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Policy Brief
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Globalization: Is It Good or Bad?

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Globalization has become a cliché, though users of the word disagree, sometimes violently, of its consequences. Many believe that it has lifted, or potentially can lift, millions of people out of poverty permanently. On the opposite side, some passionately believe that it already has driven millions deeper into poverty and has to be stopped. Some academic analysts (e.g., Stiglitz) straddle the two beliefs: While conceding the potential benefits of globalization, they believe that the power structure of national and international institutions is such that it not only prevents the potential benefits of globalization from being realized but, perversely, turns it into a malign force hurting millions.

In order to separate the signals from the noise in the intense and ongoing debate on globalization, it is essential to define the term. I define it narrowly as the process of the dismantling of state-created barriers to trade, and the economic, social, and political responses to such dismantling. It is important to distinguish exogenous factors that, in (large) part, could be driving globalization from policies that affect globalization. For example, exogenous technical progress, by reducing not only the costs of production of goods but also the cost of transportation and communication, is a powerful force in stimulating international trade. It is important to emphasize that both parties that agree to a voluntary trade gain, so that trade is not a zero-sum game. Before turning to the current debate on globalization, it is worth recalling a bit of its history.

The first wave of globalization ran its course roughly from the middle of the nineteenth century to the outbreak of the First World War. It is no accident that it coincided with major technical innovations (steam engines, railways, steamships, telegraphs, and finally electric power and telephones) and the adoption of free trade as a policy by the then major trading nations. Keynes bemoaned its end with these words: "What an extraordinary episode in the economic progress of man that age was which came to an end in August 1914!" (Economic

December 2002

Consequences of the Peace, 1919). Indeed, the current wave of globalization is in many ways a resumption and acceleration of the first wave.

Attempts to resume the first wave at the end of WWI failed because the economic structure of the combatants' economies had been changed significantly by the war. This failure led to a rise in barriers to trade and repeated devaluation of currencies in a competitive process. The attempt to avoid such destructive competition after WWII led in 1947 to the General Agreement on Tariffs and Trade (GATT) which became the multilateral framework governing international trade until it was subsumed by the newly established World Trade Organization (WTO) in January 1995. By substantially reducing tariff and non-tariff barriers to trade, multilateral trade negotiations in GATT effectively launched the second wave of globalization.

The first two and a half decades of the second wave (1950-1973) saw an unprecedented and rapid rise in world merchandise trade, exceeding 8% per year. In the next decade and a half (1973-1990) that covered the two oil shocks, inflation in industrialized countries, and the onset of the debt crises, growth in world trade slowed considerably to 4% per year and then recovered to 6.5% during 1990-2000.

The Uruguay Round (1986-1993) brought new areas, such as intellectual property rights and trade in services (including telecommunications and financial services), under multilateral disciplines. In the last two decades of the twentieth century, a revolution in information technology and communication occurred, the communist empire in Europe fell, and forms of democratic government spread elsewhere. However, many developing countries were left out of the growth in trade and, particularly, in capital flows. Further, the growth in capital flows (particularly of short-term capital) was associated with an increase in volatility, which contributed to financial crises and contagion. It is natural that those left out of the growth of trade and capital flows and their potential benefits, as well as those who are hurt by the adjustment after financial crisis, see globalization as a malign force. Their perception is shared, particularly by idealistic young people in the rich countries. Is it valid?

The argument that globalization is a benign force is a corollary of the prime tenet of liberalism in the classical sense: In a world of free and competitive markets, people would choose what is best for them, which in turn would lead to a socially optimal outcome. The liberal tenet itself envisages a vital role for national governments and international institutions to ensure the provision of public goods, the existence of a legal and contractual environment for the efficient functioning of competitive markets, and that externalities as well as anti-competitive tendencies are addressed adequately.

The critics of globalization advance several arguments. In the real world, trade is far from free. Barriers against exports of poor countries are higher than those on exports of rich countries. Rich countries subsidize their agricultural exports, thereby driving poor producers of these commodities out of world markets. In the weighted voting mechanism of international financial institutions, a few rich countries in effect have a veto. Even in the one-country/one-vote, consensus-based decision making process of the WTO, interests of poor countries do not prevail. In sum, globalization is merely unfettered capitalism that makes the rich richer, the poor poorer, and undermines democracy. At a superficial level, all of these arguments would seem persuasive, but at a deeper level almost all are exaggerated, some are wrong, and others, though valid, are remediable.

Except in the Tokyo and Uruguay Rounds, to a large extent the developing countries (DCs) opted out of GATT, which set the rules of trading. Instead they articulated their complaints against the world trading system and demands for its change in the United Nations Conference on Trade and Development (UNCTAD), which has no role in making trading rules! To the limited extent they participated in GATT, they demanded and got a special and differential (more favorable) treatment (SDT). Indeed, a strong case can be made that by asking for SDT and preferential treatment from rich countries for their exports (through the so-called Generalized System of Preferences), they were in a weak position to influence the formation of the rules of the trading system. The weakness also meant that they could not prevent the rich countries from taking trade in textiles and apparel out of GATT rules against non-discrimination and the use of import quotas to restrict trade. In any case, with the share of developing countries' world exports being small, they could not realistically have expected to have an influence over the design of world trading rules. The DCs have a large share of the responsibility for the rules of the world trading system being tilted against them.

It is a fact that in rich countries, exports of developing countries not only face higher tariffs but tariffs rise with the stage of processing. It is also a fact that domestic support for and subsidization of exports of agricultural commodities are high in rich countries. Recognition of these realities certainly does not mean that DCs should emulate the rich countries and create barriers of their own and, in any case, that they should not unilaterally liberalize their trade. Rather, DCs should hold the rich countries to their commitment to reduce tariffs and eliminate subsidies in the ongoing trade negotiations. Also, not all DCs have the same interests – some benefit from cheap food, whereas others are harmed. Because the benefits to the DCs as a group (particularly sub-Saharan African countries) would be significant, a common stand by the group against subsidies has to be forged through mutual consultation and appropriate compensation for potential losers.

It is true that in the weighted voting system of the International Monetary Fund and the World Bank, the rich countries, which are ultimately the sources or guarantors of the resources lent by the two organizations, have almost a veto power. But once again, this power should not be exaggerated; even the United States by itself cannot overrule a decision if some rich countries join developing countries. Besides, even in the ostensibly one-nation/one-vote consensus system of the WTO, as I pointed out earlier, the developing countries have not been effective.

The claim that globalization has increased poverty around the world is wrong. An overwhelming majority of the poor in the world live in rural areas of China and India. But those two countries have opened their markets and the poor have benefited. China's income grew 10% annually for the past two decades, and the proportion of poor in its rural population fell to less than 5% in 1998 from 31% in 1978, according to official data. India also experienced an acceleration in growth to around 6% per year since it began liberalization compared with 3.5% in the previous three decades, and the proportion of the poor in population dropped from an average of 50% during 1950-1980 to an average of 25% in 2000. The countries in which poverty did not decline or even increased are mostly in sub-Saharan Africa. Their lack of progress is not due to liberalization but is rooted in deeper problems of conflicts and governance. Some estimates of the proportion of world population in extreme poverty (those with income less than one dollar a day in real terms) show that it declined from around 55% in 1950 to around 24% in 1992. Other indicators of poverty, such as life expectancy at birth, show great progress as well.

Globalization is, in essence, a process that creates opportunities for faster growth and more rapid poverty reduction in those poor countries in which the domestic economic and political environment is conducive. Countries in which corruption is endemic, the legal system is not effective or is corrupt, the financial system discourages risk-taking, and civil strife and conflicts with neighbors are pervasive surely are not fertile grounds for globalization to yield its fruits. The primary challenge for the DCs who have been left out of the globalization process is domestic: how to transform the domestic environment into one that is conducive to globalization.

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SIEPR Policy Brief

A publication of the
Stanford Institute for Economic Policy Research
Stanford University
579 Serra Mall at Galvez Street
Stanford, CA 94305
MC 6015

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