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The Distributional Effects of Capital Account Liberalization

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Abstract

Episodes of account liberalization increase the Gini measure of inequality, based on panel data estimates for 149 countries from 1970 to 2010. These episodes are also associated with a persistent increase in the share of income going to the top. We investigate three channels through which these impacts could occur. First, the impact of liberalization on inequality is stronger where credit markets lack depth and financial inclusion is low; positive impacts of liberalization on poverty rates also vanish when financial inclusion is low. Second, the impact on inequality is also stronger when liberalization is followed by a financial crisis. Third, liberalization seems to alter the relative bargaining power of firms and workers: the labor share of income falls in the aftermath of capital account liberalization.

JEL Classification Numbers: F13, G32, O11.

Keywords: Globalization, Inequality, Capital Account Openness, Crises, Institutions.

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