## Is globalization going to be unravelled?

We need to remain committed to maintaining an open trade policy and not be distracted by the noise about increased protectionism in the West

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Globalization is getting very bad press in industrialized countries. From being touted aggressively only 10 years ago as a “win-win” development for all, it is now blamed for these economies’ ills. Recent election results suggest that the elites in these countries are thoroughly discredited. Inevitably, this has extended to the expertise traditionally associated with them. There is a real danger of ill-conceived populist solutions gaining traction.

**Does globalization have a future?**

Globalization is not dead but it does seem headed for a reset. It was all about freer movement of capital, people and trade. The movement of private capital continues much as before with two qualifications. First, worries about global financial stability are pervasive. Second, traditional multilateral development banks such as the World Bank and the Asian Development Bank (ADB) enjoy little support. The movement of people, an important aspect of globalization, was never free, except for the highly educated. Even that is now being restricted. The US administration is restricting H-1B visas, turning back Mexican migrants, and making work visas for foreign students more difficult. None of this violates any treaty. Brexit is an example of repudiating a treaty in order to restrict European immigration. There is opposition to non-European immigration in many European countries .

Trade is the area most governed by treaty obligations, and there is clear evidence of regression in this area. Many countries introduced protectionist measures after the 2008 financial crisis. These covered only 3% of global trade at the time and it was thought they would be eliminated as the situation normalized. Instead, the coverage has increased to 5%. The US, once the flagbearer of trade liberalization, is withdrawing from trade agreements agreed earlier such as Trans-Pacific Partnership, North American Free Trade Agreement, and the free trade agreement with South Korea. Its commitment to the multilateral trading system is also in question as it has yet to appoint an ambassador to the World Trade Organization (WTO). It has also not approved replacements to vacant positions in the WTO Dispute Settlement Body, which is one of the most important operational arms of the WTO.

**What should we do?**

The anti-globalization backlash in the West must not be allowed to swamp the recognition that globalization has been good for developing countries. These countries have grown faster than the industrialized countries, and increased their share in global gross domestic product (GDP). That is precisely what inclusive globalization should have delivered. The big gainers have been Asian countries, led by China, but India is also in this group. The end result has been a huge reduction in global poverty, and a reduction in inter-country inequality, even if inequality within countries has increased. In other words, globalization has made the world more inclusive.

We should therefore push to build support for a new inclusive “Globalization 2.0” which addresses the problems without throwing the baby out with the bathwater. We are unlikely to gain traction on migration though that is an important issue. However, on both finance and trade, there is scope to make a difference.

**Global cooperation on financial issues**

One of the successes of globalization is that private sector flows in the form of foreign direct investment (FDI) and foreign institutional investor (FII) flows have become much more important than flows from the World Bank Group and the ADB. Industrialized countries interpret this to mean that countries like India no longer need the World Bank/ADB. This is incorrect. There is a case for giving these institutions a new mandate: helping achieve the infrastructure needs of economies like India which have just entered the bottom of the middle-income category.

The ADB has recently estimated that India needs to spend $4.4 trillion on infrastructure from now to 2030. With the present annual level being $120 billion, this implies a huge increase in infrastructure investment over the next decade and more. This is only possible if we can attract private investment into infrastructure development through some form of private public partnership (PPP). Industrialized countries typically argue that there is enough capital in the private capital market to finance infrastructure projects provided implementation problems such as land acquisition, forest clearances, environmental impact clearances, etc., are overcome. These constraints are indeed important, whether the project is implemented by the public or private sector. However, the private sector will face special problems of financing because of perceived risks. This is where international financial institutions can help. They can bring in international best practice in the design of PPP contracts and suggest mechanisms of dispute resolution which would meet public approval. Most importantly, by taking a financial stake in the project, they can help reassure private investors that PPPs will not be interrupted or changed arbitrarily.

The Group of 20 finance ministers recently appointed an Eminent Persons Group under Singapore deputy prime minister Tharman Shanmugaratnam to make recommendations on reforms of international financial institutions. We should urge the group to recommend a major expansion of lending capacity of the World Bank and the ADB to enable them to provide long-term finance for PPP projects in infrastructure. The case becomes especially strong if the infrastructure is green and designed to cope with climate change.

**Trade policy issues**

We need to remain committed to maintaining an open trade policy and not be distracted by the noise about increased protectionism in the West. It is unlikely that we will be subjected to significant protectionist action. We are located in a part of the world that is expected to grow the fastest, and enjoy the fastest growth of trade, and there is no rising tide of protectionism here. On the contrary, there is a strong push for integration in the form of the Regional Comprehensive Economic Partnership (RCEP) agreement between the Association of Southeast Asian Nations (Asean) and its six partners (Japan, Korea, India, China, Australia and New Zealand).

We have traditionally viewed multilateral trade negotiations under the WTO's auspices as the best way of liberalizing trade. This remains true, but with the Doha Round all but officially dead, we have to recognize that progress on the multilateral front is highly unlikely. It is therefore particularly important to get the RCEP concluded successfully. There is a strong impression among RCEP countries that Indian industry is pressurizing the government not to come to an agreement. This needs to be countered.

Industry needs to be reassured that genuine problems will be addressed. The goods and services tax (GST) takes care of the absence of a level playing field vis-à-vis state taxes. However, the problem of inverted tariff structures remains. This can be resolved by reducing duties on inputs where these are too high. Since tariff reductions under the RCEP will come into force over a period of time, we have enough time to get our tariff structure into shape. If Indian industry knew what we propose to do, there would be less opposition. This cannot be done by the commerce ministry but by the finance ministry.

Looking ahead, Globalization 2.0 will pose new problems in trade. In future trade negotiations, industrialized countries are likely to focus less on tariff reductions and more on harmonization of standards. We have traditionally viewed these “behind the border” issues as inappropriate for trade negotiations. Economic theory does not suggest that unified standards for all countries at different levels of per capita income is ideal. However, the pressure to move in this direction will be difficult to resist, especially when it is done to protect the consumer. Examples are specifying the types of dyes used in cloth used for garments, or specifying the type of additives permitted in the case of food products.

Standards can become a new form of protectionism, since products that don’t meet the standards will be denied access to industrialized country markets. We can always refuse to harmonize our domestic standards and leave it to our producers who want to export to adopt higher standards. However, this presents two problems. First, if our competitor countries join trade groups which harmonize standards, the group may impose stricter tests for exports from countries that don’t harmonize, which would make our exports less competitive. Second, if we retain lower standards at home, firms that want to export will have to incur higher costs, putting them at a disadvantage in the domestic market, since their domestic competitors will not have to incur these costs. Since the RCEP does not deal with standards (at least not yet) there is a case for getting in now, so that if and when the standards issue is raised, we will be inside rather than out.

A new twist in globalization 2.0 will be the role of industrial policy. The successful exporters of the past—Japan, Korea and China—did not simply follow a passive policy of lowering tariffs and waiting for market competition to do the rest. They followed a much more active industrial policy and it is argued that we need to learn from that experience. There is a lot that government must do in terms of providing infrastructure and a supportive policy environment and we need to do much more of that. However, industrial policy also means singling out firms that could be potential winners, and extending to them special favours and subsidies. Given our democratic polity, and the pervasive suspicion of crony capitalism, it is doubtful whether we can do this. But there is a lot we can do proactively to do much better in a world of Globalization 2.0.

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