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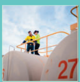
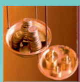
TRADE POLICIES
FOR COMBATING
INEQUALITY





Equal opportunities to firms, workers and countries

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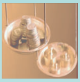

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EXECUTIVE SUMMARY

In the last four decades, international trade, along with finance and technology, has been instrumental in the development process of many countries. Trade reforms undertaken in developing countries have been accompanied by more rapid economic growth, leading to a reduction in income gaps and lower levels of inequality between countries. While the process of global trade integration has contributed to broad economic gains at country levels and convergence between developed and developing countries, yet it has also been accompanied by polarization in the distribution of income, sometimes increasing within-country income inequality. The increase in within country inequality is possibly a cause behind the current reaction against globalization, international trade and the multilateral trading system.

Despite its impact on inequality, trade remains a catalyst for economic growth and development. This is recognized in the 2030 agenda for sustainable development and the sustainable development goals (SDGs). SDG 10 on reducing inequalities within and among nations makes a limited but specific reference to the contribution of trade in terms of the provision of special and differential treatment to developing countries by way of the elimination of tariffs on imports of developing countries and least developed countries. International trade has greatly benefited global citizens by increasing economic efficiency, consumers purchasing power and product varieties. Overall, international trade has contributed to lift millions of people out of poverty and reduce inequality between rich and poor nations. Therefore, while it may be tempting to conclude that in order to reduce within country income inequality it is necessary to reverse trade integration policies, this would be clearly wrong. Despite the adverse distributional consequences of trade, resorting to protectionism is not a solution. In addition, there are many other drivers of inequality within and between nations. For example, evidence shows that skill-biased technological change has had a significantly larger impact.

The effect of trade on inequality has not been the same everywhere. There is strong evidence that the impact of international trade on inequality has been very different across countries, and that context specific factors can exacerbate or alleviate the outcome. Differences in outcomes provide compelling evidence that well thought national and multilateral policies can mitigate negative effects of trade on within-country inequality or even reduce inequality. To respond to inequality, rather than limiting trade, policymakers need to focus on encouraging trade with trade policies and on ensuring that the benefits brought by international trade become more inclusive with complementary policies. This report discusses the impact of international trade on inequality, and policy actions aimed to make the benefits brought by international trade more inclusive.

This report identifies several factors why trade has contributed to reduce between country and higher within country inequalities. The fragmentation of production processes across countries, the uneven sharing of profits across value chains and the rules governing market access and entry conditions, while greatly benefiting some, have also had negative impact on some workers, firms and countries. More in detail, the fragmentation of the production processes across countries has contributed to rising within country inequality in developing countries by increasing the wage gap between the formal and informal sectors. In developed countries, it has increased inequality by lowering blue-collar employment opportunities and reducing wages of unskilled workers relative to skilled and white collars workers. In this regard, in general both in developing and developed countries trade has provided a premium to workers at the top while negatively affecting those at the bottom of the skill ladder.

A striking characteristic of the last few decades has been the increase of market concentration. The gains from international trade have been too often captured by larger firms, leaving micro and small enterprises with little benefits from increased trade opportunities. One reason for this is economies of scale and the high entry costs which small firms need to pay to be competitive in world markets. Market concentration has also resulted in higher mark-ups which create a bias towards producers and against consumers, further increasing within country income inequality. Trade also influences inequality through market access and entry conditions. International trade is increasingly regulated through non-tariff measures. Measures such as product requirements often limit exports from countries that lack productive capacity, quality infrastructure and conformity assessment opportunities. Subsidies and quotas affect international trade in ways that are often detrimental to low-income countries. Such non-tariff measures influence international trade and can have profound effects on inequality, both within and between countries.

There is much evidence that the effects of international trade are often highly