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Future tensed over globalization?

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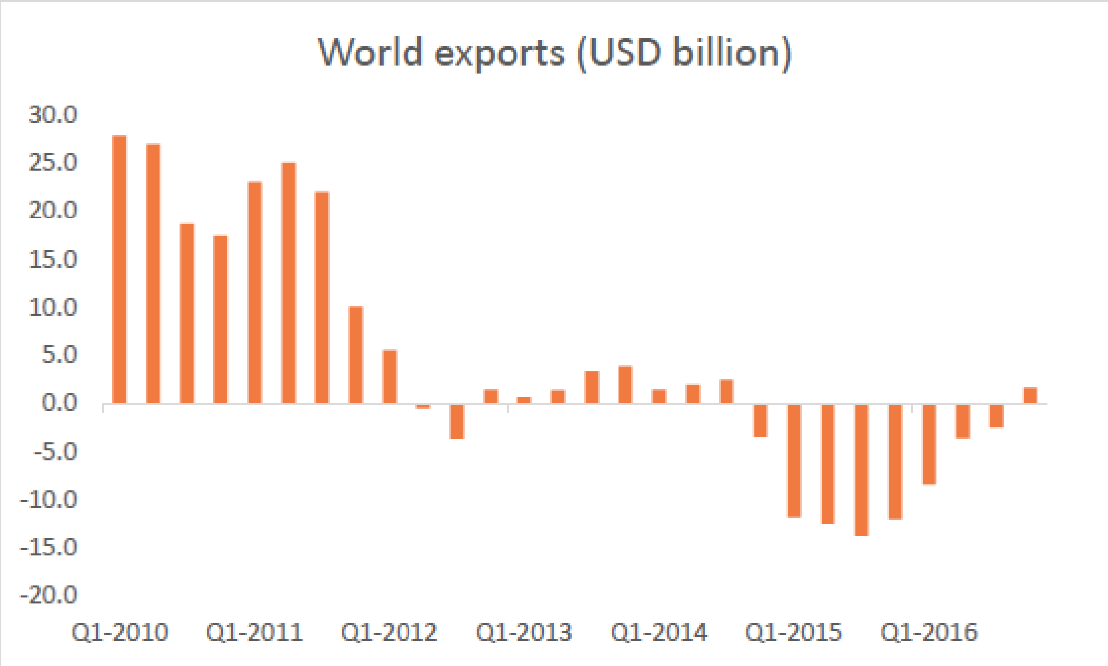
After the 2008 global financial crisis, G20 leaders signed a pledge in November 2008 to avoid protectionist measures in order to help speed up economic recovery and boost growth through increased trade. Ironically, protectionism has witnessed a concerning rise since then. Several countries, including the G20 countries, were reported as increasing trade restrictive measures.[1] Between 2008 and Oct 2016, a total of 1,671 trade-restrictive measures were recorded for G20 economies and only 408 had been removed. According to the latest data, World Trade Organization (WTO) recorded a moderate rise in G20 trade restrictions since October 2016.

Slow global growth post the 2008 financial crisis, together with this rising protectionism, appears to have impacted global trade volume, which has been declining since 2011 and was in the negative territory for two years till Q4 2016 (figure 1). In addition, rising anti-globalization sentiments and support for populist parties in the Western industrial nations are dominating political views even as mainstream policy makers of the Western industrial nations are seen co-opting policies to restrict free movements in goods, services, and resources— the factors that have been held responsible for the rising income inequality and marginalization of labor.[2] The year 2016 witnessed the traditional champions of open government and free trade—the United States and the United Kingdom—appeasing populism, while China staunchly defending globalization[3].

How big of a threat are these sentiments to the globalization process and its impact on growth, and are we already seeing a reversal of the process?

Figure 1: World trade has slowed since 2011



Source: International monetary fund, 2016

Globalization- a boon and a bane

It was not until the second half of the 20th century that globalization picked up pace benefitting many countries that were able to integrate as outward-oriented policies brought dynamism in the ways economies performed and greater prosperity leading to rising living standards. The global per capita GDP increased almost five-fold over the past three-and-a-half decades. Along with prospering nations, businesses and employment also turned more global and deeply integrated, facilitated by modern electronic communication and technology.

However, a lit candle also casts a shadow. Amid prosperity and opportunities, globalization has also helped create a widening gap between the world's haves and the have nots. The rising income inequality because of the profound changes in the workforce and society, asymmetric access to knowledge and skills, and shrinking welfare safety-nets have helped contribute to economic insecurity and social deprivation of those who have been left behind in this whole globalization gala. In addition, globalization has interconnected global risks arising from volatile capital movements and social, economic, and environmental degradation created by poverty and inequality, leaving low-income nations likely vulnerable to any external shocks, irrespective of the origin and time.

Consequently, some people belonging to the less secure strata of the society—those who perceive losing their jobs to immigrants or foreign competitors, have been unemployed for long, are at the low-end of the wage spectrum or are witnessing income stagnation, and are living on shrinking social benefits—are now raising their voice against the changes brought about by globalization. The anxiety of some about immigration and trade is now translating into a rising support for populism in several nations, including in the West, leading to policy uncertainty.[4]

Undoing globalization may not be the solution

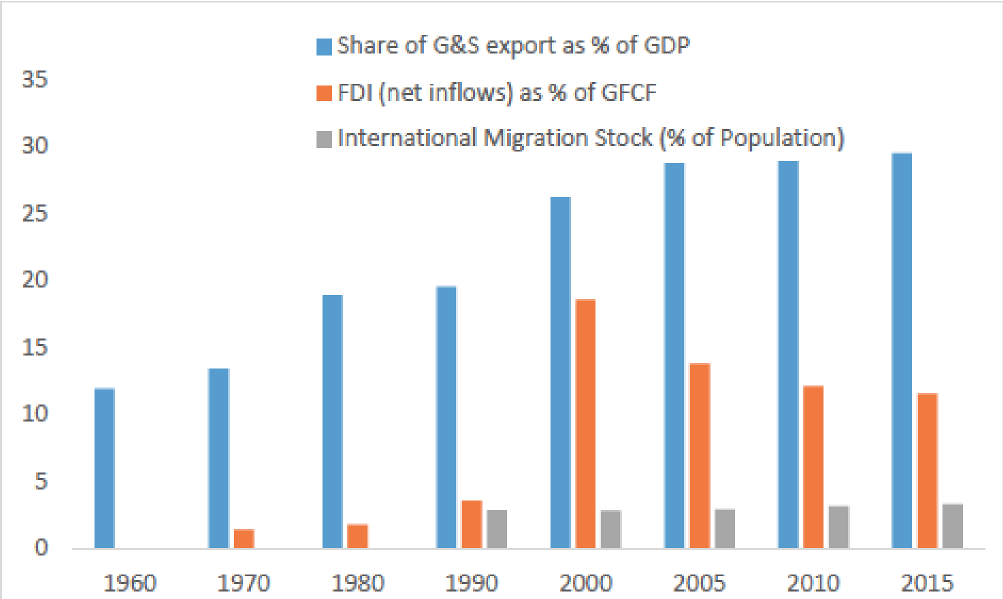
While it is true that many opportunities of globalization have not come without costs, should that be a sufficient reason to erect trade barriers and reverse the entire process? The answer may not be straight forward, but it might be important to highlight two factors.

One, the world isn't as flat as it is perceived.

While the world is believed by some to have become "flat" post 1980 because of rapid globalization, the truth is that globalization is likely far less advanced than is commonly perceived. Here are some facts that might be worth pondering about.

- The global foreign direct investment (FDI) inflows account for just about 10 percent of the world's gross fixed capital formation and the total international migration stock accounts for less than 3.5 percent of the world's population (figure 2).
- The share of global exports is less than a third of the world GDP (figure 2).
- Only 0.1 percent of the world's firms are multinationals generating 10 percent of the world GDP and more than 50 percent of the world's trade.[5]
- While the United States is perceived to be highly globalized, the share of trade relative to other nations is among the lowest indicating that the international business contribution is small relative to domestic activity.[6]
- While, it is true that emerging nations have widely practiced protectionist policies to safeguard local industries and jobs and deter competition, several advanced nations too have pursued restrictive policies for years. For instance, among the top ten G-20 countries that implemented the most number of discriminatory measures between November 2008 and the end of June 2017, five were advanced nations—the United States (ranked 1st), Germany (5th), UK (7th), Italy (8th) and France (9th).[7]

Figure 2. Export intensity, FDI, and immigration since 1960s



Source: World development index, 2016

Second, it might hurt economic entities more than benefitting them

A shift toward protectionism, which is lately being promoted among various policymakers across the globe, may not bode well for all nations, businesses, and consumers. Even in the past, nations pursuing protectionism often suffered an economic slowdown and inefficiencies.

- In today's day and age, the trade volume is too large and the interconnectedness is too complicated for business strategists and policymakers to ignore.
- Policy changes favoring localization are likely to impact several multinational corporates that have strategized toward shifting their operations beyond borders to seek new growth opportunities and benefit from the advantages of scale, access to resources, proximity to the market, and arbitrage opportunities.
- Disruptions in sectors employing low skilled labor and strong external linkages can result in cutting costs via layoffs or rising product prices that consumers have to pay from their pocket.

Awareness and targeted policies will likely be the key

A part of the problem typically is that benefits of globalization often go largely unrecognized, primarily because policymakers commonly have not highlighted them, while adverse effects often have been overstated. For example, globalization has been blamed for trends that are largely due to technological innovation, and automation. Roughly 80% of the manufacturing jobs that have been lost was because of innovation, automation, and new technologies.[8]

Policymakers should consider addressing the real cost of globalization, such as rising inequality and lesser opportunities for the marginal population, and promote inclusion to stem the rising populist sentiments. Targeted domestic policies, such as embracing better education, funding more job training and social programs, and providing a better social safety net, may help in addressing the anxiety of the displaced workers and dislocated communities and enable them to get back on their feet.

A better coordination between international and domestic policies may be essential that will likely warrant a uniform assistance program for labor upskilling, adjustments in capacity building in terms of capital investment and labor reforms, and the reduction of red tape.

Today, no man, or business, or a nation is an island, but a part of a massive, complicated interconnected system, thanks to globalization. The phenomenon that started several hundreds of years ago has resulted in greater interdependence and integration among nations. With freer movement of resources, increased trade and technology transfer, spread of knowledge, and cultural exchange, nations have seen unparalleled economic growth. Going backward and undoing globalization may impose more cost than reaping benefits and therefore, may not be the prudent way forward.

This is an abridged version of an article published in Global Economic Outlook, Q3 2017, Deloitte Insights titled "Why reversing globalization may not be a good idea". The full article is available on this link.

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5 Pankaj Ghemawat, "Globalization in the age of Trump", *Harvard Business Review*, July-August 2017, https://hbr.org/2017/07/globalization-in-the-age-of-trump
6 The shares of export and imports of the US relative to the GDP is low relative to other nations. This is supported by data from IMF. For more details, please refer to the original article titled "Why reversing globalization may not be a good idea", in Global Economic Outlook, Q3 2017, Deloitte Insights.
7 The ranking of G20 members is computed according to the total number of protectionist measures implemented since the first G20 Leaders' Summit in November 2008. The data is obtained from Centre for economic policy research, April 2015, April 2017. For more details, please refer to the original article titled "Why reversing globalization may not be a good idea", in Global Economic Outlook, Q3 2017, Deloitte Insights.
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