



# Straight Talk on Trade

## Ideas for a Sane World Economy

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Princeton UP © 2017  
336 pages

## Rating

**8** 9 Importance  
8 Innovation  
7 Style

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## Take-Aways

- While trade agreements can be good for countries, they aren't always in their best interest.
- A nation's policy makers need to balance trade practices and domestic priorities.
- People's sense of identity ties more closely to their countries than to their local towns or to their notions of global citizenry.
- Advocates of "hyperglobalization" seek a world order that supersedes nations.
- The European Union, with its combined market and single currency, is the foremost experiment in hyperglobalization.
- Democracy is not the only route to economic development in the short run.
- Markets are not self-regulating, and global free trade needs global governance.
- National governments build institutions to administer property rights and contracts.
- Corporate and political elites believe that compensating those who have lost out as a result of globalization is the way to quell public criticism. But the time for that is past.
- A free-trade policy benefits a nation when it leads to its overall economic well-being, not only because free trade is good for the global economy.

# Relevance

## What You Will Learn

In this summary, you will learn: 1) Why nations need to strike a balance between domestic interests and global trade, 2) What factors complicate globalization, and 3) What seven guidelines would help maintain a pluralistic world order.

## Recommendation

Today, international trade intertwines countries' economies more closely than ever before. This state of the world is a victory for those who, since the end of World War II, have promoted free trade as the solution to global ills. However, trade has become a target of popular backlash and new tariff battles. Many people believe that nations have created their own Frankenstein monster in complex global treaties. In a collection of his previously published articles, economist Dani Rodrik offers a wide-ranging overview of the complications of early 21st-century trade agreements. He coalesces his thoughts into seven intriguing principles for "a sane world economy." Though his text is often abstract and tends to meander, Rodrik nevertheless makes some salient points about fair and equitable trade and the need for strong nation-states. While always politically neutral, *getAbstract* recommends his thought-provoking work to executives, trade experts and economists.

# Summary

*"Trump's and other populists' rhetoric on trade may be excessive, but few deny any longer that the underlying grievances are real."*

*"What gives trade particular political salience is that it often raises fairness concerns."*

## National Interests Need Balancing

In political events around the world in 2016, international trade was the focal point of much intensive debate. While trade can be good for countries, it's not always in their best interest, as globalization proponents would make it seem. Trade is much more than the straight exchange of goods and services among countries. Trade also means that workers and businesses compete on wages and costs across borders, creating problems of fairness due to differing industrial and social practices. The "hyperglobalization" of trade leads to greater economic integration, as in the case of Europe's single market.

Globalization has driven – to a significant extent, although not exclusively – the hot-button issue of inequality in the United States. In the 2016 US presidential election, both Donald Trump and Bernie Sanders made their antagonism to trade policies a central point of their campaigns. Trump's ultimate success stems, in part, from his rejection of the proposed Trans Pacific Partnership treaty and his distaste for NAFTA. He tapped into the legitimate complaints of workers who have lost their manufacturing-based jobs due to cost-advantaged goods imported from developing countries. Also in 2016, economic dictates from the European Union fueled the United Kingdom's vote to separate from the bloc, and the EU edifice remains under fire in other member countries, like Italy.

At a national level, policy makers need to strike balances between the benefits of trade and the domestic interests of labor, businesses, financial firms, the environment and democratic forms of government. The time has come for a pluralistic world to fashion some overarching institutions that preserve strong nations and protect the world's common resources.

## The Role of Nation-States

People live in countries with geographically delineated borders and are subjects of states having the jurisdiction to enforce accepted bodies of laws. Governments, through their

*“Globalization’s cheerleaders do considerable damage to their cause by framing the issue as a stark choice between existing trade arrangements and the persistence of global poverty.”*

*“Economists deride the nation-state because it is the source of the transaction costs that block fuller economic integration.”*

*“Robust nation-states are actually beneficial, especially to the world economy.”*

*“Markets depend on nonmarket institutions because they are not self-creating, self-regulating, self-stabilizing or self-legitimizing.”*

institutions, are responsible for providing civil order as well as the economic and social well-being of their citizens. Nations encompass a wide range of communities, and they pool their resources to benefit everyone, particularly in times of crisis. For example, in response to the 2008 financial crisis, national governments “bailed out banks, pumped liquidity, provided fiscal stimulus and wrote unemployment checks.”

People’s sense of identity ties more closely to their countries than to their local towns and to notions of global citizenry. Nation-states in the early 21st century continue as vital and necessary entities for meeting the needs of the world’s diverse populations. In carrying out their missions, sovereign states often constrain the flow of trade, capital and individuals. And their varying rules, regulations and currencies create transaction costs that can limit economic gains.

### **Globalization**

Advocates of hyperglobalization seek a world order that supersedes nations. They want to build economies, citizenship and governance that are global in nature. Their ideas are rooted in the writings of Milton Friedman, a free-market economist who came to prominence in the early 1980s. US president Ronald Reagan and UK prime minister Margaret Thatcher invoked Friedman’s thinking to dismantle trade barriers. At about the same time, China began to develop a market economy, and Latin American countries started to privatize state-controlled industries.

The World Trade Organization (WTO) formed in 1995, advocating for the cross-border movement of capital and extending the scope of traded items beyond manufactured goods to include agricultural products and intangibles like services and intellectual property, among others. Prominent national leaders and economists pursued hyperglobalization policies in their desire to get rid of the transaction costs that “hinder trade and capital flows.”

The European Union, with its combined market and single currency, is the foremost experiment in hyperglobalization. Its member-states eschewed political union. Consequently, their institutions weakened, while the overruling EU economic structures proved inadequate to resolve upheavals. The 2008 financial crisis exposed the weaknesses of the European Union, with countries such as Greece being forced into liberalization reforms that sought to put their fiscal houses in order. The Greek experience demonstrates that countries cannot enjoy the trifecta of “hyperglobalization, democracy and national sovereignty all at once.” The EU continues to face challenges in the form of standstill economies, high unemployment, voter discontent and the ascendancy of extremism. It grapples with the issue of either coming together in a closer political union or of backtracking on its economic integration.

The views of Friedman and his supporters created a binary choice for policy makers, pitting free markets and an unfettered global economy against national interests. But markets are not self-regulating; they require rules. Global trade needs global governance, but no consensus about such governance exists. An orderly world economy could mean that international organizations issue and enforce universal regulations. Or global governance could be limited to voluntary guidelines for practices like fair trade and corporate citizenship.

However, nation-states need to retain their economic and social decision-making autonomy to serve the needs of local citizens. With strong nations in place, international cooperation in the oversight of the environment is essential. And primarily because of the costs

of transportation, information sharing and dispute resolution, the world needs global institutions that govern trade but do not force integration.

*“A poor country can easily compete with Sweden in a wide range of manufactures, but it takes many decades, if not centuries, to catch up with Sweden’s institutions.”*

*“‘Economics is a science of thinking in terms of models,’ Keynes once said, ‘joined to the art of choosing models which are relevant.’ It was the art that fell short.”*

*“Macron’s message to Germany has been clear: Either you help me out and we build a true union – economic, fiscal and eventually political – or we will be run over by the extremist onslaught.”*

*“When the elites’ interests differ from those of the rest of society, it is their views that count – almost exclusively.”*

### **The Developing and Developed Worlds**

The historical course of economic progress demonstrates the need for high-functioning nation-states. Developing countries typically restructure their farming economies into manufacturing sectors to reap economic growth. Thus the need for skilled labor emerges, leading to labor laws and rising incomes. Democratic forms of government evolve. Education and standards of living increase. Governments build institutions to administer property rights and contracts.

In a developed nation, workers move from manufacturing to services such as banking, education and engineering in a “deindustrialization” process, and the country becomes a “postindustrial economy” with strong institutions. At the same time, manufacturing, which can employ unskilled labor, relocates to poor countries.

Most advanced countries in the 21st century are democracies. However, democracy is not the only route to development. Nations like Egypt and Tunisia rank high on some social and economic measures, but their governments are authoritarian regimes in which corruption is rife. China is experimenting with “local democracy,” as its economic and social restructurings proceed at a rapid pace. “Market-supporting institutions” – such as unshackled media and legal systems that ensure the rule of law — are hard to achieve. However, on a global basis, pluralistic but imperfect ruling bodies can accomplish the same democratic outcomes.

### **The Influence of Economists on Global Trade Policies**

Economists rely on models that simplify human behavior, leading them to gloss over many of the impacts of trade, particularly on income distribution. They tend to see criticism of globalization as arising from protectionist motives. Economists were caught on the wrong foot in their failure to anticipate the global financial crisis and its aftermath. Contrary to free-market dogma, leaving decisions up to the market amounts to allowing global superpowers to push WTO agreements that align with the interests of profit-maximizing multinationals rather than of the world at large.

In politics, the interests of the powerful matter, but this fact doesn’t usually explicitly factor into economic analyses. Most of the available models that account for politics include the notion of “policy inefficiency,” based on the view that affected parties shape their preferences based on their own interests, that the interests of the powerful carry the most weight and that ultimate outcomes depend on the “prevailing political institutions” that make the rules. However, these inputs do not necessarily lead to inefficiency. What actually creates inefficiency is the absence of “efficient redistributive mechanisms.” Elites would rather hold on to their advantaged positions than lose them by enabling the productivity and economic growth that would empower others. Economists need to take a dynamic approach in applying models. The answers to economic questions can vary in different social and institutional settings.

### **Seven Principles for the Governance of the Global Economy**

Corporate and political elites believe that compensating those who have lost out as a result of globalization is the way to quell public criticism. But the time for that is past. The rules of global capitalism need reformulating. Matters that affect the whole world require global governance. However, international economic policies with local consequences – such as

on employment, infrastructure and innovation – merit national-level jurisdiction. Seven guidelines can form the basis for rules for a global economy:

1. **“Markets must be deeply embedded in systems of governance”** – Markets operate within the political and social institutions of laws, regulations, taxation, physical infrastructure, and investment in innovation at both national and global levels.
2. **“Democratic governance and political communities are organized largely within nation-states, and are likely to remain so for the foreseeable future”** – Nations are unlikely to abdicate significant authority to global entities, because broad-brush rules do not serve the needs of socially different populations, even those within the EU. Uniform regulations on issues such as intellectual property and investor disputes nullify national sovereignty and override democracies.
3. **“There is no ‘one way’ to prosperity”** – Advanced nations like the United States and Japan govern corporations, finance and society differently, demonstrating that multiple models of capitalism can be successful and that experimentation is healthy.
4. **“Countries have the right to protect their own regulations and institutions”** – Nations should control their own tax systems, border restrictions, and labor and health-and-safety standards.
5. **“Countries do not have the right to impose their institutions on others”** – States should not use trade sanctions to impose foreign practices on how other countries handle issues such as labor policies.
6. **“The purpose of international economic arrangements must be to lay down the traffic rules for managing the interface among national institutions”** – By eschewing one-size-fits-all arrangements, these rules would aid nations in optimizing their relationships with one another.
7. **“Nondemocratic countries cannot count on the same rights and privileges in the international economic order as democracies”** – For example, WTO import rules require evidence of goods’ sanitary conditions when health concerns arise. Such practices can encourage states to improve their national decision making.

#### **“Fair Trade and Free Trade”**

International trade among entities with dissimilar political, economic and social systems is fraught with credible concerns. A free-trade policy benefits a nation when it leads to overall economic well-being for that nation – not because free trade is good for the global economy.

Trade policies adopted by one country influence other nations, particularly when those policies involve unfair trade practices such as dumping – pricing goods below costs due to government subsidies. The concept of fair trade should expand to include the idea of “social dumping,” which undercuts domestic institutions. For instance, an item may be less expensive because cheap labor that does not benefit from legal protections produced it. The practice leads to inequality and “a race to the bottom.” Policies to counter this behavior are appropriate and can contribute to national-level discussions in which people consider the costs and benefits of engaging in such trade. That is a better approach than imposing restrictions or outright bans on global trade.

*“Policies in one country do affect others... We might be particularly concerned about instances where domestic economic advantage comes at the expense of other nations.”*

*“The global trade regime must address issues of fairness in addition to economic efficiency.”*

*“We need a pluralist world economy where nation-states retain sufficient autonomy to fashion their own social contracts and develop their own economic strategies.”*

## About the Author

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