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Impact of Trade on Poverty and Inequality: Empirical Evidence from SAARC Countries

ABSTRACT

This study investigates the impact of trade on poverty and inequality within the South Asian Association for Regional Cooperation (SAARC) countries. Using balanced panel data spanning from 1990 to 2022, the research focuses on understanding the connection between international trade and poverty on the one hand, and on the other trade and inequality. Poverty and inequality equations were separately estimated by employing pooled ordinary least squares (POLS) method on balanced panel data. Through regression analyses and econometric modelling, the study aims to uncover the nuanced relationship between trade policies, economic growth, poverty alleviation, and inequality within the SAARC region. The findings reveal a negative link between trade openness and poverty indicating that increasing trade helps in alleviating poverty in the SAARC region. However, the link between trade and inequality is positive. This indicates that trade policies must be thoughtfully crafted to promote fair economic growth. These insights are crucial for policymakers aiming to balance the trade expansion with social welfare in SAARC countries. The findings of this research contribute to the literature on the trade-poverty and trade-inequality nexus, offering insights for policymakers to formulate effective strategies for sustainable economic development and social inclusion in SAARC countries.

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1. INTRODUCTION

Trade plays an important role in reducing poverty by promoting economic growth and well-being, creating new jobs, expanding the industry, and providing more access to goods. However, its influence on income inequality often depends on how the gains of trade are dispersed across different segments of society. Numerous countries across the globe have experienced economic growth as a result of recent trade openness (Banday et al., 2021; Kumari et al., 2023; Nam & Ryu, 2024). The impacts, however, vary among nations across the region with varying stages of economic development and growth. The rise in trade openness in the developing economies has supported growth and development; however, it has also widened the income inequalities (Xia et al., 2022; Tabash et al., 2024). The subject of economic imbalance has sparked significant discussion over its effects at both the national and global levels. In an era marked by global interdependence, the intricate interplay between economic growth, trade openness, and their ramifications on poverty and inequality has taken centre stage in both scholarly discourse and policy deliberations. In the case of SAARC economies, characterized by varying levels of development, the influence of trade on poverty and inequality is particularly evident, influenced by factors such as sectoral shifts, regional disparities, and differing government policies (Ouni et al., 2025).

SAARC[1]was established in 1985 with an agenda to promote regional economic integration, promote regional cooperation, and improve connectivity to reduce the widespread poverty and economic inequality among the South Asian states. Poverty in terms of income refers to a situation where individuals or households have an insufficient level of income to meet basic needs and achieve a reasonable standard of living (Al Kez et al., 2024). It encompasses a condition of material deprivation, where limited financial resources hinder access to essential goods and services such as food, housing, education, healthcare, and other necessities required for a dignified life . However, inequality refers to the disparities in income, wealth, and opportunities that exist among individuals or groups within a society (Hwang, 2024). It can manifest as differences in access to education, healthcare, employment, and other essential resources (Atkinson, 2015). In general, the nexus between trade openness, economic growth, and poverty reduction has been a subject of considerable interest within the realm of international development. This study seeks to empirically explore this intricate nexus within the context of the SAARC countries. The overarching objective is to examine how the interplay between openness and growth influences poverty dynamics across this diverse group of nations.

Trade in SAARC economies affects poverty and inequality by shaping economic growth, altering sectoral employment, and influence the affordability of essential goods. Increased openness can lower poverty through job creation and improved access to markets, yet may also worsen inequality if benefits are unfairly distributed across the social groups. This study empirically investigates the trade–poverty–inequality linkages using region-specific evidence to examine the SAARC's unique structural and policy context. Existing empirical literature on trade, poverty, and inequality mainly focus on developed countries or cross-regional analyses, overlook the SAARC region's unique structural and institutional context. Empirical evidence explicit to SAARC economies, considering heterogeneity in trade patterns, poverty dynamics, and inequality drivers, remains scarce. Moreover, in the literature, the association between trade, economic growth, and income inequality reveals mixed results.

Existing literature does not have any consensus because the overall influence of trade and growth on poverty and inequality differs from country to country; therefore, we cannot generalize the results of one country to all other countries (Cerra et al., 2021; Dorn et al., 2022). Therefore, this study helps to find the result of the impact of trade on poverty and inequality in the case of SAARC countries with the data set that ranges from 1990 to 2022. This study addresses the lack of region-specific evidence on the association between trade, poverty, and inequality in SAARC economies. Even though increase

[1]Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, and Sri Lanka

in trade integration, outcomes for poverty reduction and income distribution remain inconsistent across the region. Understanding these different impacts is crucial for designing trade policies. This research is essential for policymakers and economists in the region to develop strategies that not only promote economic growth and poverty reduction but also address the pressing issue of income inequality, ensuring a more equitable and sustainable future for the people of SAARC nations.

2. LITERATURE REVIEW

The relationship between trade, economic growth, poverty, and inequality has been a subject of substantial scholarly interest. Literature consistently upholds the notion that trade and economic growth plays a crucial role in combating poverty and inequality. Nevertheless, it is imperative to recognize that the relationship between trade, growth, and poverty is intricate and diverse. Policymakers must adopt comprehensive approaches that take into account the unique circumstances of each country and tackle issues, i.e., income inequality, dynamics in the labor market, and the establishment of robust social safety nets. This approach ensures that the advantages of trade and growth are distributed equitably, leading to sustainable poverty reduction.

In principle, trade and economic growth are powerful instruments for poverty alleviation; they should be complemented by other measures such as investments in education, healthcare, and infrastructure to foster an environment where the benefits of growth are widely shared among the population. Previous studies have shown how trade liberalization and growth affect poverty reduction. These studies, in particular, have concentrated on the role of trade openness and growth in determining poverty reduction. The literature review highlights the intricate and context-specific nature of the connection between trade, economic growth, poverty, and income inequality in SAARC countries. While trade and economic growth have the potential to contribute to reducing inequality, their impact can vary depending on factors such as initial inequality levels, sectoral dynamics, and policy frameworks. Policymakers should consider these nuances when designing strategies to promote sustainable and inclusive development in the SAARC region. Further research is essential to deepen our understanding of the relationship between trade, growth, poverty, and inequality in SAARC countries and to guide evidence-based policy decisions that foster equitable growth and reduce income disparities.

Ghazanfar et al. (2021) document that trade openness has a varying influence on poverty across selected SAARC economies. Their empirical findings reveal that in some countries, trade openness lowers the poverty rate by enhancing employment and income levels. Nonetheless, in others, it aggravates income inequality. Rahman and Khondker (2007) examined Bangladesh and concluded that trade liberalization played a role in reducing poverty and income inequality. The relationship between economic growth, inequality, and poverty reduction has been extensively explored. Qayyum et al. (2008) studied Pakistan and found that while economic growth contributed to poverty reduction, income inequality remained a concern. Dorn et al. (2022) suggest that while trade openness in general promotes economic growth, its influence on income inequality differs depending on country-specific factors, for example, redistribution policies and labor market strategies. The authors find that in advanced economies, trade openness has a weaker connection with rising inequality, while in developing economies, increased trade can worsen income disparities, mainly by benefiting high-skilled workers more than low-skilled labor. Chaudhry and Imran (2013) report that trade liberalization reduces poverty in the long run but not in the short run. To maximize the positive effects of trade and minimize its downsides, it is important to implement complementary policies that encourage inclusive growth and equitable distribution of benefits. This entails a holistic approach that combines trade policy with investments in education, infrastructure, social protection, and labor market regulations, ensuring that the gains from trade contribute to sustainable and inclusive development. The findings of the previous studies reveal that the influence of trade on poverty and inequality is not uniform across the SAARC countries. While some nations experience substantial reductions in poverty and inequality as trade increases and economies grow, others may find more

modest effects or encounter challenges that necessitate targeted interventions (Kitole & Sesabo, 2024).

These variations underscore the importance of context-specific policies that consider unique socio-economic, cultural, and institutional factors within each country. After conducting a literature review on trade, poverty, and inequality, specifically in SAARC countries, it becomes evident that these issues are interconnected and of great importance. The studies and research indicate that promoting trade within the SAARC region can lead to increased economic growth, job creation, and poverty reduction. However, based on the existing literature, it is imperative to enhance regional cooperation, reduce trade barriers, and implement inclusive policies, which are crucial for achieving sustainable development and reducing poverty and inequality in SAARC countries. Further research and policy interventions are needed to explore innovative approaches and strategies to tackle these challenges effectively. Together, by fostering trade, promoting economic growth, and addressing poverty and inequality, the SAARC countries can work towards a more prosperous and equitable future for all.

To sum up, existing empirical literature provides mixed and ambiguous results. However, these disparities in the empirical findings can be associated with different factors, for instance, country-specific studies, estimation techniques, heterogeneity among the member countries, and also time span. Using POLS, this study investigates the influence of trade on poverty and inequality in SAARC countries over the period of 1990-2022. These countries, even though their diverse culture, norms, and languages appear to have broader parallel comparisons in terms of the infrastructure, domestic market conditions, and, most importantly, the level of their economic growth. However, there is little existing empirical evidence to hold up the claim that trade liberalization policies, particularly in developing economies, offer economic growth and reduce poverty rates and also income disparities. Nevertheless, in the literature, proponents of the trade liberalization policies argue that these trade liberalization policies in the developing world lead to benefits for the individuals and society in the long run if prudent domestic policies are adopted (Freund &Bolaky, 2008). However, on the other hand, literature also documented that trade policies can often result in greater income inequality in the developing economies (e.g., Siddiqui et al., 2012; Musila&Yiheyis, 2015; Ulaşan, 2015; Kitole&Sesabo, 2024; Nam et al., 2024).

3. METHODOLOGY

3.1 Data Source and Model Specification

The data for the sample countries are drawn from the World Bank Database, for instance, World Development Indicators (WDI). The selection of SAARC economies is purely based on the availability of data. The list of selected variables and their sources is provided in Appendix A. To empirically investigate the association between trade and poverty outcomes in SAARC economies, the study specifies two econometric models focusing on poverty and income inequality respectively. The first model as presented in Equation (1) estimates the influence of trade and other macroeconomic variables on poverty, while the second as presented in Equation (2) assesses their effect on income inequality. Both models incorporate relevant control variables to account for structural and economic differences across countries and over time. The main variables of interest are trade liberalization as a % of GDP (represented TRD), economic growth (represented by GDP), and poverty proxied by the head count ratio (represented by POV). In addition to that, the control variables are employment (EMP), population (POP), foreign direct investment (FDI), and inflation rate (INF). The study utilizes POLS method in a panel setting to investigate the impact of trade liberalization and economic growth on poverty and inequality in SAARC countries. Further, the empirical model is presented in Equation (1) below:

$$POV_{it} = \beta_0 + \beta_1 TRD_{it} + \beta_2 EMP_{it} + \beta_3 GDP_{it} + \beta_4 POP_{it} + \beta_5 FDI_{it} + \mu_{it} \qquad (1)$$

The above empirical model represents that poverty (POV) is a function of trade (TRD), employment (EMP), Gross Domestic Product (GDP), population (POP), and foreign direct investment (FDI). The

selection of these variables is based on economic theory and existing relevant literature. All these variables influence the poverty directly or indirectly. For instance, increasing trade openness and GDP increases economic development and growth by creating more job opportunities and raising employment levels across various sectors of the economy. Moreover, as businesses expand and industries flourish, overall productivity increases, new technologies are adopted, leading to higher wages and improved living standards. This economic progress, in turn, helps reduce poverty by providing greater access to resources and opportunities for individuals and communities. However, it is often observed that the unequal distribution of income results in increasing poverty in economies. To determine how the variables interact, we use the model presented in Equation 2:

$$GINI_{it} = \gamma_0 + \gamma_1 TRD_{it} + \gamma_2 EMP_{it} + \gamma_3 GDP_{it} + \gamma_4 FDI_{it} + \gamma_5 INF_{it} + \varepsilon_{it} \qquad (2)$$

In principle, the impact of trade openness on income inequality is shaped by how gains from trade are distributed among the individuals in the society, government policies, and dynamics in the labor market. However, the uneven distribution of gains can increase the income inequality in the society, whereas government intervention may decrease it. Further, the shifts in labor demands and wage rates can also play a crucial role in this connection.

3.2 Data Source

The study uses key economic variables to empirically investigate the relationship between trade, poverty, and inequality in SAARC economies. Poverty is measured as the number of people living below the poverty line, while inequality is captured through the GINI index. Trade openness (% of GDP) and annual GDP growth are included to capture the broader economic environment affecting these outcomes. The data for the sample countries are drawn from the World Bank Database, for instance, World Development Indicators (WDI). The selection of SAARC economies is purely based on the availability of data.

4. RESULTS AND DISCUSSION

4.1 Descriptive Statistics

Table 1 describes the descriptive statistics and tells that the average value of poverty is smaller than the median value, which suggests that the distribution of the poverty is leftward skewed. That is, most of the observations are concentrated around the bigger value. Also, poverty is the second volatile variable in our model, as shown by the relatively bigger value of standard deviation. Similarly, the average value of foreign direct investment is greater than the median value, which tells that the distribution of the FDI is rightward skewed. Also, the average value of employment is greater than the median value, which means that the distribution of the employment is rightward skewed. Hence, most of the observations are concentrated around the lesser value, and employment is also a less volatile variable, as shown by the value of standard deviation.

Table 1: Summary Statistics

Variable	Mean	Median	Std. Dev.
POV	26.317	29.246	12.075
FDI	1.005	0.616	0.876
EMP	1.305	0.278	1.080
GDP	5.207	5.572	3.102
POP	1.412	1.433	0.908
TRD	51.062	31.57	25.682
GINI	31.45	31.76	2.261

The average value of GDP is approximately equal to the median value, which suggests that the distribution of the GDP is symmetric. That is, most of the observations are concentrated around the average value. Also, GDP is a less volatile variable as shown by the value of standard deviation and

range. Similarly, the average value of the population is approximately equal to the median value. Which means that the distribution of the population is symmetric; that is, most of the observations are concentrated around the average value. Accordingly, the average value of trade openness is greater than the median value, which suggests that the distribution is rightward skewed; that is, most of the observations are concentrated around the lesser value. Also, trade openness is the most volatile variable in our data, as shown by the bigger value of standard deviation. Finally, the average value of GINI inequality is approximately equal to the median value, which suggests that the distribution is symmetric; that means most of the observations are concentrated around the average value. Furthermore, the GINI inequality is a less volatile variable in our data, as shown by the value of standard deviation.

4.2 Correlation Matrix

Table 2 below discusses the matrix of correlation between all variables used in this empirical analysis. Our main dependent variable, GINI inequality, is positively correlated with GDP, inflation, and trade openness. However, it is negatively correlated with FDI and employment (EMP). GINI inequality has the highest correlation with trade openness, whereas the lowest correlation is with FDI. The correlation between GINI and trade openness (TRD) is 0.3433, indicating a moderate positive relationship. This suggests that higher trade openness is associated with higher inequality. However, the correlation between GINI and FDI is -0.0029, indicating a near-zero relationship, suggesting that FDI does not have a significant linear association with inequality.

Table 2: Correlation Matrix (I)

Variables	**(GINI)**	**(GDP)**	**(INF)**	**(TRD)**	**(FDI)**	**(EMP)**
(1) GINI	1.0000					
(2) GDP	0.1828	1.0000				
(3) INF	0.0480	-0.2244	1.0000			
(4) TRD	0.3433	0.1528	-0.0448	1.0000		
(5) FDI	-0.0029	0.2889	0.0093	0.2311	1.0000	
(6) EMP	-0.2350	-0.0292	0.1792	-0.2270	0.1157	1.0000

Table 3 discusses the matrix of correlation for poverty and other explanatory variables. Our main variable, poverty, is only positively correlated with the population, and it is negatively correlated with all the other variables, such as foreign direct investment (FDI), employment, GDP, and trade openness. Poverty has the highest positive correlation with the population and the lowest negative correlation with FDI. The correlation between poverty and trade (TRD) is -0.5360. This moderate to strong negative correlation indicates that greater trade openness is associated with lower poverty levels. However, the correlation between poverty and population (POP) is 0.4811. This moderate positive correlation suggests that higher population levels are associated with higher poverty levels. And the correlation between poverty and GDP is -0.0887. This weak negative correlation indicates that higher GDP might be associated with slightly lower poverty levels, but the relationship is not strong. The correlations among other variables such as FDI, EMP, GDP, POP, and TRD show varying degrees of weak to moderate relationships, indicating complex interactions that might influence poverty and inequality in different ways.

Table 3: Correlation Matrix (II)

Variables	(POV)	(FDI)	(EMP)	(GDP)	(POP)	(TRD)
(1) POV	1.0000					
(2) FDI	-0.0138	1.0000				
(3) EMP	-0.1307	0.1157	1.0000			
(4) GDP	-0.0887	0.2889	-0.0292	1.0000		
(5) POP	0.4811	-0.0447	-0.1902	0.0898	1.0000	
(6) TRD	-0.5360	0.2311	-0.2270	0.1528	-0.3519	1.0000

4.3 Regression Analysis

Table 4 represents the results of the empirical model presented in Equation(1). In this model the dependent variable is poverty, which is represented by POV_{it} and the variable of interest is trade. The results show that the coefficient value of trade (TRD) is -0.242 and the p-value is 0.000, which indicates that trade has a significant negative relationship with poverty. It implies that an increase of 1 unit in trade will result in a decrease of 0.242 units in poverty. An increase in trade results in creating more jobs and employment levels as a result of poverty reduction. The results are consistent with the previous study (Zhu et al., 2022; Ngubane et al., 2023). Further, employment has a negative relationship with poverty. As the coefficient value of employment (EMP) is -2.429 and the p-value is 0.001, which indicates that EMP has a significant negative relationship with poverty, an increase in employment by 1 unit results in decreasing poverty by 2.429 units. Likewise, the results show that the coefficient value of GDP is -0.351 and the P value is 0.099, which describes that GDP has a significant negative impact on poverty, as a 1-unit increase in GDP will result in decreasing 0.351 units in poverty.

On the contrary to this, population and foreign direct investment have a positive relationship with poverty. The results show that the coefficient value of population (POP) is 3.660 and the p-value is 0.000, which indicates that population has a significant positive relationship with poverty. It implies that an increase of 1 unit in population will result in an increase of 3.660 units in poverty. Likewise, the coefficient value of FDI is 2.332, and the p-value is 0.009, which shows that FDI has a significant positive relationship with poverty. It is observed that FDI raises the poverty rate in our sample SAARC countries. The possible explanation can be that FDI inflows are typically directed at projects that often generate high profit and offer benefits directly or indirectly to the poor.

Table 4: Regression Analysis Considering Poverty as a Dependent Variable

Variables	Coefficients	Std. Error	Probability
TRD	-0.242***	(0.033)	0.000
EMP	-2.429***	(0.727)	0.001
GDP	-0.351*	(0.245)	0.099
POP	3.660***	(0.896)	0.000
FDI	2.332***	(0.886)	0.000
CONS	36.141***	(3.033)	0.000
Wald Chi2(5): 125.83	Prob>Chi2: 0.000	R. squared: 0.87	

In Table 5, we present the result based on the empirical model as presented in Equation (2). In this model the dependent variable is inequality, which is measured by $GINI_{it}$ and the variable of interest is trade. The results show that the coefficient value of trade (TRD) is 0.093 and the p-value is 0.000, which indicates that trade has a significant positive relationship with GINI. It implies that an increase of 1 unit in trade will result in an increase of 0.093 units in inequality. The results are consistent with the study (Ranamagar, 2022). Moreover, inflation and GDP have a positive association with GINI. As an increase in inflation by 1 unit results in increasing inequality by 0.182 units, the coefficient value of inflation is 0.182, and the p-value is 0.066, which shows a significant positive relationship between inflation and GINI.

Likewise, the results show that the coefficient value of GDP is 0.485 and the P value is 0.012, which describes that GDP has a significant positive impact on GINI, as a 1-unit increase in GDP will result in an increase of 0.485 units in GINI. On the contrary to this, FDI and employment have a negative relationship with GINI. The results show that the coefficient value of FDI is -0.986 and the p-value is 0.099, which indicates that FDI has a significant negative relationship with GINI. It implies that an increase of 1 unit in FDI will result in a decrease of 0.986 units in GINI. Likewise, the coefficient value of employment (EMP) is -1.233 and the p-value is 0.024, which indicates that employment has a significant negative relationship with GINI. It implies that an increase of 1 unit in EMP will result in a decrease of 1.233 units in GINI.

Table 5: Regression Analysis Considering GINI as a Dependent Variable

Variables	Coefficients	Std. Error	Probability
TRD	0.093***	(0.023)	0.001
INF	0.182**	(0.099)	0.066
GDP	0.485***	(0.193)	0.012
FDI	-0.986*	(0.688)	0.099
EMP	-1.233***	(0.544)	0.024
CONS	27.776***	(1.925)	0.000
Wald Chi2(5): 36.79	Prob. > Chi2: 0.000	R-squared: 0.74	

The main findings of this study suggest that there is a negative association between trade and poverty, and it is significant at the 0.001 level. The second most important component of poverty is economic growth (GDP), and there is also a negative connection between poverty and GDP, and it is significant at the 0.05 level. Among control variables, employment has a negative relationship with poverty, and it is significant at the 0.001% level. In addition to that, the other two variables, population and FDI, have a positive link with poverty, and both variables are highly significant. The second main finding of our study discusses the relationship between trade and inequality, and there exists a positive relationship between trade and inequality, and the variable is highly significant at the 0.000% level. In addition to that, we report a positive relationship between inequality and economic growth. The other control variable, inflation, has a positive relationship with inequality. Further, FDI and employment, have a negative relationship with inequality, and FDI is significant at the 0.099% level; also, employment is significant at the 0.024% level.

5. CONCLUSION AND POLICY IMPLICATIONS

The study analyzed the impact of trade openness and economic growth on both poverty and inequality in SAARC countries over the period 1990-2022. The empirical results indicated that trade openness, employment, and growth (GDP) significantly decreased poverty; while the population and FDI significantly increased poverty in SAARC countries. Furthermore, trade, GDP, and inflation significantly increased inequality, while FDI and employment significantly decreased inequality in SAARC countries for the sample period. The impact of trade on poverty and income inequality in SAARC countries presents a complex yet critical area of economic analysis. The empirical evidence indicates that trade significantly reduces poverty, suggesting that increased trade openness can create economic opportunities, enhance income levels, and improve living standards. This positive impact on poverty underscores the potential of trade as a powerful tool for economic development and poverty alleviation in the region.

The findings highlight a dual challenge for policymakers in SAARC countries. On the one hand, promoting trade can be an effective strategy for reducing poverty by creating jobs, increasing income, and fostering economic growth. On the other hand, the tendency of trade to increase income inequality calls for complementary policies to ensure that the benefits of trade are widely shared. This could include measures such as investing in education and skills development, improving access to credit and markets for small and medium-sized enterprises, and implementing social protection

programs. In principle, trade is a crucial driver of economic development in SAARC countries; its impact on poverty and inequality underscores the need for balanced and inclusive policy approaches. By addressing the inequality exacerbated by trade, SAARC countries can harness its full potential to improve living standards and promote sustainable, inclusive growth. Governments should continue to promote trade openness as it is proven to reduce poverty. Policies that facilitate trade, such as reducing tariffs, improving trade logistics, and streamlining customs procedures, can help integrate SAARC countries more effectively into the global market. To mitigate risks and maximize benefits, SAARC countries should diversify their trade partners and export products. This diversification can help stabilize economies against global market fluctuations and ensure more consistent economic benefits.

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Appendix A: Variable Description

Dependent Variables			
Variables	**Description**	**Measurement**	**Source**
Poverty	Number of people below the poverty line	Numbers	POVCAL (World Bank), 2019
Inequality	GINI	Index	World Bank
Independent Variables			
Trade	Openness	% of GDP	WDI, World Bank
GDP	Gross domestic product	Annual Growth %	WDI, World Bank
Control Variables			
Employment	Ratio to Population	% of population	WDI, World Bank
Population	Population growth rate	Annual%	WDI, World Bank
FDI	Net inflows	% of GDP	WDI, World Bank
Inflation	Inflation rate	Annual %	WDI, World Bank