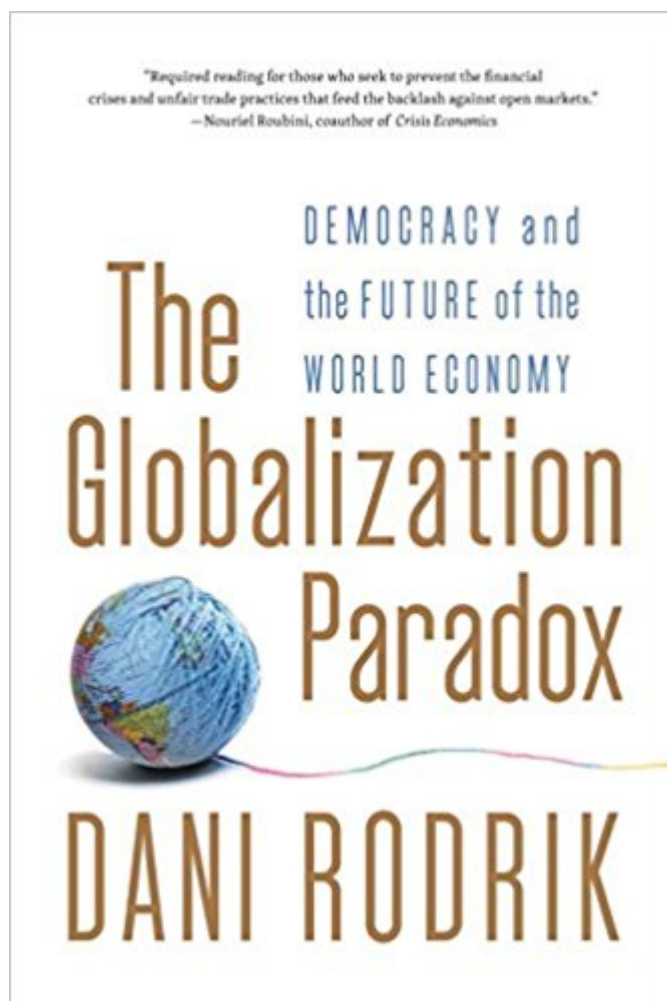


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# The Globalization Paradox: Democracy And The Future Of The World Economy



## Synopsis

"Cogent, well-written . . . critiques unalloyed globalization enthusiasts, taking aim at their desire to fully liberalize foreign trade and capital movements." *Foreign Affairs* In this eloquent challenge to the reigning wisdom on globalization, Dani Rodrik reminds us of the importance of the nation-state, arguing forcefully that when the social arrangements of democracies inevitably clash with the international demands of globalization, national priorities should take precedence. Combining history with insight, humor with good-natured critique, Rodrik's case for a customizable globalization supported by a light frame of international rules shows the way to a balanced prosperity as we confront today's global challenges in trade, finance, and labor markets.

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## Customer Reviews

"Required reading for those who seek to prevent the financial crises and unfair trade practices that feed the backlash against the open markets." - Nouriel Roubini, coauthor of *Crisis Economics: A Crash Course in the Future of Finance*

"Dani Rodrik may be globalization's most prominent and most thoughtful gadfly. In *The Globalization Paradox* he wonders aloud whether extreme globalization undermines democracy and vice versa. Read it and you'll wonder too." - Alan S. Blinder, former vice chairman of the Federal Reserve's Board of Governors

"Takes on the

biggest issue of our time—globalization—and eloquently enlarges the debate about the extent and limits of global cooperation.

—Gordon Brown, former British Prime Minister

“In this cogent, well-written book, Rodrik, a Harvard economist, critiques unalloyed globalization enthusiasts, taking aim at their desire to fully liberalize foreign trade and capital movements.

—Richard N. Cooper, *Foreign Affairs*

“Although [Rodrik’s] message is nuanced and rigorous, drawing on history, logic and the latest economic data, he manages to convey it in simple, powerful prose that any reader can follow. . . . A much-needed addendum to [Adam] Smith’s famous formulation.

—Steven Pearlstein, *Washington Post*

“Simply the best recent treatment of the globalization dilemma that I’ve read, by an economist or anyone else. . . . He gives us nothing less than a general theory of globalization, development, democracy, and the state. The book provides the pleasure of following a thoughtful, critical mind working through a complex puzzle. Rodrik writes in highly friendly and nontechnical prose, blending a wide-ranging knowledge of economic history and politics and a gentle, occasionally incredulous, skepticism about the narrow and distorting lens of his fellow economists.

—Robert Kuttner, *American Prospect*

“A Big Book, one that may shape a new way of thinking about the global economy. . . . The style is conversational, but sweeping and authoritative—professorial in the positive sense. Rodrik is less of a polemicist . . . preferring to stay inside the tent, but he can pack a polite punch when necessary.

—Duncan Green, Oxfam International, author of *From Poverty to Power*

“Mr. Rodrik is exactly what the doctor ordered because economics over the past few years has become hyper-politicized (thank you, Paul Krugman) yet never more dismal. Well-written, witty, crafted by an author who doesn’t jump the “Freakonomics” shark, *The Globalization Paradox* reminds us that economists don’t exist without data, and data comes, ultimately, from the vision and labor of those in the marketplace.

—Robert Nersesian, *New York Journal of Books*

Dani Rodrik, a prize-winning economist, is the Ford Foundation Professor of International Political Economy at Harvard’s John F. Kennedy School of Government. He is the author of *The Globalization Paradox* and *Economics Rules*.

Every student in economics is familiar with Robert Mundell’s triangle of impossibility. Based on the model that the Canadian economist developed with Marcus Flemming in 1962, this trilemma states that it is impossible to have a sovereign monetary policy, free capital flows, and a fixed exchange rate at the same time—that two, and only two, of these objectives could be met. This impossible

trinity came to dominate policy debates in Europe in the run-up to the European monetary union in the 1990s--a rare example when the result of a theoretical model had a direct bearing on policy choices. Although he doesn't develop a formal model, Dani Rodrik offers his own, more ambitious version of the impossibility triangle. The political trilemma of the world economy, as he names it, is that we cannot have deep economic integration ("hyperglobalization"), national sovereignty, and democratic politics at the same time. We have to sacrifice one of the corners of the triangle. And for Rodrik, the objective that has to be abandoned is clear and straightforward. We cannot compromise on democracy, and global governance is nothing but a distant dream. We therefore have to jettison hyperglobalization in favor of a more shallow form of global economic integration, a new version of the compromise that was embodied in the postwar system laid out at Bretton Woods. In particular, unrestricted capital mobility and indiscriminate trade openness will have to go. This will make the world a safer and better place for democracy. Dani Rodrik, who teaches at Harvard's Kennedy School of Government, is a first-class economist. In academic and policy circles, people talk about him with respect and sometimes even with awe--it is better to have him on the same side of an argument than sitting across the table. Some economists perfidiously point out that he has a talent for bending numbers to support his claims-- that he is an expert in the art of political econometrics, or the use of statistical regressions to support one's political positions. But this is how the game of economics ought to be played. Although Rodrik is sometimes considered as a maverick and a lone wolf, he speaks from inside the tent. No one would put into question his qualification as an economist. Sure enough, his arguments are often controversial and even provocative, but they are receivable and debatable by the academic community. "He is one of us", most if not all economists would acknowledge. This is why his criticism of globalization ought to be read with great attention and interest. It comes at a time when the high hopes invested in globalization have receded, and the negative aspects brought about by open borders and financial liberalization now take center stage. At this juncture, as Rodrik underscores, we need a new narrative to shape the next stage of globalization. "Economists have been responsible for the narratives that interpret development success and failure, narratives which in turn have guided policy in many parts of the world." They now have a special responsibility for shaping the debate: because they have been the cheerleaders of the previous phase of global openness, and because they can help distinguish snake oil from real ointments, and separate "the legitimate wheat from the 'protectionist' chaff". Many prominent economists are now starting to have second thoughts on globalization. True, their choir was never at unison: some had different pitches, and their endorsement of free and open markets often came with caveats and restrictions. Even a staunch free-trader like Jagdish Baghwati expressed warnings

about unrestricted capital mobility. Now more voices are beginning to worry about the consequences of deindustrialization, the growth of inequality, and the race to bottom standards and regulations brought about the current wave of globalization in developed economies. As Keynes once famously remarked, "When the facts change, I change my mind--what do you do, sir?" Rodrik, for one, never changed his mind on trade liberalization. He was one of the first economists to bring the debate from the seminar room to the political arena, and to argue against the simplistic case for free trade that is often doled out to journalists to support claims about the benefits of globalization. He comments the matter with considerable talent and great humor--never was a class discussion on comparative advantage and international trade theory so lively and refreshing. Dani Rodrik doesn't limit his argument to modern textbook economics. He excavates from the dusty shelves of economics libraries some forgotten books and tracts that are singularly relevant for today. Henry Martyn's *Consideration Upon the East-India Trade*, written in 1701, anticipates many of the arguments that economists who favored free trade would marshal much later. In 1961, James E. Mead wrote *The Economics and Social Structure of Mauritius*, and proposed the same kind of diagnostic tools and policy approach that Rodrik and his coauthors would later develop and sell out to the World Bank. This approach, called the "Growth Diagnostics framework", now serves as reference in international policy debates and is quoted approvingly by senior officials from emerging countries who are now the darlings of international gatherings. Development economics has come full circle: as Rodrik notes, "that industrial policy, in whatever guise, is once again considered acceptable, and indeed necessary, speaks volumes about how far we have retreated from the trade fundamentalism of the 1990s." Rodrik also has his weak points. He is candid about his limitations as a forecaster. He didn't see the Asian crisis coming in 1997, and he got it wrong again in 2007 when he missed the subprime crisis that was brewing in the U.S. More to the point, he picked up the wrong fight in the late 1990s, arguing against free trade when the real menace was coming from the excesses of financial globalization. One gets the feeling he still gives too much importance to the trade agenda as defined by the WTO in comparison to the new trade rules and conditions negotiated away from public scrutiny in the bilateral or regional trade agreements that now span the world in a complex web of policy arrangements. Rodrik is on less familiar ground when he discusses international finance, and his plea for an international transaction tax could have been more substantiated. In making the case for their pet theory, economists often miss the broader picture. Not so with Dani Rodrik. His list of principles and recommendations that close the book offer an all-encompassing agenda for a better and safer globalization. It is altogether fitting that the quote which best sums up his policy stance was offered by a Chinese student, who recommended to keep

the windows open, but without forgetting the mosquito screens. This utterance could have been offered by a future statesman and, considering the wide audience that Dani Rodrik's essay deserves, it could as well be picked up by one.

The Globalization Paradox adds rhetorical flair to Dani Rodrik's previous work condemning the intrusions of the WTO and IMF on the mechanisms of nation-states. Rodrik now dubs his enemy "hyperglobalization" (previously known as "deep integration") and insists that it be slayed to promote the diversity of social concerns across the world's democracies. The book augments the global economic governance chapters of "One Economics, Many Recipes" (a 2007 hodgepodge of the author's previous work) with richer historical context and topical material on the financial crisis and China's rise. I read several thoughtful reviews of Rodrik's last book in economics journals, and I am disappointed these reviews did not lead Rodrik to engage more of the recent economic literature in trade policy. Yet I still appreciate this book for asking important policy-relevant research questions that economists have often neglected. A sizeable chunk of the book is navel-gazing: humbly defending the economics profession, while criticizing its members for unequivocally endorsing free trade in public. His most pointed barb is accusing economists of using more conditional views of free trade in the seminar room. I'm reminded of Elhanan Helpman and Paul Krugman's seminal 1989 trade policy monograph, which surveys several trade models in which government intervention is optimal. Yet the authors conclude, "The design of an advantageous trade policy requires information of a kind that is simply not available." This was not one of the seven "hand-waving arguments" Rodrik cites in support of free trade, but it's an important argument he should have engaged. Rodrik downplays the concern from economists that much of trade policy in democracies is political rent-seeking. If there were a referendum for every trade policy decision, and citizens were perfectly informed about the impact of each one, would trade policy be much different from today? In other words, what share of trade policy originates from opportunistic lobbyists rather than legitimate democratic social preferences? I can imagine U.S. citizens protecting a few paper mill towns, but I don't see them keeping sugar quotas or subsidies for Brazilian cotton farmers. What gains are left for further international liberalization? Rodrik argues wisely that because manufacturing liberalization has proceeded so far already, further liberalization will lead to much larger distributional effects than gains from trade. I was disappointed that Rodrik selectively cites Andrew Rose to suggest the GATT & WTO has had little effect on expanding trade, yet economists Arvind Subramaniam & Shang-Jin Wei have shown that only countries who actually liberalized themselves gained trade from the WTO -- as theory would predict. Rodrik is correct that overall

gains from temporary migration (practically nonexistent at present) are much larger than gains from tariff liberalization. The same logic would suggest massive gains from liberalizing other forms of services trade (temporary migration of workers is but one form), and Rodrik does not mention this. Even if one disagrees with Rodrik on normative trade policy, determining the ideal global institutions for balancing conflicting policy preferences across nation-states is still practically important. Rodrik makes a convincing case for the impossibility of global federalism (fantasy-crushing for Rodrik's Harvard Kennedy School students). He makes a good case that capital controls are necessary to allow for different national priorities in regulating finance. I'm less sold on Rodrik's claim that U.S. credit rating agencies are proof that labelling and corporate social responsibility cannot succeed: his example is a closed market in which government created rents by limiting entry to three firms. Regardless, I agree with Rodrik that nation-states are not going to completely surrender their sovereignty to a WTO-like organization, and there needs to be an institution that can allow them to negotiate over their distinct policy preferences. Rodrik believes that the WTO overreached on national sovereignty, and he looks back longingly on the lighter integration of the GATT and Breton Woods regime from the late 1940s. What you won't learn from Rodrik is that Kyle Bagwell and Robert Staiger formalized such a theory, influential in the international law literature and published in top economic journals over the previous decade. Bagwell and Staiger suggest the ideal trade institution, similar to GATT, is one where nations negotiate over market access commitments, and countries should be free to choose any mixture of domestic policies and trade policies which maintains the negotiated level of market access. The mess of safeguard schemes that Rodrik instead proposes sound similar, yet it is hard to be sure without formalism. What is clear is that Rodrik believes domestic concerns are far more important than any international externalities created by trade and domestic policy choices, and he believes the market access focus of trade negotiations is problematic. Rodrik used to have an active blog on international economics, but he came to a near full stop, believing that the blog and book-writing were substitutes. Still I hope the blog can be complementary to the further development of Dani's thinking on these important issues.

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