

Why Globalization Is in Trouble – Part I

The dominant world powers historically pushed for globalization as a means of increasing wealth and influence. Yet those nations fret as the emerging powers of India and China embrace the same strategy. This two-part series by World Bank economist Branko Milanovic explores why both the world's wealthiest and poorest nations fear globalization. In the first article, Milanovic argues that citizens of wealthy nations hold two concerns: job loss resulting from competition with low-wage countries and loss of national identity resulting from increasing numbers of immigrants. With educated, skilled workforces, the two emerging economies have mastered economic globalization: China has plenty of surpluses to export, and India has become an information-technology leader. Immigration not only threatens jobs in the developed countries, but also challenges national culture and solidarity, particularly if large numbers of immigrants fail to assimilate into their new homelands. Europe, by not welcoming its immigrants or allowing them to move up career ladders, faces greater challenges than the US. In the end, Milanovic concludes, "Europe needs no less than a social revolution: replacement of its welfare state, and acceptance that Germans, French or Italians of tomorrow will be much darker in their skin color." – YaleGlobal

Job loss and worry about identity make the West reconsider the value of trade and immigration

Branko Milanovic
YaleGlobal, 29 August 2006

WASHINGTON: Historically, the dominant power tends to support globalization as a way to increase the ambit of its influence, expand trade and gain economic advantage, co-opt new citizens and possibly show the advantages of its own pax. This was the case with the Roman, British and now American-led globalizations. But recently, the rich West – which saw globalization as a prelude to "the end of history" – is having second thoughts.

Two fears drive this unease with globalization: The first is a fear of job loss due to competition from low-wage countries. The second is the fear of ethnic and cultural dilution due to increased immigration.

The cause of the first fear is a fast reemergence on the world stage of China and India. For students of history, the rise of China and India is not a surprise. The two countries are just recapturing the ground lost during the 19th and most of the 20th century. Before the Industrial Revolution, China's and India's combined output accounted for one half of the world's total. Now, after a quarter-century of China's spectacular growth, and more than a decade of India's growth acceleration, the two countries contribute less than a fifth of total world output. Although their share is, in the long-term historical sense, still below what it used to be, it has nevertheless increased dramatically compared to where it was 30 years ago. The rise of the two Asian giants, reflected in their dynamic trade, large Chinese export surpluses and India's role as an outsourcing center and a potential leader in information technology, has made the West wonder whether it can compete with such hardworking, cheap, plentiful and yet relatively skilled labor.

While the fear of job loss is driven by fast economic growth of the two giants, the fear of immigration is, ironically, caused by the slow economic



Falling income, rising migration: Increasing number of illegal Mexican immigrants are rounded up at the US-Mexico border

Two fears drive unease with globalization: job loss due to competition from low-wage countries and ethnic dilution due to increased immigration.

growth of the rest of the developing world. The people who try to reach the shores of Europe or cross from Mexico into the US come from the countries that have disastrously fallen behind Western Europe and the US during the last quarter century. In 1980, Mexico's real per-capita income, adjusted for the differential price level between Mexico and the US, was a third of that in the US. Today, the ratio is almost 4.5 to 1. The poor Africans who land daily on beaches of the Spanish Canary Islands come from the countries that have seen no economic growth in 50 years. Take Ghana, a country often touted as an African success case: Around its independence, in 1957, its income was one half of Spain's; today, it is one tenth.

Immigration puts a similar pressure on low- or medium-skilled jobs in the West as do cheap imports from China and outsourcing to India. And indeed, wages of low- and medium-skilled workers in the rich countries have failed to keep pace with incomes of educated workers at the top of the pyramid. While the median US real wage has not risen in real terms over the last 25 years, real wages of the top 1 percent have more than doubled. The richest 1 percent of Americans today controls almost 20 percent of total US income, a proportion higher than at any time since the Roaring Twenties. The U-turn of inequality – a sharp increase that started during the Thatcher-Reagan era, after a long decline – has affected, to a varying extent, all Western countries.

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But at stake is something more profound than a threat to jobs and stagnant wages in a few “exposed” sectors. After all, the West is no stranger to structural change. Ricardo in his “Principles” written in 1815 discusses labor dislocation “occasioned” by the introduction of machinery. The Western countries handled the decline of powerful industries like coal, textile and steel. Economists have never been sympathetic to the protection arguments of sunset industries: In an expanding economy, structural change is necessary and inevitable; jobs lost in one industry will reappear as new jobs in another industry.

The difference now is that the twin challenge undermines the consensus upon which the West's welfare state was built since World War II. To understand why, recall that the Western welfare states rest on two building blocks: those of ethnic and social solidarity. The first building block implies that one is willing to be taxed if certain that aid will flow to somebody who is ethnically or culturally similar. But once large stocks of immigrants with different, and not easily adaptable, social norms, arrive, that certainly is no longer. More immigrants will strain the already-tattered solidarity among citizens of rich European countries.

Economic inequality translates into a cultural divide: The elites are culturally different from their own poorer ethnic brethren.

The second building block of the welfare state is class solidarity. For it to exist, there must be relatively similar economic conditions between classes so that one can reasonably expect that for social transfers paid out of his pocket today, he may be compensated – if the need arose – by a similar benefit in the future. If, for example, unemployment rates are relatively equal across skill levels, then the highly skilled will pay for unemployment benefits; but if unemployment rates are different, the highly skilled may opt out. As the income divide widens in the West between the rich and the highly educated who have done well, and the middle classes and the unskilled who are merely scraping by, the second building block on which welfare capitalism was built crumbles. Economic inequality also translates into a cultural divide. “Ethnic” migrants

who fill the rungs of low-paid workers are not the only ones economically and culturally different from today's Western elites; the elites are also growing more different from their own poorer ethnic brethren.

So far reaching, these developments require an entirely new social contract, a redefinition of capitalism no less. Such fundamental changes are not easy to come by when the threat is subtle, continuous, incremental and far from dramatic in a daily sense. Difficult decisions can be postponed, and neither politicians nor the electorate have an appetite for change. A battle of attrition regarding who would bear the costs of adjustment ensues, and this is at the heart of Europe's present immobilism.

Why is the development of "new capitalism" and rethinking of the old social contract so much more difficult for Europe than for the US? First, for an obvious reason, because Europe's welfare state is much more extensive, more embedded in ordinary life, and its dismantlement is more socially disruptive. Second, because a low population growth – or in many countries, a decline – necessitates continuing large immigration. But, and this is the crux of the matter, Europe struggles more in absorbing immigrants than the US.

Historically, of course, Europe was not a society of immigrants. Europeans were happy to receive foreign workers as long as they would do low-paying jobs and stay out of the way. This quasi-apartheid solution preserved immigrants' culture, which then, most famously in the Netherlands, was found to clash with some European values. Immigrants, more so their daughters and sons, were not happy to remain in subaltern jobs. And while Europe was good about welcoming them to its soccer and basketball teams, it was more stingy when it came allowing them to direct operating rooms or boardrooms.

Europe is good about welcoming immigrants to its soccer teams, but more stingy about allowing them into boardrooms.

The bottom line is that Europe needs no less than a social revolution: replacement of its welfare state, and acceptance that Germans, French or Italians of tomorrow will be much darker in their skin color, composed of individuals of various religions, and in many respects indeed a different people. As fusion of Frankish ethnicity and Latin culture created France, a similar Christiano-Islamic and Afro-European fusion may create new European nations, perhaps with a different outlook on life and social norms. No society can accomplish such epochal transformation quickly and painlessly.

Why Globalization Is in Trouble – Part 2

Globalization has spurred inequality – both among citizens in the wealthiest countries as well as among nations of the developing world. The second of this two-part series by Branko Milanovic explores the growing resentment as only a few poor countries adjust to globalization. China and India compete globally, and yet only a fraction of their citizens prosper. Increasing inequality between rural and urban populations and between coastal and interior areas in China could have disastrous consequences in the event of political transition. Forty of the poorest nations, many in Africa, have had zero growth during the past 20 years. Their governments followed advice from wealthy nations and World Bank consultants, on issues from privatization to development, but millions of people suffer from poverty. Ironically the wealthiest people benefit from the source of cheap labor, and policies of the West reinforce a growing divide between rich and poor. Desperate immigrants flee their homelands, lacking confidence that their governments can ever overcome the increasing obstacles. For the world's poor, globalization has resulted in a loss of self-respect and hope. – YaleGlobal

The politics of global resentment will find many followers in the fragmented and weak undeveloped world

Branko Milanovic
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WASHINGTON: In the rich world globalization had driven the wedge between social classes, while in the poor world, the main divide is between countries: those that adjusted to globalization and, in many areas, prospered and those that adjusted badly and, in many cases, collapsed.

Indeed the Third World was never a bloc the way that the first and second worlds were. But it was united by its opposition to colonialism and dislike for being used as a battlefield of the two then-dominant ideologies. As the Second World collapsed and globalization took off, the latter rationale evaporated, and a few countries, most notably India and China, accelerated their growth rates significantly, enjoying the fruits of freer trade and larger capital flows. And although these two countries adapted well to globalization, there is little doubt that their newfound relative prosperity opened many new fissure lines. Inequality between coastal and inland provinces, as well as between urban and rural areas, skyrocketed in China. So did, and perhaps by even more, inequality between Southern Indian states, where the hub cities of Mumbai, Chennai and Bangalore are located, and the slow-growing Northeast. For China, which still may face political transition to democracy, widening inequality between different parts of the country, could have disastrous consequences.

But another large group of Third World countries, from Latin America to Africa to former Communist countries, experienced a quarter century of decline or stagnation punctuated by civil wars, international conflicts and the plight of AIDS. While between 1980 and 2002, the rich countries grew, on average, by almost 2 percent per capita annually, the poorest 40 countries in the world had a combined growth rate of zero. For large swaths of Africa where about 200 million people live, the income level today is less than it was during the US presidency of John F. Kennedy.

For these countries the promised benefits of globalization never arrived. The vaunted Washington consensus policies brought no improvement for the masses, but rather a deterioration in the living conditions as key social services became privatized and more costly as was the case, for example, with water privatizations in Cochabamba, Bolivia, and Trinidad, electricity privatization in Argentina and Chad. They were often taken

over by foreigners, and to add insult to injury, Western pundits arrived by jets, stayed in luxury hotels and hailed obvious worsening of economic and social conditions as a step toward better lives and international integration. For many people in Latin America and Africa, globalization appeared as new, more attractive label put on the old imperialism, or worse as a form of re-colonization. The left-wing reaction sweeping Latin America, from Mexico to Argentina, is a direct consequence of the fault lines opened by policies that were often designed to benefit Wall Street, not the people in the streets of Lima or Caracas.

Other Third World states – particularly those at the frontline of the battle between communism and capitalism, with ethnic animosities encouraged during the Cold War, efforts by Washington and Moscow to get the upper hand in the conflict – exploded in civil wars and social anomies. That part of the world associates globalization with disappointment (because Washington consensus never delivered), resentment (because others got ahead) and poverty, disease and war. In several sub-Saharan African countries, life expectancy at the turn of the 21st century is not only where it was in Europe almost two centuries ago but is getting worse. In Zimbabwe, between 1995 and 2003, life expectancy declined by 11 years to reach only 39 years.

Ideologies which proposed some economic betterment and offered self-respect to many people in Africa (from Kwame Nkrumah's African socialism to Julius Nyerere's "cooperative economy") and parts of the former Communist bloc (Tito's "labor management") all collapsed and have given way to self-serving oligarchies that justified their policies, not by calling on their own citizens, but by publishing excerpts from reports written by the World Bank and the International Monetary Fund.

In the Third World as a whole, globalization, at best, produced what Tocqueville, with a touch of aristocratic disdain, called a government of the commercially-minded middle classes, "a government without virtue and without greatness"; at worst, it produced governments of plutocrats or elites unconcerned about their own populations. Globalization thus appeared in the poorest and weakest countries at its roughest.

Perhaps the greatest casualty of the money-grubbing global capitalism was loss of self-respect among those who have failed economically – and they are preponderantly located in the poorest countries. The desperate African masses who want to flee their own countries leave not only because incomes are low and prospects bleak, but also because of a lack of confidence that either they or their governments, no matter who is in power, can change life for the better. This despondency and loss of self-respect is indeed a product of globalization. In the past one could feel slighted by fortune for having been born in a poor country, yet have as compensation a belief that other qualities mattered, that one's country offered the world something valuable, a different ideology, a different way of life. But none of that survives today.

The problem was, strangely, noticed by Friedrich Hayek. Market outcomes, Hayek argued, must not be presented as ethically just or unjust because the market is ethically neutral. But to buttress the case for global capitalism, its proponents insist in an almost Calvinist fashion that economic success is not only good in a purely material sense, but reveals some moral superiority. Thus winners are made to feel not only richer but morally superior, and the converse: The losers feel poor and are supposed to be ashamed of their failure. Many people do, but understandably not all take gladly to such judgment.

An interesting coincidence of interests emerges between the desperate masses and the rich in advanced countries. The latter, educated and with considerable property "interests," are, economically, often in favor of greater Third World competitiveness and migration since, either as investors abroad or consumers of

cheap labor services at home, they benefit from low-wage labor. This unlikely coincidence of interest lends some superficial justification to the claims of George Bush and Tony Blair that the opponents of free-trade pacts work against the interests of the poor. The problem that the president and the prime minister fail to acknowledge, or perhaps even to realize, is that many of the policies urged by their governments on poor countries in the last two decades have indeed brought people to their current point of desperation.

Sandwiched between this unlikely "coalition" of the global top and the global bottom, are globalization's losers: the lower and middle classes in the West, and those in the "failed" states, not yet sufficiently desperate to board the boats to Europe or cross the US border at night. They too lost in terms of their national sovereignty and personal income. They may not gladly accept, though, that they are morally inferior. At first sight, they do not seem likely to derail globalization because their power is limited. Yet in a more interdependent world with an easy access to deadly weapons, politics of global resentment may find many followers.

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