

# Under which conditions can trade be an engine for poverty reduction?

By

Augustin Kwasi FOSU\*

EXPERT GROUP MEETING ON SDGI

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\*Professor, Institute of Statistical, Social and Econ Res. (ISSER), U of Ghana; Ghana; Extraordinary Prof., Faculty of Econ and Mgt. Sciences (FEMS), U of Pretoria, S. Africa; Research Assoc., Centre for the Study of African Economies (CSAE), U of Oxford, UK.

A. K. Fosu

# BIG QUESTION: Under which conditions can trade be an engine for poverty reduction?

- Answer:
- 1. When a country is **better integrated into the world economy.**
  - Indeed, Dollar (2001 p. 17) argues that the only developing countries that have registered significant declines in poverty are those that also have **integrated faster into the world economy on the dimensions of trade and direct investment.**” (emphasis mine) Bhagwati and Srinivasan (2002, AER, p. 182)
  - Integration to take advantage of the **Global Value Chains (GVCs)**, etc.
  - **But** how?



# Answer:

- When a country has reached a **sufficiently high level of globalization (trade liberalization)**
  - Agenor (2004, IEEP) finds an **inverted U shape**.
- **But** will the threshold ever be reached?

# Answer:

- 3. When a country has **better attributes**: financial (private credit), education, strong institutions (bureaucratic quality).
  - African evidence: “Using a panel of African countries over the period 1981-2010 and testing for non-linearities in the trade-poverty relationship, we find that **trade openness tends to reduce poverty in countries where financial sectors are deep, education levels high and institutions strong.**” (emphasis mine)  
LeGoff and Singh (2014, p.1)
- **But** how?

# Answer:

- 4. General conceptual answer: When trade increases **economic growth faster than it increases inequality (alternatively, when growth generated by trade does not exacerbate inequality too much)**
  - **Evidence on the impact of trade on growth:** showing a positive impact of trade on economic growth is strong:
    - I. E.g., Based on a survey of the literature, Singh (2010) observes: “The macroeconomic evidence provides **dominant support for the positive and significant effects of trade on output and growth.**” (emphasis mine) (Singh, 2010, World Economy, p. 1517)

## Answer:

- II. Specifically, “Our survey reveals that the many empirical studies are surprisingly consistent in terms of the size of the relationship: A **one percentage point increase in the growth of exports is associated with a one-fifth percentage point increase** in economic growth. Given the power of compounding, the effect of trade on growth is very important for human welfare.” (my emphasis) Lewer and Van den Berg (2003, J Econ Surveys, p. 363)
- III. Interestingly, for **African economies**, the estimate is **.10** (instead of the above global estimate of .20); see Fosu (2001, JAE; 1990, World Dev.)

# Answer:

- 5. But how crucial is economic **growth compared with improvements in inequality** in reducing poverty?
- On average, **growth** has been the main engine for poverty reduction
  - Globally (e.g., Fosu, 2017, Res In Econ; Dollar and Kraay, 2002, JEG)
  - SSA (Fosu, 2015, Oxford Dev Studies)
- Thus, the usual (inclusive) growth policies under trade are crucial.

# Answer:

- **6. And the rate of transformation** (from economic growth and/or inequality changes to poverty reduction) is critical: the **income and inequality elasticities of poverty**.
  - These elasticities differ **significantly across regions and countries** (Fosu, 2017, Res in Econ, table 6):
    - Income Elasticity: -3.68 (EECA) to -1.26 (SSA) [Global: -2.34]
    - Inequality Elasticity: 5.71 (EECA) to 1.10 (SSA) [Global: 3.22]



## Answer:

- 6. What factors, then, influence these elasticities?
  - Conjecture: Governance factors
  - For example, for **SSA**, all the six Worldwide Governance Indicators (WGI) are significantly **negatively** associated with **poverty growth**, but are not significantly associated with either income or inequality changes, though to differing degrees. (Fosu, ongoing research)
  - Results differ by regional groups, however. (Fosu, ongoing research)
  - (WGI = Control of Corruption, Government Effectiveness, Voice and Accountability, Rule of Law, Political Stability and Absence of Violence/Terrorism, Regulatory Quality)
- **But** how can these be generated?
- - The role of **democracy** = ? (positive but weakest for **IEC** and strongest for **XCONST**, with **Polity2** in-between)

# Answer:

- 7. Does **export type: export diversification** matter? (Fosu UNCTAD paper?)
  - Apparently, yes (see table below: Fosu, ongoing research)

## Zero-order Correlation Matrix

	Developing countries	Sub-Saharan Africa
	POVgr	POVgr
Ygr	-0.4270***	-0.3348***
XDIV*Ygr	-0.4866***	-0.6462***
pcGDPgr	-0.2627***	-0.0332
XDIV*pcGDPgr	-0.2864***	-0.0599
[INEQgr	0.5134***	0.2728***]

## Answer (conclusion?):

- 8. What then determines Export Diversification? (Research interest, thanks to UNCTAD.)
  - Answer: To be discussed or next expert-group meeting?!
  - Conclusion: No simple answers!
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- Thank you!