Trade Relations and Income Distribution in Developing Countries

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Abstract. International trade can play an important role in driving economic growth. Trade can cause a shift in jobs from less competitive sectors to more competitive sectors, which can impact distribution. The method used to complete this assignment is the Systematic Literature Review (SLR) method which can be used by formulating questions clearly, explicitly, and systematically to identify, select, and critically assess relevant research. Wage Inequality and International Trade's Effect on It According to Fabian Trottner (2022), wage inequality results from unequal income distribution. The Effect of Exchange Progression and Compensation Imbalance As indicated by Wolfgang Lechtaler and Mariya Mileva, the Effect of Globalization on Pay Disparity As per Daniel Auguste (2021), The Effect of Globalization on Pay Imbalance As per Elhanan Helpman (2016), The Effect of Exchange Advancement on Pay Imbalance As per Xiaofeng Penny Li (2015). The aftereffects of observational exploration show that the connection among exchange and pay distribution in developed countries is that international trade causes unequal income distribution in the form of wage inequality. It happens because large companies that have a more professional workforce are more productive than companies that do not have a skilled workforce.

Keywords: Digital Economy, MSMEs, Economic Growth

1 Introduction

The connection between trade and the distribution of income in Developing Countries can vary widely depending on economic policy, industrial structure, and other factors. However, there are some general patterns that can be observed. The first pattern that can be observed is regarding economic growth. Developing Countries tend to have more diversified and globally integrated economies. International trade can play an important role in driving economic growth. Through exports, Developing Countries can access wider international markets, increase sales of their products and services, and create new jobs. Higher economic growth tends to have a positive impact on income distribution, with the potential to increase income for society as a whole.

Next is about employment. International trade can influence income distribution through its impact on employment. Some Developing Countries have industrial sectors that are more internationally competitive, while other sectors may be more dependent on services or high technology sectors. Trade can cause a shift in jobs from less competitive sectors to more competitive sectors, which can impact income distribution. Jobs in more competitive sectors tend to pay higher wages, while jobs in less competitive sectors may experience reduced income or unemployment.

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Trade can bring many benefits, but it can also have negative impacts on certain groups of workers. For example, the United States has an abundant workforce with high levels of education, while there are relatively few workers with low levels of education. This means that international trade has the potential to make lower-educated workers in the United States worse off – not just temporarily, but over a sustained period of time.

The negative impact of trade on low-educated employment is a persistent political problem, which cannot be addressed by policies that provide temporary relief (such as unemployment insurance). But it is important to note that some experts argue that Developing Countries must limit trade with low-wage countries if they want to remain middle class.

The next pattern is the income gap. International trade can contribute to income inequality in Developing Countries. Some countries may experience a concentration of wealth and income among smaller groups, such as large corporations or wealthy individuals. This can happen if trade is more profitable for sectors controlled by that group. However, on the other hand, trade can also provide opportunities for small and medium entrepreneurs and encourage social mobility by creating new jobs and economic opportunities.

The next pattern that can be observed is regarding government policy. Income distribution in Developing Countries is also influenced by government policies related to trade. Governments can use policy instruments such as taxes, subsidies, trade regulations, and social protection programs to influence income distribution. For example, protectionist policies that limit imports may provide protection for certain domestic sectors, but they may also increase prices for consumers and affect the distribution of household income.

It should be noted that trade and income distribution have a complicated relationship that can be influenced by a variety of factors. Various economic and social policies and changes in global economic dynamics can play an important role in shaping these relationships.

2 Theoretical Based

2.1 Income Distribution

2.1.1 Concept of Income Distribution

Each household or population has a different distribution of income from each other. The equalization is divided into two sides. First, people who are still below the poverty line can improve their lives. Second, there has been complete equality of income for each household or each individual. Efforts to reduce the division of population groups could result in a more even distribution of income, if the income of the upper-class economy population does not rise more rapidly.[1]

2.1.2 Measurement of Income Distribution

According to Todaro and Smith (2003), indicators of income distribution measurement are as followed:[2]

a. Gini Coefficient
b. *Generalized Entropy (GE) Index*
c. A Measurement of Income Quality

2.2 International Trade

An economic transaction between nations is known as international trade. Among the things normally exchanged are buyer merchandise, like TVs and dress; capital products, like hardware; as well as unrefined components and food. Different exchanges include administrations, for example, travel administrations and installments for unfamiliar licenses. Global exchange exchanges are worked with by worldwide monetary installments, in which the confidential financial frameworks and national banks of exchanging nations assume a significant part.[3]

3 Method

The method used to complete this assignment is the Systematic Literature Review (SLR) method. According to Kossyva, et al (2023), systematic literature review is a method that can be used by formulating questions clearly, explicitly and systematically to identify, select and critically assess relevant research.[4] According to Semeraro, et al (2021) there are 3 steps or stages in the SLR method, namely:[5]

3.1 Article selection: Identification and screening of literature

Literature searches were carried out on scientific databases such as the scientific databases Scopus, Elsevier, and ScienceDirect. The search was carried out by entering the keywords "trade", "income distribution", "trade and income inequality", "income inequality", "wage inequality". Relevant literature was selected by analyzing the title, abstract, keywords, contents of the paper, and main topic of the journal.

3.2 Data Collection

After the identification and screening stages have been carried out, the next step is data collection based on the inclusion criteria. The inclusion criteria used in the literature search were those related to income distribution and trade in Developing Countries. The literature obtained and analyzed is based on inclusion criteria and literature study research results. Obtained data related to keywords for 10 articles. These articles were selected based on inclusion criteria into 6 articles.

3.3 Data and Information Presentation

The next stage, the author lists the articles in a table, then reviews and examines the articles intensively in the research results section. Finally, the author compares the findings from several literatures and makes conclusions.

4 Result and Discussion

Table 1. Reference of Literature Review

Name and Year of Research	Research Title	Research Result
Fabian Trottner (2019)	Trade and Wage Inequality Within and Between Firms	Trade increases inequality by 20 percent, with changes within firms accounting for about 30 percent of the total change.[6]
Wolfgang Lechtaler & Mariya Mileva (2019)	Exchange progression and pay disparity: new knowledge from a unique exchange model with heterogeneous firm and relative benefit.	sectoral movement sponsorships for incompetent laborers might lessen intersectoral wage disparity among untalented specialists, yet fuel intersectoral wage imbalance among gifted laborers wage disparity between areas among talented and untalented specialists expanded expertise premium.[7]
Daniel Auguste (2018)	Globalization, Income Inequality, and the Welfare State	Before taxes and transfers, international trade reduces income inequality. Movement, then again, adversely affects pay imbalance before expenses and moves. In any case, no impact was found from FDI and the degree of government assistance state liberality on pay imbalance before assessments and moves.[8]
Elhanan Helpman (2016)	Globalization and Wages Inequality	Trade plays an important role in increasing wage inequality. However, the cumulative effect is not that great. In other words, although trade has an impact on wage inequality, its impact does not significantly make sense of the enormous expansion in wage imbalance in Agricultural Nations.[9]
Xiaofeng Penny Li (2015)	Wage Inequality and Trade Liberalization	trade liberalization and de-unionization (reduction in union membership) influenced the growing wage disparity in US states between skilled and unskilled workers.[10]
Bergh dan Nilsson (2011)	Globalization and Outright Destitution	Data streams and more liberal exchange limitations have a strong negative correlation with absolute poverty.[11]

4.1 The Relationship between Income Distribution and Trade in Developing Countries

4.1.1 The Impact of Trade on Wage Inequality According to Fabian Trottner (2022).[6]

International trade causes unequal distribution of income in the form of wage inequality. This happens because large companies that have a more skilled workforce are more productive than companies that do not have a skilled workforce. So, more productive companies can enter the export market well and pay high wages to their workers. Meanwhile, companies that are less productive will pay lower wages and even lay off workers in the domestic market.

The structural model in Fabian Trottner's research is used to measure the importance of the mechanism between the distributional impact of trade and wage inequality. This model estimates qualitatively and quantitatively. The finding is that the imperfect competition introduced into the labor market by an upward-sloping labor supply curve causes quantitatively relevant distortions in the allocation of skilled and unskilled workers across firms of different sizes.

To overcome this distortion, an optimal tax scheme is implemented. By implementing an optimal tax scheme, wage inequality in skilled groups is reduced by 20%, worker welfare increases by 6%.

4.1.2 The Impact of Trade Liberalization and Wage Inequality According to Wolfgang Lechtaler and Mariya Mileva.[7]

The analysis carried out by Wolfgang and Mariya focuses on changes in wage inequality in developed and developing countries. The difference between the analysis and other researchers is that the analysis of other studies only uses open economic analysis, while Wolfgang and Mariya’s analysis uses bilateral analysis.

Wage inequality varies over the medium and short term, according to the first analysis. Temporarily, intersectoral wage imbalance increments since interest for products delivered by the trading area increments. In the medium term, wage disparity between areas diminishes wage imbalance between areas since laborers move from areas that contend with imports to sending out areas. Conversely, the expertise premium doesn’t change a lot of in the present moment however just expansions in the medium term and afterward stays high. As a result, overall wage inequality continues to rise.

His second analysis led to an endogenous supply of skilled and unskilled labor, making it possible for newly hired workers to train to become skilled workers. This has significant ramifications for the drawn out effect of exchange advancement. The drawn out effect of exchange progression on wage imbalance is extraordinarily decreased in light of the fact that more changes are made through numbers (more talented laborers) and less through compensation.

Sectoral migration subsidies for unskilled workers can reduce intersectoral wage inequality for unskilled workers, but they can’t increase skill premiums or reduce intersectoral wage inequality for skilled workers. Subsidies for training make it much easier to find skilled workers, which reduces wage inequality overall and the skills premium. Consequently, preparing sponsorships are a more grounded instrument to diminish wage imbalance and to smooth change after exchange progression.

4.1.3 The Impact of Globalization on Income Inequality According to Daniel Auguste (2021).[8]

The purpose of Daniel Auguste's analysis is to ascertain how globalization affects how national income is distributed. The first analysis looked at how globalization affected income inequality prior to taxes and transfers and after taxes and transfers.

The subsequent investigation assesses the impact of Emerging Nations on pay disparity.

The principal consequence of the examination is that globalization increments pay disparity before assessments and moves and affects pay imbalance after charges and moves. globalization can apply vertically and descending tension on pay disparity, as shown by the rising impact of worldwide exchange on pay imbalance before expenses and moves and the diminishing impact of migration on pay disparity when duties and moves.

After taxes and transfers, the second analysis found that developing nations have a significant and negative impact on income inequality. Even after taking into account the forces of globalization, the welfare state's capacity to provide its members with a decent standard of living regardless of their participation in the labor market remains crucial to the distribution of income. This is on the grounds that administration social wellbeing net projects can shield people from work market difficulties, like loss of occupations and wages.

4.1.4 The Impact of Globalization on Income Inequality According to Elhanan Helpman (2016).[9]

Analysis conducted by Elhanan Helpman (2016), states that there is no strong evidence that globalization is responsible for inequality in workers' wages, even though globalization has an impact on wages for different types of workers. the fact that foreign trade, foreign investment, and offshoring have had a detrimental impact on certain workers is also undeniable.[9] Free trade in Canada can cause unemployment to increase, this is because it imports a lot from China. However, globalization cannot be immediately said to be responsible for wage inequality.

So, it is necessary to include various additional considerations, such as the choice to export, company variations in terms of productivity and intensity factors as well as technological improvements to find out the causes of wage inequality.

4.1.5 The Impact of Trade Liberalization on Wage Inequality According to Xiaofeng Penny Li (2015).[10]

Xiaofeng investigated the connection between wage inequality in the United States and trade liberalization. The difference in differences and fixed effects method is used to evaluate the impact of trade liberalization on wage inequality.

The results of his research show that trade liberalization and de-unionization (reduction in union membership) influence the increase in wage inequality between skilled and unskilled workers in US states. Evidence also suggests that technological changes that favor skilled workers do not have a significant impact on increasing wage inequality.

4.1.6 The Relationship between Globalization and Absolute Poverty According to Bergh and Nilsson (2011).[11]

This research examines the relationship between economic and social globalization and ex post absolute income poverty in more than 100 countries around the world from 1988 to 2007 using panel data. Globalization is measured using the globalization index developed by Dreher (2006), while poverty estimates use data from the World Bank.[12]

The results show that there is no evidence that globalization is associated with higher levels of poverty in developing countries. The research results also show that trade increasing growth and poverty reducing growth can hold up well in both short and long-term analysis. The researchers also found that higher trade is accompanied by lower poverty on average, but the effect is no longer significant once we control for income or growth.

Globalization reduces poverty but not through growth. A possible explanation is that there is an income distribution effect so that the income of the poor increases more than the average income. Poverty reduction can be achieved through closer economic integration and higher levels of globalization.

5 Conclusion

The results of empirical research show that the relationship between trade and income distribution in Developing Countries is that international trade causes unequal income distribution in the form of wage inequality. This happens because large companies that have a more skilled workforce are more productive than companies that do not have a skilled workforce.

To conquer this twisting, an ideal expense plot is executed. Temporarily, intersectoral wage imbalance increments since interest for products delivered by the trading area increments. In the medium term, wage disparity between areas diminishes wage imbalance between areas since laborers move from areas that contend with imports to sending out areas. establishing an endogenous supply of skilled and unskilled labor. This suggests that wage inequality will be significantly less affected by trade liberalization in the long run. Sectoral movement appropriations for incompetent specialists might decrease intersectoral wage disparity among untalented laborers, however worsen wage imbalance.

Globalization increments pay disparity before assessments and moves and affects pay imbalance after expenses and moves. After taxes and transfers, developing nations have a significant and negative impact on income inequality. Additional considerations, such as the choice to export, company variations in terms of productivity and intensity factors as well as technological improvements to determine the causes of wage inequality due to globalization. Globalization reduces poverty but not through growth, but there is an income distribution effect so that the income of the poor increases more than the average income.

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