Globalisation and inequality: is Heckscher-Ohlin theory dead?

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Globalisation → inequalities??!!

• Thirty years of research – and heated debate
• Heckscher-Ohlin: initial basis, now sidelined
  – ‘Stolper-Samuelson is dead’ (Davis & Mishra)
• Preview of conclusions of this talk:
  • Broad HO theory necessary but insufficient
  • Narrow HOS model can often be misleading
• Focus of talk: (a) intra-country inequality, (b) South, (c) fragmentation of production
In the beginning …

• Two factors (skilled and unskilled workers), a skill-scarce South, and globally mobile capital
• Fall in trade barriers causes South to specialise in export of labour-intensive manufactures
• Unskilled wage rises, relative to skilled wage and in real terms
• Broad HO factor demand and supply story
• Precise HOS relationship between changes in goods prices and in factor prices
Consistent with evidence?

• Most research done on the North (where HO looked consistent in 1980s – but contested)
• East Asia in 1960s-70s was also consistent
• Latin America in 1980s-90s: skill premia up
• Other S countries: growing body of evidence (but always serious identification problems)
• Skilled wage premia: rose in most countries
• Unskilled real wages: majority (?) of rises
HO-compatible explanations

• Not all developing countries are skill-scarce
  – Upper-middle income L Am > world average
• Split unskilled between Bas-eds and No-eds
  – Export-oriented mfg requires literate workers
  – Three skill groups (but not quite as in WIOD)
• Natural resources (land) another broad factor
  – In land-abundant countries, unskilled labour loses
  – Need land to explain S (but WIOD focus on mfs)
What HO was unable to explain

- Falls in relative unskilled wage in some low-income, literate, land-scarce countries
- Falling relative + rising real unskilled wages
- More employment shifts within sectors than between sectors (even quite quite disaggregated)
- Plus two inconsistencies with narrow HOS:
  - Absence of expected goods price movements
  - Factor prices varying with factor endowments
Skill-biased transfer of technology

- Better, cheaper producer goods or more access to expert foreign buyers, sellers, investors
- Best world technology is more skill-intensive
- Logical explanation of most HO discrepancies (two broad ones and missing price changes)
- Not much directly supporting micro evidence
- Heterogeneous/exporting firms micro research focuses on a different mechanism
Skill-biased transfer of activities

• New (locally) goods + processes in the South
• Transfer could be of all the relevant activities
• But increasing fragmentation of production + more trade in intermediates (WIOD focus)
• Another explanation of the HO discrepancies – new activities more skill-int than national average
• But could also pull wages in the HO direction – new activities less skill-int than national average
HO and fragmentation connected?

• On quantity side, yes for broad HO with only minor modifications: countries export goods whose *local value added content* is relatively intensive in their relatively abundant factors
  – Difference is empirical (WIOD), not theoretical
• Not so clearly for HOS, since if factor prices equalised, no incentive for fragmentation
• HOS also damaged by disappearance of link between prices of goods and of factors
  – Harder to theorise/measure prices of *activities*
Fragmentation a HO mechanism?

- Yes, as regards role of ‘transport’ costs:
  - Must be low for outsourcing, HO driver, and makes specialisation match endowments
- No, as regards role of ‘cooperation’ costs:
  - Arrival of new activities requires a non-HO driver: international mobility of know-how
  - Effects on factor prices depend on levels and changes of transport costs, cooperation costs and endowments of S country concerned
What about capital?

- Debate about its mobility (Feldstein-Horioka) – and barriers exist in many Southern countries
- High and rising capital share (P/Y) in WIOD
- Is it rising K/Y ($\Delta K/L > \Delta Y/L$) or rising P/K?
- Either way, seems bad for income inequality – because ownership of capital is concentrated
- How much of the profit stays in the South?
- Who in the South benefits from the profits?
Some conclusions

• Broad HO theory is alive and in good health
• Narrow HOS model is seriously challenged
• Full account of globalisation and inequality requires more than (even broad) HO theory
• HO (and other) theory should inform further development of WIOD work
• WIOD already a most useful basis for theory, empirical research and policy analysis