such micro case studies could examine may include:

- To what extent (and under which conditions) trade and FDI linkages facilitated knowledge and technology transfer?
- how much has such globalisation-induced transfer directly and indirectly been beneficial for reducing inequality and poverty?
- To what extent has globalisation created new opportunities for employment or induced rural-urban migration or international migration that could be linked to poverty reduction (i.e. the employment-creating effect of globalisation)?
- What are institutional constraints that have inhibited positive effects of globalisation to be shared more equally?
- How have globalisation- induced institutional changes, including marketing and production arrangements, affected relative and absolute welfare positions of various stake holders (e.g. small-holders, traders or wage-earners in traditional commodity sectors or non-traditional tradable sectors)?
- What are the transmission channels through which globalisation-related shocks have affected adversely on inequality and poverty, including the effects of the current global financial crisis on the poor in a specific set-up?

In addition, it is particular interesting if a country study could identify cases where globalisation (either through trade or FDI or other channels) has managed to produce dynamic externalities in a SSA context. Such externalities could take several forms such as technological spill-overs, knowledge accumulation, spatial agglomeration, or specific mechanisms of learning-by-doing. Equally, it is important to examine cases where globalisation has produced negative effects on the poor, and whether such negative effects could be effectively mitigated and addressed by policy measures such as instituting safety nets.

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