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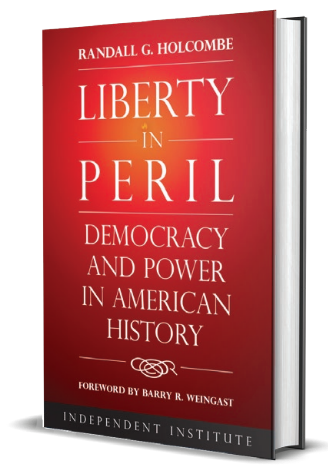

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Reflections

Will Populism Kill Globalization?

ROY C. SMITH

Every so often the world economic system must accommodate game-changing "shocks" that threaten it. Normally, these shocks come about every other decade, but we have had three since 2000: (1) two major, highly destabilizing financial crises (2000–2002) and (2007–9); (2) an outbreak of Islamic terrorist bombings beginning in 2001 and a huge wave of unwanted migration into Europe due to brutal civil wars in the Middle East and North Africa; and (3) the many effects on the labor markets of the United States and European Union from the outsourcing of manufacturing activities to China and elsewhere in Asia. One result has been the growing perception in the United States and Europe that the working- and- middle-class populations have been "hollowed out" by economic shifts that have increased income inequality and forced large portions of the population in the developed world into economic anxiety and uncertainty.

Populists say that globalization has really benefitted only large corporations and their stockholders at the expense of everyone else. Yes, Walmart can lower the prices of the goods it sells, and financial markets benefit from lower interest rates from China's trade surplus, but the benefits to the average consumer are very small compared to the cost of workers losing well-paying factory jobs to make room for the imports.

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The aggregate effects of these changes have brought about a rise in populism and antiglobalization, a disregard for the so-called governing elite, and an appetite for authoritarian solutions. These factors have generated unexpected changes in governments in the United States, the United Kingdom, Germany, Italy, Spain, Austria, Slovakia, and Ukraine. Populist sentiments from both left and right have become clear. Indeed, the question seems to be: Will these sentiments be sufficient to overturn popular support for globalized free-market economic policies and set the system back to what it had been before World War II, when neither market economics nor globalization were a high priority?

Cumulatively, these recent political manifestations are the signs of serious resistance to the idea that economic performance can be optimized by participation in the global, open-market capitalist system that was cobbled together after World War II. Beginning in the 1980s, for the first time, such economic cooperation among developed countries expanded to include developing countries and then the former Communist countries after the collapse of the Soviet Union and major reforms in China. The notion of "globalization" was encouraged and sustained by a general belief that the "new" system for economic development worked far better for all the world than the old.

President Donald Trump, however, disagrees. He says that he is an economic "nationalist" and that the "globalists" have sacrificed U.S. interests in building an international trade and economic system that has mainly benefitted other countries. Globalists counter that the system he decries was in fact responsible for the extraordinary recovery and enormous prosperity in the post–World War II world, greatly reduced world poverty, and fostered democracies in replacement of authoritarian states. In 2017, Bill Emmott, a former editor of *The Economist,* observed that we have entered a "battle to save the world's most successful political idea" (2017, 1). The idea he refers to is "liberalism" or "liberal democracy" ("liberal" in the British context of liberty being reflected in free markets and open societies, not in the U.S. sense of left-of-center politics), which, he claims, is under assault. Several other well-known, establishment figures have described the rise of authoritarianism and the weakening of democracies and also believe a battle has begun; others have focused on the erosion of the well-being of the working and middle classes in the United States and Europe, where the conflict is vigorously being fueled by both the Left and the Right. The globalized economic system may work for the world, some say, but not for a significant number of American and European workers who are losing good jobs to trade imbalances, inefficiencies, and corruption in the process.

Another Side to the Story

An alternative version of the story is that the economic division between the classes is serious but greatly overstated. The shocks have been very powerful and have taken almost two decades to be accommodated, but the system has held, as it has done before in similar crises, and is well into completing a turnaround. Financial stability has been restored. Terrorism and migration are more manageable than they were. China's export threat to the world economy is in decline (and under negotiation) and now is much less than it was. And there are signs that labor markets have adjusted and have reached the end of any hollowing out attributable to the China trade. Economic standards of living have been boosted by higher gross domestic product (GDP) growth rates, record low unemployment, rising real wages (median wage and salary earnings were up 2.7 percent in the first quarter of 2019 versus a 1.6 percent increase in consumer prices for the period [U.S. Bureau of Labor Statistics 2019]), and some policy measures (such as the expansion of the Earned Income Tax Credit in 2017) to improve the economic security of the lower half of the population. (This tax credit lifts more people out of poverty every year than any other government program outside of Social Security when it is counted as income [see Maag 2018].)

Meanwhile, the U.S. median household net worth (i.e., the value of all household financial and nonfinancial assets minus debt) has grown considerably. In 2001, it was $43,600. It rose to $67,100 in 2008 but then declined sharply to $56,700 due to the shocks in 2009. Since then, however, it has nearly doubled to $108,100 in 2018. U.S. median income also grew to $64,200 in 2018, up from $48,200 in 2010 ("June 2018 Median Household Income" 2018).

But a rise in populism in the United States and Europe is part of the residue that remains after the worst elements of the shocks have drained away. Some voters are angry and contemptuous of the elite, establishment types whom they elected to govern them in the past. Charismatic candidates for office stir up voter sentiments and claim that the new form of populism reflects the need to find different leaders who will stand up for them, however unconventionally: not only conservatives who favor tougher trade negotiations, border controls, and restrictions on immigration but also liberals who favor far greater government intervention to control corporate abuse and misconduct and to provide more benefits to those struggling with the high costs of living, health care, and education. Both sides seem to agree that China has been the main beneficiary of its globalization experience at the expense of helpless American workers undefended by their governments.

The Chinese Menace

China joined the World Trade Organization in 2001, when its global trade surplus was $360 billion. In 2006, the surplus peaked at $761 billion and has since declined by 37 percent to $352 billion in 2018 as the costs of land, labor, and public utilities soared with the country's prosperity, thus reducing the competitiveness of Chinese exports (Smith 2018). In 2018, China's current account surplus with the world was only 0.4 percent of GDP, down from a surplus of 10.3 percent in 2017. Many observers now believe that China will have a current account deficit in 2019 and subsequent years (Tan 2019). But China's trade surplus with the United States reached $419 billion in 2018, a record high, when its exports to the United States totaled $539 billion (U.S. Bureau of the Census n.d.). The U.S. economy has considerable inertia; large supply chains at giant companies such as Walmart and Apple cannot be changed or replaced quickly.

Calculating net job losses from trade with China is very inexact in a competitive economic system with lots of "creative destruction." Total manufacturing job losses in the United States since 2000 have been about 6 million, of which maybe as much as half (many from the "rustbelt" states of Ohio, Michigan, Pennsylvania, and Wisconsin) are attributable to Chinese outsourcing, according to a recent academic study by David Autor, David Dorn, and Gordon Hanson (2016).

Under the Trump administration, China is being forced to adjust its tariff and nontariff barriers to entry, its forced technology transfers, and its government subsidies to state-owned industries and other companies as well as to comply with World Trade Organization rules. Negotiations currently under way with China are very similar to efforts to curtail Asian imports undertaken by previous U.S. administrations going back to President Richard Nixon. But job losses also come from increased automation, changing technologies, and supply-and-service chain management by global companies, some of which have created new jobs for American manufacturing workers. The public's perception, encouraged by Trump, however, is that imports from China have been the major contributor to the downgrading of the working and middle classes of the United States and the European Union. In this hollowing-out process, many observers have noted, "good" jobs have been replaced by lower-valued ones, and the Great Recession and slow down (2009–16) have made full-time employment more unstable and uncertain.

Some Trump supporters have pointed to the decline in the labor-force participation rate from 65.7 percent in 2009 to 63 percent in 2018, when more than one-third of the labor force was not working. A Brookings Institute study in 2017, however, reported that 70 percent of prime working age nonparticipants in the labor force claimed that caregiving, disability, student status, or early retirement kept them out of the labor force. An additional 13 percent were out of the labor force but had had recent earnings, suggesting a temporary status to their absence (Whitmore Shanzenbach et al. 2017). Thus, only 17 percent were unaccounted for, but this number is not large in relation to the number of workers suspected of being displaced by Chinese imports.

Meanwhile, globalization adds value to the economic system in three important ways.

First, it increases the size of the global market for goods and services through trade. The United States changed its tariff policy after World War II, discarding protectionism in favor of expanding trade. In 1950, the average U.S. tariff was 4.5 percent, and total trade represented 9 percent of GDP; by 2010, the average tariff was 1.3 percent ("Tariffs in U.S. History" n.d.), and total trade was 26 percent of GDP. In the United States, imports exceed exports, so trade operates at a deficit that can affect jobs, but other jobs are created to enable foreigners to import, ship, store, sell, and service their products to and in the United States. The United States also exports various forms of services and earns income on foreign investments, which substantially offsets the trade deficit. It also benefits from the reinvestment of trade profits by our partners in U.S. securities, real estate, and corporate assets as well as from lower consumer prices.

Second, trade increases competition for the goods and services consumed by Americans. In the 1970s and 1980s, Japanese exports to the United States challenged several major U.S. industries—including consumer electronics, automobiles, and chemicals—and forced U.S. companies to adapt or die. Much of the Japanese competitive effort was not just in lower prices but also in higher quality and advanced technologies and innovation, such as the Sony Walkman, a popular music player that was not a knock-off of an American product. The U.S. companies that survived the competitive invasion were completely changed and include several that did not exist before 1970 (Apple, Microsoft). The auto industry changed as numerous new foreign competitors entered the market and often discovered that it was better for them to manufacture their cars in the United States than to import them. Indeed, the Japanese export menace proved to be temporary, lasting only about a decade. By 2018, 75 percent of Toyotas sold in the United States were made there, and non-U.S. manufacturers made more cars in the United States than U.S.-owned auto manufacturers did (Roberts 2018).

The adjustments suggest, however, that U.S. companies understand the importance of competitiveness and that they must invest in the newest technology in order to remain competitive. In 2018, the World Economic Forum announced that the United States was the most competitive of 140 countries surveyed, but that meant companies applying the benefits of globalization in their businesses (Sugden 2019).

Third, globalization increases the vast pool of financial, innovational, and other recourses available to sustain and improve competitive markets. The market capitalization of securities traded in globally integrated capital markets today is about $300 trillion (in 1980 it was less than $1 trillion), not counting an additional $4 trillion of cumulative foreign investment in factories and equipment, mergers and acquisitions, and venture-capital undertakings.[1]

Flipping Trump

But will this global capitalist system work in the future? If voters feel it cannot work, can it endure? A capitalist system can survive in a democracy only with the consent of the voters. They can vote into office economic nationalists who can change the rules. This has already begun in the United States with Trump's policies on trade, international organizations, and immigration and in the United Kingdom with Brexit, despite many instances of misleading data, obsolete claims, and appeals to emotional, patriotic issues (e.g., maintaining national sovereignty, securing borders, and limiting the activities of foreigners in trade and investment).

Trump is certainly an unusual president. His administration seems chaotic and overly personalized to many, but he thinks he knows where he is and recognizes the importance of the extraordinary powers he wields. He could readily, after a year of New York–style negotiations, complete a China trade deal that will give him some bragging

1. Estimated by the author using data from McKinsey Global Institute 2008.

rights and still enable the Chinese to save face. He can do the same with Germany and the rest of the European Union on auto exports and other issues. (Of German cars sold in the United States, 63 percent are assembled in the United States, so the car-tariff issues are largely political.) Trump wants to reduce the U.S.–EU trade deficit ($169 billion in 2018) and to get the Europeans to agree to contribute significantly to its reduction. This goal should be well within reach; the European Union has benefitted more from our generous trade arrangements than it is entitled to. The North American Free Trade Agreement/United States–Mexico–Canada Agreement and Korean trade renegotiations are largely done, waiting for a final resolution of some remaining tariff issues. Japan is awaiting its turn at the negotiating table. Trump could soon be in a position in which he could claim victory in recasting global trade practices on a more favorable basis for all countries.

Doing so would enable him to flip from being a nationalist to being a globalist.

But will he do so? Or does he prefer the high drama of protracted negotiations against stiffening resistance by powerful counterparts with their own national interests? We know that Trump has made himself personally central to all trade negotiations and that he can be unpredictable. But hardline tactics have their own risks—they can backfire and end up in a standstill, which adds to the costs and frustrations of getting something done and to the uncertainty of global investment decisions. These consequences can affect GDP adversely and affect securities-market prices, which Trump believes influences his supporters and donors. It is certainly in Trump's interest and in the interests of his foreign counterparties to get the deals done and avoid these other consequences.

So maybe Trump will flip to being globalist. He should. It would help him get reelected. He may accept that global and U.S. GDP growth is about to sink just as his reelection campaign is starting up. He promised 4 percent growth in 2016. We got 3 percent in the United States in 2018 (the best in years) and 3.2 percent for the first quarter of 2019, but the Federal Reserve in March 2019 forecasted GDP growth to drop to 2.1 percent for all of 2019 and 1.9 percent in 2020. Today, unemployment is at record lows, and employers can't find enough workers. Trump's "base" doesn't need jobs; it wants growth in incomes and opportunities, which globalization can produce more of than nationalism. The Trump base may still want a harsh resolution of the U.S.–Mexico border issues, but these issues should not affect economic growth rates very much once the remaining trade and tariff issues with Mexico are settled. Anyway, as Trump recently discovered, his border policies do not have enough support among Republicans in the Senate (in April 2019 there were five defectors from his border-wall proposal), so he should recognize that he needs to delink trade and immigration and change his approach or face greater resistance to his policies within his own party.

Finally, we should not disregard Trump's ability to surprise, especially as he becomes hemmed in by the growing political limitations of the presidency. He could, for example, decide that he, not Chinese president Xi Jinping, should become the world's principal advocate for globalization (i.e., for trade that is fair to all). He has made some progress in trade deals by bashing and threatening, so he can probably continue to do so until he can claim to have "fixed the problem" and set the world on a new Trumpian pathway toward "real" globalization.

He may also decide to rejoin the twelve-member Trans Pacific Partnership, from which he withdrew the United States early on in his presidency. Such a partnership, under his leadership, may be a good vehicle after all for enforcing economic discipline on China. He could then claim a major foreign-policy victory in containing China's political and economic reach in Southeast Asia.

Populism is with us now in the United States and Europe. It tends to come and go in election cycles, based on—essentially—how bad things are in the economic sector. This sector is improving and is well supported by the extensive infrastructure, institutional, and private-sector framework that globalization quietly has built over the years. There is no way that national populism (itself divided between right and left) today could drive globalization under the waves, but endless "disputes" can slow things down or risk becoming unresolvable because of the tactics employed.

Trump's vulnerability in 2020 is for him to be seen as someone who is so obsessed with lesser and personal things that he can't get major policy changes done, so that the economy and financial markets suffer accordingly. Democrats, though currently on a neosocialist kick, will ultimately realize that their best shot at bringing down the Trump juggernaut is to show that it doesn't actually work.

Trump would be much better off flipping and doing so fairly soon.

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