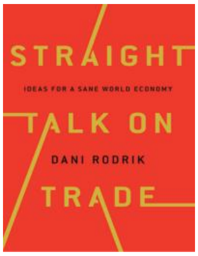

Dani Rodrick

Straight Talk on Trade: Ideas for a Sane World Economy

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Introduction

Dani Rodrick is Professor of Political Economy at the Harvard University and has been a vocal critic for over a decade of what he sees as the unbridled tide of globalization present in today's worldwide economy. Dani Rodrick's Straight Talk on Trade: Ideas for a Sane World Economy was published in 2018 by the Princeton University Press, United Kingdom. In this volume, Dani attempts to set the record straight, and not just about trade, as the title suggests, but about several areas in which economists could have offered a more balanced, principled discussion. Dani debated that when economists shade their arguments, they effectively favour one set of self-interested parties over another. Also, he pointed out that market failures, including poorly functioning labor markets, credit market imperfections, knowledge or environmental externalities, and monopolies can interfere with reaping gains from globalization. The volume presents nontechnical work on globalization, growth, democracy, politics, and the discipline of economics itself and thereby it shows how we could have constructed a more honest narrative on the world economy. Dani also suggests ideas for moving forward to create better functioning national economies, so that it ensures better outcomes from the globalization for better future for everyone in the world.

Organization

The book is comprised with well-organized twelve chapters. I thumbed through the table of contents with real anticipation, even excitement and found the topics are really interesting. This book consistently provides new and valuable insights into the various causes and consequences of globalization and economic integration which I would like to review by highlighting the important thoughts of each chapter.

Contents

A Better Balance

The first chapter explains how nations could achieve a better balance under the globalization. In light of this, Dani emphasized that at present, international trade has moved to the center of political debate and economists are struggling to find gains from recent trade agreements for the country as a whole. For instance, countries that managed to leverage globalization, such as China and Vietnam, employed a mixed strategy of export promotion and a variety of policies that violate current trade rules. On the contrary, countries that rely on free trade alone e.g. Mexico have languished. Further he emphasized that, the most phenomenal export-oriented growth experiences to date; Japan, South Korea, Taiwan, and China, all occurred when import tariffs in the United States and Europe were at moderate levels, and higher than where they are today. The important point to notice in this case is that, poorly managed globalization can bring profound effects not only in the United States but also in the rest of the developed world, especially, Europe and the low-income and middle-income countries in which a majority of the world's workers live. Dani argues that although globalization has not been the sole, or even the most important, force driving inequality in the advanced economies, it has been a key contributor. In the case of developing countries, to overcome novel future challenges emerging under the globalization, it is important to create fresh, creative strategies that deploy the combined energies of both the private and public sectors. In this chapter, Dani emphasized getting the balance between economic openness and policy space management right is of huge importance in order to reap benefits under the globalization.

How Nations Should Work

The second chapter deals with how a nation should work under the globalization to reap better outcomes. It is clear that, the surge in cross-border flows of goods, services, capital, and information produced by technological innovation and market liberalization has made the world's countries too interconnected and under such environment, to solve its own economic problems, it is need to have global rules, global agreements and global institutions. Dani recognize that the differences in currencies, legal regimes, and regulatory practices are today the chief obstacles to a unified global economy. It is worth note to recognize that economic globalization, spurred by the revolutions in transportation and communication technologies, breaks down the social and cultural barriers among people in different parts of the world and fosters a global community. It, in turn, enables the construction of a global political community and global governance that underpins and further reinforces economic integration. Dani explains that "hyperglobalization" is the attempt to eliminate all transaction costs that hinder trade and capital flows. For instance, China, which engineered history's most impressive poverty reduction and growth outcomes, was, of course, a major beneficiary of others' economic openness. But for its part, it followed a highly cautious strategy that combined extensive industrial policies with selective, delayed import liberalization and capital controls. Effectively, China played the globalization game by Bretton Woods rules rather than by hyperglobalization rules. However, it is widely understood that globalization's ills derive from the imbalance between the global nature of markets and the domestic nature of the rules that govern them. As a matter of logic, the imbalance can be corrected in only one of two ways: expand governance beyond the nation-state or restrict the reach of markets. Nevertheless, in the case of a polite company, only the first option receives much attention. At last, Dani emphasized that, we have to live in the world we have, with all its political divisions, and not the world we wish we had. Hence, the best way to serve global interests is to live up to our responsibilities within the political institutions that matter: those that exist, within national borders.

Europe's Struggles

The third chapter explains key political & economic processes and problems in Europe, relating to European Union (EU) integration, policy challenges and transformation processes. Dani recognize that the immediate problem in Europe is how to revive growth as every country is struggling for enhancing their economic growth rates. In this context structural reforms are important to enhance productivity and improve the functioning of the supply side of the economy. From the very beginning, Europe was built on a "functionalist" argument, which posited that political integration would follow economic integration. It is worth noting that Europe's economies, whittling away at national policies that hampered the free movement not just of goods but also of services, people, and capital. The euro, which established a single currency among a subset of member states, was the logical extension of this agenda. This was known as hyperglobalization on a European scale. However, Dani noticed that today it may be too late to entertain fiscal and political integration within the EU.

Work, Industrialization, and Democracy

In chapter four, Dani attempts to explain how "growth miracles" are made in different countries in the world through work, industrialization and democracy. It is worth note that, except for a handful of small countries that benefited from natural-resource bonanzas, most of successful economies owe their growth to rapid industrialization. There is one thing that everyone agrees on about the East Asian recipe, it is that Japan, South Korea, Singapore, Taiwan, and of course China all were exceptionally good at moving their labor from the countryside (or informal activities) to organized manufacturing. Earlier cases of successful economic catch-up, such as the United States or Germany, were no different.

Also, it is important to note that, economic development occurs as workers and farmers move from traditional, low-productivity sectors (such as agriculture and petty services) to modern factory work and services. As this takes place, two things happen. First, the economy's overall productivity increases, because more of its labor force becomes employed in modern sectors. Second, the productivity gap between the traditional and modern parts of the economy shrinks, and dualism gradually diminishes. Agricultural productivity increases during the process, owing to better farming techniques and a decline in the number of farmers working the land. This process enables the developing nations are becoming service economies without having had a proper experience of industrialization—a process which Dani called "premature deindustrialization."

It is interesting to note that, more economic growth will have to come from productivity advances in services. This means in turn that the partial, sectoral approaches that worked so well to stimulate export-oriented industrialization during the early stages of rapid growth in Asia and beyond will have to be replaced (or at least complemented) by massive economy-wide investments in human capital and institutions. When manufacturing is the engine of the economy, selective reforms such as export incentives, special economic zones, or incentives to foreign investors can be highly effective. Dani noted that, to date, industrial capitalism has been pretty much the only path to a productive society. Factory work was not pleasant and it generated significant social tensions, but it got the productivity job done. Hence, he emphasized that, today this path looks both less desirable and less feasible and therefore, new path will have to be invented. It will be a model based on services. It will focus more on soft infrastructure, learning and institutional capabilities and less on physical capital accumulation, plant and equipment in manufacturing industries.

Another, important point to note here is that, by definition developing countries are still poor and that the structural changes that today's rich countries underwent during the nineteenth and early twentieth centuries are perhaps still ahead of them. It is also the case that successful industrializers among them have ended up becoming liberal democracies. For instance, consider South Korea or Taiwan. In both cases, industrialization produced a significant working class, which in turn played an important role in democratization. Although, every authoritarian country that has managed to grow rapidly, there are several that have floundered. Democracies outperform dictatorships in long-term economic growth, and in several other important respects as well (for instance Lee Kuan Yew of Singapore, Mobutu Sese Seko of the Congo). They provide much greater economic stability, measured by the ups and downs of the business cycle. They are better at adjusting to external economic shocks (such as terms-of-trade declines or sudden stops in capital inflows). They generate more investment in health and education, or human capital. Also they produce more equitable societies.

Economists and Their Models

In chapter five Dani attempts to explain different economic thoughts and its implications in economic development. It shows that economics deals with human behavior, which depends on social and institutional context. That context in turn is the creation of human behavior, purposeful or not. This implies that propositions in economic science are typically context specific, rather than universal. The best, and most useful, economic theories are those that draw clear causal links from a specific set of contextual assumptions to predicted outcomes. For instance, open-economy macroeconomists examine conditions under which global finance stabilizes or destabilizes national economies. Development economists study conditions under which foreign aid does and does not reduce poverty. Training in economics requires learning not only about how markets work but also about market failures and the myriad ways in which governments can help markets work better.

Moreover, the chapter correctly explains that "Economics is a science of thinking in terms of models" and a well-known economist," Keynes once said, "joined to the art of choosing models which are relevant." It is interesting to note that in most of the situations economists become overconfident in their preferred models of the moment: markets are efficient, financial innovation transfers risk to those best able to bear it, self-regulation works best, and government intervention is ineffective and harmful. They forgot that there were many other models that led in radically different directions. The trouble is that the real world has not lined up so neatly with economists' presumptions.

The chapter also explains history of economics. It helps to open up our minds to see how different countries became successful in the world by following different thoughts of economics. Milton Friedman was one of the twentieth century's leading economists, a Nobel Prize winner who made notable contributions to monetary policy and consumption theory. He emphasized the fact that, all successful economies are built on thrift, hard work, and individual initiative. He railed against government regulations that encumber entrepreneurship and restrict markets. Adam Smith was to the eighteenth century; Milton Friedman was to the twentieth.

The history of economics is largely a struggle between two opposing schools of thought, liberalism and mercantilism. Economic liberalism, with its emphasis on private entrepreneurship and free markets, remains today's dominant doctrine. In fact, mercantilism remains alive and well, and its continuing conflict with liberalism is likely to be a major force shaping the future of the global economy. Mercantilists, view trade as a means of supporting domestic production and employment, and prefer to spur exports rather than imports. Although China phased out many of its explicit export subsidies as a condition of membership in the World Trade Organization, which it joined in 2001, mercantilism's support system remains largely in place. As a result, the new economic environment will produce more tension than accommodation between countries pursuing liberal and mercantilist paths.

The Perils of Economic Consensus

The important point that can be noted in chapter six is that, economists agree on many things that are often politically controversial. A consensus among economists can arise for both good and bad reasons. Sometimes a consensus is innocuous enough, as when you hear economists argue that one ignores the role of incentives at one's peril. Perhaps economists tend to agree that certain assumptions are more prevalent in the real world. The point that one needs to understand is that, economics is not the kind of science in which there could ever be one true model that works best in all contexts. In recent years, however, neither economic theory nor empirical evidence has been kind to the presumed trade-off. Economists have produced new arguments showing why good economic performance is not only compatible with distributive fairness but may even demand it. For example, in high-inequality societies, where poor households are deprived of economic and educational opportunities and hence economic growth is depressed. Dani pointed out that, economists and other social scientists get virtually no training in how to choose among alternative models. Neither is such an aptitude professionally rewarded. Therefore, developing new theories and empirical tests is regarded as science, while the exercise of good judgment is clearly a craft.

Economists, Politics, and Ideas

In chapter seven, Dani try to relate how economics and political ideas get interrelated. Dani noted that, economists love theories that place organized special interests at the root of all political evil. In the real world, they cannot wriggle so easily out of responsibility for the bad ideas that they have so often spawned. Also, he explained that, every rational-choice model is built on the purposive behavior of individual decision makers. Typically, behavior is determined by assuming individuals solve what economists would call a well-defined optimization problem. The point here to note that, political agents—voters, lobbies, elites, congressmen—are represented as rational individuals who solve explicit optimization problems. This means they maximize a utility function defined over consumption, rents, or political benefits; they operate within constraints imposed by the rules of the game, both economic and political; and they choose a set of actions, which in various models may include votes, political contributions, rebellion, and suppression—that maximize their objection function given the constraints. Dani's goal here is to explore the role of ideas in shaping how interests are defined and pursued, discuss economists' contributions; both good and bad and in turn open up space for new, more useful ideas.

Economics as Policy Innovation

In chapter eight Dani attempts to emphasis that economists recognize the importance of technological innovation and have made it the centerpiece of their models of long-term growth. On the other hand, in political-economy models, the working assumption is that there is no room for discovery. Hence, many political innovations are likely to remain ephemeral, inconsequential, or soon forgotten. But some, as with general-purpose technology, may prove substantial and durable. Dani also highlights that; technological change need not make everyone better off. Similarly, policy innovation could leave the non-elites worse off. A classic example for this is China's in which liberalize its trade regime in the standard way, which would have decimated the country's inefficient state enterprises, China allowed firms in special economic zones to operate under near-free-trade rules while maintaining trade restrictions elsewhere until the late 1990s. This

enabled China to insert itself in the world economy while protecting employment and rents in the state sector. This enables the Chinese Communist party to become strengthen and enriched rather than weakened as a result.

Also, it is noted that, innovation occurs, in large part, as a result of serendipity, as fundamental scientific discoveries yield unanticipated practical benefits or as experimentation and trial and error result in new products and processes. Similarly, one needs to understand that there is a strong idiosyncratic element in political leadership and political creativity. Nevertheless, as the economic literature on research and development and endogenous growth indicates, certain systematic elements are also in play. For example, technological innovation responds to market incentives—the pursuit of monopoly profits through the acquisition of temporary advantages over competitors. Likewise, policy ideas that relax political constraints can be thought of as the consequence of both idiosyncratic processes and purposive behavior. Dani put forward that, the problems of globalization, economic growth, and social inclusion require imaginative ideas and solutions. Therefore, democracies owe themselves a proper debate, so that they make their choices consciously and deliberately.

What Will Not Work

The ninth chapter is very insightful not only for academics but also for policy makers in different countries in the world. Dani begins his discussion highlighting the fact that there are two key proposals around which today's conventional wisdom revolves: compensating the losers of globalization and enhanced global governance. Both of these ideas are largely dead ends. Neither offering compensation nor global governance, as conventionally understood, can move us in the right direction. As an ordinary person, we need to accept the fact that globalization produces both winners and losers and in which case, the correct response is not to halt or reverse globalization but to ensure that the losers are compensated.

It is interesting to note that, today the advanced countries that are the most exposed to the international economy are also those where safety nets and social insurance programs—welfare states—are the most extensive. The chapter explains that the research in Europe has shown that losers from globalization within countries tend to favor more active social programs and labor-market interventions. Good economic policies, by contrast, are different. Policies such as openness, financial and macroeconomic stability, full employment, investments in human capital, infrastructure, and innovation benefit the home economy first and foremost. The price for bad economic policies is paid primarily by domestic residents. The economic fortunes of individual nations are determined largely by what happens at home rather than abroad.

Dani describes that economic policies come roughly in four different variants. At one extreme are domestic policies that create no (or very few) spillovers across national borders, such as education policies. These require no international agreement and can be safely left to domestic policy makers. At the other end are policies that relate to "global commons," such as global climate. The characteristic of a global commons is that the outcome for each nation is determined not by domestic policies but by (the sum total of) other countries' policies. The classic case here is greenhouse gases. There is a very strong case for establishing strong and binding global rules in these policy domains, since it is in the interest of each country individually to neglect its share of the upkeep of the global commons. Failure to reach global agreement would condemn all to a collective disaster. In between, there are two other types of policies that create spillovers of the type I mentioned previously. These must be treated differently. Also, it should be noted that, different types of policies call for different responses at the global level. At present, too much global political capital is wasted on harmonizing beggar-thyself policies (particularly in the areas of trade and financial regulation) and not enough on beggar-thy-neighbor policies (such as macroeconomic imbalances). Overambitious and misdirected efforts at global governance will not serve us well at a time when global cooperation is bound to be scarce.

New Rules for the Global Economy

Chapter ten explains the idea that the markets which are self-regulating also require other social institutions to support them. This means, they rely on courts, legal frameworks, and regulators. In addition, they need the political buy-in that redistributive taxation, safety nets, and social insurance programs help generate. Further, they need public investment in infrastructure and R&D to innovate. The point that should be noted here, what is true of domestic markets is also true of global once.

As Dani explains, the purpose of international economic arrangements must be to lay down the traffic rules for managing the interface among national institutions. Therefore, every country should strive to attain the maximum globalization that is consistent with maintaining space for diversity in national institutional arrangements. Advocates of globalization says that countries must change their policies and institutions to expand their international trade and to become more attractive to foreign investors. Also, Globalization should be an instrument for achieving the goals that societies seek: prosperity, stability, freedom, and quality of life. Whether globalization sets off a race to the bottom or not, we can break the deadlock between the proponents and opponents of globalization by acknowledging a simple proposition: social dumping that undermines democratically legitimated domestic practices is not acceptable. As Dani noted, "global citizenship" will always remain a poor metaphor, because there will never be a world government

administering a worldwide political community. But the more we each think of ourselves as globally minded and express our preferences as such to our governments, the less we will need to pursue the chimera of global governance.

Growth Policies for the Future

In chapter eleven, Dani discusses the challenges facing developing and advanced economies in the world. The important learning point in this chapter is; growth ultimately depends on supply-side factors—investment in and acquisition of new technologies. The stock of technologies that are available for poor countries to adopt does not disappear when growth in the advanced countries is sluggish. So, the growth potential is determined by lagging countries' ability to close the gap with the technology frontier—not by how rapidly the frontier itself is advancing. The analyst predicts that; growth will be easy for poor countries with young populations with access to cheap technologies from abroad.

In the case of developing economies, the three key growth fundamentals are as follows: the acquisition of skills and education by the workforce; the improvement of institutions and governance; and structural transformation from low-productivity to high-productivity activities (as typified by industrialization). For instance, East Asian–style rapid growth has typically required a heavy dose of structural transformation for a number of decades, with steady progress on education and institutions over the years providing the longer-term underpinnings of convergence with advanced economies. Dani noted that the developed countries needs new ideas—perhaps even more so than developing nations, which can always emulate past success—to embark on a path of inclusive economic growth. In developing nations, military intervention undermines long term prospects for democracy because it impedes the development of a democratic "culture"—habits of moderation and compromise among competing civilian groups. As long as the military remains the ultimate political arbiter, these groups focus their strategies on the military rather than each other.

It’s the Politics, Stupid!

In the last chapter, Dani question about the consequences of pushing economic globalization beyond the boundaries of institutions that regulate, stabilize, and legitimize markets. Dani thinks that, politicians will not regain lost ground until they, too, offer serious solutions that provide room for hope. They should no longer hide behind technology or unstoppable globalization, and they must be willing to be bold and entertain large-scale reforms in the way the domestic and global economy are run. Finally, Dani emphasis that, good things that the present consensus produced—a liberal, democratic order in particular—is swept away by the backlash wrought by its excesses. Politicians of all stripes, take note.

Sum-Up

The book is excellently set out and deals with complex issues in a highly readable and easy to understand way, with entertaining and historical facts and anecdotes, making it accessible to any reader. Dani Rodrik’s research to date has looked at what makes up good economic policy, and what the barriers are to achieving it, by studying different countries in depth and making valuable international comparisons. In my opinion, Dani is right about mentioning that the globalization creates winners and losers and there is a need for effective policies to compensate the losers. At present, even advanced developed countries that are the most exposed to globalization are also using safety nets and social insurance programs to protect less privileged people in the society. Also it is important to note, even the World Bank and the IMF have accepted the fact that economic liberalisation can bring better outcomes and enhance the level of welfare, they have pushed the liberalisation process too far and it has contributed to the global financial crisis as well. Hence, it can be argued that the economic development cannot be achieved by means of economic reforms alone; politics must play a central role in this regard. In the Straight Talk on Trade: Ideas for a Sane World Economy, Dani Rodrick may not have all the answers to the issues arise due to the process of globalization and also, it is unclear if his ideas are equally as applicable to countries in different stages of development, but he has made another valuable contribution to future debate and research.