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CHAPTER 2

The Backlash Against Globalization and the Future of the International Economic Order

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Political events of the past few years have called into question the future of an integrated international economy. Brexit, the election of Donald Trump, the rise of parties of the right and left that are sceptical about economic integration – whether at the global or European level – have all challenged the previously common assumption that globalization had become the natural and normal state of international economic affairs.

In reality, scholars and other analysts have been discussing a globalization backlash for some 20 years; what has changed is that we now have some idea of what it looks like. For the future of the world economy, the election of Donald Trump is by far the most important result of this backlash. The United States has been the unquestioned leader of the international economic order since it managed its creation at Bretton Woods in 1944, and President Trump has been explicit about his intention to remake that order. Although there are obstacles to his goals, the fact that he is the chief executive of the world's most important economy means that his views will have a profound impact.

Whether hostility to international economic integration continues to grow or not, the wheels are already in motion to remake fundamentally the global economy's ordering principles. Given the shift in the American government's orientation, other nations' governments have incentives to work out alternative arrangements not so reliant upon American leadership. If current trends persist, and the United States continues to abandon its traditional leadership role, the world is likely to be far more fragmented among regional trading areas. Barriers between these areas and the United States (and its closest trading partners) are likely to grow. Fragmentation in trade relations is likely to lead to similar fragmentation in international finance and investment.

The continuation of current trends is not inevitable. However, the past five years have set in motion developments that will be difficult to slow and even more difficult to reverse. The future of the world economy is likely to be substantially different from its recent past.

The World Economic Order: the Past 70 Years

The United States and its close allies constructed the contemporary international economy during and immediately after World War II. This economic order, which prevailed first throughout the capitalist world, then after 1989 in the entire world, was based on organizing principles that were similar to, and grew out of, the approach that had come to order advanced industrial societies domestically.

The central goal of the Bretton Woods Agreement was to oversee the gradual liberalization of international trade, investment, and finance after the disastrous experiences of economic nationalism and protectionism that had characterized the interwar period. However, the United States' construction of a new international economic order, in concert with its allies, incorporated an understanding that the political economies of the post-World War II industrialized world were profoundly different from those of the Victorian gold-standard era. Economic openness was eminently desirable, but it could not come at the expense of the social policies that had become standard in the advanced societies. Nor was it advisable to move too quickly in subjecting domestic industries to international trade competition, or in opening the current and capital accounts of countries that had recently experienced massive financial crises. So the Bretton Woods system was based on compromise. International economic integration would progress, but so would national commitments to counter-cyclical macroeconomic demand management and to the modern welfare state.[1]

Since World War II, the world economy has gradually, sometimes in fits and starts, become more open. In the 1950s and 1960s the process was largely restricted to the Western industrial economies, among which trade barriers came down, international investment grew, and international finance revived. The 1970s were a troubled decade of recessions, high unemployment, and high inflation, during which the desirability of an integrated global (capitalist) economy was often called into question. The issue was joined and decided over the course of the 1980s. The advanced industrial countries brought inflation down and continued their efforts to increase economic integration – including, most prominently, with substantial progress toward a single market and exchange-rate stability in the European Union (EU). In the aftermath of the debt crisis of the early and middle 1980s, most developing countries turned away from import substitution and toward export promotion, following the example of such countries as South Korea and Taiwan. Even more strikingly, China and Vietnam also chose to join the capitalist world economy, with market-oriented reforms and their own versions of export promotion. Especially important was the collapse of central planning in the Soviet Union and its allies, most of which joined the world economy – some of them eventually joining the EU.

The 1990s were the height of a certain 'globalization euphoria.' Dozens of developing and former Communist countries had joined the world economy, many of them were demoncratising, the Cold War was over, and world economic growth was healthy. For the first few years of the new century, globalization and economic expansion continued and even accelerated, turning into a boom and eventually a bubble. The bubble burst with a vengeance in 2007, leading to the longest and deepest global recession since the 1930s. Recovery was slow, but it did come. However, by 2010 it was clear that there was increasing scepticism about the desirability of globalization. Within a few years, the change in the prevailing winds had become a storm.

The Globalization Backlash

The United States is by far the most important locus of this backlash against globalization, given America's size and centrality to international economics and politics. There are certainly other countries in which similar trends are at work: Brexit in the UK and right-wing populism in Central and Eastern Europe are prominent examples. However, given this essay's focus on the trend's implications for the world economy, I concentrate on developments in the United States.

While the American public was favourably inclined toward globalization in the 1990s, after about 2000 public opinion surveys began demonstrating a growing scepticism about, even hostility toward, international economic integration. The Great Financial Crisis of 2007–9 excited and deepened this scepticism. In its wake, the Tea Party movement in the Republican Party burst onto the scene. Although its principles were never entirely clear, the Tea Party movement rejected Republican moderates and showed disdain for presidential candidate Mitt Romney's association with traditional elites.

Hostility to elites, from both the right and the left, became a direct attack on economic internationalism during the presidential election campaign of 2016. Donald Trump was explicit in his antagonism to foreign trade, investment, and immigration, while Bernie Sanders evinced analogous scepticism about international trade and investment in the Democratic primaries. This was the first time since the 1930s that both major parties had candidates for the presidential nomination who were openly hostile to economic integration, and that any major party had an actual nominee with similar views. The victory of Donald Trump in the 2016 presidential election marked the victory of an economic nationalism that had long been far from the mainstream of American politics. Trump and his supporters expressed hostility to internationalist big business, to big finance, to the international economy more generally, to immigrants, and to many traditional foreign-policy commitments.

As candidate, Donald Trump promised much more restrictive trade policies. The threats included 35–45 per cent tariffs on Chinese imports, an across-the-board border tax of 20 per cent sanctions on China for alleged currency manipulation, and a 15 per cent tax on outward foreign investment. These may have only been threats – and they have certainly not been implemented – but the broader meaning of the campaign should not be lost. Trump's position was a massive deviation from the traditional Republican position, which for 70 years has been more or less committed to open trade and investment. Indeed, for some 40 years the Democrats have been far more protectionist than the Republicans; that relationship has clearly reversed. The Trump administration is unquestionably the most openly protectionist administration in modern history; and its victory seems to presage a major turn for the Republican Party away from economic internationalism and toward something much closer to the Republican position of the early twentieth century, the years of Republican protectionism and isolationism.

There are clear economic roots to the support for President Trump's America First attitudes toward the international economy. American public opinion tends to associate international trade and investment with job insecurity and job losses. Many Americans also associate globalization with increasing income inequality, especially with the outsized growth in the income and wealth of the top 10 per cent or 1 per cent of American society – the financial, corporate and professional elite that has benefited enormously from their global ties, while leaving the middle and working classes behind.

Discontent has been building for a long time in important parts of the country, especially the mid-Western industrial belt. The region's problems started in the late 1960s and accelerated through the 1970s and 1980s, as a phalanx of developing countries embarked on export drives. The process should be seen as affecting *communities* more than disconnected individuals. American manufacturing is concentrated in the Midwest and parts of the South, and is particularly important to some towns and small cities in these regions. Many of these entered in a sort of downward spiral starting with trade and investment-related pressures on local manufacturing. Factory closings increased unemployment and underemployment, lowering wages and labour force participation. Local economic problems reduced local-government tax revenue, so that local public services deteriorated (Feler and Senses [2017] carefully discuss and document these indirect community-level effects). As the community's economic base eroded there were devastating *social* effects, including a rise in alcoholism, opioid abuse and suicidality (Pierce and Schott 2017).

These trends have had a clear political impact. Increased trade, in particular with China, has caused some regions to lose jobs and see reduced wages.[2] The political effects are multifarious. Affected regions are more politically polarized (Autor et al. 2016a). Their legislators tend to vote in more protectionist directions (Feigenbaum and Hall 2015). They were more likely to swing their votes toward Donald Trump in the 2016 presidential election (Autor et al. 2016b; see also Jensen et al. 2017).

There are undoubtedly non-material sources of America's new populism, including cultural bias and ethnic prejudice. Similarly, the economic trends the country has experienced are at least as much due to skill-biased technological change as they are to globalization. Nonetheless, globalization is a clear policy target, and economic nationalism is popular at least in part because it seems to help Americans at the expense of foreigners.

The central point is that the current direction of American international economic policy is not an aberration, and not a passing fancy. To be sure, supporters of protectionism and economic nationalism in the Trump Administration face several obstacles. Some segments of the Republican Party, and of the business community that has typically been a crucial supporter of the party, are likely to be deeply concerned if the Administration follows through on its rhetorical dismissal of the value of multilateralism, international economic cooperation, and openness to international trade and investment. The electorate may well turn against President Trump and his new-model Republican Party. Nonetheless, the 2016 election was a watershed in modern American politics. It signalled the rejection of the current international economic order by large segments of the public. So far, there has been no generally popular response, either from within the Republican

Party or from the Democratic Party. The domestic politics of international economic policy in the United States has changed fundamentally.

Implications for the International Economy

It has to be taken as given that American foreign economic policy will continue its current direction at least through 2020, and perhaps beyond. Of course, trends in other parts of the world are also relevant to thinking about the future of the global economic order. However, in the light of American international economic predominance for the past 75 years, virtually any projection into the future has to start with expectations about the position of the United States.

We assume, as discussed above, that domestic political trends in the United States mean that American foreign economic policy will continue to move away from its post-World War II commitment to economic integration, multilateralism, and international economic cooperation. In this context, other countries and regions have no choice but to attempt to adjust to a new reality.

From Brussels to Brasilia to Beijing, foresighted policy-makers have to think about how they can best move forward given the potential course of American foreign economic policy. Their most straightforward concern is to carve out alternatives to policies that had previously assumed American engagement in, and leadership of, attempts at international economic collaboration. This will place a premium upon developing economic relations that navigate the troubled shoals of American foreign economic policy and its difficult domestic politics.

In trade, we can expect that governments everywhere will search for more bilateral trade agreements with partners other than the United States. The recent Canada–European Union trade agreement, well underway long before 2016, is nonetheless an example of the sort of arrangement to be expected. The member states of the Southern Common Market in South America (Mercosur) have already expressed strong interest in a similar arrangement with the EU, and such expressions of interest will undoubtedly proliferate.

Countries outside North America are likely to redouble efforts at regional integration. The logic of economic integration suggests that, failing multilateral progress, governments will seek to strengthen trade relations with countries with which they have traditionally close ties, or with which geography and economic structure suggest strong complementarities.

The Chinese government has redoubled the efforts it began in 2013 with the 'Belt and Road Initiative' to stimulate trade and investment within Asia, assisted by the activities of the new Asian Infrastructure Investment Bank. And the Chinese are likely to be even more heavily committed to working in Africa to develop both markets and sources of supply of primary products.

Elsewhere in Asia, the eleven remaining members of the Trans-Pacific Partnership, rebranded as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, are moving forward with their efforts at regional cooperation. It may be that, with the United States no longer involved, the members of a reinvigorated TPP could be open to some involvement on the part of China. Certainly countries like Australia, Vietnam, South Korea and Japan both want closer ties with their Asian and trans-Pacific partners, and the possibility of a mild counter-balance to Chinese influence.

The EU, in addition to strengthening its economic interactions with Canada and, perhaps, Mercosur, has reasons to continue to build its economic bonds with the former European colonies in Africa and Asia. The EU's naturally close ties to the Middle East and North Africa are likely to be improved and enhanced by the Trump Administration's alienation of many governments in the region. It is also likely that the EU will find it both desirable, and eventually easier, to build closer economic links to Russia and its Eurasian allies. It is unclear how this connects with Chinese attempts to tie Central Asia more closely to its economic powerhouse, but there may be little to stand in the way of a more tightly integrated Eurasia, stretching from Ireland to Japan (with the position of the UK uncertain).

Latin America finds itself in a difficult position, given its geography and traditional economic connections to North America. Nonetheless, as mentioned, the major economies of South America are already seeking closer ties to the EU; even Mexico seems to be looking for a counter-weight to the United States.

While at this point these are just speculations about the future, there is little question that the edifice of the international economic order is being transformed. Given the difficulties of multilateral trade negotiations within the World Trade Organization (WTO), there were already indications of a regionalization of trade and investment; this is likely to accelerate. At the institutional level, the Trump Administration seems intent on undermining the authority of the WTO, especially its Disputes Settlement Mechanism, which it regards as an infringement on American sovereignty. If this attempt were to be successful, and the WTO's monitoring and enforcement functions were impeded – at least with regards to American trade – we would expect the result to be a further dampening of trade with the United States, and the greater likelihood that American trade concerns would lead to unilateral measures – and, presumably, retaliation from the targets.

One important implication of this is that even if political developments in the United States begin to change the course chosen by the Trump Administration, the political revolution of 2016 has already set in motion processes that may be difficult or impossible to reverse. It is probably the case that we are witnessing the transformation of America's role in the international trading order toward greater unilateral action, and a greater reliance upon bilateral ties, with increased levels of trade protection and more trade conflicts with other countries. Elsewhere, we are likely to see a growing regionalization of international trade and investment, as countries outside North America attempt to shield themselves from the impact of the new American stance.

What Might be Done?

What one thinks of these prospects is, of course, a purely normative question. I, for one, do not regard them as innocuous. International economic integration has been extraordinarily beneficial, especially to developing countries. Its undesirable distributional effects can be handled in such a way as to alleviate some of the suffering that globalization can cause, and has caused. Indeed, many countries have been more successful than the United States in addressing the issues that international trade and investment raise about the domestic distribution of income.

It is, nonetheless, clear that in the United States – and in many other countries – mechanisms to compensate those harmed by globalization have been insufficient. Individuals and, most important, communities that have seen their quality of life deteriorate for decades, and that have at least some reason to blame at least some of the deterioration on globalization, are right to expect that their governments take responsibility for helping to cushion the blow. Virtually no country's government has come up with a fully satisfactory and comprehensive response to the economic and social impact of globalization – and the result has been a backlash that is now calling the very structure of the world economy into question.

Existing political parties and institutions appear to offer few alternatives to populist demands. It is easy to see that the populist policies will not be successful in the long run – and probably not even in the short run – but this is not cause for celebration: the popular response to populist failures may well be to move in even more extreme directions.

Over the coming years, political parties, politicians, and political activists who believe in both progressive social policies and an open world economy face a major challenge. They need to provide effective, politically feasible proposals for policies that address the socio-economic effects of globalization. These include ways of broadening the positive impact of international economic activities to include much more of the population. This will have to involve preparing more young people for the economic demands of the modern world economy; and protecting, retraining, or compensating older people who have not yet been able to adapt.

The policies necessary to provide a compelling alternative to populism and economic nationalism are difficult to define, and even more difficult to achieve politically. However, there is little doubt that the industrialized world faces a decade of serious clashes over the way forward in the domestic and international political economies.

Notes

1. Ruggie (1982) is the classic statement of this compromise, which he called 'embedded liberalism.' For a summary of the interwar collapse and the reconstruction efforts at Bretton et al. (2006, Chapters 6–11).
2. Most of the studies investigating the relationship use some variant of the China Shock instrument first developed in Autor et al. (2013). While I am not familiar with studies on the analogous distributional implications of the integration of capital markets, there are a few on the impact of foreign direct investment ('offshoring'); see especially Owen and Johnston (2017).

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