The Seventeenth Annual John Bonython Lecture

THE CENTRE FOR INDEPENDENT S T U D I E S

trading phobias

Governments, NGOs and Globalisation

Anne Krueger

the The Centre for Independent Studies



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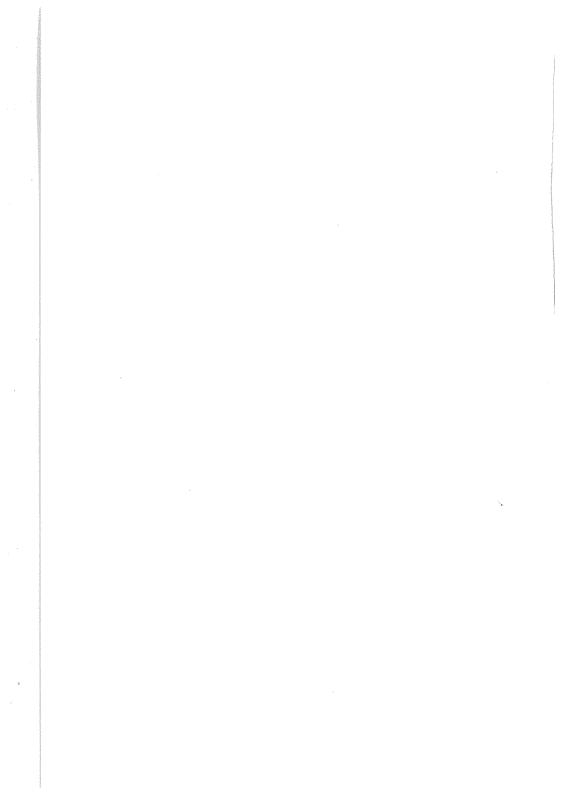
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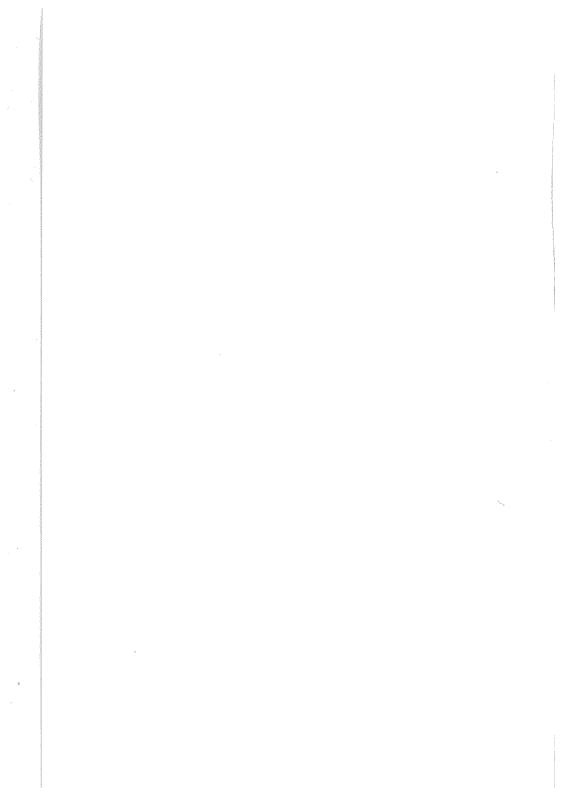
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About the Author

Professor Anne Krueger is Director of the Center for Research on Economic Development and Policy Reform at Stanford University. She is an expert in trade, international economics and the multilateral trading system; the role of multilateral institutions in the international economy; and financial institutions, corruption and economic development.

Her recent publications include *The WTO as an International Institution* (University of Chicago Press 1998), *Trade Policies and Developing Nations* (Brookings Institution 1995), and *American Trade Policy: A Tragedy in the Making* (American Enterprise Institute 1995).





Opening Remarks

Alan McGregor Chairman, CIS Board of Directors

ood evening and welcome to the 17th annual John Bonython Lecture of The Centre for Independent Studies (CIS). It is my special pleasure to welcome Professor Anne Krueger here, the 'global warrior' as *The Australian* called her on the weekend, and we look forward to her Lecture tonight. To those companies and supporters who have organised tables for themselves and their guests, many thanks to you. Finally, I should like to add my special thanks to Macquarie Bank who once again have shown their commitment to the Centre and its work by sponsoring the Lecture as they have done for the last few years.

The John Bonython Lecture was established in 1984 and named after the late John Bonython of Adelaide, who was the first Chairman of the Centre's Board of Trustees as it was then. The principal purpose of the Lecture is to examine the relationship between individuals and the economic, social and political elements that make up a free society. Over the years, the Lectures have been presented by an extraordinary range of speakers across many disciplines including, for instance, Nobel Laureate James M. Buchanan, former Czech Prime Minister Vaclav Klaus, Peruvian novelist Mario Vargas Llosa and the Chairman of News Corporation Rupert Murdoch, amongst others.

For anyone who is not a member of the Centre or involved in some way, I urge you to consider doing so. There are very few organisations like CIS in Australia and New Zealand, unlike, say, the United States where think tanks have an increasingly important role in public debates and the formation of good public policy. Having said that, CIS is now the largest and most recognised of the independent policy organisations. In the past

12 months for instance, its output and the quality of it, has been remarkable. Its recognition by way of media coverage has never been higher, and its membership and support growth at present is vigorous.

Yet we believe its best years are to come. In 2001, the Centre turns 25, a remarkable achievement given its origins and its steadfast determination to remain independent of any forces that may try to divert it from its mission. So tonight's Lecture may well be regarded as the start of its 25th anniversary celebrations with 2001 bringing a wide range of new activities to the attention of the public. In the weeks following the Lecture you will no doubt be hearing from the Centre's Executive Director Greg Lindsay, and I urge you to join those many people who are becoming a part of this very important Australasian institution.

Following the first course, Professor Krueger will be introduced by Professor Richard Snape, a long term colleague. Her Lecture will then follow. A short question session will take place after the main course. It remains for me now to say that I hope you have a great night.

Introduction

Professor Richard Snape

n introducing Anne Krueger, it is difficult to know where to start or finish, and one could talk about her achievements for the whole evening. I am not going to do that, but I will share a few bare facts.

Anne Krueger is Professor in the Department of Economics at Stanford University, and is Director of the Center for Research on Economic Development and Policy Reform at Stanford. In the 1980s she was Vice President for Economics and Research at the World Bank, where she confronted and reformed an environment heavy in planning models and *dirigiste* philosophy. She convinced the powers-that-be of the need for the Bank to take macroeconomic adjustment, market economics and open trade regimes seriously—changes which have had a lasting legacy in the Bank, and in developing countries.

Anne knows Australia very well, having visited regularly since 1973. But her interest is deeper than that. Her parents were Australian, emigrating to the US a few years before Anne was born. She has many distinguished Australian relatives, including her uncle, the late Senator Sir Reg Wright, and the late Professor Sir Roy Wright, generally known as Pansy Wright before it had that connotation, Professor of Physiology and later Chancellor of the University of Melbourne.

Anne is a prolific writer and publisher—44 books written or edited at my last count, with more coming. She has made seminal contributions in the trade and development area in particular, including cross country studies which have been the foundation of academic and policy advice. She also wrote the seminal analytical article on rent-seeking, a term that she invented.

Very many honours have been bestowed upon her—President of the American Economic Association, and honorary doctorates from Georgetown, Hacettepe (Turkey) and Monash Universities. She is a Member of the US National Academy of Science, Fellow

of the American Academy of Arts and Sciences and of the Econometrics Society, recipient of the Robertson Prize of the National Academy of Science in the US and of many other awards. Currently, Anne is a member of the US Congressional Trade Deficit Commission, which is to report in the next few months after the US elections.

I present to you Professor Anne Krueger, who will speak on 'Trading Phobias: Governments, NGOs and Globalisation'.

Trading Phobias *

Professor Anne Krueger

It is a great honour to give the annual John Bonython lecture. Not only was Mr Bonython's leadership in aiding the establishment of The Centre for Independent Studies a significant contribution, but I am honoured to follow in the footsteps of many earlier eminent speakers in this series.

For the past several years, journalists, policymakers, and others have been mesmerised by what they call 'globalisation'. On one hand, we are told that we have entered a new era, that the world has recently become linked in a way that never happened before, and that the 'new economy' has replaced old ways of doing business with consequent increased rates of economic growth and untold other benefits. At the same time, protesters castigate globalisation and the multilateral economic institutions, and seek to reverse the progress of the past several decades in liberalising international transactions.

The apparent contradiction between the manifest benefits of globalisation, however defined, and the outcry against it, is the topic of this lecture. Almost any dispassionate analysis of the evolution of the world economy will find that the past few years have seen better economic performance by almost all measures; that the past 50 years have witnessed increased well-being of a larger percentage of the world's population by a greater increment than ever before in history; and that the recent changes in the structure of the world economy do not really appear to be all that different from rapid paces of change in some earlier eras.

It is therefore a puzzle that globalisation is being blamed, and that protests seem to be the order of the day. In this lecture, I shall first discuss globalisation and the growth of the

^{*} I am indebted to Robert Bryan McNary for very helpful research assistance in tracking down the data on globalisation used in this paper.

international economy, and then address the key question: why, in the midst of all this apparent success, are the protests so vehement and apparently well-received by so many? Based on this analysis, I finally ask what can be done to assure the continuing benefits of globalisation.

What is alobalisation?

Interestingly, in all the discussions of globalisation, there is no clear definition of what it is. Sometimes the meaning seems to be simply that the communications media—television, internet, etc.—have made all of us much better informed as to events in the rest of the globe. In other instances, globalisation seems to refer to the increased importance of international transactions in affecting domestic economies. Still others seem to have in mind a phenomenon by which economic agents in any given part of the world are much more affected by events elsewhere in the world.

For my purposes, I shall accept this last definition. It is, in many ways, the broadest of the three, and I suspect it better captures the thoughts behind the angst of the protesters that will be discussed later. On this third definition, which I shall use, the globe is becoming increasingly economically integrated, and the process of doing so is the process of globalisation.

An interesting thing about this definition is that globalisation has been going on for a very long time, and economic integration has been increasing almost throughout recorded history. It is unclear when to date the beginning of the process: with the transSiberian (and perhaps Polynesian) migrations of 50,000 years ago? With the explorations of Alexander the Great? With Marco Polo? The spice trade? And what of the printing press? True, not many could read, but it certainly enabled the communication of ideas and information over much greater distance without face-to-face encounters than had earlier been possible. And early globalisation no doubt increased contacts between peoples on the same continents before it increased contacts between continents, but both processes undoubtedly have been going on for a long time.

Most economic historians, however, focus on two episodes in economic history. The first is the period of great discoveries, from about 1490 to about 1550. During that period, of course, Columbus discovered the New World, and sailing ships greatly increased their range. The second is the period from 1790 to about 1840, when steam power became important for transportation (especially sea-going vessels) and for powering machinery. During this latter period, transportation costs evidently fell fairly steadily and remarkably: Douglas North estimates that the cost of shipping a bushel of wheat across the Atlantic fell by 97% between 1790 and 1900 (part of this decline in costs was due to the eradication of piracy so that vessels did not have to carry heavy armament on their decks). Already by 1800, it is estimated that per capita income in Europe had been growing at about 0.5% per year for several centuries.

The second wave of falling transport costs—from 1790 to 1840—enabled the economical shipment of many more goods than had been feasible at an earlier stage. Earlier trade had been confined largely to high value, low bulk commodities such as spices. The very fact that they were high value indicates that their consumption was mostly confined to the relatively rich. By the 19th century, however, bulk commodities—wheat, other grains, minerals, etc.—could also be economically shipped, and cost differentials between countries fell drastically. Then came the railroads, with further declines in transportation costs. When refrigeration became feasible, the range of goods that could be shipped widened substantially.

Thus, the volume and value of both interregional trade within countries and international trade both in absolute terms and as a proportion of economic activity rose sharply in the first half of the l9th century due to falling transport costs. The discovery of the telegraph greatly shortened communications time—the laying of the transatlantic cable, for example, is estimated to have cut settlement times between New York and London from ten days to three hours. (It is often forgotten that, several decades earlier, the growth of the House of Rothschild was greatly facilitated by their being the first to use carrier pigeons to carry business news between London and Brussels).

By the middle of the 19th century, as is well known, tariffs and other trade barriers were falling sharply as well, especially for European countries. That also intensified trade flows. By that time too, Japan was beginning to open up; trade with China was increasing; and the earlier economic integration—often involving integration of village economies 20 miles apart—which had been primarily confined to Europe, became a much more genuinely global phenomenon.

During the 19th century, living standards were already rising at a rate much more rapid than had earlier occurred. They rose in part because of the direct contribution of falling transport and communications costs. But, in addition, they rose because of the benefits of increased economic integration: cheaper grains and minerals for Europe, cheaper machinery for the United States, etc. A larger market area permitted economies in production that could not be realised when, for example, almost all furniture could only be economically produced within a few miles of the building it was to occupy. The United Kingdom was the lead industrial country in the 19th century; it is thought to have had the most rapid growth of per capita income of any country in the world—just less than 1.5% annually.

If one seeks the period which is often being most closely contrasted with our own, it is the late 19th century. During that period, electricity came into its own, and of course the automobile (along with discoveries of petroleum) revolutionised the ease and convenience of transport for business and personal activities. Electric power in turn had a great deal to do with the introduction of assembly-line techniques, but those also required the larger market that low transport and communication costs permitted. There is strong evidence¹ that total factor productivity growth increased with a lag of about ten years, and that electricity provided much of the impetus to more rapid economic growth and a faster rate of increase in living standards.

Since the introduction of the automobile and electricity, there have of course been further innovations and further declines in transport costs. Ocean shipping added about 30% to the free on board value of exports in the late 1940s; that figure had fallen to

3% by the late 1990s. And it is estimated that the cost of a three-minute phone call from New York to London fell, in constant dollars, from \$244.65 (1990 dollars) in 1930 to \$188.50 in 1940 to \$53.20 in 1950, \$31.58 in 1970 and \$3.32 in 1990. There is now discussion that breakthroughs in fiber-optics will soon permit free international calling, much as there is already free intra-city telephoning in the United States. The average air transport revenue per passenger mile, over that same period, has fallen from \$0.68 to \$0.11. In addition, the ability to ship goods speedily by air enabled all sorts of transactions that could not earlier occur: for example, Hong Kong assemblers of high-fashion apparel were, by the 1970s, accepting early-morning orders from New York for replenishment of retail inventories, shipping the goods by air 12 hours later, so that they arrived in New York the next day.

In the postwar years, declines in costs of transport and communications were significant, but less important than fairly dramatic drops in the levels of protection. The result has been at least a doubling of the relative importance of international trade in GNPs of most major countries. Even in the United States, which has historically had a low trade-GNP ratio because of its large continental size, exports rose from just over 4% of GDP in the 1950s to 10.6% in the 1990s, while imports rose from about 4% to 12% of GDP over the same period. Trading volumes are a larger proportion of GDP than ever before in most countries. By contrast, net capital flows are still not as large as they are thought to have been in the late 19th century, although their rate of increase is sufficiently high so that they may become equally important—on present trends—within another decade. And, of course, the volume of international currency transactions is now huge.

That increased integration through trade has contributed to economic well-being cannot be doubted. Not only have goods become available more cheaply and the varieties available increased due directly to reduced barriers to trade, but in addition, the availability of foreign supply sources has increased the competitive environment within which all firms operate,

with attendant improvements in quality and services surrounding the goods, as well as much smaller opportunities for monopolistic pricing.

Now, of course, we have the information technology revolution in the late 20th and early 2lst century. In addition, there are major developments in materials technology and in biotechnology that may, a century from now, be regarded as even more important. But, for whatever sets of reasons, focus today seems to be on information technology, including especially the internet with its potential for b2b business and low-cost communications. Whether it is better economic policy, increased trade flows, or the internet, the world economy is thriving, and the American and global economies are in an unprecedented period of expansion and non-inflationary growth.

We care about all of these things, of course, because they have delivered standards of living never before regarded as possible. In the industrial countries, living standards of almost everyone are well above what was thought feasible even for the few a century ago. Integration with the world economy has permitted the transformation of poor developing economies such as Korea and Taiwan into industrial economies with relatively high standards of living within a space of 30-40 years. The open economies of the industrialised countries have permitted rates of economic growth and of rising living standards for developing countries with appropriate policy stances that were regarded as absolutely impossible only a few decades ago.

And for those who question per capita GDP figures as measures of well-being, other corroborating evidence can be found. Life expectancies have risen sharply, from 48 to over 70 years in the United States over the 20th century; and from 39 to 60 years in India since 1950-55. In Korea, the increase was much more dramatic, as life expectancies were much like India's and are now almost the same as in the U.S. Infant and child mortality has fallen dramatically, other indicators of health and nutrition are greatly improved, educational attainments of the populations are greatly increased, and so on. Indeed, it is hard to dramatise how greatly things have improved for almost all of us. Literacy

rates in developing countries have risen from an average of 40% in 1950-55 to 70% in the 1990s.

Why all the concern?

In the midst of all the unprecedented prosperity, there nonetheless appears to be a considerable backlash—or at least sympathy with those who are protesting—against globalisation. This backlash was highlighted by the events in Seattle, and subsequent meetings of the international economic institutions have brought further organized protests. I will argue later that the Seattle protests were not what led to failure of the meetings (although some of the issues raised by those concerned about globalisation contributed to the meeting's failure). But quite aside from Seattle, it seems clear that there are large groups who are at least to some degree dismayed by the ongoing process of economic integration.

In light of all the benefits that increasing integration of the international economy has brought, this seems highly puzzling. At first, it is tempting to dismiss the malaise and the protests as Luddite in nature, with even less basis than those who opposed change several centuries ago had for their fears.

In fact, to do so would probably be a mistake. While it is simple to scoff at protesters who claim that the World Bank is harming poor people (when in fact the most negative case that could be made is that it is helping them less than it might) or that trade is impoverishing millions whose lot has in fact improved, it would be risky to do so. For, whether the unease is firmly grounded in reality or is instead based on irrational fears of the unknown, there are risks that failure to address it could lead to a serious backlash against the international economy, and with it, political pressures to resurrect trade barriers and reverse the potential future benefits of further increases in integration.

The big risk, probably, is that a slackening or slowdown in the rate of economic growth—especially in the United States which has been the leader both in the accelerating pace of economic growth and integration and in the move toward more

open markets—could lead to a sufficient downturn in economic activity to trigger a backlash amongst those who are now silent, but not necessarily supportive, of globalisation. Protectionist pressures always increase during downturns, and, should those pressures be translated into strong protectionist measures, there could be a real risk of reversal of the liberalisation of the past half century. If that happened, it would of course intensify the downturn, and could also reverse the long period of successful economic growth that the world has enjoyed. Such an outcome would deprive many of those in industrialised countries of a more prosperous life; it would also, and perhaps more seriously, deprive many of the very poor in developing countries of a chance for rapid improvement in their condition as happened in Korea and other countries during the heyday of trade liberalisation.

So let me attempt to fathom what underlies the unease. Because it is the country I know best, and because the benefits of rapid economic growth are so visible in the United States, let me focus primarily on American developments. There are no doubt different weights attaching to specific aspects of integration that arouse concern in other countries, but I suspect that the overall mix is not significantly different.

A recent article in the American *Mercury News* attempted to summarise the protesters' discontents as follows:

Isn't economic globalisation exacerbating income disparities around the world, where more than half the people on Earth live on less than \$2 a day? People are worried that the interests of the business and financial elites are trumping widespread concerns about disappearing forests, sustainable development, worker rights, and other issues of fundamental human importance.

These questions underlie the antiglobalisation feelings that exploded into the mainstream on the nightly news at the World Trade Organisation's disastrous meeting in Seattle in December...²

Obviously, there are several elements all mixed together. First, there are expressed fears and concerns that are just plain wrong.

There, education and discussion seem to provide the only appropriate remedy. Second, there are criticisms of globalisation that address phenomena that are largely the result of other factors in ongoing evolution. These, I will argue at the conclusion, are probably issues which require addressing both because they have legitimacy in their own right but also because if they remain unaddressed the danger of serious reversals of globalisation increases. Third, there are criticisms which have some validity and where the difficult issue is finding remedies that do not undermine the very process of globalisation which is so valuable.

Turning first to the grounds for unease, there are several. A first concerns an unease that national governments may no longer 'be in control'. A second focusses on income distribution and, in particular, concerns that the rich are getting richer while the poor are, at best, being bypassed by globalisation. A third, related to the second, focuses on trade as the source of increasing disparities in workers' *earnings*. Fourthly, there are assertions that, despite higher pay and good jobs, many employees are more economically insecure than ever. Fifth, some argue that the international mobility of capital either has done significant damage or poses grave threats of doing so. Sixth, concerns are expressed about the environment and other 'human values', as was reflected in the newspaper quote I cited.

Let me address each of these in turn. The sense that somehow control has been lost is often cited as a factor in the globalisation backlash. International capital markets are seen to be dictating to governments, as Thomas Friedman in *The Lexus and the Olive Tree* is at pains to point out. And employees are concerned that their management no longer has control, as it once did, over the market in which it operates. To a degree, of course, this loss of control is real. But much of it is fancied in at least two ways:

1) it is unclear how much 'control' individual manufacturing firms or farmers had over their fortunes in earlier eras; and 2) much of the 'control' that was there was the 'control' that goes with monopoly power. Insofar as globalisation has reduced monopoly power and reduced control, that is an outcome of which most would approve.

However, to the extent that this sense of loss of control is blamed on the multilateral economic organisations, there are measures which can be taken, some of which probably are meritorious in their own right in any event, which may ameliorate the problem. I return to this in the final section.

Turning to the misperceptions, any reading of economic history suggests that small-scale producers, the self-employed, workers, and farmers probably had a great deal less control over their economic lives 200 years ago than they do at present. In part, this is because increased affluence means more independence from the employer; in part, legislation and conventions governing employment have provided grievance and representational procedures; and in part the greater mobility of the labour force gives individuals more choice over where they wish to work.

Even when one thinks of capital flows and the impact of their reversal into Thailand, Korea, and other East Asian countries three years ago, those who were adversely affected were laid off, or threatened with layoffs, from jobs paying eight times what they did 30 or 40 years ago. While the social safety net was inadequate to the level of development that had been achieved, that level of development could not have been achieved without capital flows. It is often forgotten that the United States, other lands of new settlement, and even the European countries experienced periodic financial crises in the 19th and early 20th century (not to mention the Swedish and Japanese experiences within the past decade or so). There is of course a challenge to provide better macroeconomic management and stabilisation in light of these capital flows, but the appropriate remedy seems to be strengthening the mechanisms of macroeconomic policy, rather than greatly reducing the undoubted gains that have arisen when poor countries with relatively realistic economic policy stances have been able to accelerate their rate of economic growth through reliance on the international capital market.

The second allegation, that segments of society are being left behind in the process of globalisation, is serious. Further,

that there are groups within society—at least in the United States—that have not benefited greatly from the economic boom of the past decade seems unquestionable. I should mention that there is evidence that, in the past three years, real wages have begun to rise even for those in the lower part of the scale. But nonetheless, the charge that some are marginalised is undoubtedly correct and deserves attention.

A first question is how much marginalisation is a result of globalisation and how much a result of economic growth. Economic growth has always meant change, as old skills and ways of doing things have been abandoned in favor of more productive alternatives. With that, those who had the older skill sets, or settled patterns of employment, have lost out throughout history. Among groups one can think of who were left behind, there were such occupations as horse-shoers; milkmen and others who delivered ice door-to-door; village shoemakers, tailors, and other artisans who lost out to factory-made goods; bank clerks who kept the books in back rooms; and lighthouse keepers, to name just a few. Of course, others have been affected by changing tastes (such as the switch from butter and eggs to pasta or from palm oil to olive oil), poor management, and other phenomena associated with economic growth and/or change. When the change hits a town or region particularly severely, hardships can be even greater as real estate prices fall, shops close, and people leave the area.

The negative impact of these sorts of changes has been a concomitant of economic growth and is not new. Earlier political movements objected to aspects of economic growth and measures were taken to reduce the impact of it (such as unemployment insurance and farm price supports). People have the impression that change is more rapid than in the past, but it is an open question whether even that allegation withstands close scrutiny. Whether it is more rapid or not, and whether the negative impacts are proportionately greater or smaller than in the past are both open questions, but there is surely a greater propensity to blame globalisation for these negative side effects of change.

What is certainly true is that we are richer as societies, and as such the hardships inflicted are perhaps more avoidable, or at least can be ameliorated to a greater extent than in the past. There are two other circumstances, however, that may make things worse. First, it is of course also true that in the past, migration, especially to lands of new settlement or to new frontiers in newly-settled regions, provided something of a safety valve for early industrialisers in Europe. Those safety valves are no longer there to the same degree. Second, life expectancies are considerably longer (a good thing). But there is increasing evidence that the really sizable human costs to economic change come about when older individuals lose their source of income. Young people have the time and the flexibility for acquiring new skills: older workers face a great many more obstacles to doing so. In my closing remarks, I shall mention some of the means proposed for addressing the special problems of laid-off older workers.

Related to, but not the same as the increasing inequality allegation, is the phenomenon that differentials in earnings between skilled and unskilled workers, which were falling in the United States at least from 1900 to the 1970s, were seen to be increasing again during the 1980s and early 1990s. The initial tendency of most popular discussion was to blame increased trade with countries with abundant supplies of unskilled labour for this reversal. Subsequent research has focussed instead on technical change, with the development of industries and techniques that rely much more heavily on capital and skilled workers, and less on unskilled workers, as the major factor accounting for increased earnings differentials.

The bases for these findings cannot be fully explored here. Suffice it to mention three reasonably compelling facts. First, if trade with developing countries had been responsible for increased earnings differentials in industrialised countries, one would have expected the relative wages of unskilled workers in developing countries to rise while those in industrialised countries were falling. That has not happened. Secondly, if imports of goods intensive in the use of unskilled labour were

a major factor accounting for increased earnings differentials, one would have expected that non-traded goods industries would have substituted unskilled for skilled labour, as they were not exposed to competition from abroad and could, presumably, benefit from substituting now low-priced unskilled labour for skilled labour. That, too, has not happened. Third, if imports of unskilled labour-intensive goods were a major culprit in increased earnings differentials, one would have expected to find the same pattern across the industrial countries that increased their imports. In fact, that has not happened. Canadian relativities, for example, have not increased (because Canada achieved a greater increase in educational attainments of its population in the 1980s and early 1990s than did the U.S. and Western Europe). Moreover, relative earnings of skilled workers have increased in developing countries as well. These and other phenomena are consistent with the proposition that technical change was biased in favour of skilled and against unskilled workers. To be sure, imports of particular goods intensive in the use of unskilled labour may have exacerbated trends, but in the academic literature, no more than 20% of the increased differential is attributed to imports in the research results reporting the greatest impact of trade.

That earnings differentials have increased is undoubted, and that trend constitutes a challenge for policymakers. But globalisation is not the main culprit. Again, the blame seems to be being placed on the wrong phenomena.

In the United States, many of those who express concerns about globalisation recognise the benefits to date, and most of the counter-arguments to the 'globalisation as devil' hypotheses I have already discussed. They nonetheless maintain that globalisation has increased the insecurity of most members of the labour force and that, as such, it is and should be a source of concern. Interestingly, there is little objective evidence to support this view. The average length of time American workers remain in one job has shortened by less than 5%, and data are not available to determine how much of that shortening was attributable to the increased willingness of employees to move to better jobs as contrasted with that part resulting from layoffs

by earlier employers. And it is difficult to believe that concern with insecurity is greater now in the United States—with an overall unemployment rate of just over 4%—than it was in earlier periods when unemployment rates were much higher. Indeed, to the extent that increased economic insecurity appears to be a real issue, its incidence seems to have risen among middle-level executives and others in the middle and upper parts of the earnings income distribution.

The fifth stated source of concern about globalisation is the perception, or stated perception, that capital flows are now very large relative to individual governments and that, in that sense, they have removed power from domestic policymakers and that the 'capitalists' are controlling the world. This concern is closely related to the more general 'loss of control' concern discussed earlier, but it focuses on capital flows, rather than trade. Since I want, in concluding, to focus on trade issues, let me just make several quick points here. The first is that net capital flows, as already stated, are not yet as important proportionately as they were in the late 19th century in the world economy. The second is that policymakers' concerns about capital flows often constrain them from undertaking economically costly measures (such as high rates of inflation) which hurt poor people. The third is that a large part—though not all—of the damage that occurred during, for example, the Asian crisis of the late 1990s, would have been avoided through reforms in either or both the financial system and the exchange rate regime. To a considerable degree, changes are already underway to reduce the future incidence and severity of sudden reversals of capital flows.

This leads me to the sixth and final concern expressed regarding globalisation. That is, that the human values cited in the *Mercury News* article—labour standards, environmental concerns, human rights, and so on—may be impinged upon by trade flows. It is this allegation which is in most regards the hardest to deal with, in large part because the evidence goes the other way. Poor countries are able to achieve more rapid gains in living standards for their people, and especially for the poor, when they have open trade policies and have access to

markets in developed countries. People in many developed countries are so rich that they cannot conceive of poverty of the type that is prevalent in many poor countries. They do not perceive that child labour is not because parents are cruel: it is because the alternative to child labour is starvation (or what is more likely but equivalent malnutrition to a degree that makes people more susceptible to fatality from bacteria and other sources that healthy, well-nourished people can fend off), or forced early marriages (for girls) or prostitution, or life on the streets as a beggar. In most industrial countries, child labour was used until people became rich enough so that they could afford to let children attend school. There is ample evidence that people choose schooling for their young when they can afford to do so, and the quickest path to that result is through more rapid economic growth.

For poor countries, access to markets and an open trade regime permits the rapid expansion of exports of labour-intensive goods, which in turn enables the rapid increase in employment of unskilled workers in 'good' well-paying jobs where they may receive training as well. Obviously, absorbing individuals with low levels of educational attainment and little or no prior experience into the labour force can be undertaken only when wages are reasonably low, making it profitable (despite low labour productivity) to take on new workers and to expand. When people in developed countries talk about 'decent wages' for people in poor countries, they are often talking about a wage that would be sufficiently high that any competitive advantage of businesses using unskilled labour on the international market would be eroded. Indeed, in some developing countries, there is as strong suspicion that unions in developed countries want labour standards as a protectionist measure to avoid the inflow of imports!

The call for 'labour standards' is therefore somewhat suspect. On one hand, there are no doubt instances of abuse of children and of other workers. But there is ample reason to believe that in most developing countries there is an excess supply of labour, that people compete for jobs in the exporting sectors, and that

in consequence there is little or no artificial suppression of wages. Even if some existing investors could pay more, that would reduce further new investment, in addition to creating a 'dual' economy between domestic and foreign firms.

When proposals are made to link trade to labour standards. the issues become operationally cloudy as well. If, for the sake of argument, it were decided that there should be a universal 'code', an interesting question arises as to what penalty would be assessed, and against whom, for violations, Should an entire country's exports be shut off because some firms within the country violate the 'code'? Obviously, such a measure would be extreme, and would harm many workers. Should instead a firm's exports be prohibited or otherwise penalised only when the firm itself undertakes measures perceived to be in violation of the 'code'? If so, exporting firms could simply subcontract whatever parts of their processes they feared would be in violation, undertaking only those finishing or other steps that might be in violation. What should be done if the 'code' were violated in home goods industries, such as construction or electric power generation? And when governments in developing countries have little administrative capacity, should the international community be encouraging its application to labour standards above other pressing concerns?

Environmental issues raise many of the same concerns. Many now-developed countries, including Australia and the United States, despoiled their environment during their early period of economic growth. Since that time, we (and others) have grown rich enough so that we value a cleaner environment and have been willing to commit public and private resources to improve it. The evidence is reasonably convincing that, at an income level of around \$5,000 per capita, people begin choosing to invest in cleaning up and preventing pollution, the exact income level depending in part on the particular kind of pollutant.

Moreover, there are different types of pollution. Poverty is normally associated with unclean drinking water, inadequate sewage, and related environmentally-induced pollution. Wealth is associated with environmental damage resulting from high

levels of production and consumption. If one examines where in the world pollution is greatest, it is in the developed countries. Calls by the rich for standards not observed by them during their period of industrialisation are regarded with great suspicion in developing countries, and viewed as an effort to prevent their development.

It may be worth it to the rich to call for environmental measures that the poor cannot yet afford to undertake. But the way to achieve those measures is to negotiate over environmental issues with the poor, helping to finance those measures which are not yet attractive at low levels of income. It is ironic that, should extreme and costly measures for environmental protection be imposed on poor countries, it is possible that the resulting costs could sufficiently slow down growth so that the long-run impact on the environment could be negative.

Human rights concerns are the final issue that I wish to touch upon briefly here. Given that the demand for democracy and representation seems to rise sharply with income and that openness does not seem possible with a very high degree of repression, it seems clear that encouraging rapid economic growth under conditions of openness would, in itself, be highly conducive to the adoption, over time, of improved standards of human rights. As with environmental issues, shutting off trade can have negative effects both because it enables greater violations of rights (as international public view is diminished) and because the resulting lower economic growth is likely to reduce the demand for more rights. There are also important questions as to how trade might be tied to human rights issues: one can only use trade threats so far, and their potency seems to be highly limited, based on historical experience.

Addressing the concerns

I already stated that there is a danger from the globalisation backlash, even though many of the issues raised are either spurious or they are the fault of phenomena other than globalisation. Here, I wish to focus on the issues raised by trade, and the proposals put forth to tie trade to the globalisation

issues. There are other concerns with the World Bank and the International Monetary Fund which are being addressed in other fora, and I will not focus on those here, other than to say that it seems clear that in an increasingly interdependent world, some institutionalised mechanisms for international economic consultation, decisionmaking, and dispute settlement among governments are essential. For trade in particular, some institutional arrangement for rule making and dispute settlement seems so essential that it is hard to understand opposition to it. Strengthening of the World Trade Organisation, and especially of its secretariat functions, seems to be well-warranted. If this were done, perhaps some of those additional resources could be put to use in increasing public awareness and understanding of the Organisation and how it functions. But that alone will not suffice. The underlying unease regarding globalisation probably needs to be addressed.

To start, however, let me just point out that there were more fundamental concerns at work in Seattle, that led to the failure to launch a new round, than those voiced by the demonstrators. Almost nothing in the text had been negotiated in advance: almost everything was bracketed for discussion at Seattle. Then, too, there had never before been a Ministerial where the chairman of the meeting was also head of the largest delegation. There was always a big question as to why Seattle should be scheduled just a year before an American presidential election: given American politics, an election year is not a time for rapid negotiations, and, since it was certain that there would be a new Administration in January 200l, there seemed little point to starting then. And, finally, never before had the developing countries been so receptive to involvement and so threatened (because they have opened their economies) by discussion of inclusion of labour standards without prior consultation. Seattle failed fundamentally because there had been inadequate preparatory work, and because the major parties were not as yet committed to negotiate on the important issues.

That said, political unease in the United States and in Europe regarding trade no doubt facilitated that inadequate preparation. The lack of strong support for a new round arose partly because

of the perceptions I have been discussing above. At least in the United States, even those politicians sympathetic to free trade are concerned about the extent to which the electorate is lukewarm, at best, toward free or freer trade.

The issue, however, is not whether continuing with trade liberalisation is a good thing. It is, and a reversal of the trend toward trade liberalisation would also reverse the acceleration of economic growth, with all its benefits, as well as dooming the prospects of poor countries currently reforming their economic policies. The issue is how to address the underlying malaise, which is real enough, even if trade is taking an unfair share of the blame.

First of all, and as already indicated, there is certainly an educational job to be done, in the sense of attempting to more appropriately identify the very large benefits of trade and globalisation on the one hand, and in showing the extent to which issues of concern have their origins in economic growth more generally, and not in trade.

Beyond that, however, there does seem to be a lack of appropriate social policy to deal with those who lose from economic growth, regardless of the causes of their losses, at least in the United States. Trade adjustment assistance has been tried, but assistance has been available only when it was shown that trade was a 'major' source of injury—a very difficult thing to determine judicially—and there is in any event a question as to why social policy should examine the source of discomfort, as contrasted with the symptoms.

An alternative that many are considering is to strengthen the social safety net for older workers and simultaneously to require suitable retraining for younger workers as a condition for support and to limit severely the period of time during which compensation will be paid. If current concerns about trade are focussed on employment security, then it would seem to make sense to address that security regardless of the fact that trade is not the major cause of insecurity.

Measures to soften the blow of job losses, regardless of the reasons, would surely reduce opposition to further trade liberalisation if the measures are effective. There remains,

however, the question of how to handle environmental, labour, and other issues raised in connection with globalisation. On all of these, the arguments that I have briefly sketched out above for not using trade measures seem to me to be compelling. It is not clear how they could be applied; if they were applied, they carry severe dangers of being protectionist in effect; and they would certainly reduce rates of economic growth in some developing countries, thereby possibly having the opposite effect of that intended, and slowing down the rate at which environmental, human rights, and other measures were adopted in those countries.

Measures such as these will not be adopted in the near term. For that reason, those who recognise and benefit from the open multilateral trading system need to become more effective at dealing with the false impressions carried by many of those with global phobia. Evidence that economic growth through trade liberalisation has delivered tremendous increases in living standards in poor countries is overwhelming; the intimate linkage between improvements in living standards in industrial countries since the industrial revolution is well documented; data showing that earlier economic growth was also accompanied by dislocations related to growth and not to trade are readily available. All of these need to be publicised repeatedly and widely.

While the objectors have a point which can be addressed to some degree, globalisation has brought, and is bringing, great benefits to the great majority of the world's population. Mobilising the support of the beneficiaries is clearly essential in staving off the backlash. Finding ways to strengthen the political support from those groups is and should be a major challenge for those supporting the open multilateral trading system.

Endnotes

- ¹ See the data and references in Kevin O'Rourke and Jeffrey G. Williamson 2000, 'When Did Globalisation Begin?', National Bureau of Economic Research Working Paper 7632, April, for further analysis supporting this interpretation.
- ² San Jose Mercury News, 1 October 2000: 3H.

Closing Remarks

Professor David Robertson CIS Academic Advisory Council Member

As one of the newest associates of The Centre for Independent Studies, it is a genuine pleasure to be asked on behalf of this audience and this organisation to thank Anne for her address this evening. It is always a pleasure to pay tribute to her ability to apply economic analysis to difficult social and political issues.

Anne is a frequent visitor here and I hope she continues to come back and that she keeps us on the right track because here in Australia we do need prodding from time to time. This evening she made a number of points that we should all take to heart, particularly about the role of governments in the globalisation debate.

I am amazed that governments have done so little to confront the non-government organisations or the anarchists who are behind recent anti-globalisation demonstrations. Governments play a low-key role, letting demonstrators get on with their disruption while journalists produce inflammatory material, never letting the truth spoil a good story! The WTO is an intergovernmental organisation. The Australian government has a say in what goes on there. It is not an independent body. One of my friends who was an ambassador to GATT used to say, 'The Secretariat? All they do is put out the pads and pencils and switch out the lights at the end of meetings.' That is true. Governments make agreements, and for them to pass the buck to these multinational institutions misses the point.

What we have heard from Anne tonight gives me some hope that globalisation is going to maintain its present thrust and not become reversed by some of the idiosyncratic opposition from NGOs. Every generation has its revolution. Each of us was probably involved in some kind of demonstration against one thing or another when we were students. Now it is someone

else's turn, although there are a few rather nasty individuals that get involved too.

The problem is that globalisation is a catch-all phrase. Everything is covered by globalisation, so that if you are antiglobalisation, you are anti whatever you want to be. Look at Prague, situated in a country where for 50 years the people fought for independence, both from West and East. At last, they have achieved some democratic independence. Then at the annual IMF and World Bank meetings, a bunch of hooligans smashed up one of the most beautiful medieval cities in Europe. That seems to me to demonstrate what these people are about. Not about anything important, just protest and violence.

Now my role here is really to thank Anne. Her address gives me faith that there are people around who think about the genuine concerns behind anti-globalisation demonstrations and try to put them into perspective. We seem to be moving from an Age of Reason back into an Age of Belief. People do not want to hear the argument, they just want to believe what suits them. What we have to do is to keep reason at the front of the debate.

Having said that, Anne thank you very much for coming all this way, for attracting such a large audience that is a tribute to your reputation as well as to Greg's efforts in promoting this evening. Thank you for giving us such a stimulating presentation and for your thoughtful analysis of some important global issues.

Trading Phobias

Anne Krueger

e live in an era of unprecedented material prosperity, and yet the post-war multilateral trading system largely responsible for the creation of this wealth is under threat. The threats and challenges include preferential trading arrangements, criticism of the IMF and the World Bank as well as the coalition of non-governmental organisations, environmentalists and labour unions.

In this Occasional Paper, Anne Krueger examines these threats and their antiglobalisation rhetoric, as well as what efforts might be made to achieve a workable international order. She warns that although it may be tempting to dismiss the malaise and the protests as Luddite in nature, it would probably be a mistake to do so. The failure to address this unease could lead to a serious backlash against the international economy, and with it, political pressures to resurrect trade barriers and reverse the potential future benefits of further increases in economic integration.



ANNE KRUEGER is Director of the Center for Research on Economic Development and Policy Reform at Stanford University. She is an expert in trade, international economics and the multilateral trading system; the role of multilateral institutions in the international economy; and financial institutions, corruption and economic development.

Her recent publications include The WTO as an International Institution (University of Chicago Press 1998), Trade Policies and Developing Nations (Brookings Institution 1995), and American Trade Policy: A Tragedy in the Making (American Enterprise Institute 1995).

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