

GLOBAL INEQUALITY ON THE RISE

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DIRECTOR'S MESSAGE



this May brought together experts from Hong Kong, China and Russia who discussed the opportunities and challenges that this initiative presents for China and other emerging markets. In an accompanying workshop, academic researchers presented their analysis of specific BRI projects in Indonesia, Pakistan, Russia, Kazakhstan, Ethiopia and Kenya.

Also in May, we co-hosted the first IZA / World Bank / Network for Jobs and Development (NJD) Conference on Jobs and Development in Bogota, Colombia. We also co-organized the 5th Annual Meeting of the International Consortium of China Studies at HKUST campus. In Spring 2018 we organized a full schedule of academic and business seminars on topics such as trade policy and US-Asian trade relations, highlights from World Inequality Report 2018, financing responses to rural road connectivity and moral incentives for debt repayment. The Institute also awarded 6 competitive research grants and welcomed 6 new Faculty Associates.

China's Belt and Road Initiative (BRI) will connect China and over 60 countries along the old Silk Road's land and maritime routes, and will be the main platform for China's global integration efforts in the foreseeable future. With the support of the HKSAR Central Policy Unit's Strategic Public Policy Research Funding Scheme, HKUST IEMS is carrying out a multi-year research program on the BRI. Our panel discussions titled "The Belt and Road: From Vision to Reality"

This Fall, we are looking forward to hosting the launch of the 2019 World Development Report. The report studies how the nature of work is changing as a result of advances in technology. We will also be continuing our Emerging Market Insights Series with a discussion on the Belt and Road Initiative, jointly hosted with EY Hong Kong and EY China. We will also host several academic seminars on topics ranging from enforcing regulation under illicit adaptation based on a study looking at over-fishing of the critically endangered Pacific hake, to industry relatedness and comparative advantage in China. We hope you will participate in these events and contribute to the exchange of ideas that makes the IEMS what it is. We look forward to seeing you there!

ROADS AND LOANS

One of the basic tenets of finance is that capital flows to its most productive use. Does financial capital move to areas with greater productive opportunities even in emerging economies? **Abhiroop Mukherjee** (HKUST) and coauthors have examined this question in the context of a rural road expansion program in India.

A growing literature argues that infrastructure projects can unlock large productivity gains. For example, infrastructural improvements allow business growth, emigration of surplus labor to better economic opportunities, and transitions from subsistence farming to profitable cash crops. However, these mechanisms can only work if they are funded through financial investments.

Mukherjee and coauthors ask this first-order question: Does financing respond to changing productive opportunities created by infrastructure projects? They exploit the institutional features of a major public road construction program in India, the Pradhan Mantri Gram Sadak Yojna (PMGSY) that generated plausibly exogenous variation in the probability that two otherwise-identical villages would receive a new road. They find that a private bank was more likely to give out loans in villages that became connected, than in otherwise-identical villages that did not receive a new road. What is more, there is no evidence that the roads had distributionally-adverse consequences: the bank was disproportionately likely to lend to village residents with low education and low levels of wealth. These findings provide an important piece of the explanation for how infrastructure projects promote growth and reduce inequality.



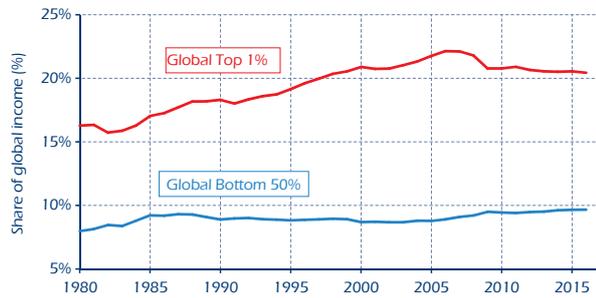
Academic Seminar, "Roads and Loans"
2018.03.07

More about this seminar here:
<http://iems.ust.hk/roads>



RIISING INEQUALITY IN CHINA AND GLOBALLY

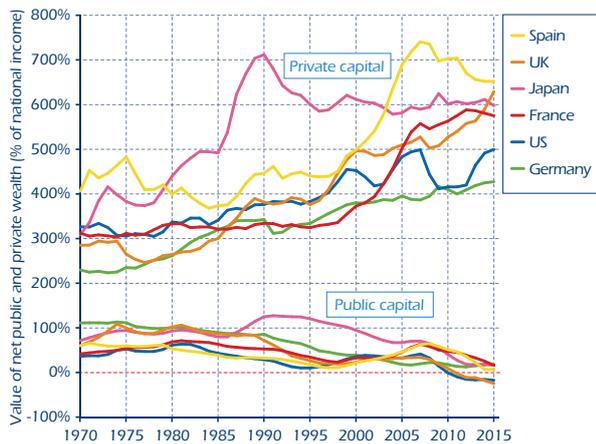
The rise of the global top 1% versus the stagnation of the global bottom 50%, 1980-2016



Source: WID.world (2017). See wir2018.wid.world for data series and notes.

In 2016, 20% of global income was received by the Top 1% against 10% for the Bottom 50%. In 1980, 16% of global income was received by the Top 1% against 8% for the Bottom 50%.

The rise of private capital and the fall of public capital in rich countries, 1970-2016



Source: WID.world (2017). See wir2018.wid.world for data series and notes.

In 2015, the value of net public wealth (or public capital) in the US was negative (-17% of net national income) while the value of net private wealth (or private capital) was 500% of national income. In 1970, net public wealth amounted to 36% of national income while the figure was 326% for net private wealth. Net private wealth is equal to new private assets minus net private debt. Net public wealth is equal to public assets minus public debt.

Despite strong growth in emerging countries, global income inequality between individuals has increased sharply since 1980. The World Inequality Report 2018 argues that this trend is likely to continue into the foreseeable future.

Coauthors of the report, **Lucas Chancel** and **Yang Li** (Paris School of Economics) presented the key findings from the report at an HKUST academic seminar co-hosted by the Division of Social Science and the French Centre for Research on Contemporary China (CEFC). They argued that trends in global inequality depend on the relative strength of convergence forces, such as the rapid economic growth in emerging economies, and divergence forces, such as increasing inequality within countries. The latter has clearly dominated in the recent past. Between 1980 and 2015, the top 1% of the world's individuals with the high incomes, captured two times the increase in global incomes as the bottom 50% did. Wealth-to-income ratios have also risen since the 1980s, possibly due to large transfers of wealth from public to private owners in emerging and rich countries. While national wealth has increased substantially, public wealth is now negative or close to zero in rich countries such as France, Germany, Spain, Japan, UK and US. Arguably, this limits the ability of governments to tackle inequality.

Inequality has risen both in China and in India. However, perhaps due to China's greater investments in education, health and infrastructure, the increase in Chinese inequality has been more moderate. This serves to highlight a key point, namely that government policy plays an important role in determining inequality. The report argues that the Continental European policy and institutional context favors lower- and middle-income groups, which has helped this region contain inequality. It projects that if all countries adopt a European inequality pathway by implementing progressive taxation, a transparent global financial registry and equal access to education and well-paying jobs, they could lower global inequality by 2050.

Academic Seminar co-hosted by the French Centre for Research on Contemporary China (CEFC), "Rising Inequality in China and Globally - Highlights from World Inequality Report 2018" 2018.02.02

Access the report here:
<http://iems.ust.hk/inequality>



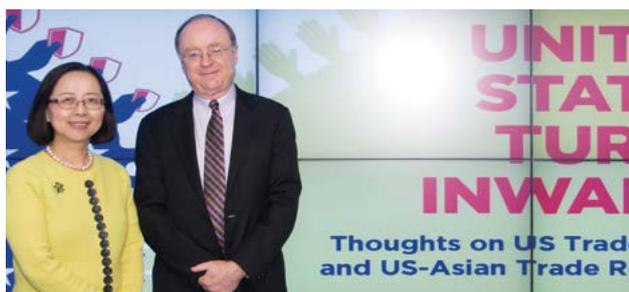
Watch Lucas Chancel's video interview. "Highlights from the World Inequality Report 2018"



Watch Yang Li's video interview. "Rising Inequality in China and Globally"



THE UNITED STATES TURNS INWARD



Reflecting current trends of growing trade skepticism and nationalism, the Trump Administration has been raising American trade barriers. The actions began with US's withdrawal from the Trans-Pacific Partnership (TPP), continued threats to the North American Free Trade Agreement (NAFTA) and the US-Korean Free Trade Agreement (FTA), and now the tariffs on steel and on \$200 billion worth of Chinese imports. **Keith Maskus** (University of Colorado and former Chief Economist at the U.S. Department of State) gave a topical IEMS & IPP – EY Emerging Market Insights lecture on the causes and consequences of these actions for the Asia-Pacific region.

Maskus explored the popular argument that this anti-trade sentiment in the US reflects a growing discontentment with globalization. Between 1979 to 2010, the US has lost 8 million manufacturing jobs, mainly due to technological change, the Great Recession and import competition. He explained that there is a tendency to ascribe these problems to offshoring, the emergence of production networks, and the growing volume of imports from China. This narrative is further fueled by the growth of the US trade deficit, two-thirds of which is the trade deficit with China.

In Maskus' view, the Trump Administration's approach to trade revolves around 6 "America first" pillars that are founded in ideology rather than analysis. These are: the belief that national security interests take precedence over trade relations, that competition for technological leadership is about national security and future market shares in leading industries, that American manufacturing and mining workers have paid too much of the burden of globalization and need protection, that trade agreements and the multilateral system place too many constraints on US policymaking and not enough on countries that do not follow the rules, that the rule-based approaches of past administrations were ineffective at changing behavior, that confrontation and uncertainty will achieve better results and finally that the US can benefit more from bilateral trade agreements than from regional deals. Maskus cast doubt on the claim that temporary trade protection will help industries deal with long-term structural problems. Instead, he recommended that the US put in place programs of skill development, training and trade adjustment. He urged the US government to cooperate with other major economies with similar concerns, rather than linking trade policy with international relations. In particular, he argued that China and the United States need a strong and sustainable bilateral economic relationship so that they can become reliable economic partners for the rest of Asia.

IEMS & IPP – EY Emerging Market Insights Series, "The United States Turns Inward: Thoughts on US Trade Policy and US-Asian Trade Relations" 2018.04.20

Watch the presentation here:
<http://iems.ust.hk/insights>



TARGETING OF LOCAL GOVERNMENT PROGRAMS AND VOTING PATTERNS IN INDIA

In the 1990s, India restructured its governance architecture to create directly elected local government institutions. These local governments administer programs of poverty alleviation, economic security, rural infrastructure and agricultural subsidies. It was hoped that these reforms would increase transparency and create greater accountability, in turn improving program targeting and reducing waste and corruption. To what extent have these goals been realized? Have these reforms instead had unforeseen consequences? **Dilip Mookherjee's** (Boston University) academic seminar examined whether electoral competition affected how resources were allocated across local governments, and how this affected voter behavior. Mookherjee and coauthors also used data from a straw poll conducted with households from 89 villages in West Bengal to examine how citizens' votes were affected by the receipt of benefits from local governments.

They found that higher levels of government responded to political competition by manipulating resources to local village governments, which in turn affected the benefits that citizens received. Voters responded to the delivery of benefits in a manner that accords with the phenomenon of "political clientelism", i.e. the idea that politicians may strategically give out benefits so as to maximize their re-election chances. Personalized help and short-term benefits generated more votes for the party in power than



did infrastructural improvements or more substantial one-time benefits, such as receiving a land title or having a tenancy contract registered. Voter responses were also stronger when incumbents were more likely to be re-elected. Mookherjee argued that such clientelism can shift local government allocation from long-run investments in local public goods, to short-run private goods and services, creating adverse impacts on rural development.

Academic Seminar, "Targeting of Local Government Programs and Voting Patterns in West Bengal, India" 2018.04.12

More about this seminar here:
<http://iems.ust.hk/voting>



WHAT TO BUY WHEN THE AMERICAN DREAM FAILS



Although marketing professionals routinely explain and predict consumers' behaviors on the basis of their socio-economic status, we know little about the shopping preferences of individuals transitioning from one socioeconomic status to another. IEMS Post-doctoral Fellow, **Wei-Fen Chen** gave an academic seminar on how consumers' tastes are influenced by their experiences of socio-economic mobility. Using data collected from interviews and experiments with upwardly and downwardly mobile young consumers, Chen and coauthors examine the causal relationship between social mobility mindsets and shopping preferences.

Participants were shown advertisements of products that either appealed to their economic capital (such as money, assets, and fortune) or to their cultural capital (such as socially rare and distinctive tastes, involvement in art, music and literature).

Their results suggest that consumer responses to the perception of upward and downward mobility are asymmetric. Whereas upwardly mobile individuals were equally likely to purchase products with economic and cultural capital appeal, downwardly mobile customers appeared to prefer products with a cultural capital appeal. This suggests that these customers cope with their loss of economic capital by shifting focus to high-culture consumption instead.

Chen concluded that consumer behaviors are affected not only by the likelihood of economic mobility, but also by the trajectory of social mobility. This can explain why consumers with different social mobility experiences or expectations may shop differently even if they appear to be in the same economic bracket.

Academic Seminar co-organized with the Department of Finance, "What to buy when the American Dream fails?" 2018.04.26
Watch the presentation here:
<http://iems.ust.hk/chen>



MORAL INCENTIVES IN DEBT REPAYMENT

The ability to enforce debt contracts is a pillar of any financial system. What are the forces that cause borrowers to repay their loans? **Martin Kanz** (World Bank) gave an academic seminar about his research examining the role of moral considerations in debt repayment decisions in Indonesia.

Islamic banking is a large and rapidly growing industry not just in Indonesia, but also around the world. Kanz and coauthors used this setting to conduct a series of field experiments aimed at varying the salience of the moral obligation to repay, in the minds of credit card customers. In the main treatment condition of the experiment, late-paying customers received a text message on their phone that quoted the Shahih-al-Bukhari, one of the main religious texts of Sunni Islam, to invoke the Islamic commandment that it is a borrower's moral obligation to repay his/her debt. The authors find that this appeal increased debt repayment. They argue that in fact, moral appeals are more effective than substantial monetary incentives to repay. Their results survive even when any religious connotation is removed and the message simply states that non-repayment of debts violates a moral norm, suggesting that moral appeals may also be effective in contexts where religiosity is less pronounced.

These findings are consistent with the idea that even in financial decisions, people experience a cost when they consciously violate

a moral norm. Accordingly, they suggest that the study of moral incentives in other financial decision making is an interesting avenue for future research.



Academic Seminar, "Moral Incentives in Debt Repayment" 2018.03.02
Find out more at:
<http://iems.ust.hk/kanz>



THE BELT AND ROAD FROM VISION TO REALITY



China's Belt and Road Initiative intends to increase connectivity between China and over 60 countries along the old Silk Road's land and maritime routes, and will be the main platform for China's global integration efforts in the foreseeable future. Often referred to as "the most significant and far-reaching initiative that China has ever put forward", the Belt and Road Initiative (BRI) will play a transformative role in the future development of China and much of the world.

In May, the HKUST IEMS organized a panel discussion titled "The Belt and Road: From Vision to Reality" at the HKUST Business School Central campus. The event brought together a panel of experts to share evidence-based thought leadership on the opportunities, challenges and implications of this Initiative for China and other emerging markets. HKUST IEMS Director, **Albert Park**, placed a spotlight on Indonesia. He reported that by providing a platform for high level meetings between Chinese and Indonesian officials, the BRI has paved the way for a surge in Chinese outbound foreign direct investment (FDI) and trade in the region.

HKUST IEMS Faculty Associate, **Naubahar Sharif** looked closely at how the Chinese government has approached investments and infrastructure in Pakistan. He traced the China-Pakistan collaboration on the BRI back to a long history of diplomatic and trade relations and argued that maintaining close relations with China is a central part of Pakistan's foreign policy. The China-Pakistan Economic Corridor (CPEC), as the BRI is referred to in Pakistan, is a road linking the Chinese border to Pakistan's deep water ports on the Arabian Sea. It seeks to leverage Pakistan's

strategic location and create a short trade route between China and its markets in Asia, Europe and the Middle East.

However, the CPEC has its detractors as well. Sharif cited local concerns that the CPEC may displace locals from their jobs, resistance from Pakistani industry leaders wary of Chinese competition, the fear of economic subservience, environmental degradation and adverse effects on inequality in Pakistan.

Alexey Kalinin, Director of SKOLKOVO Institute for Emerging Market Studies, reported on the BRI from the perspective of the Eurasian Heartland. He reported that nearly half of the Chinese investment in Eurasia between 2011 and 2017 was directed to Russia and Kazakhstan, mostly in the mineral resources and energy sectors. He argued that China hopes to become a leader in the development of energy industries in the region.

Research presented at this panel discussion was funded by the Strategic Public Policy Research Funding Scheme administered by the Hong Kong Special Administrative Region Government's Central Policy Unit.

Panel discussion, "The Belt and Road: From Vision to Reality" 2018.05.17
More about this event:
<http://iems.ust.hk/reality>



STATE ABSENTEEISM IN INDIA'S REVERSE MIGRATION?



Return migration is not a new phenomenon; however, it has recently become a perceptible trend. In emerging economies like China and India, more and more migrants across skill levels are returning home. **Alwyn Didar Singh**, (Former Secretary General, Federation of Indian Chambers of Commerce and Industry) and IEMS Faculty Associate, **David Zweig** compared and contrasted the reverse migration experiences of these two countries.

They argued that much of the difference in experiences is policy-induced: whereas the Chinese government has specifically incentivized the return of high-skill individuals, the Indian state has been relatively laissez-faire. Perhaps coincidentally, in their 2016-17 interviews, Indian returnee entrepreneurs were more likely to report that they returned in order to give back to the country,

whereas the Chinese were more likely to cite the government programs that facilitated their return. Singh argued that while the Indian policy view has shifted over the years to become more favorable to the Indian Diaspora, policies to attract return talent have tended to largely remain on the books, with limited effort at local implementation. He emphasized that India could learn from China's experience and institute targeted measures aimed at easing bureaucratic procedures, streamlining regulations, increasing administrative transparency and providing training and information about markets opportunities, the range of available financing and up-to-date legal and regulatory advice. These measures would promote entrepreneurship more generally, and would also facilitate the return and effective reintegration of emigrants and drive innovation.

Academic Seminar, "State Absenteeism in India's Reverse Migration? A Comparison with the Chinese Experience" 2018.04.09
More about this seminar here:
<http://iems.ust.hk/singh>



FIRST IZA / WORLD BANK / NJD CONFERENCE ON JOBS AND DEVELOPMENT



How should we address a world that is increasingly becoming unequal? Speaking at the Jobs and Development Conference 2018, **Michał Rutkowski** (World Bank) argued for an integrated set of policies that places people and jobs at the center stage and fosters inclusive growth. This event, co-organized by the IZA Institute of Labor Economics, the World Bank Jobs Group and the Network on Jobs and Development, and held at Bogota's Pontificia Universidad Javeriana, brought together 80 researchers from 25 different countries. Participants presented and discussed the latest policy-relevant research on jobs challenges around the world.

Daniel Hamermesh (IZA) gave a provocative lecture titled "Labor(ing) in Development Economics" where he lamented a current movement in labor and development economics, namely, to write empirical papers with little or no theoretical arguments. Using data he collected from various high-ranking economics journals, he showed how this trend has taken over the profession in the last 60 years. He argued that theoretical predictions from first principles play a significant role in the accretion of knowledge and that it is time to go back to taking economic theory seriously and investigate mechanisms. In an HKUST IEMS Special Session on Technology and Jobs in Asia, **Sameer Khatiwada** and **Elisabetta Gentile** (Asian Development Bank or ADB) presented findings

from 2018 ADB's flagship report titled "How Technology Affects Jobs". Despite growing concerns that emerging technologies such as robotics, three-dimensional printing and artificial intelligence will displace jobs, the report argues that new technologies generate more jobs, drive higher productivity, and create the foundation for better-paid jobs and economic growth. However, these new jobs may require skills the current worker does not possess. For this reason, governments should respond to this challenge by coordinating action on skills development, labor regulation, social protection, and income redistribution.

The IZA / World Bank / NJD Jobs and Development Conference 2018 followed the successful 2016 conference organized by the Network on Jobs and Development (NJD), a World Bank initiative supporting research on the global jobs agenda.

First IZA / World Bank / NJD Conference on Jobs and Development 2018.05.11-12
Find out more at:
<http://iems.ust.hk/jobs4dev>



Also in Spring/Summer 2018

Juanyi Jenny Xu (HKUST) gave an academic seminar examining how and why the co-movement of real exchange rates and other macroeconomic aggregates differs between emerging economies and developed small open economies.

More about Xu's seminar here:
<http://iems.ust.hk/realex>



HKUST IEMS co-sponsored the 4th Asian Population Association (APA) Conference at Shanghai University. IEMS Faculty Associate, Stuart Gietel-Basten, explored the relationship between age and voting propensity in various East Asian regions. He used the Asia Barometer Survey to identify whether there is an age gradient, and projected voter turnout rates up to 2050.

Find out more here:
<http://iems.ust.hk/apa>



Keith Maskus (University of Colorado) gave a joint IEMS-ECON academic seminar on how intellectual property rights (IPRs) and international agreements affect the composition of trade. Consistent with predicted relationships from previous research on IPRs and trade, his empirical work shows that rigorous IPR protection significantly impacts the composition of world trade with the US and the European Union.

Watch Maskus' seminar here:
<http://iems.ust.hk/maskus>



HKUST IEMS co-hosted the 5th Annual Meeting of the International Consortium of China Studies entitled "China's Developmental Challenges and Opportunities after the 19th Party Congress". Researchers presented on a range of topics from city-town relations in China to transformations of the state owned economy for China's technological "Great Leap".

Find out more about the consortium here:
<http://iems.ust.hk/iCCS>



New Faculty Associates

The Institute welcomes the following new Faculty Associates effective 1 June 2018



Yatang Lin
(Economics)



Wooyoung Lim
(Economics)



Kai Li
(Finance)



Yanzhen Chen
(Information Systems, Business Statistics and Operations Management)



Melody Chao
(Management)



Kim-Pong Tam
(Social Science)



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