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# Globalization and its Effect on World Poverty and Inequality

## **Abstract**

James D. Wolfensohn who is the former World Bank President stated that poverty amid plenty is the world's greatest challenge until now. In 1996, United Nation General Assembly came to terms that eradicating poverty is an ethical, political, social and economic imperative of humankind. International development, trade organizations, and financial, as well as practitioners and academics in this field confirmed to this statement (World Bank, 2001) In a world of 7 billion people, 80 percent live on less than \$10 per day and 3 billion people, about half of the world, live on less than \$2.50 a day. About 5 percent of global income was generated by the poorest 40 percent of the world's population, while the wealthiest 20 percent of the population generates 75 percent of world income (Shah, 2013). The United Nations Children's Fund (UNICEF, 2011) estimates that poverty is the cause of daily mortality for 22,000 children ages five and younger in 2009. Thus, in a calendar year, more than eight million children do not progress past the age of five years. Poverty literally has two central meanings. The first refers to an absolute standard of living which is reflected in satisfying the minimum basic needs required for survival. The second is relative poverty reflected in the income gap between the rich and the poor, which often is measured by economists in the form of artificial currency called "purchasing power disparity dollars'. In the world of globalization and without boundaries, one would wonder how in certain parts of the world, poverty is still a major issue. Why is the standard of living in certain countries far better than the others and why is a large part of the world poor? Typically defined as the process by which different countries become more closely integrated through international technology transfers, trade liberalization, and greater mobility of information and capital, whether globalization helps or hurts the world's poverty level is a constant debate.

## **Keywords**

Globalization, poverty, inequality, pro-globalization, anti-globalization

## **Disciplines**

Business | Economics | Public Affairs, Public Policy and Public Administration



Review

# Globalization and its effect on world poverty and inequality

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**Poverty is the world's biggest challenge and the inequality of global wealth distribution is frightening. 80% of the 7 billion people in this world live less than \$10 dollar a day and only 5% of global income was generated by the poorest 40% of the world population while 75% of the global income was generated by the wealthiest 20% of the world's population. Numerous numbers of studies has been made linking globalization towards poverty and the issue has been debated and inconclusive. Thus, this paper discussed the two schools of thoughts regarding this matter - the optimists that believe globalization as the solution of poverty and inequality, and the pessimists that believe globalization as the cause of poverty and inequality.**

**Keyword:** Globalization, poverty, inequality, pro-globalization, anti-globalization

## INTRODUCTION

James D. Wolfensohn who is the former World Bank President stated that poverty amid plenty is the world's greatest challenge until now. In 1996, United Nation General Assembly came to terms that eradicating poverty is an ethical, political, social and economic imperative of humankind. International development, trade organizations, and financial, as well as practitioners and academics in this field confirmed to this statement (World Bank, 2001)

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in satisfying the minimum basic needs required for survival. The second is relative poverty reflected in the income gap between the rich and the poor, which often is measured by economists in the form of artificial currency called "purchasing power disparity dollars". In the world of globalization and without boundaries, one would wonder how in certain parts of the world, poverty is still a major issue. Why is the standard of living in certain countries far better than the others and why is a large part of the world poor?

Typically defined as the process by which different countries become more closely integrated through international technology transfers, trade liberalization, and greater mobility of information and capital, whether globalization helps or hurts the world's poverty level is a constant debate.

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It is known and agreed that globalization and poverty share a complex relationship with globalization portrayed both as a cause of poverty and as a solution to the same problem.

Those who are in favour of globalization, the optimists, argue that globalization raises incomes across the board so that even those at the bottom of the income distribution gain in absolute terms. The views of the optimists are compatible with the Kuznets hypothesis, which holds that even if inequality at first ascends, it declines once a country develops. The pessimists, who oppose globalization, dispute that the benefits of globalization are not equally distributed so that some may even lose in absolute terms.

## GLOBALIZATION AND POVERTY

### Globalization

Globalization is the growing integration of economies and societies around the world (Collier and Dollar, 2001). It ranges from the issues of trade and services, movement of capital, growth and poverty of the world population, international migration to easier transportation and communication around the world. It is a complex process that affects many lives and above all, increased economic interdependence among countries. The International Monetary Fund (IMF) outlined four basic aspects of globalization - capital and investment movements, trade and transactions, dissemination of knowledge and the migration and movement of people (International Monetary Fund, 2000). The process of globalization affects and are affected by political, economics, socio-cultural, legal and natural factors. Globalization has in many ways been linked to development across the globe, of which one of the ultimate goals of development is poverty reduction. With the unprecedented entry of developing and low-income countries into the global economic integration, the discussion on globalization and poverty has heightened. Scholars and economists debate on whether globalization is the cause or cure for poverty.

### Poverty

Poverty is generally explained as the scarcity or the situation in which a person lacks a certain amount of material possessions or money. It is a condition in which a community or a person lacks the essential needs to enjoy a minimum standard of living in the society (Lister, 2004). The United Nations defines poverty as the inability of getting choices and opportunities. This is explained in different scenarios as not having enough to feed and clothe a family, not having access to education and a school to go to, not having access to medical facilities or a clinic to go to, not having the land to grow food for personal consumption and/or not having the opportunity to hold a job to earn one's living. The United Nations sees this a violation of human rights as the lack of basic capacity to participate effectively in society

results in insecurity, powerlessness and exclusion of individuals, households and communities into the societies' mainstream.

The World Bank defines poverty as a deprivation in well-being of which many dimensions are considered. These include low incomes and the inability to acquire basic goods and services deemed necessary for survival with dignity. Other dimensions included are poor access to clean water and sanitation, low levels of health and education, inadequate physical security, lack of voice, and inadequate capacity and opportunity to better one's life. Poverty is usually measured as either absolute or relative. In relative form, equality is shown as an index of income inequality. The study of poverty is often linked to globalization as the effect of globalization on the world's poor is highly debated.

### Issues

Debates on globalization and poverty generate extreme views. With many viewing the process of globalization as a crucial engine of growth which resulted in unprecedented gains in the welfare of human, many too has opposite views of the impact of globalization on poverty. A large body of the IMF literatures support the opinion that globalization has boosted incomes and living standards in many parts of the world (Masson, 2001). The World Bank (2001) holds a similar view on globalization. Others, including government, non-government organizations and scholars have argued that many poor people are not able to share the benefits of globalization and trade.

There have been different claims within the development community on how much progress has been made against poverty (Ravallion, 2003). Conflicting arguments and estimations were reported with some researchers claiming that overall poverty is on the decline, while others claiming that poverty is on the rise.

The World Bank's (2001) figures show that between 1987 and 1998 the share of the population in developing and transition economies living on less than \$1 a day fell from 28 percent to 24 percent. In addition, it is estimated that the number of the people who suffered poverty in the world were 200 million fewer in 1998 than in 1980 (World Bank, 2002). The millennium development goals (MDGs) reported that the world reached the poverty reduction target five years ahead of plan. In developing regions, the percentage of people living on less than \$1.25 a day fell from 47 per cent in 1990 to 22 per cent in 2010. About 700 million less people lived in conditions of extreme poverty in 2010 than in 1990 (United Nation Statistic Division, 2014). Chen and Ravallion (2004, p.1) estimate that there were almost 400 million fewer people living in poverty in 2001 than 20 years earlier, adding that if the trends over 1981 to 2001 continue then the collective \$1 per day poverty rate for 1990 will be almost halved by 2015.

However, many others do not agree with these findings and present contrary estimates to support their

argument that the international community seems incapable of coming to grips with the poverty menace and thereby reach the goal of halving poverty by 2015, as established in 2000 by the United Nations, as a main element of the millennium development goals (MDGs) Questioning the empirical basis of the neoliberal argument, Wade (2004) considers that the World Bank's poverty estimates contain a large margin of error for a number of reasons mainly that poverty headcount is very sensitive to the precise level of the international poverty lines and to the reliability of household surveys, particularly that the bank introduced a new methodology in 1990, making assessment with previous estimates unreliable. Deaton (2002) presented a similar argument.

The United Nations Conference on Trade and Development (UNCTAD, 2006) suggests that the incidence of poverty did not decline in the 1990s in the least developed countries (LDCs) as a group and has remained at 50 percent of the total population. If this trend persists, the number of people living in poverty in the LDCs will increase from 334 million in 2000 to 471 million in 2010. The Human Development Report 2005 (UNDP, 2005) offers a more sombre picture stating that about 2.5 billion people live on less than \$2 a day (40 percent of the world's population), 10.7 million children each year do not survive to their fifth birthday, while in 2003 the HIV/AIDS pandemic claimed three million lives and left five million more people infected with the virus, and the MDG target of universal primary education is not achievable on current trends. World Health Organization (WHO, 2006, p. 16) estimates that some diseases associated with a lack of access to safe drinking-water and inadequate sanitation results almost 1.7 million deaths each year.

The historical association between globalization and poverty reduction, however, hides substantial variations among countries and also within countries in their experiences with international economic integration. With the depressing figures and the yet inability for a consensus on the outcomes of globalization on world poverty, the topic leaves much room for discussion. The violent street demonstrations surrounding the ministerial meeting of the World Trade Organization (WTO) and similar protests at World Bank and International Monetary Fund meetings suggest that this debate is still going strong.

### **The optimist and pessimist of globalization**

Several decades of rising trade and capital flows, growing numbers of multinational corporation, and increasingly globalized cultural exchange have not silenced the public debate over the merits of globalization. Bardhan (2003) noted that both sides of the globalization debate have had an inclination to claim an unreasonable degree of causation between liberalizing policies and observed trends in poverty. The claims of causation are so confounded that both sides claim the success of the Asian tigers as the result of their

own policies, and the letdown of many of the African states as the result of the opposite policies. Thus, globalization's proponents claim China's and Taiwan's growth in recent decades as the result of liberalization of their economies, while globalization's critics allege that these same countries have been able to capitalize on the opportunities afforded by globalization because of broad government involvement both in the past and in the present.

Similarly, globalization's proponents claim that many of Africa's economic problems are due to lack of openness as well as inappropriate government intervention. Globalization's critics argue that Africa's woes come from other sources (including corrupt or incompetent governments), but the forced liberalization imposed by structural adjustment programs and other lending conditions has not delivered the promised growth. Instead globalization has only made living conditions worse for the poor as government services are cut back and instability is increased.

Therefore, research on the links between globalization and absolute poverty, as measured by the population share living below one purchasing power parity (PPP) dollar per day, has been unable to provide conclusive evidence on their relationship.

### **Pro-Globalization (Optimist)**

Globalization proponents advocate that poverty is on the decline, due principally to the powers of globalization and the development it causes. In other words, these proponents accord great importance to globalization as a main and pertinent engine of growth and in the battle against poverty.

Globalization is a surprisingly controversial process. Astonishing, that is, to the many economists and policymakers who believe it is the best means of bringing prosperity to the largest number of people world-wide. Supporters of economic globalization have had a tendency to conclude that dissent and criticism are the result of ignorance or vested interest (Bardhan, 2003). Bhagwati (2000) provides a good example of the way that some proponents of globalization have reacted to critics:

*"No one can escape the antiglobalists today.... This motley crew comes almost entirely from the rich countries and is overwhelmingly white, largely middle class, occasionally misinformed, often wittingly dishonest, and so diverse in its professed concerns that it makes the output from a monkey's romp on a keyboard look more coherent. (p. 134)"*

In considering the effect of globalization on world poverty, there has been a general argument in favor of endogenous growth theory, which suggests that the link between globalization and growth can be attributed to aspects of globalization, such as trade liberalization, which leads to faster integration and thus growth (Dollar and Kraay, 2001). It has then been further argued that

the growth made possible through globalization has had a beneficial effect on world poverty, and evidence seems to suggest that the more liberalized an economy is, the quicker the rate of progress will be. Thus, Dollar and Kraay (2001) famously concluded that liberalization of economic policies had been responsible for the vast improvement in the alleviation of world poverty through growth

The World Bank (2000, p. 5) adopt an identical view holding that globalization, through its effect on growth, has played an significant catalytic role in global prosperity and in lifting more people out of poverty in the last century, than in all of human history. It asserts that it is not openness, but somewhat the lack of it is what increases inequality among countries, citing that closed developing economies have achieved much more poorly than more open ones.

On the same grounds, in a conference on humanizing the global economy, Kohler (2002) posits that the spread of knowledge, better division of labor, increased productivity, and access to foreign direct investment, as a result of globalization, is a pertinent drive behind growth and has contributed to unmatched gains in human welfare over the past 50 years.

In a sample of 92 countries spanning the past four decades, Dollar and Kraay (2001) found that several causes of growth—such as openness to international trade, good rule of law, and developed financial markets—have little systematic outcome on the share of income that amass to the lower quintile. Consequently, these aspects benefit the poorest fifth of society as much as everyone else. There is little weak evidence that stabilization from high inflation and reductions in the overall size of government not only increase growth but also increase the income share of the poorest fifth in society.

Collier and Dollar (2002) attempted to address the concerns raised about globalization. In an extensive examination of issues surrounding globalization, they seek to identify the benefits of globalization and chart a course ensuring that the benefits of globalization are widely shared. Collier and Dollar ascertained that globalization helped to reduce poverty, but also postulated that supporting policies could help better to harness these benefits.

### **Anti-Globalization (Pessimist)**

Conversely, proponents of pro-poor, while recognizing the mandatory role played by openness and growth, contends that it does not represent sufficient conditions for poverty reduction. The United Nations (2005) stated that though some parts of the world have experienced unprecedented growth and improvement in living standards in recent years, poverty remains unshakable and much of the world is trapped in an inequality situation. This report also focuses on the chasm between the widening gap between skilled and unskilled workers, the formal and informal economies, the growing

disparities in education, health and opportunities for economic, social as well as political participation.

Many view the empirical evidence in favor of globalization skeptically because they see globalization as a process through which power is concentrated upward and away from the poor. In particular, they see transnational firms as gaining a lopsided amount of both political and market power. Critics of globalization are also steadfastly of the opinion that firms will use their increased power in ways that profit themselves and harm the poor.

To determine the impact of globalization on poverty over the period 1980 to 2005, Salvatore and Campano (2012) adopted the macroeconomic perspective to examine the income distributions of the people living in developing countries, as one group, and the people living in the developed countries as another group. They also further subdivided the developing countries into two groups: those that globalized and those that did not globalize, as not all developing countries have globalized during this period of study. Their study found that real personal incomes grew and flourished in both developed and developing countries, but more rapidly in the developing countries, such as in China and India. However, when looking at the estimates of real personal income in terms of the three major measures of central tendency, they found that the ratios between developed and developing have been substantially reduced in the period, especially at the mode where the most severe poverty lies.

Akoum (2008) attempted to present empirical evidence on whether countries registering high growth rates do necessarily succeed in reducing the incidence of poverty. In his study, he recognized that there are various data and methodological problems in examining the relationship between growth, globalization, and poverty. Using simple statistical methods, he concluded that *higher economic growth rates are not necessarily translated into lower poverty rates.*

Bergh and Nilsson (2011) used panel data from more than 100 countries around the world starting from 1988 through 2007, to examine the relationship between economic and social globalization and absolute income poverty (Table I).

They found that there is no evidence that globalization is associated with higher poverty levels in developing countries. They concurred that less trade restrictions and larger information flows are robustly associated with lower poverty levels thus indicating that globalization decreases poverty more when the informal and the rural sectors are relatively bigger. They also found clear evidence that the main part of the poverty-decreasing effect is not mediated via the growth channel. Finally, they stated that although the fact that many low-income countries embarked on programs of external economic liberalization in recent decades has been intensely debated, their analysis suggests that the underlying premises of current and previous poverty reduction strategies are correct: poverty reduction can be

**Table 1.** Relationship of economic and social globalization towards absolute income poverty

| Type of globalization               | Economic  | Social   |
|-------------------------------------|---|--|
| Measure                             | <i>Flows:</i> Trade, investments and international transfers (% of GDP).<br><i>Policies:</i> Mean tariff rates, taxes, import barriers, and capital account restrictions. | <i>Information flows:</i> Internet hosts, Internet users, cable television and radios (all measured per capita), trade in newspapers (% of GDP).<br><i>Personal contacts:</i> Outgoing telephone traffic, transfers, tourism, and foreign population in percent of total population. <i>Cultural proximity:</i> McDonald's and IKEA per capita, trade in books (% of GDP). |
| Short-run effects                   | Prices and wages via changes in supply and demand.  | Available information. Supply and demand.  |
| Long-run effects                    | Growth and innovation, human capital (Stark, 2004).   | Social norms and lifestyle (Medez and Popkin (2004), Yach et al. (2007)).  |
| Expected effect on absolute poverty | Ambiguous in the short run, negative in the long run.   | Ambiguous both in the short and long run.  |

achieved by means of closer economic integration and higher levels of globalization.

The evidence from reading criticisms of globalization is that people are more interested in the optimal policy mix to maximize the benefits to the poor while minimizing the negative impacts on any subgroup of the poor that is made worse off by such policies. They are also interested in ensuring that growth is socially, economically, and environmentally sustainable. Social sustainability, it is assumed, requires that inequality be kept under a certain limit.

## DISCUSSION

Different claims have been heard within the development community about how just much progress has been made against poverty (Ravallion, 2003). Research has presented conflicting arguments and estimations, with few claiming that overall poverty is on the decline, while others claim the opposite. While Aminat (2002) and Harrison and McMillan (2007) concluded in their studies that globalization has boosted incomes and helped raised living standards and that the poor are more likely to share in the gains from globalization, there are pro-poor growth advocates who find the idea that globalization produces losers more than what can be called 'winners.' For Stiglitz (2002), globalization fails in promoting development and hence continue to create poverty and instability. This finding is shared by Klasen (2005) in his study in which he concluded that globalization does not necessarily result in poverty reduction.

Fortunately, the debate over the impact of globalization and growth on poverty and income inequality has not been entirely contradictory. For instance, between the extreme views insisting that growth through globalization, have increased world's wealth and reduced poverty, and the opposing extreme view fault globalization for escalating poverty and perpetuating economic reliance of poor countries. Globalization is not in itself a folly (Sen, 2001); it can be a force for good and has the potential to benefit all, including the poor (Stiglitz, 2002).

Globalization seems to be irreversible. It produces both winners and losers among the poor. Thus, the question that needs to be addressed is how we can better govern this process to make it more inclusive and fairer than the current conditions. That is, it is not globalization ought to be abandoned, but rather it is poor governance of globalization is what needs to be challenged. If managed correctly and fairly for the benefit of all, globalization could be a positive force. International community should act together in an effort to make available the resources necessary to wage a war against poverty and inequality (Akoum, 2008). Naturally, this requires fundamental adjustment of the global status quo, starting with a true political pledge of the developing and developed countries to conceive an enhanced global financial and economic landscape.

Generally, it has been found that the poor are more likely to share in the gains from globalization when there are complementary policies in place, such as access to credit, technical know-how, and other complementary inputs. This can range from countries implementing minimum wage policies to protect unskilled workers who are most likely to be poor to encouraging export and incoming foreign investment, which has been linked to reduction in poverty levels in many countries (Harrison and McMillan, 2007).

There is also a need for a Global Collective Action to sustain a steady global economic expansion and reduce the likelihood of and contain the effects of global volatility as it is the poor countries that are known for its volatility. This international policy coordination should mobilize adequate and more effective aid for poverty reduction in order to eliminate debt of poor countries. It should provide for information and knowledge sharing, removes barriers to trade, provide preferential access to the poorest countries, provide increased international support in protecting global commons and combating global diseases.

Whatever the methods and measurements used, it is important that poverty reduction via economic growth becomes the ultimate aim of development endeavors towards a more peaceful, prosperous, and accountable economic world. It cannot be said that poverty can only

economic world. It cannot be said that poverty can only be reduced if globalization effort is halted or vice-versa.

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