

EC 380: Lecture 12

Effects of Globalization

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Prologue

Recap

Previously

- Welfare gains and losses from trade agreements are complex and require case-wise assessment
- Market failures require direct government intervention through quotas, taxes and property right allocations
- Trade highly detrimental to environmental outcomes, both through production and transportation of tradables, but welfare gains may outweigh (Shapiro 2016).

Today

- Economic issues with respect to globalization patterns

What is it?

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The term is used broadly. We focus on international trade and some of the investment flows among advanced economies, mostly focusing on the United States.

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Understanding the relative costs and benefits can pave the way for alleviating problems **while sustaining the wider payoffs.**

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Followed by postwar **protectionism**, the Great Depression, and WWII.

History

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Second wave of globalization, which remains ongoing, though buffeted by periodic downturns and mounting political scrutiny.

History

"I saw that you could not separate the idea of commerce from the idea of war and peace. ... [and] that wars were often largely caused by economic rivalry conducted unfairly. ...I embraced the philosophy that...unhampered trade dovetailed with peace; high tariffs, trade barriers, and unfair economic competition, with war. ...[I]f we could get a freer flow of trade—freer in the sense of fewer discrimination and obstructions - so that one country would not be deadly jealous of another and the living standards of all countries might rise, thereby eliminating the economic dissatisfaction that breeds war, we might have a reasonable chance for lasting peace."

Cordell Hull, Secretary of State under President Franklin D. Roosevelt, written in his memoirs in 1948.

Era of Trade Liberalization

US import taxes dropped considerably post-World War II

Average US tariff rates on dutiable imports (1790–2016)



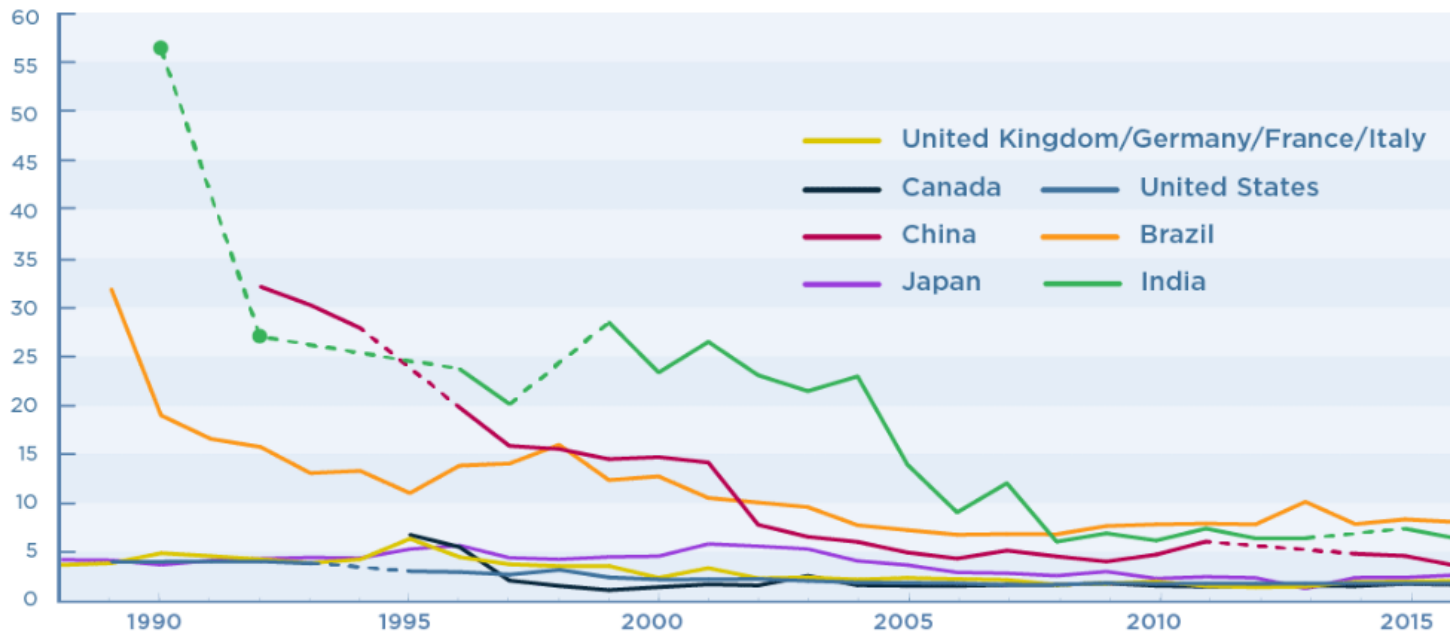
Note: Rates are weighted by trade value. Dotted line indicates years when data are not available.

Source: US International Trade Commission. Compiled by Douglas A. Irwin.

Era of Trade Liberalization

Major economies dropped tariff rates and kept them low

Average applied tariff rates (1988–2016)



Note: Shows world's ten largest economies, 2016. Rates are weighted by trade value. Dotted lines indicate years when data are not available.

Source: World Bank DataBank.

Global Value Chains

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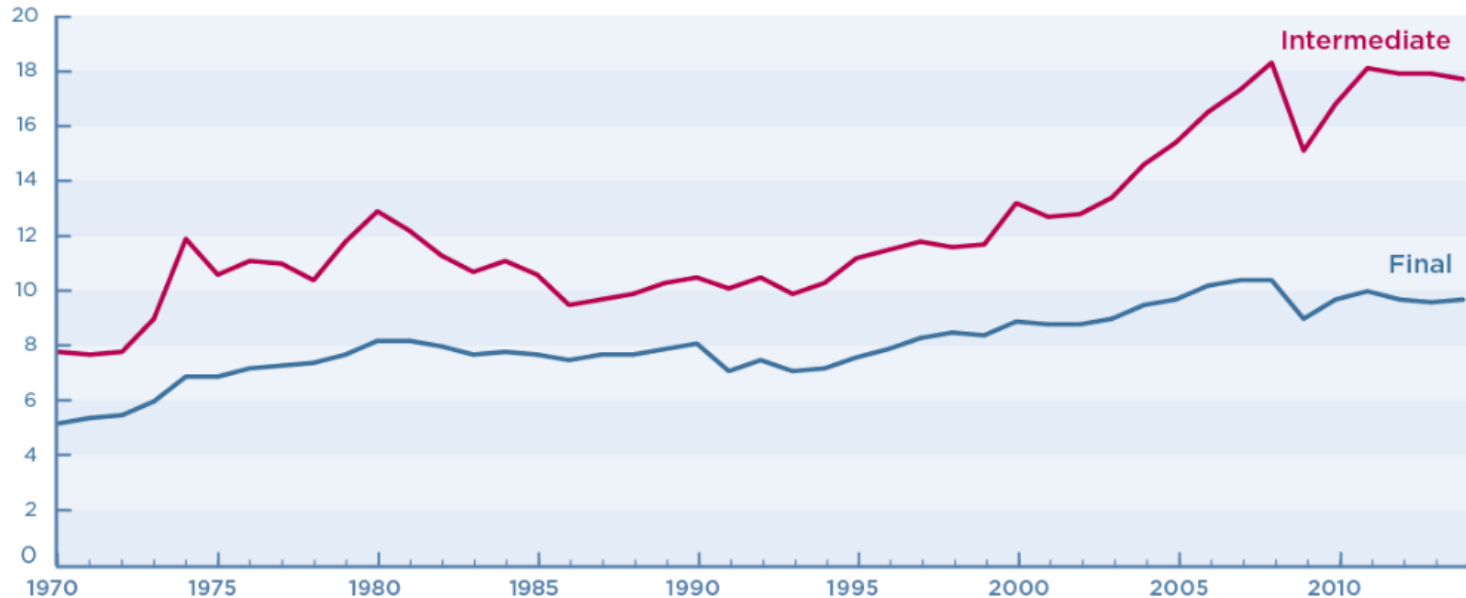
Today, **80 percent of world trade** is driven by supply chains run by multinational corporations.

Trade in intermediate goods is now nearly **twice as large** as trade in final goods and is especially important in advanced manufacturing, like autos.

Global Value Chains

Global supply chains dominate world trade

World trade in intermediate vs. final goods as percent of GDP (1970–2014)

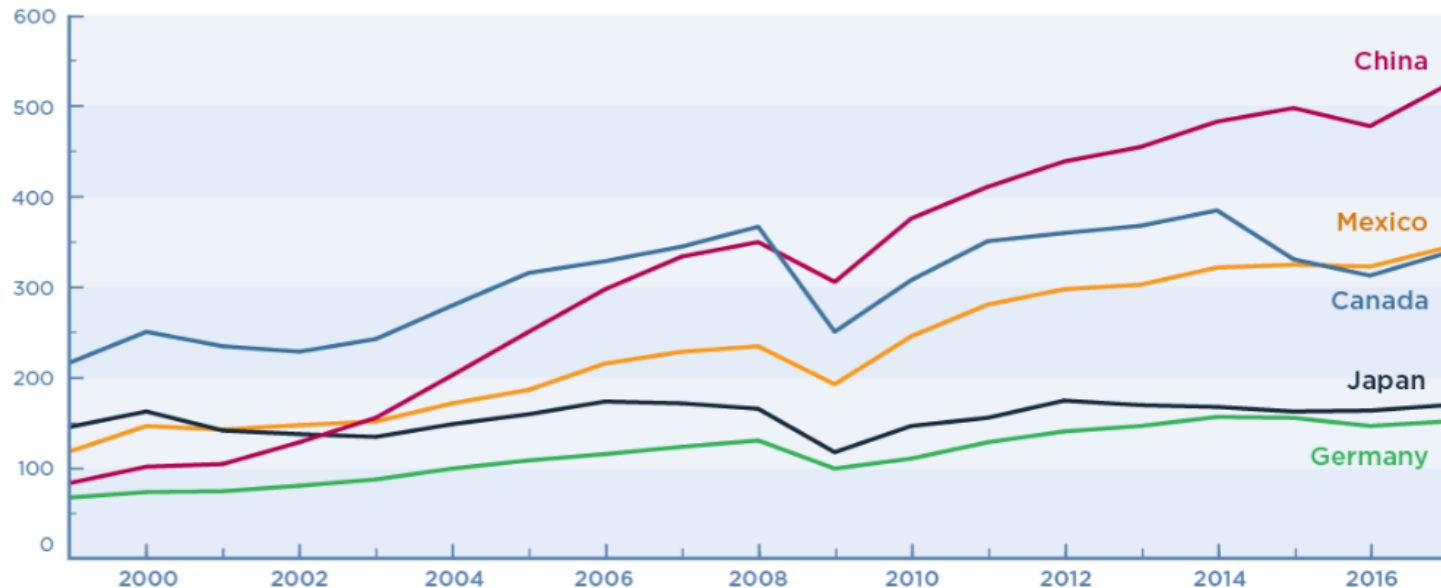


Source: Agustín Carstens, "Global market structures and the high price of protectionism," remarks at the Federal Reserve Bank of Kansas City's 42nd Economic Policy Symposium, Jackson Hole, Wyoming, August 25, 2018 (<https://www.bis.org/speeches/sp180825.pdf>).

Global Value Chains

China has become the biggest source of US imports

Top sources for US imports of goods and services, billions of dollars (1999–2017)



Sources: US Census Bureau/Haver; top trading countries from US Census Bureau (<https://www.census.gov/foreign-trade/statistics/highlights/top/top1810yr.html>).

Financial Integration

Separate from trade in goods and services, global **financial integration** is a much-debated but important topic. Here is a quick summary.

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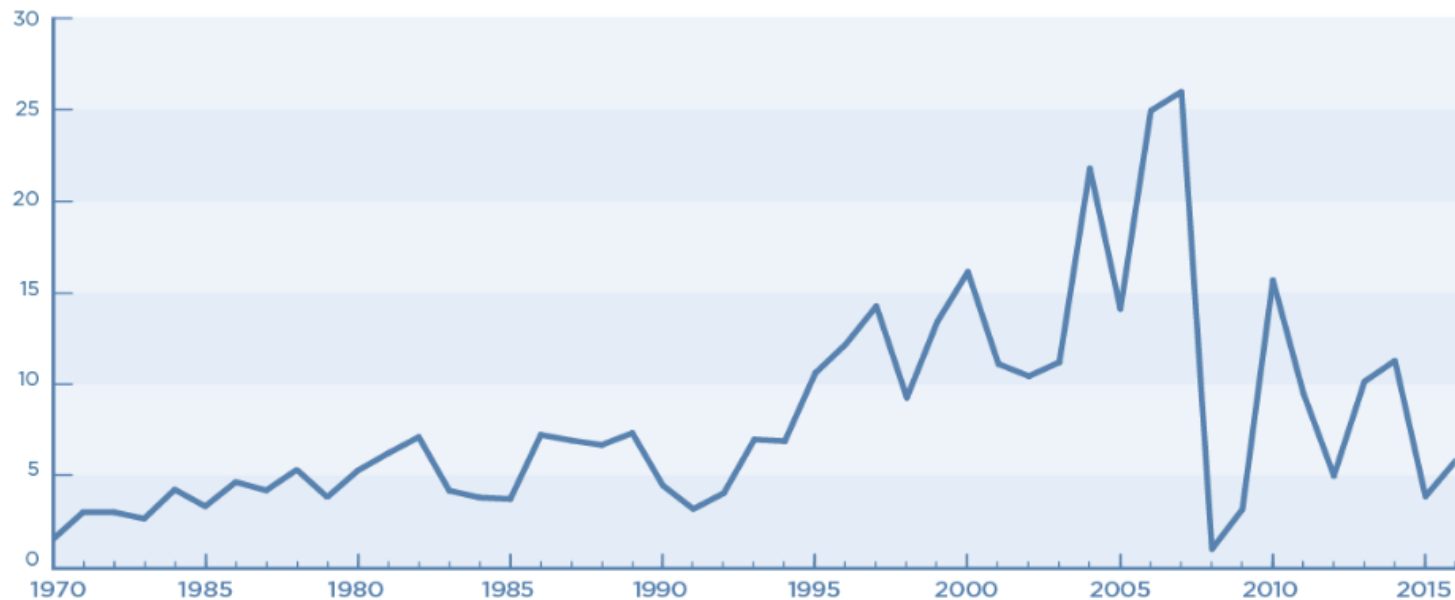
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- US flow of foreign investments has been **declining since 2008**, off-trend from previous stance.
- Many countries have **large international financial flows** or investments, consisting of assets and liabilities (FDI, securities, and debts).
- Countries have become susceptible to **sudden stops and surges** in these flows, leading to greater economic volatility for developing nations.

Financial Integration

Globalization also encompasses the purchase and sale of financial investments

Yearly US transactions in foreign assets plus liabilities as percent of GDP (1970–2016)

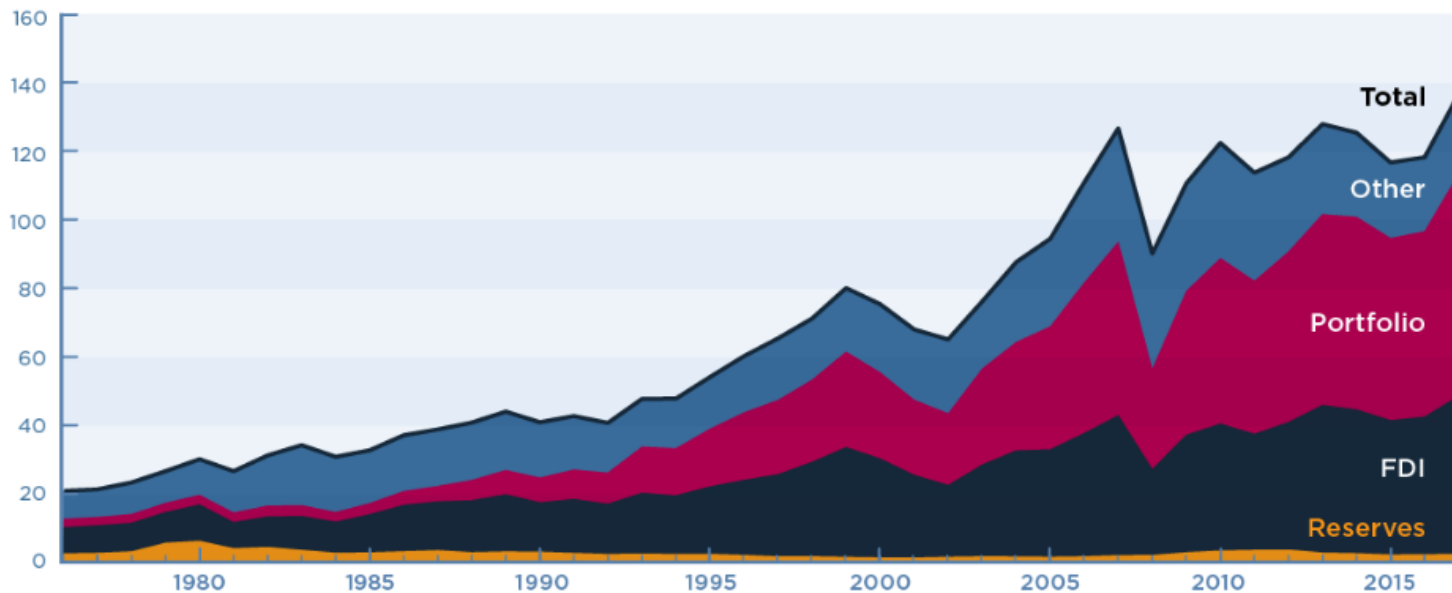


Source: IMF Data Warehouse.

Financial Integration

Some types of investment are relatively stable. Others are more volatile.

Composition of US foreign assets as percent of GDP (1976–2017)

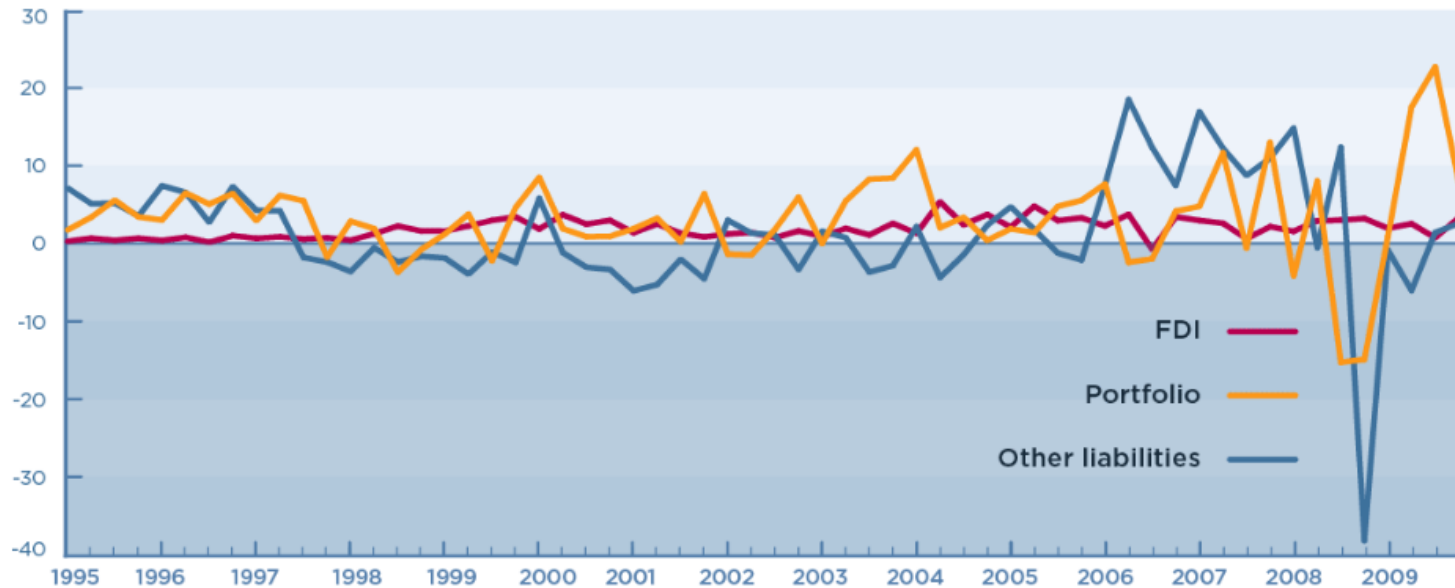


Source: Bureau of Economic Analysis.

Financial Integration

As a result of financial globalization, countries can be susceptible to crises from sudden stops in capital inflows

South Korea's financial account liabilities, billions of US dollars (Q1 1995–Q4 2009)



Source: IMF Data Warehouse.

Goal of Globalization

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Free trade and the **rule of law** were mainstays of the system, helping to prevent most economic disputes from escalating into larger conflicts.

Key Institutions



IMF

**International
Monetary Fund**

Established 1944
190 member countries

Works to stabilize the system and help countries facing balance of payment and debt crises.



UN

United Nations

Established 1945
193 member countries

Seeks to prevent conflict with global security norms and assistance for humanitarian crises.



World Bank

Established 1945
189 member countries

Founded to help reconstruct postwar Europe, it now provides loans and policy advice to developing countries.



WTO

World Trade Organization
Established 1948, as the General Agreement on Tariffs and Trade (GATT)
Replaced 1995, by the WTO
164 member countries

Sets rules for international trade and adjudicates trade disputes. Member countries agree to WTO rules, but can also negotiate free trade agreements with each other. The United States has trade deals with 20 countries.



NATO

**North Atlantic
Treaty Organization**

Established 1949
30 member countries

Bulwark of Western security alliance.

Effects of Globalization

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- More goods at lower prices through exploiting comparative advantages
- Scaled up enterprises, multinationals, allowing for large-scale technological developments
- Better quality and variety of goods, as a result of increased product-level competition
- Supports new job opportunities but also contributes to job displacement.

Globalization: Jobs

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Represents **less than 1%** of the workers laid off in a typical year.

Globalization: Jobs

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Better-paying positions have opened up in manufactured exports - especially in **high-tech areas**, such as computers, chemicals, and transportation equipment.

Globalization: Income

Decline in global income inequality but **has risen in the US**.

Globalization helped narrow inequality between poorest and richest people in the world, number living in extreme poverty cut by half since 1990.

A **consensus of scholarly work** holds that globalization contributed marginally to rising US wage inequality (10% to 20%).

Leading explanation - technology reducing low- and middle-wage worker demand and increasing demand for high-skilled, higher-paid workers.

Countries exposed to globalization have alleviated inequality to different degrees through tax and welfare systems. US has done **the least among advanced economies** to mobilize government policies **to reduce inequality**.

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We've seen some of this in our review of Autor et al. (2016)

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The same is true of US firms that invest abroad.

Globalization: Why Support?

Between 1950 to 2016 trade expansion

- Increased size of US economy by 2.1 Trillion USD, 18k per household every year
- US manufacturing employment +100k from job creation, -200k from import competition dwarfed by overall -4 mil between 2001-2016
- 51 to 1 payoff to US GDP compared to wage losses of affected workers since the end of WWII.

Wage losses are temporary while the gains are recurrent and accumulating over time.

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Source: Gary Clyde Hufbauer and Zhiyao (Lucy) Lu, The Payoff to America from Globalization: A Fresh Look with a Focus on Costs to Workers.

Public Views

How do Americans feel about globalization?

- Listening to the debates can be confusing.
- Not surprisingly, polls vary widely depending on how and when the question is posed.
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Public Views

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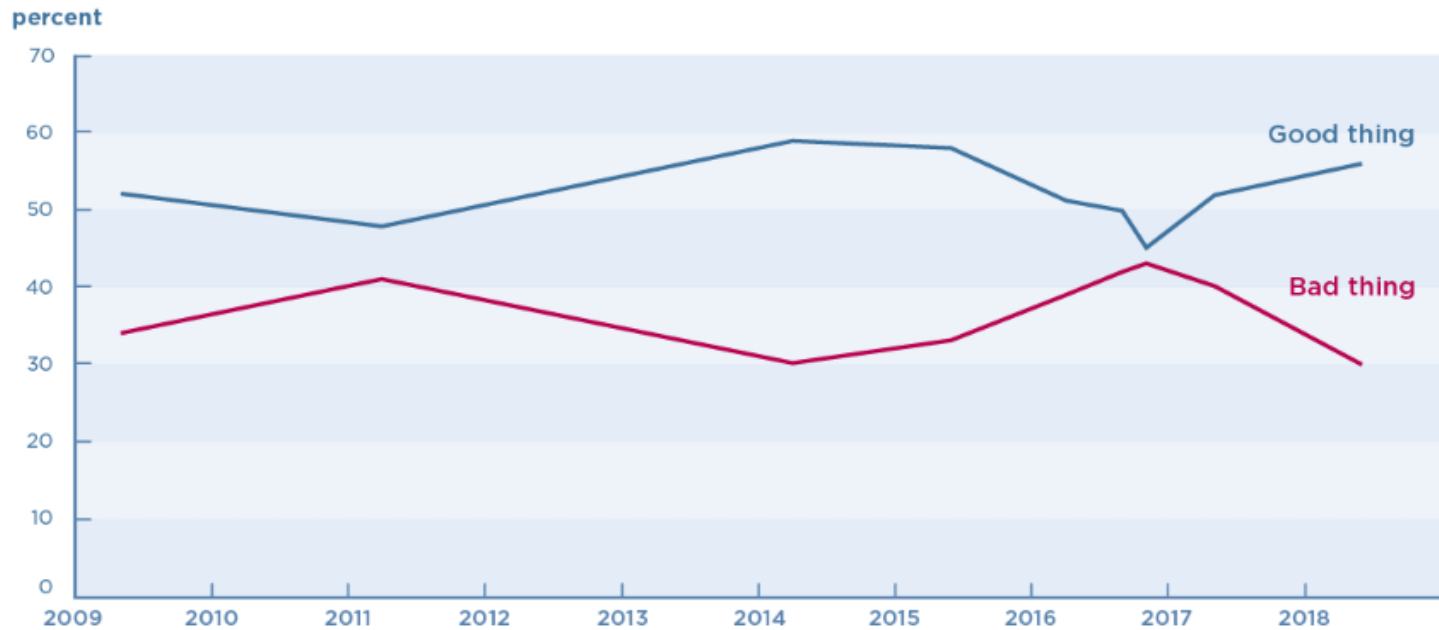
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Not helped by the US's inaction at helping temporarily displaced workers

Public Views

Survey Question:

In general do you think that free trade agreements between the United States and other countries have been a good thing or a bad thing for the United States?



Source: Pew Research Center.

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President Trump canceled TPP and threatened withdrawing from NAFTA, the Korea-US Free Trade Agreement (KORUS) and the WTO. The Trump administration pushed for more power to impose tariffs.

Policy Action

The global economy has yielded enormous economic gains for the United States, but **problems undoubtedly remain**.

- Abuses within the system and rules need to be updated.
- Trade agreements should account for the modern digital age.
- Disputes continue on the trade of certain goods - flooding other markets too much, industries being subsidized, lingering protections on specific goods or economic sectors, etc.

Solving these issues, which will inevitably arise and change over time, is best done through negotiation and coordination with trading partners

Policy Action

Ideally, stakeholders aim to prevent costly trade wars, where more and more barriers end up hurting all sides.

- Trade negotiations can only go so far. Not enough done to help those who have lost out from import competition.
- Manual work is increasingly being automated, lowering demand for workers. Wages stagnant, as health care and higher education costs rise.
- Inequality is widening.

Policy Action

Here are some of the crucial areas that economists have proposed the United States should focus on:

- Invest in better and more inclusive education.
- Give all displaced workers sufficient financial and administrative support
- Address growing income inequality through the tax system and spending programs.
- Make sure the healthcare system does not impede workers from finding new jobs
- Coordinate with allies to confront trade abuses.