ESSAYS ON INSTITUTIONS, INEQUALITY, AND THE RESOURCE CURSE

Classification: Internal

Abstract

Since the dissolution of the Bretton Woods system and the two oil crises of the 1970s, the world economy has undergone profound transformations. The most observable of these is the increased economic integration and global trade facilitated by advancements in transportation, communication, and information technology, especially involving the rapidly rising participation of developing countries in global trade. Developing economies, particularly those in Asia, experienced rapid industrialization and rising exports of manufactured goods starting in the 1980s, while industrialized countries benefited from access to cheap consumer goods and emerging new markets. This period also brought huge achievements in economic growth and poverty reduction in the developing world, especially in Asian countries. However, the last wave of globalization has brought challenges and risks as well. Two of the most pressing ones are growing inequality and climate change. Since the trade war between the United States and China began in 2018, and with the rising geopolitical tensions that have come thereafter, worry now abounds that the last era of golden globalization may have ended in the late 2010s.

A particularly noticeable phenomenon during the wave of globalization from the early 1980s to the late 2010s was China's economic rise, due to domestic factors such as market-oriented reforms, fiscal decentralization, and trade openness. China's rapid integration into the global economy is recognized as an exogenous 'China trade shock' involving a surge in Chinese exports of manufactured goods, particularly to high-income countries, and increased imports of raw materials from natural resource-rich countries. The economic consequences of China's trade shock have been widely studied. Scholars have examined its effects on employment, wages, industrial productivity, and overall trade performance in different countries and regions. In the meantime, concern has grown that China's economic prowess might be gradually transformed into political soft power, and that China and Western countries might compete for political influence in developing countries, especially in Africa. For example, there is widespread speculation that if African countries channel an increasing portion of their natural resource exports to China, this could lead to an institutional 'race to the bottom'.

Against this background, a large proportion of this thesis is devoted to understanding the economic and political consequences of China trade shock in developing countries, as China's establishment as a manufacturing hub has substantially altered global trade patterns. This thesis focuses on the consequences of China's demand for natural resources in the global market, as most developing economies are still heavily reliant on resource exports. The existing literature argues that revenues from exporting natural resources could prompt sectoral adjustments, such as 'Dutch disease', that hinder economic growth in the long run or create a 'voracity effect' that deteriorates institutional quality. This thesis touches upon the political consequences of China's rising trade with African countries, then goes on to examine some of the economic effects of China's trade shock in the raw commodity market in developing countries. Lastly, it attempts to explain variation in inequality across countries by the ownership type of capital.

The first empirical chapter thus investigates the impact of China's rising share in natural resource imports on democratization and corruption in the exporting countries in Africa. Indeed, China' economic engagement with Africa has accelerated since the 1990s. Yet, findings show that participatory democracy and control of corruption have improved as a result of these countries' rising resource exports to China.

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Empirical findings suggest that improvements in corruption control could be attributed to increasing national incomes due to the resource windfalls generated by the growing exports to China. Overall, the empirical analysis provides support for an 'institutional resource blessing' (rather than a 'resource curse') for African countries as a result of natural resource trade with China.

The second and third empirical chapters investigate developing economies' responses to China's demand shock in the raw commodity market under the 'resource curse' and 'Dutch disease' propositions with a shift-share design. Findings indicate that the resource boom brought about by China's skyrocketing demand for raw materials derailed economic growth in developing countries between the early 1990s and early 2010s, as predicted by the 'resource curse' hypothesis. On average, resource revenue booms wiped out 40% of economic growth from 1994 to 2013 in the 100 developing countries in the sample. When the price of raw commodities collapsed around the mid-2010s, due to slowing demand from China, natural resource-rich countries' economic growth was again negatively affected. Empirical findings also confirm heterogeneity between sub-Saharan African (SSA) countries and non-SSA countries. Natural resource-rich countries in SSA grew more slowly than natural resource-poor countries in the region during resource boom periods, while resource windfalls had no significant impact on growth in non-SSA countries.

Following from these empirical findings, and based on the same econometric models, chapter 3 examines sectoral adjustments in the sample of developing countries as a result of China's trade shock in the global primary commodities market. At the aggregate level, the analysis finds that resource booms increased the growth rate of the manufacturing sector but decreased the growth rate of the public sector. Disaggregated industrial-level analyses find piecemeal evidence supporting 'Dutch disease', as output of the textiles industry was negatively affected by resource booms and the average wage in the textiles industry seems to have stagnated, while the average wage increased across a range of other industries. As the textiles industry is regarded as an entry-level traded manufacturing industry in developing countries, these findings suggest that economic activity shifts from the traded sector to the non-traded sector during resource booms.

The fourth empirical chapter tackles the rising trend of economic inequality in the past several decades by examining the distributive effect of different types of capital accumulation. The findings show that a higher proportion of public capital in aggregate capital stock could lower both market and net Gini coefficients. The findings also suggest that greater public capital as a proportion of gross domestic production (GDP) is associated with reduced income inequality, while greater private capital as a proportion of GDP affects income inequality in the opposite direction. More importantly, the negative impact that public capital has on income inequality is most salient and the magnitude of the impact is larger in low- and middle-income countries compared to high-income countries.

Overall, this thesis draws on empirical data to shed light on the consequences of the China trade shock and the causes of rising inequality across countries roughly during the two decades before and after the new millennium. This thesis provides robust evidence of the economic 'resource curse' in developing countries, though its occurrence may hinge on history, geography, and timing. The asymmetric effects of positive price shocks and negative price shocks also suggest that the volatility of commodity prices could be an important culprit in the economic misfortune of natural resource-rich countries. Nevertheless, concerns for an institutional 'race to the bottom' in fragile developing countries when China becomes a

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significant trading partner seem to be unfounded. Indeed, China's imports of natural resources from Africa brought positive changes in terms of democratization and corruption control. This thesis, finally, suggests that public investment could be an effective solution to tackle rising inequality in developing countries.

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