

Routledge-ERIA Studies in Development Economics

GLOBALISATION AND ITS ECONOMIC CONSEQUENCES

LOOKING AT APEC ECONOMIES

Edited by

Shujiro Urata and Ha Thi Thanh Doan



Globalisation and its Economic Consequences

Given the rising criticisms of and growing doubts about globalisation, this timely edited volume looks at globalisation and its economic impact on eight countries in Asia and the Pacific region, namely Australia, China, Indonesia, Japan, Malaysia, Thailand, the United States (US), and Vietnam. The eight selected countries are members of the Asia-Pacific Economic Cooperation (APEC) forum and yet the economies of these member countries have benefited differently from globalisation.

This book summarises findings from existing academic literature in a coherent framework and reviews them critically to provide a balanced analysis. It also identifies the mechanisms through which globalisation impacts economies and explains how understanding of such mechanisms can be useful for formulating policies, which would benefit from globalisation while achieving inclusive economic growth in the context of rising nationalism and protectionism.

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Foreword

The project “Fostering Free Trade and Overcoming its Challenges in ASEAN and East Asia Region” supported by ERIA, was presented at the symposium in Tokyo on 22 and 23 April 2019, organised by the Japan Institute of International Affairs (JIIA). This project treats an issue of current significance, namely the effects of globalisation accelerated by liberalisation and facilitation of trade and investment on the economic structure and society in the Asia-Pacific region, through providing historical analyses and empirical studies. I highly value this project and express my deep respect for the efforts made by the honourable professors led by Professor URATA Shujiro and the JIIA who took part in the project.

As each chapter shows, the globalisation contributes to improving society and economy in various means, which consequently highlights the importance of pursuing liberalisation and facilitation of trade and investment as one of the key enablers of the economic growth. As Japan is keen on supporting the rules-based multilateral trading system and deepening global and regional economic integration, it is determined to continuously work on the eventual realisation of the Free Trade Area of the Asia-Pacific. Its effort has recently seen significant progress including the entering into force of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the successful signing of the Regional Comprehensive Economic Partnership (RCEP) Agreement. Simultaneously, Japan has been taking initiatives in the reform of the WTO as a pressing issue for maintaining and strengthening the multilateral trading system and promoting the stability and predictability of international trade flows.

Through pursuing the globalisation, it is important to recognise that the world today, especially the COVID-19 pandemic reminds us again of the importance of fostering sustainable and inclusive growth. This unprecedented crisis might add to already existing sceptical perspectives against trade liberalisation, influenced by its negative aspects such as job bi-polarisation and wage inequality that are rightly argued in the book. I, therefore, believe that it will become increasingly crucial to discuss various economic policies to realise ‘quality growth that brings palpable benefits and greater health and wellbeing to all, including MSMEs, women and others with untapped economic potential,’ as set out as one of the long-term objectives of our region in the APEC Putrajaya Vision 2040 launched by the APEC Economic Leaders. Japan will continue to work together with partners in

the region to achieve this objective through various international fora such as APEC.

From this perspective, this valuable analytical work will contribute not only to further understanding on the economic aspect of the globalisation but also to being a source of inspiration to potential policies to be taken by the governments in the wake of the crisis. I sincerely hope this book will be referred to by a wide range of readers.

TAJIMA Hiroshi,
APEC Senior Official of Japan,
Ambassador in charge of Economic Diplomacy,
Deputy Assistant Minister, Economic Affairs Bureau,
Ministry of Foreign Affairs of Japan

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This book is based on the findings of the ERIA's research project "Fostering Free Trade and Overcoming Its Challenges in ASEAN and the East Asia Region" (July 2018–May 2019), conducted at the Japan Institute of International Affairs (JIIA). The project, which was led by Professor Shujiro Urata, invited prominent experts from Australia, China, Indonesia, Japan, Malaysia, Thailand, the United States, and Vietnam. In the course of the project, the JIIA held an international symposium in collaboration with the Ministry of Foreign Affairs of Japan on 22–23 April 2019 in Tokyo.

The possible adverse effects of globalization accelerated by rapid technological progress and the movement of people are not limited to the economy but cut across society. Today, we are witnessing spread of populism and anti-globalism around the world. We see an erosion of public trust in politics and weakened social cohesion in many countries. States have become more prone to pursue their self-interest, leading to the rise of protectionism and nationalism. The politics of blame and divisive social norms are seen at the forefront of our daily lives. Multilateral liberal institutions are being threatened and eroded from within and without.

To tackle these problems, there are at least two essential approaches. First, we need to curb adverse effects stemming from rapid structural changes by promoting sustainable and inclusive growth through various policies. These include investment in both human and physical capital. Second, there needs to be a coordinated and integrated policy framework across different entities that involves diverse stakeholders in the policy-making process.

This book provides information and analysis on what contributions free trade has made to improve people's quality of life, especially employment, and what policies are possible to tackle the negative aspects of globalisation using the lessons learnt from the experience of various countries in the Asia-Pacific.

I sincerely thank Professor Shujiro Urata for his leadership in bringing international experts together for this project and for making it possible to publish the project's findings as a book. I am confident that readers will find valuable information and insightful policy proposals that help advance sound globalisation in the Asia-Pacific.

Kenichiro Sasae,
President and Director General,
The Japan Institute of International Affairs (JIIA)

1 Introduction and overview

Shujiro Urata and Ha Thi Thanh Doan

1 Introduction

In 2020, the coronavirus disease (COVID-19) pandemic changed the world so remarkably that few believe a return to the pre-COVID-19 economic and social situation is possible. Since January 2020, when the first COVID-19 infection was officially detected in Wuhan, China, more than 49.0 million cases – including more than 1.2 million deaths – have been reported worldwide as of 7 November 2020. The economic impacts of the COVID-19 pandemic have been devastating; various lockdown and stay-at-home policies, implemented by many countries to deal with the situation, have virtually stopped economic activities for several months. Indeed, the International Monetary Fund (IMF) projected global economic growth rate for 2020 is –4.4%, down from 2.8% for 2019 (IMF, 2020). This marks the worst economic situation since the Great Depression of the 1920 and 1930.

A view has emerged that globalisation, which brought high economic growth before the pandemic, will be reversed. Indeed, governments around the world have intervened in the market to secure sufficient supplies of medical and health products, such as face masks and medical gowns, by restricting exports and by promoting domestic production of these goods, against the recommendations of international organisations such as the World Trade Organization (WTO) and international fora such as the G20. Moreover, it is undeniable that the rapid and sizeable movement of people, which became possible thanks to globalisation, has contributed to the spread of the coronavirus.

Anti-globalisation views did not emerge as a result of the COVID-19 pandemic, however; protectionist movements began to trend after the Global Financial Crisis in 2008 and 2009. The pace and magnitude of protectionism then grew after United States (US) President Donald Trump began to apply such measures mainly by raising import tariff rates. It has been argued that an increasing number of his constituents, such as unemployed workers who did not benefit from globalisation, are supporting this trend.

It has been well-established, however, that globalisation, which had been propelled by the liberalisation of trade and foreign direct investment (FDI) policies as well as technological progress that reduced trade and FDI costs, has

contributed to rapid global economic growth – especially in East Asia, which has grown more rapidly compared to the rest of the world. Protectionism, therefore, could have serious impacts on this region, as important engines of economic growth (i.e. trade and FDI expansion) could be slowed or stopped.

In light of protectionist policies resulting from the growing anti-globalisation sentiment, the Japan Institute of International Affairs (JIIA), with financial assistance from the Economic Research Institute for ASEAN and East Asia (ERIA), conducted a study of the economic consequences of globalisation for eight selected members of the Asia-Pacific Economic Cooperation (APEC) – Australia, China, Indonesia, Japan, Malaysia, Thailand, the US, and Vietnam – in 2018–19. As there are many lessons to be learned from these countries that have experienced globalisation through trade and FDI liberalisation, the study aimed to deepen the understanding of the benefits and costs of globalisation to provide insight for policy makers in formulating foreign economic policy. Today, as many countries are rapidly adopting protectionist policies in response to the COVID-19 pandemic, it is hoped that this study brings about new insights that will help overcome the economic crisis spurred by the pandemic as well as achieve economic growth in the post-pandemic era.

As many studies already exist on this subject, it was decided that this study would collate and analyse important findings and lessons from past literature rather than conduct original research. The authors of each chapter have aimed to draw policy implications from examining past studies, focusing on impacts on productivity, employment, inequality, and innovation.

This chapter is organised as follows. Section 2 presents a brief overview of globalisation, with a focus on the study's sample countries. Section 3 reviews previous studies on the economic impacts of globalisation in the forms of trade and FDI. Section 4 presents major findings from this study, while Section 5 provides policy implications. Section 6 presents a synopsis of each chapter.

2 Economic globalisation: an overview

Several indicators can be used to examine the extent of economic globalisation, a phenomenon in which economic activities, such as trade and investment, are conducted on a global basis to result in active cross-border movement of goods, services, capital, people, and data. The most popular indicators are trade and FDI, because they have been important international economic activities for decades, and data on these activities are generally collected. The international movement of people, labour, capital other than FDI, services, and data are also important activities contributing to globalisation, but they suffer from a lack of reliable data.

Figures 1.1 and 1.2 show the changes in trade–gross domestic product (GDP) and inward FDI stock–GDP ratios for the world and APEC member economies from 1989 (i.e. the year of APEC establishment) to 2018 (i.e. the year for the most up-to-date available at the time of writing). The upward trend of these indicators shows the advancement of globalisation of the world economy and

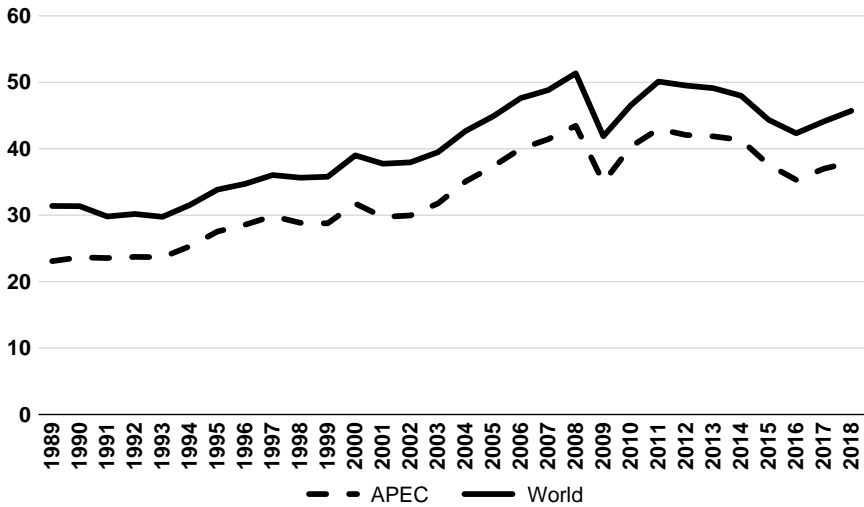


Figure 1.1 Trade–GDP Ratios of Selected APEC Member Countries and the World (%). Source: APEC, *StatsAPEC*, <http://statistics.apec.org/> (accessed 7 November 2020). Note: APEC = Asia-Pacific Economic Cooperation, GDP = gross domestic product.

APEC member economies, because international economic activities indicated by trade and FDI increased faster than domestic economic activities indicated by GDP. Both indicators declined in 2008–09, however, because of the Global Financial Crisis. It should also be pointed out that the trade–GDP ratio did not increase after 2011, with only a slight increase after 2016. This was due to several reasons, including growing protectionism, the reshoring of Chinese production, the global shift in demand away from goods and towards less tradable services, and the possible saturation of the development of global value chains (GVCs) (Rodrik, 2018). Moreover, the level of globalisation for APEC member economies is lower compared to that of the rest of the world, because the three largest economies in the world – China, Japan, and the US – are APEC members and exhibited relatively low levels of globalisation. Generally speaking, dependence on international economic activities is low for large economies, although trade and FDI have made significant contributions to these countries’ economic growth.

In recent decades, there has been an active interaction amongst – and rapid expansion of – different types of international economic activities, especially regarding trade and FDI. A typical pattern of their interaction may be described as follows. Think of a multinational corporation (MNC) that is operating various activities, processes, or tasks in an integrated form in the same location. Faced with a reduction in transport and communication costs, it recognises the benefit of breaking up the operation into various tasks, putting them in different locations through FDI, and linking these production bases by trade in components

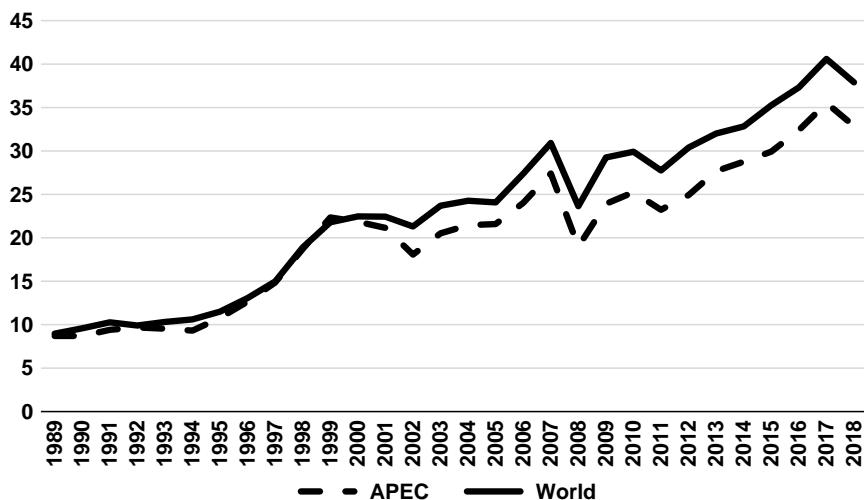


Figure 1.2 Inward FDI Stock–GDP Ratios of Selected APEC Member Countries and the World (%).

Source: APEC, *StatsAPEC*, <http://statistics.apec.org/> (accessed 7 November 2020).

Note: APEC = Asia-Pacific Economic Cooperation, FDI = foreign direct investment, GDP = gross domestic product.

to achieve efficient production systems. Adoption of such a fragmentation strategy leads to the formation of a GVC, promoting trade in components between the affiliates set up by FDI. Indeed, as noted earlier, the rapid economic growth of East Asian economies can be attributed to the remarkable expansion of trade and FDI.¹ Other international economic activities also interact with trade and FDI; for example, a Chinese student in Japan finds a business opportunity in exporting high-quality Japanese products to China, and sets up a trading company. This is a case where movement of people results in FDI and trade.

Several factors have contributed to the rapid expansion of globalisation. One was a sharp reduction in the cost of undertaking trade and FDI.² Many countries – especially developing countries – undertook trade and FDI liberalisation unilaterally during economic difficulty under the pressure of international organisations, such as the IMF and World Bank, to receive financial assistance. Some countries liberalised trade and FDI regimes bilaterally and regionally with like-minded countries in the form of free-trade agreements (FTAs) to promote economic growth. In addition, the members of the General Agreement on Tariffs and Trade (GATT) and WTO carried out trade and FDI liberalisation multilaterally by implementing commitments made under various international agreements. A reduction in trade and FDI costs occurred through decreasing transport and communication costs, which, in turn, resulted from rapid technological progress and deregulation in such services.

Table 1.1 Trade and FDI for Sample Countries

	<i>Exports/GDP</i>		<i>Imports/GDP</i>		<i>Outward FDI Stock/GDP</i>		<i>Inward FDI Stock/GDP</i>	
	1989	2018	1989	2018	1989	2018	1989	2018
Australia	12.4	17.9	15.0	16.4	11.3	34.1	24.0	47.4
China	15.1	18.3	17.0	15.7	0.8	14.3	3.8	12.0
Indonesia	23.5	17.3	17.4	18.1	0.1	6.9	6.4	21.7
Japan	9.0	14.8	6.9	15.1	5.1	33.4	0.3	4.3
Malaysia	64.5	69.0	57.9	60.7	2.5	33.6	20.8	43.0
Thailand	27.8	50.1	35.7	49.1	0.3	24.0	7.4	44.1
US	6.4	8.1	8.7	12.7	14.7	31.4	9.4	36.2
Vietnam	30.9	99.4	40.8	96.6	--	4.4	1.0	59.3
APEC	10.7	18.7	11.3	19.3	10.3	32.2	8.7	32.9
World	15.4	22.7	16.0	23.1	--	36.7	9.0	37.9

Note: APEC = Asia-Pacific Economic Cooperation, FDI = foreign direct investment, GDP = gross domestic product, US = United States. Source: APEC, *StatsAPEC*, <http://statistics.apec.org/> (accessed 7 November 2020).

Most countries saw the acceleration of globalisation in the forms of trade and FDI, as trade–GDP and FDI stock–GDP ratios increased from 1989 to 2018 (Table 1.1). Two exceptions are Indonesia in its export–GDP ratio and China in its import–GDP ratio. Indonesia’s export–GDP ratio fell due to the declining value of oil exports, partly due to a drop in oil prices. In China, the import–GDP ratio did increase from 17.0% in 1989 to 28.9% in 2005 but then declined to 15.7% in 2018, due to a shift in the country’s development strategy from an outward to an inward orientation, reflecting the government’s attempt to reduce external dependence. Trade friction with the US also caused a substantial decline in imports from that country. It must be noted, however, that the presence of foreign companies increased in China from 1989 to 2018, indicating their growing importance in China’s economic activities. Based on these findings, it is not clear if external dependence declined for the Chinese economy.

The extent of globalisation widely varies amongst the eight countries examined in this study. The degree of globalisation is high in Malaysia, Thailand, and Vietnam; amongst these three countries, all of which are ASEAN members, Vietnam globalised its economic activities at a remarkably high rate, transforming its economic system from a centrally planned to a market economy. However, Australia, China, Indonesia, Japan, and the US show low trade ratios, mainly because of their large economic size.

The patterns are different for FDI stock–GDP ratios. All eight countries, except Indonesia and Vietnam, increased outward FDI stock–GDP ratios, indicating that firms in these countries were active in expanding their operations in foreign countries, also reflecting that the number of successful firms with capable management increased in these countries. Regarding the inward FDI stock–GDP ratio, China and Japan are exceptions with low ratios – despite an increase in

these ratios. As noted earlier, adaptation of an inward-oriented development strategy may be behind China's low ratio; for Japan, multiple factors, including high wages and office rental costs, have discouraged FDI by foreign companies there, despite the fact that the government has been eager to promote inward FDI.

3 Economic impacts of globalisation: a brief literature review

This section reviews previous studies on the economic impacts of globalisation. It is divided into two sections: economic growth, and unemployment and inequality. Within the discussion of the impacts of globalisation on economic growth, trade and FDI are examined separately.

3.1 *Economic growth*

3.1.1 *Trade*

Expansion of trade can contribute to economic growth by improving resource allocation, known as the resource allocation effect, which may be realised at the sector and firm levels. At the sector level, foreign trade leads to a shift of resources, such as labour and capital, from low-productivity sectors (i.e. those with a comparative disadvantage) to high-productivity sectors (i.e. those with a comparative advantage), resulting in improved use of resources (Alessandrini et al., 2011; McCaig and Pavcnik, 2018). At the firm level, trade-induced competition forces low-productive firms to contract or to exit from the market, reshuffling resources to more productive ones (Pavcnik, 2002; Ha and Kiyota, 2014). For a multi-product firm, trade can also trigger resource reallocation within the firm through adjustment of product structure (Goldberg et al., 2010; Bernard, Redding, and Schott, 2011; Lopresti, 2016).

An expansion of trade, both exports and imports, is also likely to improve the productivity of the countries involved. Exporting firms are shown to have higher productivity compared to domestic firms (Melitz, 2003). Exporting requires firms to overcome various barriers or fixed costs, such as obtaining market information and setting up distribution channels, which may be overcome by high-productivity firms (i.e. a self-selection effect). In addition, exporting firms improve productivity if they acquire technical and managerial knowledge by being exposed to foreign markets and competition (i.e. a learning-by-exporting effect). A similar argument on a productivity-enhancing export effect has been made; exporting enables firms to exploit a benefit-of-scale effect, as exporting leads to expanded production (i.e. a scale effect).

Empirical evidence supports these predictions. For example, Bernard and Jensen (1999) found robust evidence of a self-selection effect for US exporters, although the learning impact was less clear. Alvarez and Lopez (2005) found supporting evidence for both self-selection and learning-by-exporting hypotheses

amongst Chilean firms. Using data from Slovenia, De Loecker (2013) showed substantial productivity gains associated with export entry, ranging up to 7.35%. Kim (2000) found that trade liberalisation improved productivity performance, increased competition, and promoted scale efficiency in Korean manufacturing industries.

Increased imports can contribute to the improved productivity of importing and import-competing firms. For importing firms, an increase in imported intermediate goods may improve their productivity, because this enables them to use high-quality intermediate goods (i.e. a high-quality import input effect), especially in developing countries. This effect was observed by Amiti and Konings (2007), who showed that input tariff reduction increased productivity in Indonesia.

An increase in final good imports can lead to improved productivity of import-competing domestic firms, as they face greater competitive pressure from increased imports (i.e. the import-discipline effect). Increased imports may force out inefficient domestic firms, which cannot compete against increased imports. The exit of inefficient firms from the market is, of course, undesirable from the exiting firm's point of view, but it leads to improved productivity for the industry and economy. The negative impacts of increased imports on importing countries can occur through declining employment and incomes. Two studies, de Melo and Urata (1986) and Levinsohn (1993), found support for the import-discipline hypothesis in Chile and Turkey, respectively.³

Although the role of innovation in promoting productivity is implicitly assumed in the discussions of the impacts of trade on productivity, some studies have emphasised the importance of a trade–innovation link for promoting productivity. Specifically, a firm may acquire technological knowledge through its international contacts and demand–supply links with foreign firms through trade. In addition to opportunities to learn from foreign firms, a firm exposed to foreign competition through trade faces competitive pressure, providing an incentive to carry out innovation. Damijan and Kostevc (2015) found that firms, learning from both imports and exports, innovated in Spain. Furthermore, they found a sequence in the relationship between trade and innovation to follow from imports to innovation to exports.

3.1.2 Foreign direct investment

FDI is shown to have different impacts on investing (i.e. home) countries and receiving (i.e. host) countries in a simple static theory. In the home country, the amount of capital declines, leading to a drop in output, while in the host country, the opposite situation arises, leading to economic growth. The host country can achieve additional economic growth if technology is transferred from foreign investors or MNCs to the host country.

For a host country of FDI, successful technology transfer from MNCs is key to achieving economic growth. Technology transfer takes place in two steps: (i)

intra-firm technology transfer, where technology is transferred from MNCs to their foreign affiliates in the host country by on-the-job training and the exchange of workers between the parent office and affiliates; and (ii) inter-firm or technology spillover, where technology is transferred from foreign affiliates to domestic firms through the business environment, such as sales and procurement. Domestic firms may also obtain technology by hiring workers who used to work for foreign affiliates.

Horizontal technology spillover takes place within the same industry, while vertical technology spillover takes place between different sectors. Vertical technology spillover is further divided into backward and forward technology spillover, depending on the nature of inter-industry relationships. Backward technology spillover takes place through procurement of intermediate goods from the procurer (i.e. buyer) to the supplier, while forward technology spillover occurs from the supplier to the buyer. The success or failure of technology acquisition by domestic firms largely depends on their absorptive capability. Specifically, domestic firms can successfully acquire technology if they have capable workers and conducive environments for adopting new technology.

Early empirical studies of the impacts of FDI on economic growth have been conducted using country- and sector-level analyses. Many studies found positive impacts of FDI on economic growth. By analysing 124 cross-country data sets for 1971–2010, Iamsiraroj (2016) found that FDI and economic growth positively affect each other. Several studies also found that FDI contributes to the economic growth of FDI-receiving countries when certain conditions, such as the availability of human resources and openness in trade, are satisfied (Borensztein, De Gregorio, and Lee, 1998; Balasubramanyam, Salisu, and Sapsford, 1996). Unfortunately, country- and sector-level studies did not explicitly consider technology transfer in their analyses of the impacts of FDI on economic growth.

Few studies have been conducted on intra-firm technology transfer, although several exist on inter-firm technology transfer. Some studies also did not distinguish between these two types of technology transfer. Urata and Kawai (2000) studied intra-firm technology transfer using data on parent firms and foreign affiliates of Japanese firms. They found that, on average, approximately 89% of technology was transferred from parent firms to their foreign affiliates, and that absorptive capability was most important for obtaining technology.

Regarding technology spillover, empirical findings showed positive, neutral, and negative effects. According to Rojec and Knell (2018), in a comprehensive survey of the literature on technology spillover, this lack of a consensus is due to a variety of reasons. They pointed out possible problems in the empirical studies, which include inappropriate methodology and lack of adequate data. They found greater similarity in the results from the studies; backward vertical technology spillover was found in many but not horizontal or forward vertical technology spillovers.

As discussed above, outward FDI may have a negative impact on economic growth of the home country as capital moves out. However, outward FDI may

contribute to economic growth of the home country, particularly in the medium to long term, if outward FDI improves the productivity of FDI firms or MNCs. Possible reasons for productivity improvement for MNCs are similar to those discussed for exporting, such as acquiring technology and management know-how from recipient countries. This impact is significant, particularly when outward FDI takes the form of acquisition of foreign companies owning high-quality technology.

Empirical analyses of the impacts of outward FDI on MNCs and home countries showed mixed results.⁴ Based on the literature survey, Hayakawa, Kimura, and Machikita (2010) argued that such results can be attributed to the differences in the types of outward FDI, which were not considered in many studies. When classifying outward FDI into vertical and horizontal types, previous studies only found a positive impact on the productivity of vertical FDI. Vertical FDI is undertaken to seek efficiency, while horizontal FDI captures the market. These differences in motives or mechanisms can lead to different impacts.

3.2 Unemployment and inequality

Globalisation is often accused of creating unemployment and increasing inequality within countries. It has been argued that the inflow of imports that are in competition with domestic production replaces domestic production, which, in turn, leads to reduced employment. Moreover, outward FDI relocates production from the home country to a host (i.e. foreign) country, leading to reduced employment in the home country. These reasonings rest on the validity of certain assumptions, however, such as the perfect substitutability between imports or foreign production and domestic production.

Many empirical studies have examined the impacts of increased imports on unemployment. Autor, Dorn, and Hanson (2013) studied the impacts of increased imports from China on US employment (i.e. ‘the China shock’). By considering not only the direct effect but also the indirect effect through input–output links, Acemoglu et al. (2016) found that import growth from China between 1999 and 2011 reduced the employment of 2.4 million US workers.⁵ Similarly, Hayakawa, Ito, and Urata (2019) examined the impacts of increased Chinese imports on Japan’s labour market, finding that these imports had a negative impact on total employment, especially for industries that produced competing products, as well as a positive impact on industries that purchased Chinese imports as intermediate inputs.

Studies on the impacts of outward FDI on home employment exhibited mixed results. In one on US manufacturing firms, Harrison and McMillan (2011) showed how the motive of outward FDI and its location affected the impact of FDI on parent firms’ employment. Overseas operation in low-wage countries substituted for home employment, but overseas operation conducting different tasks from parent firms complemented home employment. They showed the net effect of FDI to only be a small decline in employment at home.⁶ Moreover, several studies on Japanese manufacturing firms, such as those by Ando and

Kimura (2015) and Kodama and Inui (2015), did not find negative impacts of outward FDI or foreign operations on employment in Japan. Indeed, many studies found positive impacts of outward FDI on home employment, particularly for MNCs that expanded their overseas operations.

Many studies have also been conducted on globalisation and inequality.⁷ An important theoretical explanation of the impacts of globalisation on income distribution is based on the Stolper-Samuelson Theorem within the Heckscher-Ohlin trade model. According to the Stolper-Samuelson Theorem, globalisation expands the production and exports of abundant factor-intensive products while reducing the production of scarce factor-intensive products by increasing imports of scarce factor-intensive products. Consequently, trade liberalisation leads to an increase in the price of abundant factors relative to the price of scarce factors. Assuming that skilled and unskilled labour exist and that developing (developed) countries are relatively well endowed with unskilled (skilled) labour, an application of this theorem indicates that an increase in trade by trade liberalisation leads to an improvement (deterioration) in income distribution or a narrowing (widening) of the wage gap between unskilled and skilled labour in developing (developed) countries.

A survey of empirical studies on the impacts of trade on inequality by Urata and Narjoko (2017) found that country and cross-country studies, conducted on the relationship between trade and income distribution, showed different patterns. Some country-level studies showed that an increase in trade-GDP ratios worsened inequality, while others did not detect significant impacts of trade on income distribution. Yet cross-country studies found that trade improved income distribution, although the impacts were small. These mixed results indicate the need for more analyses.

The impacts of FDI from developed to developing countries on income inequality are basically the same if FDI promotes trade. However, income inequality may deteriorate even in developing countries if the demand for high-skilled workers increases, because MNCs hire high-skilled workers to adopt to high-skilled worker-intensive management styles, for which they have an advantage. Few rigorous studies have been conducted on this issue, but Jaumotte, Lall, and Parageorgiou (2013) found an inequality-deteriorating effect of inward FDI in a cross-country econometric analysis.

Many empirical studies found that technological progress has negative impacts on income inequality as well. Specifically, Jaumotte, Lall, and Parageorgiou (2013) found that the introduction of skill-biased technologies, or labour-saving technologies, contributed to worsening income inequality. Having noted the negative impact of technological progress on income distribution, a bidirectional relationship between technological progress on one hand and trade and investment on the other should also be noted. For example, an exporting firm facing intensive competition in foreign markets will conduct research and development to create new technologies to improve competitiveness. Recognition of this point shows the difficulty in separating the impacts of trade and FDI as well as technological progress.