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Globalisation Under Pressure: International Trade Suffers

By Barry Desker

Synopsis

An era of globalisation is drawing to a close as international trade comes under pressure of protectionist policies. TPP has yet to be ratified while RCEP has stalled.

Commentary

THE CURRENT American presidential campaign has drawn attention to those who have paid the price for open markets, rapid international economic growth and the rise of the new economy over the past two decades seeking to change the nature of the debate. Inward-looking protectionist policies have attracted growing support.

An era of globalisation may be drawing to a close, just as an earlier era of globalisation at the beginning of the 20th century was destroyed by the First World War and the rise of protectionist policies during the Great Depression of the 1930s.

Growing Protectionist Sentiment

Contrary to the long standing position of Republican candidates, Donald Trump has attacked the proposals for trade and investment liberalisation signed by the 12-member Trans-Pacific Partnership (TPP) and the current negotiations for the European Union/United States Transatlantic Trade and Investment Partnership (TTIP). Faced with a strong challenge by Bernie Sanders in the Democratic primaries, Hillary Clinton has been forced to disavow her support for the TPP in its current form and suggested that she would not back the TTIP.

The strong reactions from the Rust Belt in the American mid-West to the loss of manufacturing has outweighed the benefits gained by the services sector especially

in areas like the tech-savvy Silicon Valley, the financial sector in Manhattan and the cities with diverse American companies with global value chains that have expanded rapidly in recent years.

This 'pushback' was also seen in the British vote in the June 2016 referendum for exit from the EU, which is likely to result in a hard Brexit as concerns over immigration trump the desire to retain access to the single market. The growing uneasiness over immigration and the resettlement of refugees is also having a toxic impact on politics in the EU. Angela Merkel, Chancellor of Germany, has been forced to retreat from her open door policy towards refugees.

Even in Singapore, which has benefited from open markets as an entrepot, is an immigrant society and has an aging population with a declining birth rate, there is resentment of new immigrants and foreign workers. They are seen as competing for jobs, causing over-crowding and reducing opportunities for locals. This has forced a cutback in the employment of foreigners and the setting of more modest targets for GDP growth. Surprisingly, for an economy whose trade is three times its GDP and which has benefited from market-opening measures, at campaign rallies during the 2015 general election, the opposition Singapore Democratic Party rejected the TPP and criticised free trade agreements such as the India-Singapore Comprehensive Economic Cooperation Agreement (CECA) for leading to an influx of foreign workers, a view frequently articulated on social media.

Open Markets and Global Trade

Over the past 30 years, merchandise and services trade has increased by about seven per cent annually on average, with the growth in services playing a larger role. World trade increased twice as fast as world production. Particularly significant was the shift away from autarkic policies by China, India and many developing countries, which moved away from policies of the 1970s and 1980s promoting self-sufficiency, protection of infant industries, nationalisation of the industrial and commodities sectors and the promotion of state-owned enterprises.

According to the World Trade Organisation (WTO), exports of developing countries have grown fastest since the 1990s. While developing countries accounted for 34 per cent of world exports in 1980, by 2015, their share had risen to 43 per cent. China's share of world exports grew from one per cent in 1980 to 14 per cent in 2015.

The US, Japan and the EU recorded declining shares of world exports. An interesting and often overlooked aspect is that trade between developing countries has increased significantly. The share of such 'South-South' trade increased from eight per cent in 1980 to almost 25 per cent in 2015.

The rapid economic growth in this period also reflected the impact of international supply chains. The importance of logistics and efficient supply chains meant that companies such as Hong Kong's Li and Fung, which managed the entire supply chain for global brands, earned four dollars for every dollar earned by original equipment manufacturers. Similarly, branded luxury goods companies in the US and

EU increased their earnings by outsourcing production to manufacturers in a range of emerging economies.

East Asian Transformation

In East Asia, the rise of distributed manufacturing resulted in the growth of electronics as well as the textiles and garments industries throughout the region. These industries were the key to the initial economic transformation of the region. Beginning with simple 'screwdriver' electronics assembly operations, manufacturers in the region upgraded their skills and capabilities over time, with simpler assembly operations moving to other parts of the region. While domestic manufacturers were significant, especially in South Korea and Taiwan, openness to foreign ownership facilitated the entry of multi-national corporations (MNCs) into the region.

In textile and garment manufacturing, the existence of quotas in the US, EU and other developed countries up to the beginning of 2005 resulted in Singapore, Taiwan and Hong Kong retaining significant manufacturing capabilities, even though their labour costs had risen significantly. WTO agreements protected their exporters from competition by lower cost producers such as Bangladesh, Vietnam and Indonesia that were late comers to manufacturing textiles and clothing for export.

At the same time, East Asian exports were supported by the rapid upgrading of infrastructure. World class airports, ports and highways were constructed. State-of-the-art telecommunications and IT infrastructure was built while schools and universities aspired to reach the standards set by leading institutions in their fields.

As late comers, they benefited from the innovations that had taken place in the developed countries. By contrast, the US faced the challenge of creaky legacy infrastructure in a period where there was a push for lower taxes and smaller government, leaving state and federal authorities with a reduced capacity to implement major infrastructure projects.

East Asia has been a major beneficiary of open global markets. Today, China has emerged as the world's leading exporter and has the capability to participate in the entire manufacturing value chain, from the simple assembly tasks to sophisticated skills and research-based innovative solutions. The newly industrialised economies of South Korea, Taiwan, Hong Kong and Singapore have been followed by Malaysia, Thailand, Vietnam and Indonesia. After being a laggard for three decades, the Philippine economy has performed well in recent years and recorded the highest growth rate of 6.9 per cent in ASEAN in the first six months of 2016.

Pushback in America and Europe

Such trends, which have been replicated in Mexico, Brazil and elsewhere in the developing countries, have resulted in the 'pushback' seen in the American election and the British referendum. The losers in international trade are upset that high paying jobs requiring minimal skills have now moved to distant shores where the same product can be manufactured at a much lower cost. Trump has won support in the Rust Belt by claiming that he will 'Make America Great Again' by raising tariffs and bringing back manufacturing to the American heartland.

It has also had an impact on European politics. Chancellor Merkel has stressed that the EU accounts for seven per cent of global population, 25 per cent of world production and 50 per cent of social services. Such levels of social services are not sustainable. But democratically-elected governments in the EU face pressures for the continued provision of social services as well as demands for increased benefits such as free university tuition and inflation-linked pensions in countries where such benefits are not provided.

Failing Global Institutions

The risk of rising trade protectionism has increased. The failure of the Doha Round has highlighted the impasse in global trade negotiations. Trade negotiators emphasise that agreements can only be reached through such negotiating rounds where 'nothing is agreed, until everything is agreed'. As there are now 164 WTO members with the admission of Afghanistan in July 2016, and many members have no significant role in international trade, it is impossible to reach agreements where every member has a veto.

The problem is compounded as many developing countries see the WTO as a social welfare agency. On the other hand, developed countries push the envelope in seeking 'behind the border' agreements on issues like the environment, labour standards, intellectual property, competition policy and state-owned enterprises, which have an impact on domestic governance and are contested by developing countries.

This has led to a flight to bilateral and regional preferential trading arrangements, often mistakenly termed 'free trade agreements'. However, these agreements have generally had minimal impact in expanding trade and have often been dominated by political considerations. While the TPP is intrusive, it has the potential to increase regional trade, although it is unlikely that the US will obtain ratification by its Senate before the inauguration of the new President.

By contrast, the current negotiations among the ten members of ASEAN and six partner countries (Australia, China, India, Japan, New Zealand and South Korea) for a Regional Comprehensive Economic Partnership (RCEP) have stalled. RCEP is likely to codify existing agreements reached on a bilateral basis but it is unlikely to achieve major breakthroughs in expanding regional trade. Like the TPP, it runs the risk of being politically unpopular as the mood turns away from open markets and freer trade.

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