

# **Global Economic Governance Through the Lens of Inequality and Sustainable Development:**

Overview background paper for the IISD workshop  
Geneva, Switzerland, September 13, 2019



## INTRODUCTION

It is not easy in the current climate to think about trade policy in a “big picture” exercise. Trade policy as a weapon of mercantilist statecraft seems to be the new norm, led by an energetic U.S. drive to revitalize its economy and to pursue broader domestic policy aims such as immigration policy, and further energized by the inevitable retaliatory and copycat policies taken by other countries. Moreover, the fundamental shared belief in a rules-based multilateral trading system is ever more seriously eroded by a lack of progress on the mostly-dormant Doha Round issues, and by the impending crisis of the WTO dispute settlement mechanism’s Appellate Body.

Nonetheless, there are reasons to explore how trade policy might serve (or fail to serve) higher objectives such as the UN’s Sustainable Development Goals. For one thing, the present multilateral difficulties are not the final chapter for trade policy, and the policymakers of a more multilaterally oriented future might be well served by today’s thoughtful analysis. For another thing, even at present there is dynamism at the level of regional and bilateral trade agreements, where some types of innovations are more easily adopted. Finally, even at the national level there is scope for policies that amplify trade policy’s potential for increasing wellbeing.

The objective of this workshop is to start thinking about how trade and investment regimes (including the WTO, and the network of international investment agreements) would look if their express purpose were to help achieve the Sustainable Development Goals, including a survey of how they look currently, and where governance and research gaps may exist. That objective requires some caveats at the outset.

- The multilateral trading system (MTS) was not initially developed to address sustainable development.<sup>1</sup> It was created to help global recovery post-WWII through the reduction of trade barriers, with the expectation that this would facilitate progress in other areas, of course. Most of the MTS’ instruments therefore do not directly factor in equity or distribution.
- The SDGs are an unwieldy set of objectives for any single policy area to carry, and were only adopted four years ago, long after many of the existing global economic frameworks were developed. In the present context, the job is made more manageable by the fact that trade policy’s most important impacts are limited to a sub-set of the SDGs, and the understanding that trade policy is not the only, or even the most important or appropriate, driver for achieving many of those goals.
- The focus on this workshop will be mostly on the contributions of trade policy specifically to achieving (or frustrating) SDG 10: reduce inequality within and among nations. The discussion below makes the case for this as an important focus. But we nonetheless understand that a broader assessment is ultimately needed.

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<sup>1</sup> Nonetheless, sustainable development is now acknowledged as an objective, with explicit reference in the Preamble to the Marrakesh Accord establishing the WTO and the Doha Ministerial Declaration.



- The greatest value in thinking along these lines is not in the original insights obtained in any of the sub-areas of analysis. Most of the areas surveyed here have been the subject of years of in-depth policy work by multiple institutions and individuals. The value added is rather the beginnings of a coherent picture of how the pieces might fit together – a vision of trade law and policy that successfully finds a path between the dogmatic denouncers of globalization and the dogmatic promoters of neoliberalism.

Some precision in language and scope is in order at the outset. As noted above, our focus is the influence of trade and investment regimes, within the wider context of global economic governance. In terms of law this comprises, at least, the following: the WTO; the various regional, plurilateral, and bilateral trade agreements; the web of bilateral and regional investment agreements; and the various investment chapters in trade agreements. It also comprises trade policy, here defined as trade and investment laws and regulations propounded at the national level. To keep the discussion focused, we are not currently looking at related topics such as development financing and taxation, though we recognize that these topics and others are also important elements to consider.

Within the trade and investment regimes, our focus will be on income and wealth inequality. Much of the research cited below focuses on the former, data in that area being more robust. While wealth inequality is not explicitly mentioned in the SDGs, it is an important indicator of disparities in wellbeing and capabilities, and in some ways more revealing than income inequality. Other forms of inequality dealt with elsewhere in the SDGs, such as gender inequality, are not considered here in much depth, though they should be part of a longer-term program of work in this area.

## TRADE AND THE SDGS

As noted above, trade and investment regimes have a number of points of intersection with the SDGs. The most direct is as a means of implementation: SDG 17 sees trade, along with finance, technology, and capacity building, as enablers of the various other goals. In this context, trade provides its contributions via the poverty alleviation and equity benefits made possible by market access and a rules-based global system.

But there are other important ways in which trade and investment regimes, under the right circumstances, can contribute to the achievement of the SDGs, and, in the wrong circumstances, work against their achievement. Bellmann and Tipping (2015) focus on food security, sustainable energy and oceans. Hoekman (2016) focuses on the role of trade facilitation. The SDGs themselves call for removing “restrictions and distortions in world agricultural markets” (Goal 2: ending hunger); improving aid for trade support to developing countries (Goal 8: decent work and economic growth); integrating developing country enterprises into global value chains and markets (Goal 9: industry, innovation and infrastructure); implementing the principle of special and differential treatment in the WTO (Goal 10: reduce inequality); and disciplining harmful fisheries subsidies, while incorporating special and differential treatment (Goal 14: life below water). Ultimately, it is hard to imagine



any of the SDGs being seriously implemented in ways that do not have implications for, and the need for coordination with, trade and investment regimes.

As noted above, reducing inequality has no inherent priority over the many other impacts trade and investment regimes can have on SDG implementation. However, it is an important avenue for considering how they interact with a key element of the SDGs towards which they are most immediately directed. Schillinger (2016) argues that trade-induced inequality has featured prominently in the public backlash against globalization, which has a host of negative spillover impacts. Milanovic (2016) argues that inequality may ultimately lead to political turmoil in the form of plutocracy and autocracy, and all their attendant problems. Citizen backlash against inequality was arguably front and centre in the minds of the G7 leaders when they organized a dedicated session in 2019 on “A G7 Fighting Inequalities.”<sup>2</sup> Dabla-Norris *et al.* (2015), Ostry *et al.* (2014) and others document the deleterious effects of income inequality on prospects for economic growth, the former calling widening income inequality “the defining challenge of our time.” In the same way that trade itself is seen as an enabling factor in achieving the SDGs, rising inequality within and between nations can be seen as a cross-cutting impeding factor.

## TRENDS IN INEQUALITY

A foundational theory in the explanation of inequality *within* countries was propounded by Kuznets (1955), who argued that countries during their early stages of development will experience growth of inequality attributable to skills premiums and a shortage of skilled workers, as well as urbanization. Further development, however, would bring more educated workers, and demands for social programs and taxation measures to benefit the poor. As a result, according to Kuznets, inequality would fall in later stages of development, yielding a graphic inverted-U shape: Kuznets’ curve.

This decrease in income inequality predicted by Kuznets held true in most countries from the 1920s until the 1980s, a period referred to by some as the “Great Levelling”. But thereafter all countries, to varying degrees, saw rates of inequality climb again (Alvaredo *et al.*, 2018). In the US, the share of income earned by the top percentile almost doubled from 1980 to 2014, from 11 percent to slightly above 20 percent, while the bottom 50 percent of the population saw no income growth whatsoever (Ibid). In India, China, and especially Russia, surges in inequality followed from periods of opening and liberalization. In all developed countries—but particularly in the US—the top 1 percent thrived, while the bottom 50 percent of income earners saw incomes stagnate (Western Europe) or precipitously decline (US) (Ibid). Some Western European and Northern European countries (Denmark, Finland, Netherlands, Norway, Sweden) were less susceptible to the general rise in inequality, but they are notable exceptions.

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<sup>2</sup> See the Biarritz Chair’s summary at <https://www.elysee.fr/admin/upload/default/0001/05/88ec564627711aa69725915c6c1533edad604554.pdf>.



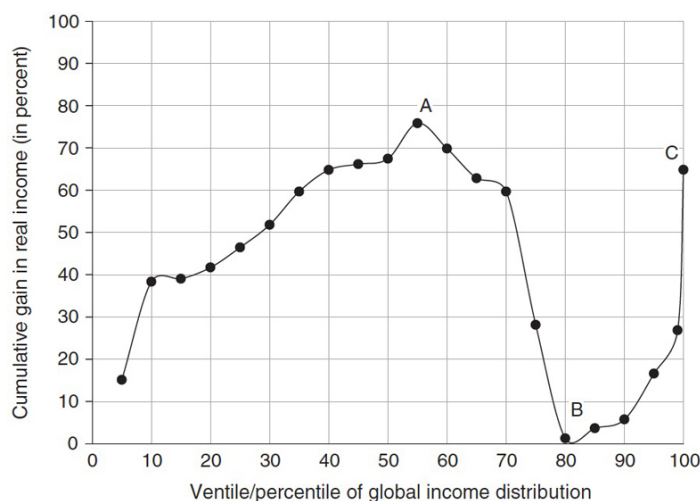
Picketty (2014) attributes the post-1980s rise in inequality to the termination of forces (such as wars) that suppressed the “natural” tendency of capital holders to gain more wealth and income over time. Milanovic (2016) describes “Kuznets’ waves” that since the 1980s have been responding to new technologies, globalization and the rising importance of heterogeneous jobs in the service sector, among other things. Stiglitz (2016) and Lindsay and Teles (2017), with reference primarily to the US, focus on the role of national institutions and policies such as anti-trust regulations, tax law, and regulatory protection of professionals. Dabla-Norris *et al* (2015) focus on the inequality-exacerbating effect of the skills premium—higher wages offered for higher skilled workers—and note further that at all levels of development better access to education and health care, and well-targeted social policies, results in less income inequality. Galbraith (2019) focuses on national responses to global turning points, in particular the debt crisis of the 1980s, the 1997 financial crisis that followed the collapse of oil and commodity prices, and the turning point in 2000 when low interest rates, high commodity prices, and social welfare policies led to moderate declines in inequality in Latin America, Russia, and China.

*Among* countries, the situation is somewhat different. From the late 1980s until the beginning of the 21<sup>st</sup> century, inter-country income inequality was basically stable. Since then, however, the world has seen an unprecedented catching up, led by China—with a real per-adult national income growth rate of 831 percent from 1980 to 2016, compared to 106 percent from 1950 to 1980—and India. (Alvaredo *et al.*, 2018:44). It should be noted that there is no contradiction between China’s role in this historical drop in *inter-country* inequality and the fact that inequality *within* China has grown during that same period; all incomes grew, but those at the top of the income distribution grew significantly more than those at the bottom. (*Ibid*:106)

While it is instructive to consider how average incomes in various countries have shifted relative to those in other countries, another important aspect of the inequality picture can be seen by considering what gains were made during that time by which segments of the global population. Figure 1 shows the relative gain in per capita income at different points of the global income distribution. The greatest gains were made at point A, at just above the median, with a roughly 75 percent increase. These income earners are primarily the rising middle class of the emerging developing countries. Ninety percent of these are from Asian emerging economies – primarily from China, but also from India, Thailand, Vietnam, and Indonesia. Point B, at the 80<sup>th</sup> percentile, showed no real growth at all during this period. These are the lower middle class in what could be called the “old rich” OECD countries: those Western Europe, North America, Oceania, and Japan. Point C is the top percentile – the ultra-rich, dominated by the citizens of the US, but also with significant representation from Western Europe, Japan, and Oceania – which saw incomes rise by about 65 percent over this period.



**Figure 1**



RELATIVE GAIN IN REAL PER CAPITA INCOME  
BY GLOBAL INCOME LEVEL, 1988–2008

Source: Milanovic (2016), p. 11.

It is worth noting that while this chart makes it look like there is equivalence between the experience of the developing country middle classes and the ultra rich, these figures are *percentage* increases, and the latter are starting from a much higher baseline than the latter. As such, the absolute gains of the richest percentile (point C) are orders of magnitude greater than those of the median percentile shown at point A. If we consider *absolute* gains in income rather than relative changes, the richest 5 percent of people worldwide received 44 percent (with almost 20 percent going to the richest 1 percent), while the “emerging middle class” clustered between the 40<sup>th</sup> and 70<sup>th</sup> percentiles received less than 15 percent.

## WHAT ROLE DO TRADE AND INVESTMENT REGIMES PLAY IN INEQUALITY?

The literature hosts an energetic debate about the role of trade in fostering the observed intra-country inequality. OECD (2017) and Dabla-Norris *et al.* (2015) argue that “globalization” is a minor player, with technological change playing a dominant role, driving up skills premiums and replacing low-and medium-skilled jobs with automated processes.<sup>3</sup> Autor, Dorn, and Hanson (2013) focus on the related question of employment, and find significantly larger employment effects in the US in sectors exposed to Chinese import competition, and fewer overall employment effects in sectors ripe for automation. UNCTAD (2017) argues that the trade-technology dichotomy is too simplistic and ignores power imbalances and the “financialization” of the global economy, which are major forces for inequality and instability.

<sup>3</sup> Both the OECD and Dabla-Norris appear to use increasing share of trade and foreign direct investment flows in global GDP as a working definition for “globalization”.





For our purposes there is no need to settle the precise modicum of contribution that trade makes to inequality within and between nations relative to other contributors like technology. It is sufficient to find that some elements of trade and investment regimes are linked to SDG 10 by:

- Contributing to increased inequality within or between nations;
- Contributing to decreased inequality within or between nations; or
- Holding the (unexploited) potential to increase or decrease inequality within or between nations.

Where those linkages can be identified, a concern for equality compels us to ask what sorts of pro-equality policy options might be available within the context of trade and investment regimes. More pragmatically, we must also consider questions of governance: where in the architecture of trade and investment regimes might such solutions fit? What aspects of the current architecture are no longer fit for purpose for these challenges, if they ever were? Where are there governance gaps that could be addressed, and by whom?

## INEQUALITY AND FOUR ASPECTS OF TRADE AND INVESTMENT REGIMES

This workshop will survey the linkages between inequality and four aspects of trade and investment regimes:

- Market access, with a focus on agricultural policy;
- E-commerce policy;
- Industrial policy; and
- Competition policy.

This is hardly an exhaustive list of those areas in which trade and investment regimes impact the achievement of SDG 10. A more comprehensive exercise would, for example, involve assessing the impacts on inequality of investment law, as well as trade-related intellectual property rights. It might also assess the extent to which special and differential treatment in the WTO – a topic of particular current interest – helps to address inequality between nations. It may also consider the equity impacts of duty-free market access for developing and least-developed countries, which has increased measurably since the adoption of the SDGs (UN Economic and Social Council, 2019: para. 31), and quota-free market access. It would certainly consider the role of trade in perpetuating or resolving gender inequality – a set of issues pursued since 2017 by over 120 WTO Members and Observers following the launch of the *Buenos Aires Declaration on Women and Trade* at the WTO's MC11 (WTO, 2017). Trade in services, and efforts such as the LDC services waiver, might also be on the list, as might the specific terms and impacts of the various accession agreements, and the process by which they are negotiated.

But this selection of topics, limited as it necessarily is, should help us better understand the governance structures around them and the links to inequality, and allow us to begin to think



about what international economic governance would look like if it were re-imagined to serve the SDGs. The working hypothesis is that the answers to that question take us down a path between the extremes of, on the one hand outright rejection of globalization and, on the other, dogmatic support for free trade. They start to clarify how trade and investment agreements and policies might be crafted to pursue important goals like greater equality, and about where best to locate the many related pieces of the web of governance that would encompass such efforts.

DRAFT





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