8 LINKING INCLUSIVE GROWTH AND TRADE AND INVESTMENT: IDENTIFYING TRANSMISSION CHANNELS

A. FROM GROWTH TO INCLUSIVE GROWTH

Inclusive growth refers to growth that is accessed and shared equitably by all segments of society (Kamel, 2013). Inclusive growth should be broadly based; involving all economic sectors and large parts of a country's labour force, both as contributors and beneficiaries (Ianchovichina and Lundstrom, 2009).

Growth that is classified as pro-poor and "only" reduces poverty does not necessarily meet the inclusive growth criteria, as it may not affect existing inequalities. Likewise, there are concerns that if the focus of policymakers shifts from confronting poverty to improving the distribution of income, in situations of low growth (as in recent years) the focus on poverty alleviation would be lost. Jorge and Rafalowicz (2013) argue that making strict distinctions between different types of economic growth may, in the end, not be helpful, as policymakers and stakeholders could end up more concerned with terminology than actions and results. Instead, they propose a concept of sustained growth which holistically captures and takes account of concepts of growth, poverty and inequality at the same time and promotes also stability of growth to reduce vulnerability and economic insecurity of poor. For instance, high levels of poverty and/or inequality may make it hard to sustain fast economic growth in the long-term. Therefore, this Report opts to treat inclusive growth in a holistic sense, linking it with: the principles of equality and social responsibility; poverty reduction; enhanced economic security; reduced vulnerability; and improving general well-being.

FIGURE 8.1 Growth that we all (should) want

CHANNELS	RELATIVE OUTCOMES
• Creating economic opportunities	• Lower poverty
• Ensuring access to created opportunities (jobs, education, finance, information, property rights)	• Reduced inequalities
• Preserving social cohesion	• Improved quality of life

Figure 8.1 reflects the main channels for achieving inclusive growth. Income re-distribution schemes alone (via taxes and subsidies) will not be enough to reduce poverty and ensure greater equality. Policies that enhance productivity and create productive and decent employment will also be necessary, as well as other complementary policies.[85] In other words, however dynamic economic growth may be, the benefits will not be automatically or equally shared by all contributors.[86] In order to achieve improvements in quality of life and reduce poverty and inequalities, economies must generate access to abundant, decent and productive jobs, as well ensuring non-discriminatory access to these opportunities. We will discuss how international openness through trade, trade facilitation and investment has a direct effect on the creation of economic opportunities. However, the impact of international openness depends on certain pre-requisites, including: the existence of an appropriate regulatory environment; institutions; infrastructure; and transparent social dialogue.

B. WHAT MAKES TRADE AND INVESTMENT INCLUSIVE?

However dynamic economic growth may be, the benefits will not be automatically or equally shared by all contributors - we need policies to achieve that outcome.

Despite the term "inclusive growth" only being forged about a decade ago,[87] there is already much literature on the topic. The term is now recognized in both professional and public circles. On the other hand, this is not the case for "inclusive trade and investment". A recent publication of ECLAC lists the various definitions of concepts involving inclusive growth and trade, in the broadest sense, put forward by international organizations. These concepts also incorporate links among inclusive growth, trade, globalization and economic openness. Table 8.1 presents the concepts with their concise definitions; none of which defines "inclusive trade and investment" directly.

TABLE 8.1 Approaches to defining inclusive growth from a perspective of trade and globalization

Concept	Organization	Definition
To promote trade for inclusive growth and development	World Bank (2011)	Trade that facilitates the adaptation and movement of both workers and firms towards sectors with growing demand, and the incorporation of new technologies with the objective of promoting productivity and employment growth of a wide group of workers and firms.
Globalization and inclusive development	UNCTAD (2007)	A process of globalization that brings more benefits for countries and population sectors previously excluded.
ILO declaration on social justice for an egalitarian globalization	ILO (2008)	Globalization that obtains better results through a more equitable distribution, in order to respond to the universal aspiration of social justice, achieve full employment, secure the sustainability of open societies and the world economy, achieve social cohesion and fight against poverty and inequality.

TABLE 8.1 (continued) Approaches to defining inclusive growth from a perspective of trade and globalization

Socially-sustainable globalization	ILO and WTO (2011)	Trade that improves access to employment, salaries and stability.
Trade and growth to benefit the poor	OECD (2010)	Trade that generates the kind of growth that will reduce poverty. Five policy categories are listed: trade policy and regulations, trade development, trade-related infrastructure, enhancement of the productive capacity, and trade adaptation facilitation.
Growth of inclusive markets	United Nations Development Programme (www.growing inclusivemarkets.org)	The contribution of firms to human development through the inclusion of the poor in the value chain as consumers, producers, business owners or employees.
Inclusive value chains	Food and Agriculture Organization of the United Nations (n.d.)	Value chains that include the small farmers, especially in the African, Caribbean and Pacific regions.
Inclusive businesses	Inter-American DevelopmentBank (IDB) (2011)	Activities that promote an improvement in the quality of life of sectors with few resources through the supply of basic services or products, as well as the inclusion in value chains of disadvantaged productive groups.
Fair trade	FINE (Fairtrade Labeling Organizations International (FLO), World Fair Trade Organization (WFTO), Network of European Worldshops! (NEWS!) and European Fair Trade Association (EFTA))	Trade that contributes towards more sustainable development, offering better trading conditions and securing the rights of marginalized producers and workers, especially in the South.
Trade and inclusive development	ECLAC (2013)	Trade that generates a virtuous circle between the reduction of structural differences and growth that improves the wellbeing of a majority and reduces inequality.

Source: ECLAC, 2013; pp. 28-29 (informal translation from Spanish by ESCAP staff.

Further, the *Asia-Pacific Trade and Investment Report 2009* (ESCAP, 2009; pp. 54-57) offered a description of "inclusive trade policy". This effort is summarized in Box 8.1. While the description is given in terms of "pro-poor trade policy", the objectives of such a policy are consistent not only with reducing poverty but also with providing fairer and more equitable access to benefits of economic openness.

Pro-poor trade policy would prevent the poor from bearing the burden of trade reforms and will equip them to maximize benefits from trade and investment.

Following the preliminary work of ESCAP (2009) and ESCAP (2012),[88] recent work by ECLAC, and building on the body of knowledge in available literature, this Report hopes to make a further contribution towards conceptualization of inclusive trade and investment. Also, and more importantly, it seeks to identify the main drivers of inclusive trade and investment, and by doing so help frame policymaking.[89]

Inclusive trade and investment imply that all people can participate in, and benefit from those activities.

Box 8.1 An early attempt by the United Nations to define inclusive trade

In order to make trade work for development, trade should be pro-poor and contribute to human development (UNDP Regional Centre in Colombo, 2006). The 2007 United Nations report clarifies that a pro-poor trade policy should be formulated so that it: (a) prevents the poor from bearing the burden of trade disciplines and liberalization; (b) equips poorer people to derive maximum benefit from trade and globalization; and (c) contributes to achieving the Millennium Development Goals.

In particular, trade policy should aim at: (a) enabling poorer people to compete in a globalized world market by increasing their productivity; (b) ensuring that the benefits of trade are shared in the most equitable manner; (c) ensuring that poor people, women and other disadvantaged groups can draw benefits from exports and that equality within the country and between social groups, regions and genders can be promoted; (d) shielding vulnerable groups from the impact of trade liberalization when this threatens their livelihoods; and (e) ensuring that the liberalization of goods and services effectively contributes to these objectives (Gibbs, 2007, see also a diagram below).

A pro-poor trade policy would pursue market access for products and services where production is dominated by the poor and develop their supply-side capacity. Such a policy would preferably not include trade distorting measures which may have negative effects in the long run. Such a policy would target underdeveloped areas within countries, in particular rural areas, boosting agricultural and industrial production. The agricultural sector has often been overlooked in favour of industrialization but it remains an essential sector not just in terms of development and economic growth, but in particular in reducing poverty. It has also been a traditional stumbling block in multilateral trade negotiations. This has prevented better access to developed country markets for agricultural products from developing countries.

In addition to agriculture, trade policy should increasingly focus on the services sector (ESCAP, 2008). Trade in services has grown rapidly as discussed in part I of this Report. Developing countries have developed strong competitive advantages in selected services sectors such as information technology (IT) and tourism. While services do not always directly help the poor such as the IT industry in India, the revenue generated from such industries helps Government invest in trade-related infrastructure which does benefit the poor. But there are many more possibilities. Improving services related to transport and communications yield an immediate development dividend and indirectly strengthen the supply-side capacity of domestic industry. Here again, Governments need to ensure that the promotion of the services industry is inclusive and sustainable.

While trade and trade liberalization generate winners and losers, Governments need to ensure that ultimately society at large benefits in the long run, and that in the short run trade at least does not disproportionally affect vulnerable groups. This is particularly important for women. In most developing countries in Asia and the Pacific, women still constitute the majority of temporary, casual, seasonal and contract labourers and low-skilled workers. In South Asia, agriculture remains the biggest employer of female workers, whereas in East Asia, South-East Asia and the Pacific, the majority of women workers have moved into industry and services. These workers are the most vulnerable to job losses because they are unlikely to be covered by formal unemployment insurance or social protection schemes. As a result, women, especially those working in export-oriented industries such as textiles, garments and electronics, have been disproportionally affected by the crisis (ILO, 2009). Women also represent a large proportion of the workers in the informal economy. They are assuming increasing roles as owners and managers of SMEs but face routine discrimination when applying for finance or Government support. Their vulnerability increased with the recent global economic crisis, as when formal sector workers switch to the informal economy during crises, it depresses the wages of the informal economy. As a result, women are considered as part of the “flexible” workforce that can be easily discarded during economic downturns. Inclusive trade policies therefore need to include gender appropriate measures and specifically target export-oriented enterprises which are owned or managed by women. Women entrepreneurship needs to be promoted and access to credit, including micro-credit should proceed on a non-discriminatory basis.

Source: ESCAP 2009, pp. 54-57.

Trade and investment will only be inclusive if it is fully consistent with the principles of inclusive growth, explained above. These principles imply that all people can contribute to and benefit from international transactions. However, more often than not, trade and investment will not be enough to create inclusive growth; rather trade and investment policies must be nested in an enabling environment and accompanied by complementary policies. Only then can inclusive growth be achieved.[90] Similarly, a pre-requisite for inclusive trade and investment is equal opportunity for all and often positive discrimination for those most vulnerable and presently excluded, particularly in terms of access to employment, entrepreneurship, technology and finance; as well as in terms of access to social services, such as education, health and information. Equality of opportunities may then contribute to inclusiveness. Inclusiveness or inclusivity combines aspects related to the creation of employment, the integration of specific groups in the labour force such as women, young and unskilled workers, as well as migrants, the compensation and productivity of workers (including an appropriate balance between compensation and productivity, and "decent pay"), and the creation of new (micro) firms and innovation in high-tech sectors. Furthermore, inclusivity is related to the level and variety of consumption, as well as the price of consumption (with respect to food, health and education). Lastly, poverty and inequality as well as quality of life (well-being) dimensions are also included in the concept of inclusivity[91] (see also foldout table presenting a status of inclusivity indicators, as well as openness indicators, for the Asia-Pacific economies).

Inclusivity is multifaceted comprising reduction of poverty and inequality, creation of decently paid jobs especially for those previously excluded, enhanced entrepreneurship, improved consumption choices, and quality of life in general.

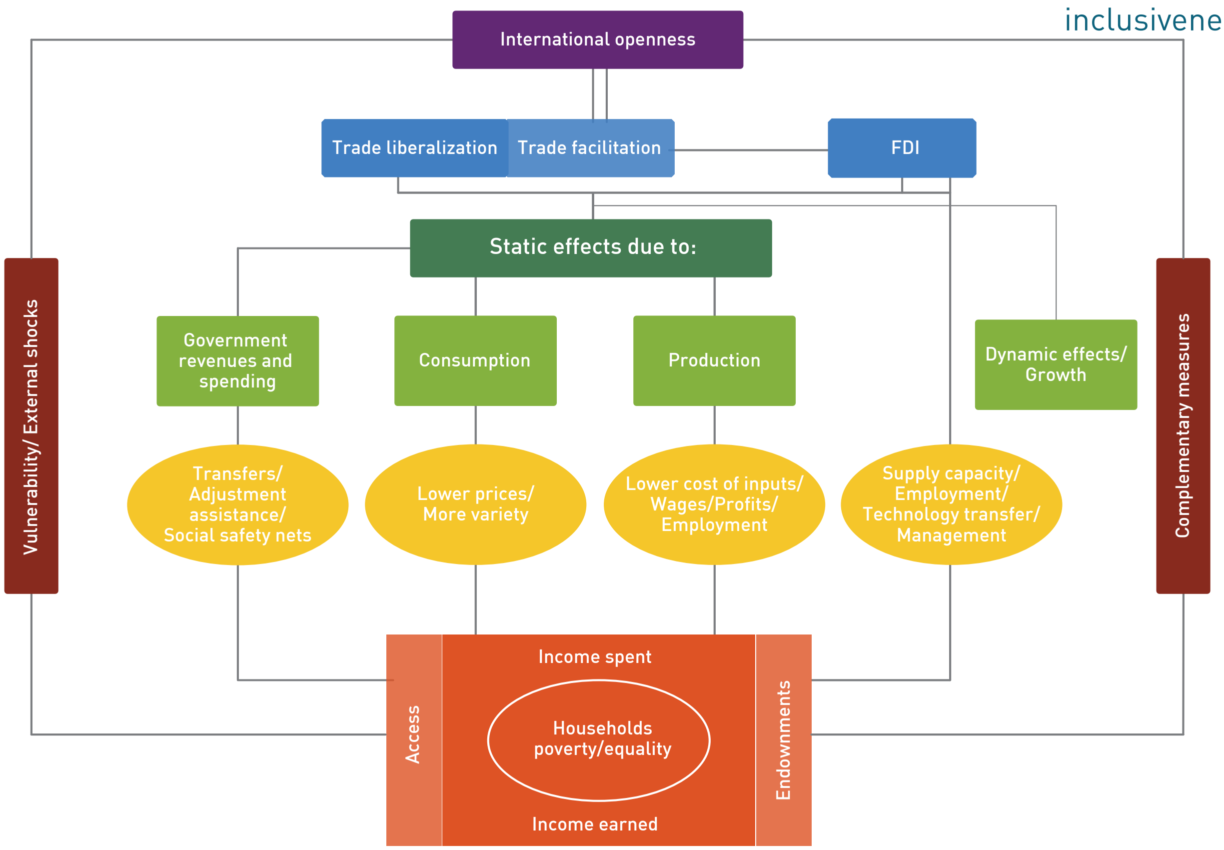
Orthodox approaches have prioritized trade liberalization on the assumption that global markets are efficient and greater openness to them will increase overall economic efficiency. As it is accepted that trade liberalization produces both winners and losers, these approaches suggest using the tax system to redistribute the gains that emerge from the overall rise in efficiency. This, however, ignores the other dimensions of inclusivity mentioned above. For instance, employment creation and decent wages do not emerge automatically as a result of liberalization.[92] Wage earners may also not get a proportionate share of the value created by trade (cf. UNCTAD, 2012). Displaced workers often can not find equally well-paying jobs and may remain unemployed. Adjustment to shocks caused by trade opening can be slow, leading to more significant and long-lasting negative impacts on the health and education prospects of workers and their families, as the Philippines' experience with trade liberalization shows (Intal, 2008).[93] The orthodox prescription simply does not go far enough to tackle all aspects of inclusiveness.

C. HOW DOES IT WORK?

So what are the linkages between trade and investment and inclusive outcomes? Here we have to keep in mind multidimensionality of inclusivity, which includes, as discussed, the following outcomes: productive, stable, decent and gender-balanced employment; enhanced entrepreneurship; improved consumption choices; reduced poverty and inequality; greater well-being.

The literature on interlinkages between trade and investment liberalization, growth, poverty and inequality has grown significantly in the last 15 years. However, a large portion of the work is based on, or responding to, the transmission framework described in Winters (2000), McCulloch, Winters and Cirera (2001) and Winters, McCulloch and McKay (2004). Our framework (shown in figure 8.2) builds on these original representations of transmission channels. This is done by adding details on the

FIGURE 8.2 Direct and indirect impacts of international openness policies on inclusiveness



Source: ESCAP, based on Winters (2000).

international openness side (that is, trade policy, trade facilitation and foreign direct investment (FDI)) and linking them directly and indirectly through to households (and individuals) affected.

The sections below explain in more detail the linkages between three different avenues of international openness related to trade and investment - trade policy, trade facilitation and FDI and related promotion policies - and households' welfare but a summary description is offered here. The most obvious impacts of international openness are those that reflect the reallocation of resources and associated static efficiency gains in response to changes in relative prices. Households could be affected through changes in the prices of goods; or through changes to incomes which may vary as the employment sector either expands because of new export opportunities or contracts due to import competition. Trade liberalization or trade facilitation measures reduce trade costs, and could directly benefit households by reducing prices of goods and services. Through the production channel, trade policy and trade facilitation could lower the cost of imported inputs supplied for the production of other goods, including for exports. Such impacts have been instrumental for the Asia-Pacific developing countries. These contribute to the region's production-sharing under the "factory Asia" model, and are of crucial importance for small and medium-sized enterprises (SMEs).

New business opportunities could also lead to a rise in a demand for unskilled and semi-skilled labour. On the other hand, tougher competition (owing to economic opening) may cause some micro and SMEs to exit the market, because of their lack of competitiveness compared with international rivals. Public sector revenues may also be affected by changes in economic openness, which will, in turn, impact on expected government assistance for micro and SMEs. However, impacts on the government purse are difficult to predict on *a priori* basis. Many Governments have found themselves collecting higher tariff revenue, despite a cut in import or export tariffs. Effectively implemented trade facilitation measures also often lead to higher compliance levels by traders and therefore higher revenue collection. This could sustain government spending on social programmes, and other necessary supports, during reform implementation. Furthermore, FDI inflows are often crucial to correct for short-term capital immobility which prevents firms adjusting production in accordance with new incentives. FDI inflows may directly influence supply capacity of the private and public sectors and, thus, affect employment, productivity and other factors which impact on households. Further dynamic and growth generating effects are very important for reducing poverty and inequality above and beyond these static efficiency impacts.

But international openness does not stop at taking goods, services and capital across borders. It also brings: technology embodied in capital goods; market and product knowledge that arise from the trading relationships; scale economies and market development; and institutional arrangements and processes that underpin expanded movement of goods and services inherent in international exchange (Intal, 2008). These additional dynamic and growth generating effects are very important for reducing poverty and inequality. The long-term impacts of international openness on sustained inclusive development involve the creation of a virtuous circle between the static efficiency effects of international openness and dynamic forces, such as growth and structural transformation (see ECLAC, 2013 for more details).

> ***How a country participates in the regional and global economy and if it is part of global value chains or not, goes a long way to determine impacts on poverty and inequality.***

It is important to remember that there can be both pro- and anti-poor effects from each channel; therefore there must be caution in making generalizations about whether a particular type of international openness increases or decreases poverty, and how it might then affect inequality. While in the long-run growth is expected to benefit the poor, the effects are likely to vary between households and across countries. Therefore, due attention has to be given to a country's specific mode of participation in the regional and global economy as well as understanding their position in global value chains. For example, are they mostly suppliers of manufacturing goods, services or raw materials? Are they linked to reciprocal or non-reciprocal preferential trading agreements? Is the country landlocked or a small island economy?

The framework illustrates the complex linkages at work in transmitting benefits from trade- and investment-led growth through to households. This clearly points to putting in place a coherent and integrated set of policies, coordinated at different levels,[94] in order to deliver inclusiveness. To better understand how different areas of openness contribute to inclusiveness and poverty eradication (and to formulate coherent policy mixes) their impacts are analysed separately through three specific aspects: (1) trade policy related changes, including preferential trade liberalization; (2) trade facilitation measures and policies, and (3) FDI and related promotion policies. Additional insights are then brought through the case studies in chapter 10.

1. Trade policy measures

Trade policy refers to measures undertaken by national Governments to influence the movements of goods and services (as well as factors of production) across its borders. This can include: various measures and instruments; regulations; international agreements and negotiating positions. Trade policy mostly aims at enhancing the market access of domestic firms (producers) in both national and foreign markets, while attempting to also provide access to imported goods, services, and technology, under the best conditions for domestic producers and consumers.[95] To meet these objectives, trade policy frequently turns to restrictions, limiting the free flows of goods and services. However, limitation on cross-border flows can have costs as there are many known benefits of free exchange between individuals, communities, and nations. This is not only due to its effects on prices and therefore, incomes. International exchange enables production specialization, thus increasing efficiency; and it makes available goods, services and resources that are not available locally (or are more expensive), including intermediates. In turn, this improves both consumption and productive potential.[96]

Consequently, restrictions on exchange reduce economic opportunity and limit potential improvements in welfare. Sen (1999) argues that the freedom to transact is an important aspect of a well-functioning market system. Curtailment of that freedom through, say, trade taxes or quotas, imposes not only efficiency costs, but the freedom lost should also be valued in-and-of-itself. Thus, trade restrictions are considered to reduce efficiency as well as denying opportunities, and possibly leading to higher poverty. Sen (1999) suggests that people have a right to transact and improve their condition; denying them that right must be adequately justified.

Possible legitimate justifications for limits on exchange do exist. For instance they may include negative externalities from trade that flow onto third parties, such as: pollution, loss of biodiversity, destruction of natural habitat, unemployment and structural adjustment costs. It is claimed that many of these costs fall disproportionately on the poor and, therefore, exacerbate poverty rather than ameliorate it (Bhagwati and Srinivasan, 2002). Likewise, if some trade policies create market imperfections, rent-seeking and policy-related distortions,[97] these could cause inequality, in addition and above those that would have existed in a text-book "free market based economy"; where inequalities are considered a natural byproduct of productivity and preference differences (Mankiw, 2013). When imperfections exist, they can create inefficiency; removing distortions, including in asset ownership, is thus expected to increase the overall size of the economic pie, and hence reduce poverty and inequality.

> *People have a right to transact and improve their condition; denying them that right must be adequately justified as in case of negative externalities.*

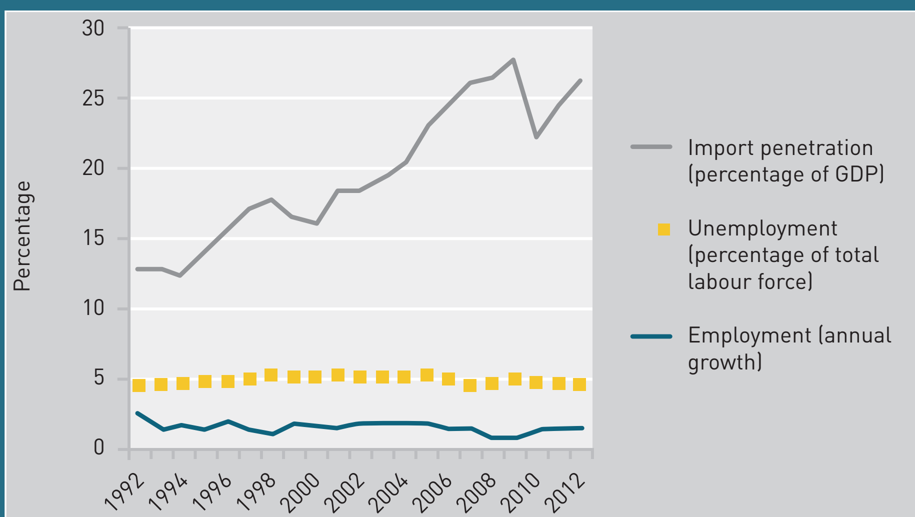
Importantly, literature points to trade being an ally in the fight against poverty, as it increases average incomes and, thus, provides more resources to mobilize in the struggle. However, trade policy changes will hurt someone.[98] Therefore, the fundamental challenge is how to implement policy changes in a way that maximizes its benefits for poverty alleviation; and concurrently what to do about any poverty created or exacerbated by those policy changes (McCulloch, Winters and Cirera, 2001). How to expand the benefits of international trade to more people, while minimizing the costs it imposes, so that trade liberalization and increased engagement of the domestic economy with the rest of the world ends up being growth inclusive? The analysis here, and in the literature, reinforced by real world case studies, shows that the resolution of this challenge rests on the quality of complementary policies.[99] Thus it should be possible for policymakers to develop suitable responses to ensure that the poor gain from trade liberalization (cf. Winters, 2000).

The contribution of trade liberalization to inclusiveness is measured by the increase in households' welfare. This depends on behavioural responses to the changes in relative prices within two dimensions: (1) for firms, the change in relative prices affects the cost/profit ratio and influences the production mix, the sourcing of inputs, and also employment and wages; (2) for households, changes in prices have a direct effect on the price of the consumption basket and indirectly affect the sources of a household's income (box 8.3). Firms and households' reaction

Box 8.2 Trade and jobs: some Illustrations from the region

The trade-led growth of the Asian and Pacific economies has led to a marked increase in import penetration measured as a share of imports of goods and services in GDP. This has risen from low double-digit figures in the early 1990s to close to 30% just prior to the beginning of the global economic crisis in 2008. This rise in import penetration did not, on the whole, adversely affect unemployment; it stayed between 4 and 5% from 1992 to 2012 (figure A). However, the rate of job creation did decline during that period. Average employment growth was around 1.45%, which barely accommodated the rise in the region's labour force.

Figure A Import penetration and jobs in the Asia-Pacific region, 1992-2011

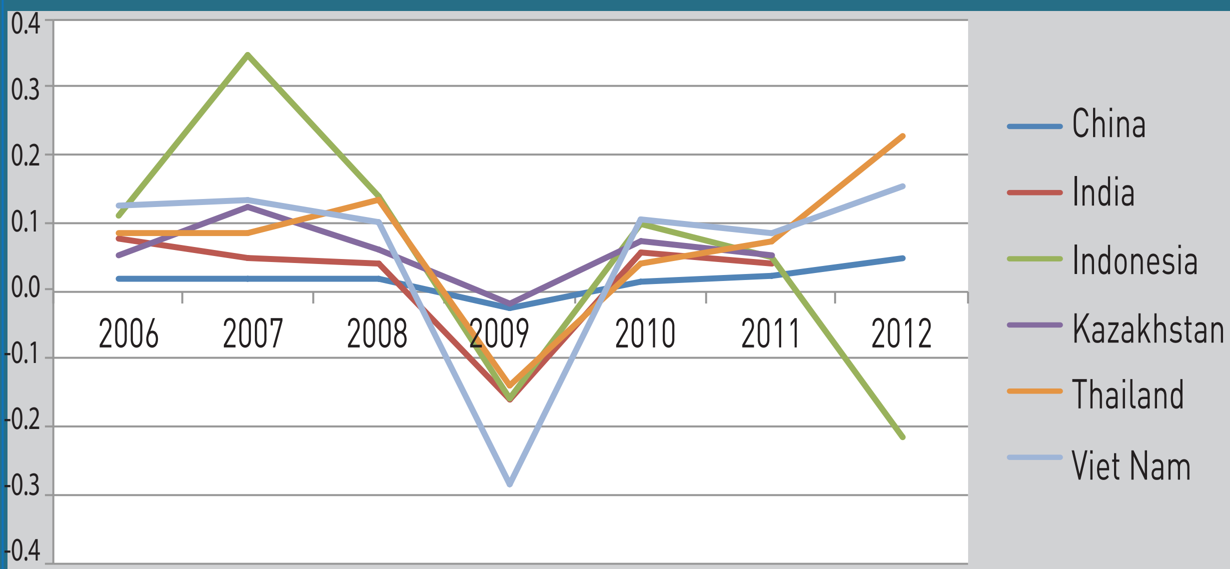


Source: ESCAP based on data from ESCAP Online Statistics Division data (accessed October 2013).

Empirical studies in general do not offer much evidence that international openness matters either for overall employment or for aggregate unemployment. In line with these findings, Asian and Pacific economies do not display clear relationships between trade opening and levels of employment or unemployment. However, while aggregate employment may remain broadly stable, this can conceal large impacts on workers affected by import competition in individual sectors and companies. When domestic production is displaced by imports, it is hoped that workers will be able to shift quickly, and with little cost, into other sectors that are expanding – typically related to exports. In reality, this relocation is not automatic – it takes time and requires additional resources. When more disaggregated sectoral or even firm-level data are used it is possible to identify surges in unemployment related to import competition. Therefore, a key challenge is to gain a better understanding of the reasons for slow adjustment and to facilitate the movement of workers between sectors, thus minimizing the time during which people are under- or unemployed.

What is the responsiveness of employment to the demand created by an expanding export sector? The facts are rather disappointing. While in the two major developing countries of the region, China and India, from 2006 to 2012 exports grew by 16% and 21%, respectively, employment rose by only 0.4% and 1.5% per year, respectively. A similarly weak association is found in several other developing countries that are ranked among the 10 top Asian exporters. It is notable that the overall correlation between export and employment is rather low, meaning that exports have to grow considerably (with no change in other external or internal conditions) in order to produce a noticeable increase in the number of jobs. In the case of China and India, the 1% of export growth was associated with only 0.02% and 0.05%, respectively, of employment growth. In other countries, employment was slightly more responsive, but on average stayed at a level below 0.15% (figure B). This finding is quite alarming for those countries that were counting on using export-led growth as the main engine of development. It points to an urgent need for policymakers in Asia and the Pacific to explore the possible reasons for this

Figure B Export sensitivity of total employment, selected countries



Source: ESCAP, based on CEIC data (accessed October 2013).

jobless export growth. Furthermore, it is also important to understand what is happening at the sectoral and firm levels. It appears that industrial and services employment might be more responsive to exports than agriculture. For example, a 1% increase in industrial exports is associated with a rise in the industrial sector employment of 0.08% and 0.30 % in India and China, respectively. Similarly, a services export growth of 1% is associated with an average employment growth of 0.06% and 0.56 % in India and China, respectively. In contrast, agriculture employment shows a different sensitivity to changes in agricultural exports. Sensitivity indices are lower than for the industrial and services sectors, and are negative on average in China, Indonesia, Kazakhstan and Viet Nam, despite the high share of agricultural exports by Indonesia and Viet Nam.

There are several possible explanations for these results. In order for agricultural exports to rise, products must be competitive; often, this means a shift from labour- to technology-intensive production (akin to jobless growth). In addition, export growth is sometimes unrelated to production increases, as in the case of surplus stocks being exported. Often, jobs in other sectors offer higher monetary or other returns, so even if agricultural exports grow, employment might not. Agriculture appears to be the sector most affected by structural adjustment as countries continue to industrialize and enjoy dynamic growth. Even when growth slows or contracts, workers who are laid-off from the industrial sector find it more difficult to move back to the agricultural sector because of the cost of reallocation or other reasons. These workers therefore often remain unemployed or, while waiting for a new job, end up taking unskilled and lower paid jobs in the services sector.

In efforts to strengthen the role of agriculture in inclusive development, in addition to introducing policies related to improvement of productivity and a reversal of disincentives, linking that sector more closely to domestic and foreign markets through specific enabling measures – including training, marketing and access to credit, together with trade reforms and trade facilitation – would enable the benefits of trade-created jobs to be shared with the majority of the populations of many countries.[1]

[1] See the cases in chapter 10 in which new jobs and/or higher productivity and wages were realized from exports of agricultural products following the implementation of trade promotion and trade facilitation measures. For econometric testing see also Chapter 9, section A in this Report.

to the price changes such as their adjustment to new incentives depends on many factors, most notably existing capabilities, mobility costs, access to finance, operation of labour and financial markets, upgrading of skills, incentive framework for product innovation and technology adoption. These are in turn dependent on access to various markets and public sector services.

Removal of trade obstacles changes the prices of tradable versus non-tradable goods and services, as well as the cost of capital. Since this creates incentives to engage in international transactions with trading partners, it is likely that the share of trade and investment will be boosted and, in turn, the country will become more trade dependent. Subsequently, the country may be more vulnerable to shocks, which, when they occur, can be easily transmitted from trading partners to the local economy. Transmission is increasingly through shared production and participation in global value chains (GVCs) (see

Box 8.3 Removal of barriers to trade

Removal of barriers to trade is expected to change:

(1) Households consumption, through changing the prices of tradable goods and services and improving access to new products and services;

(2) Firms' production, through changing the prices and availability of inputs;

(3) Firms' production, by changing the relative wages of skilled and unskilled labour and the cost of capital, thereby affecting the decisions on amount and structure (gender, skill) of employment (and affecting a household income generation);

(4) Government revenue from trade, corporate and other taxes, and thus its ability to transfer income to adversely affected segments of population, finance trade adjustment programmes and those for the poor;

(5) Productive capacity and growth, by changing incentives for investment and innovation, and affecting economic growth.

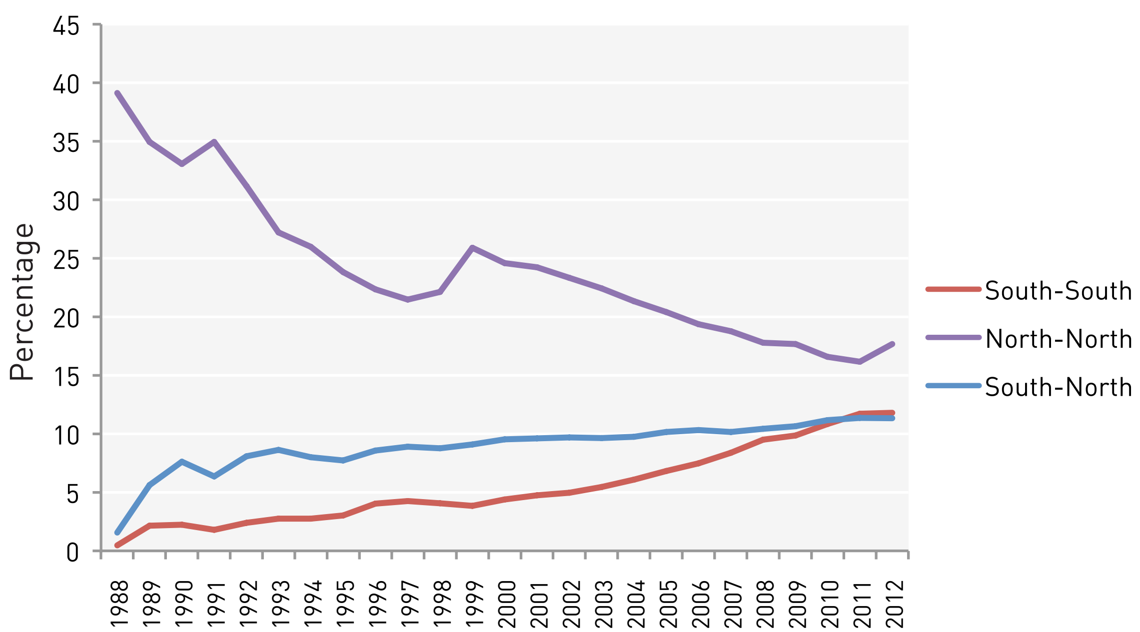
also ESCAP, 2009). The interdependency brought about by production fragmentation and GVCs can be weakened or intensified depending on sophistication of the country's traded products, and the level of concentration in its export and import markets. Less sophisticated export baskets (cf. Hausmann, Hwang and Rodrik (2007), and as applied to some Asian least developed countries in Freire (2012) could be associated with a weaker capacity to supply higher value added components, thus also adversely affecting the share of income captured by national producers. Similarly, the greater the geographic concentration of exports and imports, the stronger will be the pass-through of shocks to domestic economy from affected overseas markets. This was well observed during the recent global economic crisis, where economies which were more dependent on exporting parts and components to China (the centre of the "factory Asia" model of production sharing) experienced more serious contractions of exports and therefore had to deal with tougher adjustments (ESCAP 2009, 2011 and 2012). However, their relatively high vertical integration and participation in GVCs also helped their fast recovery, as it complemented domestic demand by balancing export demand sources of demand from traditional Northern markets with the new demand in the South.

(a) Is South-South trade likely to be more inclusive?

South-South trade has grown considerably faster than North-South growth (see figure 8.3). This has led some commentators to propose that South-South trade has some other characteristics which may have higher propensity to deliver inclusive outcomes than traditional trade flows.

According to the UNDP (2013), South-South exports of merchandise and manufacturing have surpassed South-North exports in volume, while also increasing the intensity of skills and technology embodied in them. Although, most of the South-South trade used to be driven by demand and supply emanating from so-called BRICS countries, recently this trade has spread to other parts of the South. According to Bartels and Vinanchiarachi (2009), these trading BRICS countries include: Brazil, agribusiness; the Russian Federation, technology; India, services; China, manufactures; and South Africa, auto-aerospace and minerals. An example of the spread

FIGURE 8.3 South-South trade as a share of world trade



Source: ESCAP, calculated based on WITS database, accessed September 2013.

of trade linkages among the South can be seen in China and India capitalizing on new opportunities in Sub-Saharan Africa, which has now become a major source and destination of South-South trade. China has increased its trade in the region, from $1 billion to more than $140 billion during 1992 to 2011. Indian companies have invested in a range of industries, including infrastructure, hospitality and telecommunications (UNDP, 2013).

However, if South-South trade is measured in terms of value added, a slightly different picture emerges. Namely, gross data often suffers from double counting as products cross borders multiple times and it can ignore the role of intermediates in global or regional value chains. Thus, when using the OECD Trade in Value Added (TiVA) data, South-South trade appears to be significantly lower than South-North and North-North trade (BBVA, 2013; Canuto, 2013). Lower values for South-South trade when using value added terms are the result of general lower value retention when Southern countries export to other Southern countries, rather than when they export to the North (e.g. 35% vs. 47% of gross figures in manufacturing activities according to BBVA, 2013). Moreover, the manufacturing share of South-South trade falls from 71% on a gross value basis to 42% on a value added basis, indicating higher than previously accounted share for services and commodities. These revised figures then suggest that South-South trade should not be viewed as a substitute but rather as complement to South-North trade.

Notwithstanding the necessary revisions of trade dollar values, the benefit of South-South trade is that the goods supplied are often more affordable, more appropriate to needs, and more closely aligned with energy conservation and sustainability principles when compared with those originating from richer countries. Therefore, these products offer more development potential if appropriately acquired, adopted and imitated (UNDP, 2013). Least developed countries also benefit from such trade; importing from China many inputs that improve productive capacity and infrastructure, for example road vehicles, industrial machinery and equipment, chemicals, iron and steel. Leather and textiles, such as yarn and fabric, dominate other import categories. These are used as inputs into apparel for export from the least developed countries to the North. Therefore, cheaper imported inputs may allow least developed countries a more competitive position in global production networks.

The South-South trade is better aligned with the needs of developing countries.

Trade in services also provides opportunities for developing countries, which many have seized. These may include lower-skill employment, such as work in call centres and data entry; medium-skill work, such as back office accounting and programming; and high-skill work, such as architectural design and software development. The services sector is expected to expand rapidly as domestic consumer markets grow, allowing the benefits of scale to promote even more trade.

Tourism has become one of the world's largest services exports, accounting for almost 30% of all commercial services. The most popular destinations include many developing countries in the Asia-Pacific region. The United Nations World Tourism Organization projects that by 2020 almost a billion tourist arrivals will occur within this region (UNDP, 2013).

An emerging South-South trade profile indicates windows of opportunity for converting relatively static comparative advantages into dynamic competitive advantages, especially through development of more vibrant South-South value chains.

(b) Preferential trade

For national producers, international trade not only brings easier access to imported goods and services but also the ability to export to larger and often richer, overseas markets. This can increase their earnings and encourage greater employment - bringing benefits to the wider community. Therefore, access to foreign markets (as well as protection from foreign competition at home) matters for firms and can be crucial in their survival. As a result, national firms expect their Governments to work on their behalf to secure the best terms in both domestic and foreign markets.

Governments thus pursue preferential trade terms through the negotiation of trade agreements. These can be bilateral, regional or plurilateral. Recent years have seen rapid growth in the number of these reciprocal preferential trade agreements (as reported in chapter 6). Additionally, developing countries may also be eligible for trade preferences under unilateral preference schemes, known as the Generalized System of Preferences (GSP).

Following decisions at the WTO 2005 Hong Kong Ministerial Conference, most developed economies and several developing countries (including some in the Asia-Pacific region) have introduced additional duty-free quota-free (DFQF) access schemes explicitly for least developed countries' products.

However, while securing preferential market access can provide important advantages to producers from least developed countries, tariff reduction alone is often not sufficient to secure access to a foreign market. Non-tariff measures can create even more significant border barriers to small exporters from the poorest countries. These often consist of regulatory standards, such as sanitary and phytosanitary measures (SPS). "Behind the border" barriers (including unnecessary regulations) can seriously reduce or limit market access by increasing the costs of trade (this will be discussed in relation to trade facilitation later). Furthermore, as tariffs have also fallen under multilateral liberalization[100] (in some cases to zero) the margin of preference for products by the least developed countries' exporters gets squeezed with adverse impacts on their relative competitiveness (Edo and Heal, 2013).

Nevertheless, preferential trade access is still necessary and desirable to enable countries and producers, who rely on trade as engine of growth, to participate in trade. It is important to improve these schemes, and bring maximum benefits to the least developed countries' producers. Preferences providers should, therefore, consider adapting existing schemes to better meet least developed countries' needs. This could be done by:

(i) Ensuring that preferences cover export products in which least developed countries have a present comparative advantage or clear development potential in the future;

(ii) Offering "true" preferential market access – over and above what is offered to other developing countries through GSP or via most-favoured-nation;

(iii) Simplifying Rules of Origin to reflect the current reality of international commerce. This is especially necessary where much trade is in parts rather than in finished goods. Well designed Rules of Origin are: easy to comply with; sensitive to sectors of importance now and in the future; and allow cumulation over least developed countries by adopting of so-called "open cumulation" (see chapter 6 in this Report).

Current DFQF schemes have further to go in meeting these requirements. DFQF schemes offered by other Asia-Pacific developing countries, notably China and India, are to be welcomed and it is hoped they will expand product coverage in future.[101] All schemes should aspire to the best practices in product coverage and rules of origin regimes.

> ***Trade agreements can lower barriers but should include provisions to enhance supply capacity and ease adjustment shocks to have an inclusive outcome.***

In addition to the unilateral preferential schemes, negotiated reciprocal exchange of preferential treatment through regional or bilateral free trade agreements have become, somewhat paradoxically, very popular since the establishment of the WTO in 1995. This type of liberalization may deliver more inclusive outcomes when compared with either autonomous or multilateral liberalization. Firstly, preferential trade agreements are typically done with partners selected for some specific reasons. This may allow for either more gradual or selective liberalization (as in APTA) or a complete exclusion of some items, thus sheltering those most vulnerable to import competition.[102] Secondly, inclusion of provisions for economic cooperation may deliver wider benefits. This co-operation may include: human capital development; mobility of labour; and financial cooperation, thus directly contributing to more inclusive gains. Moreover, in the case of regional trading or economic blocs, such as ASEAN, countries may also stipulate provisions with a more direct impact on closing the development gaps among the members. These types of agreements may allow for intra-bloc mobility of labour and FDI, as well as extending public-private partnerships to the regional level and improving access to various important markets, such as IT, energy, and finance. Projects also combine resources for infrastructure development and exchange or access to education and health services.

While trade liberalization creates many opportunities for inclusive growth, increased import competition may create adjustment problems for certain companies and workers. These adverse effects are expected to be short-term as resources are reallocated across the economy. In order to prevent this restructuring worsening poverty and inequality, a country can put in place so-called trade adjustment assistance programmes (see box 8.4 for the case of the Republic of Korea). Such programmes assist companies, and thus individual workers, undergo restructuring while minimizing vulnerabilities and unpredictability.

2. Trade facilitation measures

Trade facilitation aims at increasing the cost effectiveness of international trade transactions by streamlining regulatory and other trade procedures (see ADB-ESCAP, 2013 for a list of definitions by various international organizations). Trade facilitation measures are expected to reduce trade costs and make trade processes simpler and more predictable, while maintaining appropriate levels of regulatory controls of goods flowing across borders. Such measures are often considered essential for firms in developing countries to participate effectively in regional and global production

BOX 8.4 Trade Adjustment Assistance Programme of the Republic of Korea

The Government of the Republic of Korea introduced the Trade Adjustment Assistance (TAA) program to facilitate restructuring of domestic companies which are exposed to adverse impacts from Free Trade Agreements (FTAs). TAA is designed to provide domestic companies which have been harmed or are expected to be harmed from the increase of imports resulting from liberalization of trade with the FTA trading partners with loans or consulting service to support their smooth restructuring. The Act on Trade Adjustment Assistance following FTAs was enacted in 2006 and the TAA has been in place since 2007.

To receive the benefit of TAA, companies which are designated by the Act need to meet several criteria. First, they should have been harmed or to be harmed for at least six months. Second, damage need to be attributable to the increase in imports of the same or a directly competitive product or service. Third, the companies' restructuring plans should be enhancing their competitiveness. If the companies meet the conditions, the Government makes a decision on offering a loan based on the company's credit (up to a maximum of KRW 4.5 billion for facilities per company and a maximum KRW 0.5 billion for operations). The evaluation on trade damage is done by the Korea Trade Commission and the assessment on the award of benefits is done by the Small and Medium Business Corporation. The companies can also be provided with consulting services to assist with the restructuring plan covering 80% of the total cost (maximum KRW 40 million).

Strict eligibility has led to low utilization of the scheme and triggered domestic criticism. Consequently the Government revised the enforcement decree in 2012. The criterion of damage (the decrease in sales volumes or production compared to the previous year) was lowered from more than 20% to 10%, and new activities related to consultancy and application preparation were added. Up to 8 Oct 2013, KRW 7.6 billion (approximately USD 7.2 million) for 23 companies have been provided by TAA. Despite these improvements, it has still been suggested that the TAA program should be reformed to encourage more substantial structural adjustments in the affected companies.

Source: Ministry of Trade, Industry, and Energy and Korea Trade Commission, the Republic of Korea (n.d.).; Cheong and Cho (2011).

networks. They can be expected to not only increase trade but also revenue collection as trade procedures and controls at the border become more transparent through automation and the application of modern information and communication technologies. Beyond simplification of regulatory requirements and "at the border" procedures, trade facilitation reforms increasingly include enhancing access and efficiency of trade-related services, such as logistics and financial services, as well as improving the overall business environment.

How can trade facilitation lead to inclusive outcomes? One way is through its positive impact on trade flows. Improved trade facilitation significantly contributes to increased trade (e.g. Layton, 2008). As argued earlier, increased trade, in turn, can have positive impacts on the poor or vulnerable groups. These trade-led impacts are certainly wide in scope and can operate through multiple channels (Higgins and Prowse, 2010).

It is the small traders who should benefit the most from simplified trade procedures.

Trade facilitation can also deliver inclusive outcomes because various social and economic groups benefit from trade facilitation or use the services offered by trade facilitation (ODI, 2010). Generally, trade facilitation can be expected to have a positive effect on the inclusiveness of trade given that simplification of procedures can be expected to make it easier for small traders and firms to participate in international trade. However, this is only the case if simplified procedures are offered in a non-discriminatory manner to both small and large traders, which is not always the case. Accordingly, inclusive outcomes can be further increased through specific trade facilitation measures targeted at "excluded" groups or sectors. Benefits can range from enhanced access to trade related information for agricultural producers, to women's ability to participate in trade, or to easier access to trade related services (e.g. financing) previously only available to big traders. Because they are often restricted to a certain geographic area or sectoral in nature, these benefits may also be smaller relative to those arising through increased trade, although the very limited literature available in this area precludes any definitive conclusion on the matter.

(a) Impact of trade facilitation through trade

Increased international trade from trade facilitation initiatives can achieve inclusive gains. As noted, the key purpose of trade facilitation is to reduce trade transaction costs and time, both for exports and imports. Costs can be reduced by faster processing of trade documents, higher predictability of goods supply, and improved information exchange. In turn, this increases international competitiveness and trade.

Assuming that trade facilitation reforms in port and customs efficiency, domestic regulations, and the e-business environment can bring countries in Asia and the Pacific with below-average performance closer to the regional average, it is estimated that intraregional trade could increase by over $250 billion (Mann, Wilson and Otsuki, 2004). More recent analysis suggests that reducing direct export costs in Asia to OECD levels (a 14% reduction on the average across the region) could increase Asian exports by up to 14%, translating in an expected 2.5% rise in per capita GDP in Asia and the Pacific countries (ADB-ESCAP, 2013).

Reducing direct export costs in Asia to OECD levels could bring a 2.5% rise in per capita GDP in Asia and the Pacific countries.

Increased exports could also lead to additional employment and higher incomes for the poor. In India, organic spice exports increased from $290,000 in 2000 to $1.13 million in 2003, due to support measures for: improving production techniques; organic certification; and standards development. This led to an increase in small-scale organic spice producers. In some areas, producers tripled their income (DMI Associates, 2006). Bangladesh's export-oriented textile industry employs more than 3.5 million factory workers, with most being women who have migrated from villages (Ahamed, 2012). Increased exports can also lead to higher income opportunities for other actors along the supply chain.

Costs associated with inefficient trade procedures are estimated to account for up to 15% of the cost of goods traded (ADB-ESCAP, 2013). Savings from reduced trade transaction costs can be shared by the producers, wholesalers and other players involved in the supply chain, while consumers may also enjoy lower prices depending on market structure. Governments would also gain through increased revenue. For example, the Malaysian Customs has been able to increase its customs revenue through adoption of national single window for one-time submission of transaction information to trade control agencies (UNNExT, 2010).[103]

Reduced transaction costs from trade facilitation can contribute to lowering consumer prices through imports. In particular, cheaper food commodities for mass public consumption are extremely important for many regional developing countries. Ensuring food security and nutrition to the poor and vulnerable groups, including women and children, can be achieved through accessibility. Cheaper food commodities imports can also stabilize consumer prices for essential goods. Cheaper imports of raw materials, machinery or intermediate products also mean lower input costs for export-oriented industries.

Time and cost reduction in "behind the border" trade procedures should also result in greater benefits for SMEs and poor individual traders, who are more vulnerable to delayed deliveries, order rejections or corrupt practices. In comparison to larger enterprises, this group faces greater challenges in accessing information and/or knowledge. A survey in Bangladesh found that SMEs mostly use customs agents because of their lack of knowledge about customs procedures and resources (Hossain, Deb and Amin, 2010). On the accrual of benefits, a Philippines study showed that 65% of SMEs experienced a reduction in lodgment time for customs documents after electronic submission of information was implemented (de Dios, 2010).

(b) Importance of international and domestic trade linkages

An important contribution of trade facilitation to inclusive growth is through its impact on domestic trade and business practices. Duval and Uthoktham (2010) found that improving the domestic business (investment) environment has a similar or greater impact on export competitiveness than implementing international trade specific facilitation measures (e.g. reducing export time). In other words, a firm's international trade efficiency is strongly linked to domestic trade efficiency and the business environment in its own country. Given such a strong link, it is reasonable to expect that efficient international trade practices may also have positive spill-over effects on domestic trade and practices, contributing to more inclusive trade. This argument is supported by recent research (e.g. Shepherd and Stone, 2013) which provides evidence that knowledge flows from global value chains can contribute to industrial upgrading of quality standards in developing countries' domestic markets.

Domestic markets are a significant source of economic growth in many developing economies in the Asia-Pacific region. For example, in Indonesia, micro, small and medium enterprises (MSMEs) are 99% of the total enterprises and drive local economic activities (Tambunan, 2013). These MSMEs are made up of a few employees, or are family-run. They are not generally linked with international trade. However, Tambunan in ESCAP-ARTNeT (2013) study shows that improvements in international trade benefits MSMEs involved in domestic trade. This is essentially through spill-over effects on business environment, transport regulations, access to trade-related information and logistics, and financial services.

logistics and transportation in the Dongfeng village of Eastern China, in addition to increasing income of villagers making the furniture (Chinese Academy of Social Sciences, 2010). Increased growth can also attract new domestic players into international trade. In developing countries, many exporting companies cater both to international and local markets. Domestic trade facilitation measures, such as developing a warehouse in a rural area for food commodities, can be used for storing products for local producers. In turn, producers are able to respond to price fluctuations, and can gain from selling products when market prices are high (Higgins and Prowse, 2010).

> *Improving access to domestic markets is part of the solution to making trade and investment inclusive.*

Growth of a specific export industry can develop local support services and contribute to higher incomes for communities. A case in China (more in chapter 10), shows that through e-commerce, furniture exports created opportunities for development of support services. This includes

Improved logistics services that connect rural areas to urban collection centres also act as boosters to local producers by reducing post-harvest loss. For example, the e-choupal in India established by a large food export and retail company, provides improved logistics services, which reduce handling loss of soy beans (there is further detail of the e-choupal case study in chapter 10).

In another forthcoming ESCAP-ARTNeT study, Karunaratne and Abaysekara (2013) found that in Sri Lanka, export processing zones (EPZs) considered as a trade facilitating measure, have created economic opportunities for SMEs to open up hotels, restaurants and business support services, such as printing and telecommunication, to cater to the needs of zones employees. To serve the businesses inside EPZs, logistics service providers, freight forwarders and recruiting agencies have opened offices in the area. These enterprises have created additional employment for people from the surrounding areas, as well as other locations across the country.

Measures based on improving access to and use of information and communications technologies (ICT) are often seen as a big component of trade facilitation. ICT applications can include: computer automation of operations; use of mobile technology; risk management systems; track and trace systems; e-commerce; Electronic Data Exchange (EDI); and development of electronic Single Windows. Economic gains for the poor from the widespread use of mobile communication technology are noteworthy. One UNCTAD report (2010) indicates that reduction in information search costs and improved communication within supply chains and overall improvement in market efficiency' as the biggest gains for the poor through ICT enabled services or application. There are examples where dairy farmers in Bhutan or "mobile ladies" in Bangladesh have improved their livelihoods using mobile phone based services.[104]

Finally, economic corridors are a good example of local communities benefiting from increased economic activity. As shown in the forthcoming ESCAP-ARTNeT study by Cheewatrakoolpong, Mallikamas and Phupoxsakul (2013), the construction of the second Thai-Lao Friendship bridge has resulted into more jobs (in addition to trade), and, in turn, a reduction in people under the poverty line for Thailand's Mukdahan province.[105] Jobs have been created to support the greater economic activity taking place in the province. However, the study concluded that the economic opportunities created by the bridge can be better utilized with the provision of micro-finance facilities, which can be considered a domestic trade facilitation measure.

3. Foreign direct investment and related promotion measures

Foreign direct investment (FDI) can generally lead to economic growth, as well as providing revenues for the host country (through capital and tax returns) that can be used for development financing. To encourage FDI, government intervention is required in order to establish an enabling and conducive investment climate. To create such an investment climate, Government must put a set of rules and regulations in place, which guarantee a stable and predictable system. The Government must also find a balance between regulation and liberalization, as too much of either can lead to undesirable results (ESCAP, 2009). Too much regulation may prevent the market from functioning efficiently or FDI benefits from fully accruing to the host economy; too little regulation may give companies the opportunity to exploit the host economy. Governments need to pay attention to the rules and regulations, including the legal framework, stipulating the minimum wage and standard working conditions. This can range from the protection of private (including community) property rights to labour laws. Also to be put in place are social safety nets that protect the society's most vulnerable. Moreover, environmental standards are important to ensure that companies operate and use resources in a sustainable manner.

Both the public and private sectors have a role to play in making FDI inclusive. On one hand, Governments can secure policies that channel FDI to support marginalized groups, place limitations on damaging business activities, and use increased revenue to provide redistributive social benefits. On the other hand, businesses can provide overall employment and training, while also providing direct benefits to disadvantaged groups.

Improved employee motivation is an important gain from inclusive development promotion. This could be done either directly through wages or indirectly through non-wage working conditions. Foreign investors can enhance worker motivation, while contributing to

FDI can be a driver of growth and proponent of inclusivity with the right balance between regulation and liberalization.

inclusive development, through established fair working conditions, chances for upward employee mobility and training schemes for local employees. Governments are responsible for ensuring implementation of decent standards of work and income.

Foreign and domestic investors can benefit from actively contributing to inclusive growth in host countries. Inclusive growth can empower larger segments of the local population to become consumers, in turn, increasing the size of local markets. Consequently, companies can increase revenue by selling their services and products to a larger segment of the local population. Therefore, it makes good business sense to offer training to people who may become potential customers, productive workers or suppliers. For example, companies that offer irrigation or other farming products could also offer training to local farmers in order to increase productivity. This may, in turn, increase purchases of a company's goods and services. Additionally, it would also make business sense for foreign companies to involve local suppliers as much as possible in their supply chain. This could increase local employment, as well as increase the potential for more customers of goods and services offered by foreign investors. FDI can also contribute to inclusive growth through adoption of inclusive business models and the implementation of responsible business practices, or corporate social responsibility (CSR). Inclusive business models refer to core business activities, which have a tangible impact on economic and social opportunities for low-income groups (Business Innovation Facility, 2011). Inclusive business models help to promote inclusive growth as they involve socially-disadvantaged groups in the value chain of companies' core business. This can be as suppliers, distributors, retailers, or customers. Responsible business practices (CSR) involve ensuring implementation of the good governance principles. These are related to human rights, labour, environment, and anti-corruption in core business activities.

Impact investment has the potential to channel private capital flows where they have the greatest effect on inclusive growth.

Another pathway for FDI to facilitate inclusive growth is through engagement of foreign investors in impact investment and social enterprises. At the heart of impact investment and social enterprise is the specific objective of improving social development, instead of solely maximizing profit. ADB defines impact investment as investment that aims not only to secure financial returns, but also to generate positive social and environmental impacts. Impact investment has the potential to channel substantial private capital flows into initiatives that address challenges faced by developing countries. Through its potential for promoting inclusive businesses and social enterprises, impact investment can contribute to inclusive growth. Social enterprises are characterized as business-oriented not-for-profit or for-profit enterprises, with the latter putting primary focus on social impact as well as focusing on financial objectives (ADB, 2013). Additionally, foreign investors can make positive contributions to community and social development by supporting and initiating efforts in fields such as infrastructure, education and health. What have been particularly promising, in this regard, are private-public partnerships.

Making FDI inclusive requires action both from the private and the public sector.

In summary, as with other dimensions of international openness, FDI needs to be supported by a host of complementary policies to lead to inclusiveness. With such support, FDI can lead to increased employment, wages, productivity, and skills that all have the potential for benefiting marginalized groups. This requires complementary policies and regulations that channel FDI to inclusive areas, guide investor behaviour in line with inclusive activities, and/or use FDI revenue to finance social development objectives. Flows from foreign investment have the potential to help groups such as women, youth, minorities or the disabled. Flows from foreign investment have the potential to help groups such as women, youth, minorities or persons with disabilities with the right set of national policies and regulations in place. FDI could have more direct impact by engaging businesses in more socially responsible behaviour. This can be done through the adoption of international standards for responsible business practices, social and impact investment, and public-private partnerships.

CONCLUSION

Analysis of the linkages between international openness and households' welfare offers many different paths through which households can be affected. Clearly, it is difficult to isolate the role of individual effects, as more than one can be at work at the same time. However, several themes recur across all three dimensions of openness: (1) opportunities for employment are critical as employment affects the income that a household can spend on consumption – of both basic commodities and purchases that improve well-being (2) productivity gains can be driven by exports as well as access to new technology through FDI; (3) wages impact directly on poverty and income inequality; and (4) equal employment opportunity between genders is one indicator of access. Therefore the next chapter turns to exploring the linkages of those inclusivity indicators and trade and investment in more detail.

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ENDNOTES

[85]See later part of this chapter as well as chapter 9 for details on complementary policies.

[86]This does mean that those who could not have contributed (for multiple reasons) should still be included in sharing the gains.

[87]The first mention of "inclusive growth" is linked to a paper by Lin (2004). Previously this concept was known as "growth with equity" (Fei, Ranis and Kuo, 1979).

[88]ESCAP organized an expert group meeting on 14 December 2012, calling upon a number of experts in the field of development and international economics, as well as from all sectors and including international organizations. This Report benefited greatly from deliberations in the Expert Group Meeting on Inclusive and Job-Enhancing Trade: Asia-Pacific opportunities. Materials from the meeting are

available from www.unescap.org/tid/projects/ijet.asp. Additionally, a number of background papers and written contributions were made available to the drafters of the Report, and these are accessible on the APTIR webpage www.unescap.org/tid/ti_report2013/home.asp .

[89]Furthermore, in the preparation process of a report such as this, a deeper understanding and clarification of methodology and data is gained. This proves to be useful in the ESCAP secretariat's work on building capacity for further analytical work in the region.

[90]The fact that other policies need to accompany policies of international openness (such as trade liberalization) to guarantee that the benefits are shared by all suggests that one should not rely only on this (trade) policy to reduce poverty.

[91] One important factor impacting inclusiveness and not addressed in this report is access to assets, especially land.

[92]More generally, the reasons for departure between model-based outcomes and reality relate to various complications arising from inefficient factor markets and thus inadequacy of assuming that necessary adjustments will happen quickly and without additional investment, local or foreign, or new labour skills (see more in Intal, 2008). As discussed later, this partially could be fixed by pairing trade liberalization with a number of complementary policies (other than distributive measures) which are often ignored in the simplistic prescriptions on trade liberalization.

[93] It is not only in developing countries that workers and poor carry the cost of trade liberalization. Autor and all (2013) examined the impact of exposure to rising trade competition on the employment and earning trajectory of United States workers between 1992 and 2007. They found that workers bear substantial costs as a result of the "shock" of rising import competition.

[94]A need for local and national coordination is clear. International cooperation is necessary to enable smoother and beneficial participation of least developed and developing countries in trade and global value chains. Often policies of trading and investment partners (related to for example their overseas development assistance (ODA), Aid for Trade, or GSP schemes), or rules set at regional (trading blocs) or international level such as WTO, WIPO and OECD may (adversely) affect the effectiveness of national efforts to implement pro-poor and pro-development trade and investment.

[954]It is beyond the scope of this Report to go into discussion of desirable features of national trade policies, but it is still important to just mention that stability, transparency and predictability are of crucial importance.

[96]These are results of trade having positive impacts on and allowing use of competition, economies of scale, learning by doing etc.

[97]Examples of trade policy related distortions include market barriers in general, tariffs, non-tariff barriers (NTBs), and trade-related regulations. These are not justified by public policy concerns or evenly distributed across economic sectors, differences in market entry barriers and incentives to rent-seeking behaviour, trade-distorting effects of policies that discriminate goods, services and factors by geographical origins of trade (such as preferential trade agreements and GSP schemes). The problem is that many distortions also arise from infrastructural management, regulation and complimentary policy areas such as macroeconomic, financial and labour markets, governance and human capital creation (Giordano and Li, 2012).

[98]However, the orthodox presumption is that the total loss will fall short of overall gains (except in the case of Bhagwati's (1958) "immiserizing growth"), thus creating sufficient resources for making sure that no one is worse off. While this theoretical prescription works in a long-run, in reality there are many challenges to making it operational. Consequently, some people end up being hurt by policy changes. But, "rejecting any reform that adversely affected any poor person would be a recipe for long-run stagnation, which would ultimately increase, not reduce, poverty" (Winters, 2000, p. 2).

[99]Intal (2008) uses the case of the Philippines to identify these important complementary policies: quality of the investment response, the workings of the labour market and industrial relations, the overall macroeconomic environment, and the quality of government institutions and related policies, among others.

[100]The preference erosion also arises from a host of preferential trade agreements between developed and developing countries, further increasing competitiveness challenges of the least developed countries' exports.

[101]While a number of developed countries DFQF schemes cover 97% of the items (as mandated by the Hong Kong Declaration), the United States never implemented a similar scheme covering all least developed countries.

[102] Even the partial preferential trade agreements focused only trade in goods can positively influence trade and investment flows and thereby help with inclusive development. See, for example, the positive spillover effects of the India-Sri Lanka Free Trade Agreement on growth of FDI and employment in chapter 10. .

[103]Although this estimate should be taken with caution given the difficulties in quantifying linkages between trade facilitation and poverty, a forthcoming ESCAP-ARTNeT study

on China concludes that a 1% increase in port efficiency may be associated with a 1% decrease in poverty index (Wu, 2013).

[104]Based on UNCTAD (2010). Bhutan's dairy farmers use mobile phones to access market information, avoid intermediaries, collective pricing etc. Grameen Phone of Bangladesh has facilitated mobile phone services including internet based facilities to the rural people through more than 350,000 village ladies.

[105]Thailand's Mukdahan province is located at the border of Thailand and the Lao People's Democratic Republic in the East West Economic Corridor and is close to Savannakhet of the Lao People's Democratic Republic.