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Challenges to Globalization
An Overview

Robert E. Baldwin and L. Alan Winters

Introduction

The failure of the World Trade Organization's (WTO's) 1999 ministerial conference in Seattle was a shock to the traditional trade-policy community. Most member governments and outside observers believed that trade ministers would be able to hammer out an agenda for a new round of multilateral trade negotiation, difficult though this would be and vague or ambiguous the language might be on some points. Instead, not only did ministers fail to establish an agenda or set a date for a new round of trade negotiations, but the meeting revealed deep divisions among governments and private-sector groups concerning the nature of the globalization process as it was being shaped by such public international organizations as the WTO, the International Monetary Fund (IMF), and the World Bank, as well as by multinational private corporations.

Fortunately, as a consequence of much hard work by the WTO director general Mike Moore and the country representatives stationed in Geneva, plus several key compromises by ministers, the ministerial meeting on trade held in Qatar in November 2001 was successful in launching a new round—the Doha Development Agenda—in January 2002. However, one agenda item important for some industrial countries, namely core labor standards, was rejected outright, and negotiations on a number of other

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key items were postponed until after the next ministerial meeting, and then only if there is "explicit consensus" among members to proceed.

Observers of trade negotiations have long been accustomed to bitter disputes among members on such issues as agricultural liberalization, the appropriate tariff-cutting rule to adopt, and the extent and timing of liberalization obligations on the part of the developing countries. But the run-up to Seattle and the meeting itself highlighted two sets of deeply held beliefs about the WTO and the trading system that industrial-country governments had largely been able to ignore until that time.

First, and most important, most developing countries felt that the benefits they received from the Uruguay Round negotiations fell far short of what they had expected in return for signing the agreements promoted by the developed countries during this round. They concluded, for example, that the adjustment burdens placed on them under the agreements on trade-related intellectual property rights (TRIPs) and trade-related investment measures (TRIMs) were much greater than those imposed on the developed countries in areas such as agriculture and textiles/clothing. The developing countries also felt that the time schedules established for them to implement the obligations assumed in previous agreements were too short and inflexible and that the developed countries were not fulfilling their parts of the bargains struck on such issues as agriculture and textiles/apparel. Furthermore, they were frustrated by what they perceived to be the misuse by developed countries of certain WTO rules for protectionist purposes, especially those related to antidumping. All these views made developing-country governments reluctant to agree to developed countries' proposals to establish new WTO rules in trade-related areas such as competition policy, environmental standards, labor rights, government procurement policies, and foreign direct investment. Moreover, developing countries felt isolated and marginalized in the WTO's internal processes, especially as they worked at Seattle itself. As a consequence of these views, the developing countries were quite prepared to see the Seattle ministerial meeting (as well as the later Doha ministerial conference) fail, unless the agenda included action items that would seriously address their concerns.

Second, as became evident in Seattle from the street demonstrations and the harassment of delegates, many nongovernmental organizations (NGOs) were deeply dissatisfied with certain consequences of the globalization process resulting from the international liberalization of trade, investment, and finance. These groups tended to be mainly concerned about three issues: the environment, human and worker rights, and inequality and poverty, particularly in developing countries (see chapter 1 in this volume by Elliott, Kar, and Richardson). Environmentalists are concerned with such matters as the maintenance of biodiversity and pollution in critical ecosystems. They fear that trade liberalization and the resulting competition for international markets may lead directly to unsustainable con-

sumption of natural resources and excessive pollution and indirectly to a reduction in existing environmental standards. Similarly, according to many worker-rights and human-rights advocates, trade liberalization and unrestrained foreign direct investment in developing countries lead to lower wages; to unhealthy, unsafe working conditions; and, in some instances, to the loss of basic human rights in these countries. The NGOs interested in promoting greater income equality and reducing poverty are also skeptical about the merits of freer flows of goods, technology, and capital in furthering their goals.

As with the views of developing countries, trade officials and interested parties in the private sector had been aware for several years that a growing number of NGOs opposed the international liberalization of trade, investment, and finance. Yet these NGOs did not receive much attention from the governments and international economic institutions that were promoting this liberalization until the late 1990s, when they began to organize large street protests at the meetings of such key trade and financial institutions as the WTO, the IMF, and the World Bank and at the meetings of intergovernmental organizations such as the Group of Eight (G8) and private groups like the World Economic Forum.[1] Even then, the protesters were initially largely dismissed as being anarchists and economically irrational. However, as those who seem bent on violence have been relegated to a less-prominent role and as more and more formal and informal contacts have been established between proponents and opponents of further liberalization of trade, finance, and foreign investment, the anti-globalization movement has become an important force to be reckoned with in public and private decision making in these areas. Nevertheless, the divergence of policy positions between the groups is still very wide.

Given the new willingness of the developing countries to assert their power over the form of international liberalization efforts and the growing influence of NGOs highly critical of previous efforts to increase the worldwide flows of goods, technology, and investment funds, the nature of future globalization is very much in question. An important reason for the continuing disagreement and misunderstanding is both a lack of careful case studies and statistical analyses (in contrast to anecdotal evidence) concerning the effects of various aspects of this process, and a lack of information among many affected by globalization of the knowledge we already have on the subject.

This conference volume aims both at informing those concerned with globalization issues about the knowledge that economists have already gained in studying various aspects of the topic and at providing new knowledge based on the research of the authors. We focus largely on the

1. One exception was the World Bank's attempt to create a dialogue with the NGOs from 1995 onward.

economic effects of globalization over which there is disagreement between pro-globalists and anti-globalists, and then we focus on only a small number of the many points in dispute. We believe, however, that the papers included here cover the issues of greatest interest to policymakers and the general public. Globalization is a large, complex, and relatively new subject, so the papers of the volume do not adopt a standard approach or methodology. Rather, each is tailored to the subject it treats, aiming efficiently to communicate to the reader what is known and not known in the various areas. In some cases we deal with precisely defined research issues whereas in others the need is for a broad account of a topic. The papers are grouped under five headings.

The Critics

The first group of papers deals directly with the critics of globalization, describing them, characterizing their objectives and discussing their views in economic terms.

In chapter 1, Kimberly Elliott, Debayani Kar, and J. David Richardson contrast the "talkers" about globalization—the critics—with the "doers." They describe who the critics are, where they came from, and what they want, and then they ask how economists and others might understand them better and what their views imply for globalization. They note that many critics are themselves strongly internationalist and want to see globalization proceed, but under different rules. Some, particularly the protesters in the streets, focus mainly on what is wrong with the world. But some of them put forward broad alternative visions, while others offer detailed recommendations for alleviating the problems they perceive in the current style of globalization. Most of the critics have their roots in longstanding transnational advocacy efforts to protect human rights and the environment and reduce poverty around the world. What brings them together today is a concern that the *process* by which globalization's rules are being written and implemented is undermining democracy and preventing the benefits from being shared broadly.

Elliot, Kar, and Richardson translate the issues and concerns that motivate the critics of globalization into the terms, concepts, and analytical approach of mainstream economics. They attempt to capture the concerns of Southern as well as Northern critics and to analyze the issues that divide them as well as those that bring them together. The authors find more resonance for the critics' agenda in existing economic analysis than is commonly recognized by either the critics or the "doers" of globalization. Finally, chapter 1 evaluates those issues and alternative proposals on which even globalization enthusiasts and the critics might come together cooperatively.

In chapter 2, Carl B. Hamilton considers directly the charge that globalization undermines democracy. He finds a superficial plausibility to the

view, but argues that, in general, it does not stand up to scrutiny. In particular, he reports survey results suggesting considerable support for globalization among the peoples of the world, although certain countries (e.g., France, Australia, Turkey, and Argentina) buck the trend, which is possibly, in the latter pair, a reflection of their recent financial crises. There is, however, a fairly widespread suspicion that globalization is bad for jobs. Hamilton argues from these results that the NGOs' hostility to globalization is not well grounded in popular support. But even if it were, he argues, the NGOs display a marked democratic deficit themselves: They are responsible to no one and are heavily biased toward the rich industrial countries rather than being representative of the South.

In the second part of chapter 2 Hamilton argues that democracy has both an intrinsic and an instrumental value, and that the World Bank, which is now heavily focused on issues of governance, should be less coy about promoting it directly. (He would not make democracy a condition for receiving World Bank loans, however.) He also argues that openness and globalization are positively associated with democracy—either promoting it or resulting from it—and from this he concludes that concerns about the democratic consequences of globalization are exaggerated.

Trade Flows and Their Consequences

Part II of the book considers the extent to which different countries can take advantage of globalization to expand their trade and two sets of consequences for any such expansion—the decline in prices facing primary product producers and the relocation of production to "pollution havens" that permit dirty technologies.

Chapter 3 by Stephen Redding and Anthony J. Venables investigates the determinants of countries' export performance, looking in particular at the role of international product-market linkages. It begins with a novel decomposition of the growth in countries' exports into the contributions from increases in external demand and from improved internal supply. For any exporter, the former is derived from aggregate expenditure in each market deflated by its local prices and its internal trade costs and aggregated over markets using a function of distance between the exporter and the market as weights. The latter (supply) component of export growth reflects the exporter's size (the number of varieties it produces) and its own internal trade costs. Among the notable results of this decomposition is the dominance of supply capacity growth in Southeast Asian exports over 1970–1985, but the importance of market access growth during the subsequent period 1985–1997, with the majority of that access growth coming from within the region. For sub-Saharan Africa, on the other hand, market access growth was below average over the entire 1970–1997 period and supply capacity growth was actually negative.

Building on the results of this decomposition, Redding and Venables move on to an econometric analysis of the determinants of export performance. Their results include the finding that poor market access, poor internal geography, and poor institutional quality contribute in approximately equal measure to explaining sub-Saharan Africa's poor export performance.

In chapter 4, Christopher L. Gilbert and Panos Varangis consider the effects of the trade and marketing liberalizations of the 1980s and 1990s on the West African cocoa producers. They pay particular attention to the "adding up" problem: Although each cocoa producer is small enough to have virtually no effect on world prices individually, if all liberalize simultaneously their aggregate effect is to drive world prices down. Since African exporters account for 60 percent of world production, such global effects are likely to be larger in cocoa than in any other commodity market.

Gilbert and Varangis' results show that a 3 percent reduction in taxes and intermediation costs (internal marketing) results in a 1 percent fall in the world cocoa price. Farmers in the liberalizing countries remain better off (by 2 percent), but developed country consumers also benefit (by 1 percent). Approximately one-third of the cost reduction in the African cocoa-producing countries arises out of efficiency gains and two-thirds from tax reductions. Thus the farmers' benefit is approximately equal to the governments' (and taxpayers') loss, while the benefits of the efficiency gains accrue more or less to developed-country consumers.

None of this implies that liberalization is undesirable, but it does suggest that the calculus of costs and benefits from liberalization is more complex than the proponents of liberalization programs have sometimes suggested. In particular, advocates of liberalization may have insufficiently distinguished the benefits of increased competition in commodity marketing from those of reduced taxation.

Jamie De Melo and Jean-Marie Grether join the debate on globalization and the environment in chapter 5. They ask whether trade and investment liberalization have allowed firms to relocate activity toward countries with low pollution controls, or "pollution havens." If so, there will be more pollution per unit of output and more output since lower abatement costs will induce greater demand. They work with a sample of fifty-two countries over the period 1980–1998, analyzing shifts in production, consumption, and trade in the five most polluting industries.

Globally, de Melo and Grether find that revealed comparative advantage in polluting products fell for developing countries for the five polluting products as a group, as one would expect if the environment is a normal good in consumption. However, this overall result was due to the influence of one important product, namely, nonferrous metals, for which the revealed comparative advantage ratio in developing countries fell significantly.

De Melo and Grether then fit a panel gravity model on bilateral trade data for dirty industries and show that, compared with nonpolluting industries, dirty industries have higher barriers to trade in the form of larger elasticities of bilateral trade with respect to transport costs. These results confirm the intuition that most heavy polluters are both weight-reducing industries and producers of intermediate goods. For these sectors, proximity to users will enter location decisions more heavily than for consumer goods, which are typically high-value products. Thus, they identify natural barriers to trade in the typical heavy-polluting industries as one of the factors accounting for less-than-expected relocation of such industries to the developing countries. Utilizing the difference in per capita income as a proxy for the regulatory gap between countries (the greater the per capita income difference, the wider the regulatory gap) and controlling for several factors that influence the volume of bilateral trade, the authors find little evidence in their statistical analysis that bilateral trade is influenced by regulatory gaps.

Overall, de Melo and Grether conclude that there is only limited support for the pollution-havens hypothesis. They do note, however, that they have examined only manufacturing and hence cannot take into account the resource-extracting industries that may have sought pollution havens.

Factor Markets: Labor

Part III contains three chapters on the labor market, covering the influence of globalization on relative skilled versus unskilled wages, the brain drain, and the economics of sweatshop labor in the developing world.

Increased trade (or potential trade) with developing countries is frequently blamed for the depression of unskilled wages and employment in the Organization for Economic Cooperation and Development (OECD) countries. Many economists have argued, however, that trade flows are not large enough to have had such effects or that commodity prices have not evolved in the way that such a hypothesis requires. Recently, however, research has revealed that vertical specialization—slicing up the value chain to take less-skilled operations abroad—could affect unskilled wages without final commodity price changes or large actual trade flows. Vanessa Strauss-Kahn explores this possibility in France over the period 1977–1993 in chapter 6. She shows that a decrease in trade costs (globalization) modifies the international structure of production toward vertical specialization, and that shifting relative labor demand across countries increases skilled and unskilled wage inequality in a way that is observationally equivalent to skilled-biased technological progress. She evaluates the contribution of vertical specialization in explaining the observed within-industry shift away from unskilled workers in France, using detailed input-output tables and labor data. She finds that vertical specialization, defined as the

share of imported inputs in production, rose from 9 percent in 1977 to 15 percent in 1996. Then, regressing industry employment against a scale variable, capital intensity, and the extent of vertical specialization, she finds that the last contributed 11 to 15 percent of the decline in the share of unskilled workers in French manufacturing employment over 1977–1985 and around 25 percent of the decline experienced over 1985–1993.

Chapter 7, by Simon Commander, Mari Kangesniemi, and L. Alan Winters, surveys current thinking on the brain drain, specifically from the point of view of developing countries. Estimates of the relative migration rates of educated individuals show that developing countries (especially small ones) can lose large proportions of their skilled workforces. Large countries, on the other hand, such as China and India, which supply a high proportion of the developed countries' skilled immigrants, lose only small proportions of their overall stock of skills. However, in recent years, migration has been particularly strong among information-technology workers, and the migration of health workers has long given rise to concern, and in these sectors outflows are proportionately significant, even for India.

Early theoretical models of the brain drain hinge around labor market distortions, such as wage rigidity and subsidies to education. They typically suggest negative implications from outflows, and, although these models were rarely tested empirically, their authors frequently advocated strong policy interventions, like taxes, to combat the brain drain. This conclusion ignored the role of remittances in sharing the benefits of emigration as well as the possibility that the improved skills of returning migrants and the business networks created by expatriates could also add to the local benefits of brain drain.

The most telling recent attempts to model the implications of the brain drain stress the formation of human capital and the positive impact that it can have on economic growth. If the chance of working abroad at high wages is related to levels of education, opening up the possibility of emigration raises the expected returns to education, which, in turn, increases the incentives to obtain human capital. Provided that not all the additional human capital so created actually emigrates, there is a possibility that the supply of human capital at home increases, thus leading to higher economic growth. General empirical evidence suggests that there may be a grain of truth in these models: private education has expanded considerably in developing countries. There is a caveat, however. Immigrants to the main receiving countries are carefully screened; if only the best are selected, the increased incentives due to emigration will be relevant only for the individuals with highest ability who would have chosen education anyway. The less able may never qualify for emigration, and so will not have any incentive to undertake additional education. Under this scenario the developing country would lose its best workers but create no additional skilled workers; it would unambiguously lose. Commander, Kangasniemi,

and Winters thus argue that such screening must lie at the heart of thinking about the "beneficial brain drain."

A frequently heard charge against globalization is that multinational firms in developing countries are exploiting their workers by paying them low wages and subjecting them to sweatshop working conditions. In chapter 8, Drusilla K. Brown, Alan V. Deardorff, and Robert M. Stern examine the empirical evidence on this issue as well as what economic theory has to say about the effects of foreign direct investment (FDI) and multinational firms on wages and investment. They begin by reviewing the campaign by American students against sweatshop conditions in poor-country firms producing apparel with logos of their universities and colleges and the controversies arising from the efforts to establish codes of conduct and monitoring systems for these firms. This is followed by a brief survey of what economic theory has to say about the effects of FDI and multinational firms on wages and working conditions in host countries. The chapter concludes with an examination of the empirical evidence on wages and working conditions associated with multinationals.

The authors are critical both of the lack of broad consultation in the processes by which many university and college administrators agreed to establish codes of conduct and monitoring systems, and of the practicality of the codes and monitoring systems themselves. They also conclude that whether transfers of capital, technology, or parts of the production processes to developing countries by multinational firms raise or lower wage levels in these countries is basically an empirical question. A theoretical overview of this issue yields ambiguous conclusions. Their review of the empirical studies of the issue finds virtually no solid and systematic evidence that multinational firms adversely affect their workers by paying lower wages than in alternative employment or worsen their working conditions. In fact, the opposite appears to be the case.

Factor Markets: Capital

Part IV of the book turns more directly to the activities of firms. Two chapters consider the behavior of multinational firms and foreign direct investments, and the third considers the implications of the recent wave of mergers and acquisitions.

In chapter 9, Robert Lipsey presents a detailed analysis and appraisal of the empirical findings concerning the home- and host-country effects of FDI. He first summarizes the empirical evidence concerning the effects of FDI on home-country exports and on home-country factor demand and then discusses wages, productivity, exports, and the introduction of new industries on the host-country side.

Debate over the possible substitution of U.S. firms' foreign production for U.S. exports began with worries about the U.S. balance of payments in

the 1960s. From his review of the many studies on this issue, Lipsey concludes that concerns over this possibility have mostly dissipated. His suggested interpretation of these studies is that foreign production by a firm or industry has very little influence on exports from the parent firm or its home country since trade is determined by other factors, such as countries' changing comparative advantages in production. Direct investment, he states, is mainly about the ownership of production, not its location. There is some evidence, however, that multilateral operations have influenced the demand for home-country factors of production. Specifically, they have led to a shift in the United States toward more capital-intensive and skill-intensive production, while unskilled labor–intensive production has been allocated to affiliates in developing countries.

Consistent with the conclusions reached by authors of other chapters in the volume, Lipsey finds abundant evidence that foreign-owned firms pay higher wages than domestically owned firms. In part this is because foreign-owned firms tend to be in high-wage sectors of the economy, to hire more educated and better qualified workers than locally owned firms, and to be larger and more capital intensive. There is also some evidence that foreign-owned firms pay a higher price for labor of a given quality, but there are not many studies that include data on worker characteristics. Comparisons of total factor productivity in foreign-owned versus domestically owned firms almost always find productivity levels to be higher in the foreign-owned firms. But evidence of spillovers of the higher foreign productivity to domestically owned firms is mixed. There is general agreement, however, that FDI leads to the introduction of new industries and products in the host-country economy and to an increase in knowledge about demand and world markets and how the host country can find a place in the worldwide allocation of intermediate steps in global production. Finally, inward direct investment is associated with faster economic growth, both through productivity effects and through the introduction of new products. Lipsey points out, however, that faster growth also involves disruptions and the destruction of old skills and production techniques, and some may not find foreign involvement to be beneficial, on balance.

In chapter 10 David Carr, James Markusen, and Keith Maskus examine whether multinational firms transfer production to developing countries largely to take advantage of the low wages of unskilled labor in these countries. They first point out that summary statistics comparing average per capita income in developing countries to average FDI per capita in these countries show FDI per capita to be the lowest in the poorest countries. For a given level of per capita income, they also find that FDI per capita is higher the larger a host country's gross national product. The authors conclude from these relationships that FDI is not aimed solely at exploiting cheap labor for export production and, moreover, that a significant pro-

portion of the existing foreign production in developing countries is intended for local sale.

Carr, Markusen, and Maskus next briefly review recent FDI theory, especially the knowledge-capital model developed by Markusen that allows for motives for both horizontal and vertical FDI. They then utilize data on outward investment from the United States for a large number of developed and developing countries (but, due to lack of data, excluding the least developed countries) over the period 1986–1997 to test hypotheses from this model about the patterns and determinants of FDI flows to developing countries. A feature that differs from their earlier empirical work is the addition to their econometric estimation of a measure of infrastructure quality to accompany such host-country characteristics as size (in terms of gross national product), labor force composition, investment barriers, and trade costs.

Their main conclusion is that U.S. outward investment generally seeks large, skill-abundant countries. However, outward investment in small host countries (both developed and developing) seems to be unskilled labor seeking. As far as production for local sales versus exports is concerned, affiliates in developing countries are not more export oriented than affiliates in developed countries. Inward investment from the United States is also encouraged by high-quality infrastructure and low barriers to investing and discouraged by a country's distance from the United States.

As the authors point out, these findings run completely counter to the contention of some anti-globalists that multinational firms are primarily attracted to countries with low-wage labor. They explain that very low-wage countries receive almost no FDI because branch-plant production (particularly setting up the branch plant) requires a certain minimum level of labor skills that are lacking in the very poorest countries. In addition, the absence of reliable legal institutions and infrastructures in these countries make them unprofitable locations for production.

In chapter 11, Simon Evenett explores the boom in cross-border mergers and acquisitions in the late 1990s. To establish a benchmark, he compares it with its predecessor in the late 1980s. The recent one is found to be at least five times larger (in real terms), to involve firms from more OECD nations, and to include many more service-sector transactions than the earlier one. Even so, in comparison to the size of national stock market capitalizations, foreign acquisitions of domestic firms during this latest wave were small, especially in the Group of Seven leading industrial economies. Thus, concerns that large shares of economic activity in OECD countries are falling into foreign hands are greatly exaggerated.

In the second part of chapter 11, Evenett examines the effect of cross-border mergers and acquisitions on performance in one important service sector, banking. Specifically, he estimates the relative importance of cross-border mergers and acquisitions, domestic mergers and acquisitions, do-

mestic entry and exit, and strategic alliances and joint ventures in explaining changes in interest-rate spreads in thirteen OECD nations. The principal findings suggest that the effects of these firm-driven changes in banking market structure differ markedly between European Union (EU) economies and non-EU industrialized economies. In the EU, cross-border strategic alliances appear strongly to increase spreads—that is, to be anticompetitive—whereas full cross-border mergers appear to reduce them, presumably via efficiency gains. Domestic changes in industry structure seem to have little net effect. Outside the EU, on the other hand, domestic changes have tended to increase spreads while cross-border alliances and mergers have reduced them in almost equal measure. These results highlight the importance of differentiating between types of cross-border interfirm agreements and the pitfalls of generalizing about the effects of the latest wave of cross-border mergers and acquisitions.

Macroeconomics

Finally, part V of this book considers the effects of globalization in the large—first on financial stability and second on economic growth.

In chapter 12, Joshua Aizenman evaluates the empirical evidence on whether opening up developing countries to short-term capital flows increases the chance of financial crises and then appraises various recent proposals for reducing this possibility.

On the basis of his survey of recent research into financial crises across countries, Aizenman argues that there is solid evidence that financial opening increases the chances of such crises in developing countries. This research also finds tenuous evidence that financial liberalization increases growth over time. Thus, there may be a complex trade-off between the adverse intermediate-run and beneficial long-run effects of financial opening. The core of the problem, he argues, is that we deal with incomplete financial markets, exposing creditors to sovereign risk and moral hazard. But, since greater trade integration erodes the effectiveness of restrictions on capital mobility, financial opening for successful emerging markets that engage in trade integration is not a question of *if*, but of *when* and *how*. Aizenman maintains there is no quick fix to the exposure to financial crises induced by financial opening and, instead, that we should focus on reducing the depth and frequency of such crises.

Aizenman is rather skeptical about the effectiveness of many of the new proposals aimed at reducing the costs of financial crises on the general grounds that any significant reform will change agents' behavior in ways that are hard to predict without a better understanding of the fundamental forces explaining sovereign borrowing and default. For example, he doubts the degree to which such ideas as insurance, which is based only on meeting ex ante conditionality, will survive the time-inconsistency and

transparency challenges. Similarly, in view of the greater weight of nonbank lending and the great increase in the number of institutional investors, he expects recent reform proposals dealing with better coordination among creditors and with formation of international bankruptcy procedures to be vigorously tested by coming crises.

In the final chapter, Robert Baldwin reviews and appraises empirical research since the 1950s concerning the manner in which the international economic policies of governments affect the rates of growth of their economies. The first set of detailed empirical studies of the impact of international economic policies on economic growth were undertaken in the early 1970s in response to the growth difficulties faced by a number of developing countries that had seemed to successfully pursue import-substitution policies after World War II. The early widespread support by economists for these policies was based on an extension of the infant-industry argument to the manufacturing sector as a whole and on earlier experiences with protecting home markets in various developed countries. However, case studies of most of the developing countries showed that their levels of import protection measured on a value-added basis were not only extremely high and variable across industries, but also penalized export activities. Later case studies that broadened the policy framework to include monetary, fiscal, and exchange-rate policies further strengthened the argument that import-substitution policies were holding back growth rates and helped to convince many developing-country governments to shift to an export-oriented approach to development.

Stimulated by new theories of endogenous growth and improved econometric techniques in the early 1990s, a succession of large cross-country statistical studies have found a strong positive relationship between outward-looking policies and growth rates of gross domestic product (GDP) or total factor productivity. These studies have recently come under criticism, however, especially by Francisco Rodriguez and Dani Rodrik, on the grounds that the tariff and nontariff components in the authors' broad measures of openness do not by themselves support this conclusion or that they fail to do so in a robust manner under reasonable respecifications of their econometric models.

Baldwin's evaluation of this controversy is that, while we should be grateful to Rodriguez and Rodrik for pointing out that a liberal trade policy alone is not always associated with faster growth rates, these authors adopt an overly narrow policy viewpoint when they contend that the main implication of the studies is that countries should dismantle their barriers to trade. Authors of both the case studies and cross-country statistical analyses almost uniformly argue that a whole set of policies—ranging from sound monetary, fiscal, and exchange-rate policies to responsible government behavior and a transparent legal system—is necessary for raising developing-country growth rates in addition to trade liberalization.

Some Conclusions

The chapters of this book do not examine every criticism that has been made of globalization, but especially on the real (as opposed to the financial) side of the economy they deal with the main ones. The book demonstrates that most of the current complaints have already been addressed by economists in their serious academic research. While most criticisms are valid in theory under some sets of circumstances, and while many of them can be identified to have occurred in specific cases, most turn out not to be major systemic problems. Thus, for example, openness to trade (accompanied by appropriate policies elsewhere) generally assists growth, multinationals do not generally drive down wages or labor standards, and trade does not generally lead to a race to the bottom in environmental standards.

On the other hand, the chapters have confirmed that globalization can cause problems for some people under some circumstances—for example, in reducing the prices of primary exports, reducing competition in sectors subject to mergers and interfirm agreements, and via the emigration of talented workers. In these cases, however, appropriate policy responses can often serve to alleviate or bypass the problems.

The fact that globalization can cause problems for some people, or in some circumstances, sometimes appears to be enough for critics to reject it out of hand. We—and most economists, we believe—would reject that response. Virtually every issue of public policy involves trade-offs of some sort. If a society gains on average from a reform, there is a strong case for making the reform and compensating the losers.

Considering compensation brings us face to face with the issue of the distribution of welfare—not only of income but also of things like human rights and social inclusion. These are important issues on which opinions differ, and it is legitimate for different groups to debate their views and to reach different conclusions about economic policies on the basis of them. Economists as a group have no particular position in these debates, nor expertise in ruling one view better than another. They do, however, seek to be explicit about the value judgments entailed in their models and to distinguish between judgments on issues such as these and positive economic analysis (the way in which the economy operates). It is frequently the case that, once value judgments and analysis are separated, it becomes evident that objectives can be met more effectively by policies that maximize economic welfare than by any others. This is precisely the case for globalization: by maximizing economic activity and organizing it efficiently it becomes easier to achieve the goals to which society aspires.