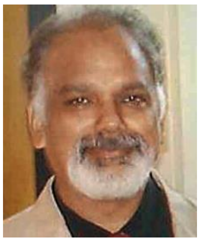
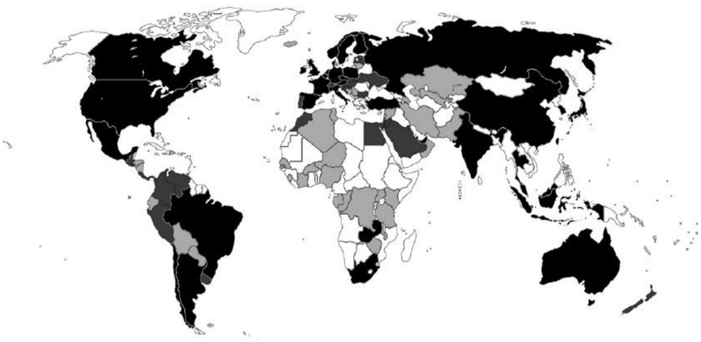


Globalization Process going nowhere?

Sourced & Compiled by Mr. Arvind Sinha - CEO

Serious thinking required to restart the process



For many decades after World War II, a broad range of countries shared a fundamental economic vision. They endorsed an increasingly open system for trade in goods and services, supported by international institutions; allowed capital, corporations, and, to a lesser extent, people to flow freely across borders; and encouraged the rapid spread of data and technology. As trade expanded, global living standards improved dramatically, and hundreds of millions of people escaped from poverty.

Today, every aspect of this globalized economy is under assault. A popular backlash against free trade and unrestricted cross-border movements of capital has picked up momentum. The ideal of freely flowing information has clashed with growing calls for privacy rights, the protection of intellectual property, and increased cybersecurity. Across the developed world, sentiments have turned strongly against immigration, especially as waves of Middle Eastern refugees have flooded Europe. And after several successful rounds of multilateral trade negotiations in the postwar years, new agreements have become much rarer: the World Trade Organization (WTO) has not completed a single full round of successful negotiations since its creation in 1995.

Last June, the United Kingdom voted to leave the EU, sparking the worst political crisis in the union's history. Meanwhile, in the United States, President Donald Trump has vowed to put "America first." In his first week in office, Trump withdrew from the Trans-Pacific Partnership (TPP), the 12-nation free-trade deal orchestrated by Trump's predecessor, and he has pledged to renegotiate the North American Free Trade Agreement, which he has called "the worst trade deal maybe ever signed anywhere, but certainly ever signed in this country." The Transatlantic Trade and Investment Partnership, a deal currently being negotiated by the United States and the EU, also faces an uncertain future, bogged down in strong opposition on both sides of the Atlantic.

As the United States loses interest in nurturing the international order that it played the lead role in building, the future of globalization will depend in large part on China. So far, Beijing appears committed to preserving an open global system. But for now, China will struggle to replace the United States as the sponsor of an open, multilateral order. In an era of rapid and disruptive technological change, politicians and policymakers all over the world will need to push for reforms that can preserve the achievements of globalization—and fix its flaws—before it's too late.

PITCHFORK POLITICS

Over the past seven decades, and especially since the end of the Cold War, globalization has accelerated steadily. For much of this period, most countries accepted the open global trading system. But governments often erected barriers to manage the pace of change. Developing countries, for instance, frequently delayed opening certain sectors of their economies to foreign trade to protect so-called infant industries, and they imposed capital controls to avoid destabilizing their financial systems. Although developed countries generally accepted the costs of the open economic system, they, too, sometimes intervened to reduce the disruption caused by trade. In a largely unsuccessful attempt to help the domestic auto industry, for instance, the Reagan administration imposed restrictions on car imports and pushed Japanese automakers to build plants in the United States.

In the past two decades, however, developed countries have failed to mitigate the negative side effects of international trade and rapid technological change.

Western publics have blamed free trade for the decline in manufacturing jobs and for widening income inequality, and anti-trade sentiments in middle America helped catapult Trump into the White House. Among the traditional champions of globalization—the United States, the United Kingdom, and continental Europe—support for economic openness has declined precipitously. In November 2016, a YouGov/Economist poll found that less than half of Americans, Britons, and French believed that globalization was a “force for good.”

Such attitudes are hardly limited to the grass roots; antiglobalists have come to power or have grown closer to achieving it. And they are finding common cause: on the day after the United Kingdom voted for Brexit, Steve Bannon, now Trump’s chief strategist, invited Nigel Farage, then the leader of the UK Independence Party, onto his radio show. “The European Union project has failed,” Farage announced. “It is doomed, I’m pleased to say.” “It’s a great accomplishment,” Bannon said. “Congratulations.” Ahead of France’s recent presidential election, Trump expressed support for the National Front leader Marine Le Pen and her protectionist agenda.

Although Trump’s unorthodox tenure in Washington has dominated headlines, in Europe, too, the globalized economy is facing intense challenges. The United Kingdom, home to Europe’s most important capital market, is about to exit the EU; the terms remain unclear, but there is no question that Brexit represents a victory for antiglobalization, nativism, and nationalism. Meanwhile, much of the rest of Europe is plagued by low growth and high unemployment, factors that, alongside the refugee crisis, have fueled support for populist parties across the continent. Europe is trapped in a failing economic system that has too few adjustment mechanisms. Growth and inflation remain too low to reduce high unemployment and debt levels, and debt restructuring would be almost impossible without breaking up the eurozone. The euro’s exchange rates with other major currencies are too low for Germany and some other countries in the north, driving up their trade surpluses, but too high for those in the south, which remain far less competitive.

In the current political environment, as nationalism rises across the continent, sensible economic reforms, such as increased fiscal integration, are unlikely to gain traction. But the British vote to leave the EU and Trump’s election might serve as a wake-up call for European elites, triggering real reform. Nonetheless, with a new and inexperienced president in France and with elections looming in Denmark, Germany, and Italy, Europe will remain preoccupied with its internal political and economic challenges for the foreseeable future.

Multilateral institutions that have played a key role in the post–World War II order will also struggle to provide global leadership. Institutions such as the International Monetary Fund and the World Bank have had trouble adapting to the rise of the emerging economies: the United States and Europe still dominate them, eroding their credibility and influence among developing countries, especially in Asia. Yet neither the United States under Trump nor the EU, which has been embroiled in a conflict with the IMF over Greece’s debt, is likely to invest many resources in these organizations in the coming years. As the multilateral institutions are marginalized, the global economic system will become more vulnerable to local and systemic financial crises.

Meanwhile, the early optimism about the Internet and the free flow of information, another central element of globalization, has faded. The disclosures by the National Security Agency leaker Edward Snowden regarding U.S. surveillance programs, Russia’s alleged cyberattacks during the U.S. presidential election, the rise of “fake news,” and terrorist organizations’ use of digital communications to recruit followers and plan attacks have made clear that information technology can subvert the globalized liberal economic order as well as support it. The Internet faces a much more complicated, regulated, and fragmented future than the one imagined by many in the 1990s. In China, stringent regulations have built a sort of digital Great Wall that partially seals off Chinese Internet users from the rest of the world, and the EU has taken strong positions on privacy, attempting to constrain the practices of some Web-based platforms created by Facebook and Google through legal action. In the next few years, other governments are also likely to restrict the free flow of information, data, and knowledge in the name of security.

WHERE IT ALL WENT WRONG

Many of the global economy’s current challenges have their roots in the years around the turn of the millennium.

In 1999, the euro was launched, setting the stage for Europe's recent economic woes. Nearly three years later, in December 2001, China joined the WTO, opening its domestic markets to imports and gaining full access to the global economy. Meanwhile, the economic impact of automation and digital technology began to accelerate.

In the United States, manufacturing jobs had been declining for two decades, but they dropped sharply in the early years of this century: between 2000 and the present, the number of U.S. manufacturing jobs fell by between six million and seven million. As the number of jobs in the so-called tradable sector, which produces goods and services that can be consumed anywhere, barely grew, the nontradable sector absorbed around 25 million new entrants to the job market, in addition to the displaced manufacturing workers. It was a buyer's market for medium- and low-skilled labor, and as a result, wages stagnated.

For many years, automation has been eliminating blue-collar jobs and some lower-paying white-collar jobs. But recent breakthroughs in sensors, machine learning, and artificial intelligence have left even more jobs vulnerable. In almost every developed economy, middle-income jobs are decreasing while lower- and higher-paying jobs are increasing.

Countries have responded in different ways. Some have acted to reduce inequality by redistributing wealth through the tax system, expanding social security programs and other safety nets, and increasing support for education and job training. These efforts have proved successful in countries such as Denmark, Germany, and Sweden, where organized labor wields strong bargaining power, businesses and unions trust each other, individual and corporate wealth have limited influence on politics, and egalitarian cultural norms prevail. In all three of these countries, inequality remains below the average for the Organization for Economic Cooperation and Development, a group of mostly rich countries.

But in countries where these factors are absent—especially the United Kingdom and the United States—disparities of income, wealth, and opportunity have widened dramatically. The absence of a meaningful policy response, and the apparent lack of concern among these countries' elites, has aroused deep anger among those who have lost out in the changes wreaked by globalization and technological progress.

The rejection of the old order was not immediate. For a while, people believed that their economic woes were a temporary result of the global financial crisis of 2008. But over time, they began to suspect that disappearing jobs and stagnant wages had become lasting features of the economic landscape. They turned against the elites they held responsible, including business leaders, academics, and the political establishment. And as they watched powerful economic and technological forces buffet their countries—forces over which policymakers at the national level appeared to exert little control—they sought to regain ownership of their destiny and reassert national sovereignty. This has played out most dramatically in Europe, where real and perceived erosions of sovereignty, above all concerning immigration, played a major role in the British vote to leave the EU. Even privileged citizens who had thrived in an open global system voted for Brexit, believing that doing so would allow them to take greater control over their lives.

GLOBALIZATION WITH CHINESE CHARACTERISTICS

As the United States and Europe turn inward, much of the responsibility for maintaining a globalized liberal economic order will fall to China. In his address at the World Economic Forum, in Davos, in January, President Xi Jinping reaffirmed China's commitment to globalization. By sponsoring numerous economic initiatives, including the Asian Infrastructure Investment Bank (AIIB), the Belt and Road Initiative, and the New Development Bank (formerly known as the BRICS Development Bank), and by making substantial overseas investments, Beijing has signaled that it intends to support an inclusive, multilateral form of globalization.

As the world's second-largest economy, China will undoubtedly help shape the future of the global economy. But for now, it remains unclear whether China can replace the United States as the primary champion of globalization. China is in the middle of a challenging domestic structural shift, as it transitions from an economy led by exports and investment to one based more on consumption and services, and its economy faces strong headwinds, including excess capacity and high corporate debt.

Should the United States withdraw from its leadership role, China would not be able to supply the world economy with a large and accessible market for other countries' exports, deep capital markets, or the kind of strong institutions, such as the Federal Reserve and the IMF, that have allowed Washington to stabilize the global financial system for decades. And China has recently tightened its capital controls in an effort to stem capital flight—backtracking, at least for now, from its attempts to internationalize the renminbi.

Still, Beijing's support for multilateral structures represents an important step forward. A world based on bilateral relationships might work for the most powerful countries, but multilateralism has built a big tent in which the smaller, poorer countries can participate and prosper. They will suffer if they have to fend for themselves. China's embrace of multilateralism has already enhanced its stature among countries with smaller economies. Despite strong opposition from Washington, 57 countries joined the Chinese-led AIIB, many of them long-standing U.S. allies, such as Australia, France, Germany, Israel, Saudi Arabia, South Korea, and the United Kingdom. In the first quarter of 2017, another 13 countries agreed to join, including Afghanistan, Belgium, Canada, Hungary, Ireland, and Peru.

But if Washington retreats into bilateralism and Beijing wants to fill the void, the Chinese economy must keep growing and other emerging economies must increase their access to the Chinese market. Among the members of the aborted TPP, the vast majority, including Australia, Japan, and South Korea, already depend on exports to China, by far their largest trading partner, as do emerging economies all over the world. But if the United States turns toward protectionism, the $12 trillion Chinese economy is still not large enough to support global growth alone.

The new U.S. administration has blamed trade deals for manufacturing job losses and trade deficits and has threatened to impose sanctions on some of the United States' top trading partners, such as China, Germany, Japan, and Mexico. In the short run, the U.S. government may introduce targeted hikes in tariffs on, for instance, steel imports, as well as aggressive antidumping penalties and broader trade restrictions justified by the alleged currency manipulations of China, Germany, and Japan. The Trump administration may also try to browbeat companies, urging them to set up factories in the United States. So far, aside from tearing up the hard-won TPP agreement and sharply criticizing trade deals and trading partners alike, Trump has refrained from launching more aggressive actions. But if his domestic agenda runs aground, a frustrated Trump administration could turn toward more strongly protectionist policies and, in the worst-case outcome, ignite full-scale trade wars with other countries.

But there is a more optimistic scenario. Tax reform, public investment in infrastructure, and deregulation—all goals of the new administration—could stimulate private investment and boost U.S. growth and, with it, global growth. But to achieve this outcome, Trump must avoid becoming bogged down in unnecessary and divisive fights with the media and the courts and must firm up congressional support in his own party. In the meantime, policymakers and businesses in other countries should hope for the best but prepare for the worst.

THE AGE OF AUTOMATION

For all the focus on globalization, in the long run, the most important force shaping the labor market and income inequality will be not trade or politics but technological change. Automation has already transformed the economies of the developed world and the nature of employment there, and almost all experts believe that the scope for expanding automation is enormous. As costs fall and the pace of innovation accelerates, the impact of automation will spread to middle-income countries and, eventually, to lower-income ones, as well.

As capital-intensive technology replaces labor-intensive manufacturing, early stage developing countries across Africa and Southeast Asia will cease to enjoy the comparative advantage offered by lower wages and production costs. Overall trade in goods will probably decline as the price of labor no longer determines where goods are produced, allowing production to move closer to consumers and cutting the costs of transportation and logistics.

Of course, no one knows with certainty how quickly such changes will occur, and every country should invest in education, technology, and infrastructure so that it can anticipate them better. For now, trade will continue to play a crucial role in allowing developing economies to grow rapidly. Although trade in physical goods may decline, trade in services will probably rise, as more and more services can be carried out remotely.

As a result, developing countries should seek to grow their service sectors, especially in the tradable sector. They should also invest in innovation hubs, which can help replace lost manufacturing jobs.

As developing countries advance into middle-income status, they can no longer offer cheap labor. Such places should follow China's lead by investing heavily in the high-tech sector. Doing so has helped China transition away from traditional manufacturing and leapfrog over some of its competitors in a number of promising new industries, such as robotics, renewable energy, mobile messaging, and e-commerce.

As the history of technological change has demonstrated, technology displaces only specific kinds of jobs; it does not displace labor, at least not in the longer term. But in the short term, automation renders certain kinds of human capital redundant. This can cause difficult and sometimes lengthy transitions, both for individuals and for whole economies. In the end, however, machines raise human productivity and increase incomes and prosperity. As the economists Erik Brynjolfsson and Andrew McAfee have explained, economies shift from creating jobs for which machines are substitutes to creating those for which they are complements.

Smart investment in job training can accelerate and ease these transitions. Policymakers should learn from the Nordic countries, where governments have combined training programs with various forms of income support and redistribution. Governments should not offer training only to the unemployed. Displaced middle-income workers, who often end up in lower-paying service jobs, can benefit from retraining that will help them compete for higher-wage work.

SAVING GLOBALIZATION

Predictions that the era of globalization will soon end are too pessimistic. To be sure, the rapid expansion of trade, rising cross-border capital flows, and, above all, the spread of new technologies have transformed the global economy. They have created difficult challenges, and countries will continue to struggle to increase growth and productivity, while reducing inequality and creating good jobs. But there are also enormous opportunities. Turning back the clock to restore the old frameworks is impossible. The challenge is to build new ones that work.

Waving the banner of protectionism and nationalism may attract popular support, at least temporarily. But history has shown that, ultimately, it may well threaten global peace and prosperity. The United States, China, and the world at large would be far better off if they could find a path to a more sustainable globalization, reforming the existing global order rather than tearing it down completely.

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