Trump and Globalization

Joseph E. Stiglitz

Columbia University, 3022 Broadway, New York, NY 10027, USA

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1. Introduction

Trump’s campaign for the presidency exploited discontent amongst large swaths of the American population. Blaming others—migrants and “unfair” trade practices of other countries—for their economic plight was much easier and more satisfying than blaming, say, changes in technology and other changes in the economy and the way the country had managed those changes.

Responding to this diagnosis, Trump promised to renegotiate trade agreements, and to assert America’s market power. He threatened to impose trade restrictions—in the case of Mexico and China, tariffs of 20% and 45% respectively—if our trading partners did not respond “appropriately”. He focused on bilateral trade deficits, promising to reduce those, and by implication, even more strongly, the multilateral trade deficit. The reasoning was simple: with less imports (or more exports), employment and wages of his constituents would increase.

For almost three quarters of a century, the US had led the world into a rules-based system of trade-globalization, culminating in the creation of the WTO in 1995 and a rash of subsequent bilateral and multilateral trade agreements. Trump thus proposed a major change to US international economic policy. This paper assesses the extent to which, more than one year on, he has fulfilled those promises, and describes the likely consequences of what has happened.
The central thesis of the paper is that it is fortunate that Trump has largely failed to deliver on what he has promised; these failures are in part based on a flawed understanding of the determinants of trade deficits, including the role of trade agreements, and on the political economy of trade agreements themselves. The likelihood is that over time, Trump will continue to move the US towards a more protectionist stance. While the chances are small that he will succeed in any major revision of, say, NAFTA or the WTO—beyond an updating of these agreements, such as by making them more relevant for the 21st century by including provisions related to the digital economy—there are some chances of nightmare scenarios where Trump pulls the US out of NAFTA. In virtually all likely scenarios, the trade deficit will increase and American workers, including those who had been adversely affected by globalization and turned to Trump in desperation, will be worse off. Moreover, while he has by and large failed to deliver (so far) on his campaign promises, there are likely to be significant adverse effects of what he has already done, both to the global trade regime and to US geo-political interests.

Section 1 explains the major “accomplishments” to date, including the state of play of some of the trade negotiations. Section 2 identifies flaws in understandings of international trade that underlay Trump’s failures. Section 3 explains why Trump is unlikely to succeed in meaningful renegotiations of US trade relations. Section 4 argues that Trump policies are likely to lead to increased trade deficits and shows that, more broadly, his policies, to the extent that they are successful, are likely to lead to decreased competitiveness of the US and a lowering of standards of living. Section 5 discusses the global response to America’s new protectionism, the likely impact on US economic and geo-political interests, and the long-run impact of Trump’s policy on the global international economic order.

2. Accomplishments

The most significant “accomplishment” of Trump in the arena of trade occurred on his first day in office: fulfilling a promise, he withdrew the US from the Transpacific Partnership (TPP), the controversial agreement among 12 countries around the Pacific Rim, heralded by the Obama administration with usual political hyperbole as the biggest trade agreement ever. In reality though, it was not: even by the government’s own estimate, after it was fully implemented in 15 years, it would have boosted real GDP only 0.15% over what it would be otherwise—essentially having zero effect on growth.2 Others suggested that even this number was a gross exaggeration.3 The agreement had been widely criticized not so much because of its (largely insignificant) “trade” consequences, but because of the other provisions, those affecting investment and intellectual property, in particular those making access to generic medicines more difficult.4 What has happened after the US pull-out is significant: the other members are going forward with a modified version of the agreement, stripped of at least several of these provisions.

While the Trump Administration has begun renegotiating NAFTA, the talks seem to have stalled. The Administration is making some demands that Mexico, Canada, and the business community everywhere reject, such as that the agreement be subject to renegotiation every 5 years.

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2 See United States Trade International Commission (2016). The usual champions of trade liberalization found, perhaps not surprisingly, somewhat larger effects, at least by 2030: Peter A. Petri and Michael G. Plummer (Peterson Institute for International Economics) estimated that the TPP would increase annual GDP by 0.5% and the World Bank estimated the TPP would increase U.S. GDP by 0.5% by 2030.

3 Capaldo, Izurieta, and Sundaram (2016) found negative effects on growth for the United States.

4 See, for instance, Stiglitz (2016).
(all agreeing that a main benefit of a trade agreement, certainty in future trade policy, would be eviscerated).\(^5\) Other demands made by the administration have not only been rejected but are also totally out of the spirit of a free trade agreement: for example, that half of a car be manufactured solely in the US to qualify for 0 tariff.\(^6\) Reportedly, there are at least tentative agreements on some provisions updating NAFTA, e.g. related to the digital economy, provisions similar to those included in the TPP.\(^7\) Finally, there is new found consensus that some provisions, notably investment (chapter 11), should be stripped away, with the Trump administration’s concern about sovereignty joining concerns from Mexico and Canada about widespread abuses of provisions within investment agreements providing for compensation for regulatory takings (the decrease in profits resulting from a change in regulations). These provisions inhibit regulations, especially with regards to the environment. But here, the (big) business community has already made itself clear: they will oppose any NAFTA which does not include a strong investment agreement. Thus, at this point, it is not clear that the Trump administration will be able to negotiate a new NAFTA with significant changes that would be approved by Congress, beyond the updating of NAFTA provided by the TPP. And in particular, it is not clear that any of the provisions which are likely to get agreement, both with Canada and Mexico and both houses of Congress, would significantly affect the bilateral trade deficits.

After taking office, Trump started criticizing the free trade agreement with Korea (“KORUS”), calling it a “horrible deal,” and reflecting one of his obsessions, referred to it as a “Hillary Clinton disaster,” even though it was largely negotiated by President Bush, and Obama had improved upon the terms that Bush had negotiated. Trump’s faulty perception of the problem reflects a critical misunderstanding discussed in Section 2: while there was a $27.7 billion goods deficit with Korea in 2016, there was a services surplus of $10.7 billion that year, for an overall trade deficit (in goods and services) of $17 billion.\(^8\) Like all trade liberalization measures, there were winners and losers in both countries. The US auto sector has a deficit of $24 billion—accounting for a large fraction of the overall trade deficit. But Koreans’ failure to buy US cars is not the result of trade barriers: Koreans produce cars that Americans like, but the US does not produce cars that Koreans like.

But here, as in other areas, Trump’s economic aggressiveness has had to be moderated by broader security concerns, most importantly, by concerns about North Korea. Moreover, “America First” economic policies will inevitably result in Korea moving closer into China’s economic orbit.

At a global level, Trump has criticized the WTO, threatened not to recognize WTO decisions that run adverse to the US, but so far has not actually done so and has not taken any action to withdraw from the WTO. At the same time, the US has blocked progress within the WTO; the trade ministers ended their meeting in December 2017 unusually, without any consensus statement. EU Commissioner for Trade Cecilia Malmström put it bluntly: “[All WTO Members] have to face a simple fact: (…) we failed to achieve all our objectives, and did not achieve any multilateral outcome.” Optimistically, she went on to say, “Now, I hope that several WTO members, whose

\(^5\) Mexico has countered with a five-year review, without automatic termination.

\(^6\) Canada and Mexico presented data showing that the US proposal would harm the auto sector. The Trump administration has also demanded an increase in the threshold of the “rules of origin” in the auto industry from 62.5% to 85%.

\(^7\) Progress has reportedly been made in the minor and more technical sectors of the pact such as digital trade, the establishment of a NAFTA Trilateral Small and Medium Size Enterprise (SME) Dialogue, food safety, sanitary and environmental standards. Source: Forbes. https://www.forbes.com/sites/nathanielparishflannery/2017/11/30/have-nafta-talks-reached-a-breaking-point/#106cbac8276b.

\(^8\) Source: US Trade Representative.
actions here in Buenos Aires prevented an outcome, will use the time following this Ministerial meeting for valuable self-reflection.” And perhaps intending to contrast the EU with Trump’s America First policies, she argued: “Luckily, we still have the WTO’s current agreements, its structures of cooperation, and its invaluable dispute settlement system. It is a global public good, and the EU attaches enormous value to it.” Malmstrom’s comments reinforced. EU Agriculture Commissioner Phil Hogan’s point: “The WTO is not a zero-sum game, it is a positive-sum game when everyone plays their part.”

More importantly, the US has blocked the appointment of new appellate judges, and if this continues, a central function of the WTO, adjudication of disputes, will be upended. (The Trump Administration seems to prefer “negotiations” for resolving disputes, presuming that “power” would work more to America’s advantage than “fairness,” but seemingly ignoring the possibility of negotiations breaking down and a trade war breaking out.\footnote{At the beginning of the Buenos Aires conference, U.S. Trade Representative Robert Lighthizer complained that the WTO had become too “litigation-centered,” with countries filing lawsuits to obtain what they could not obtain at a negotiation table—that is, complaining about the rule of law.})

The Trump administration has brought a large number of “unfair competition” (anti-dumping, countervailing duties, safeguard) cases, but while these can have major effects on particular sectors, they are a far cry from the across-the-board 45% tariffs against China promised early in the campaign. In January 2018, the US imposed trade restrictions on solar panels and washing machines. Earlier, Obama had also imposed tariffs against solar panels—and in both cases it was bad environmental policy and bad economic policy. Cheap solar panels are important in combating global warming, and there are far more jobs in the installation of solar panels than in their manufacture. Indeed, there is considerable doubt whether the trade restrictions will result in a return of any significant manufacturing capacity to the US. And, of course, higher tariffs on washing machines mean that consumers will have to pay higher prices.

While it is too soon to assess whether these individual actions will differ significantly in scale or scope from actions undertaken under previous administrations\footnote{There has been an upward trend in antidumping and countervailing duty investigations (see Fig. 1 below). For the first time since 1991, the US Department of Commerce “self-initiated” a case (on Chinese common alloy aluminum sheet).} (and in any case, such judgments are particularly difficult, since the extent, for instance, of dumping itself may have changed), one major shift is the threat, not yet realized, of restricting imports of steel on grounds of national security (under section 232 of the Trade Expansion Act of 1962). Such an action would entail restrictions of imports not just from the so-called perpetrators of unfair trade practices, but from all countries: it would be global in scope, engendering a global response.\footnote{So far, the US has not taken action, though shortly before this paper went to press, the Department of Commerce recommended that action be taken, and provided the president with three alternatives. It is widely expected that if the US were to do so, Europe would not wait for a WTO decision to take countervailing actions, which they are allowed to do under certain circumstances. The irony is that by early 2018, steel prices had recovered significantly from their earlier low levels (https://data.bls.gov/timeseries/WPU101?data_tool=XGtable), and China—seemingly the main target of the action—had largely restructured its steel industry and was exporting relatively little to the US. (The US ranks 26th as a destination for China steel’s exports. See https://www.trade.gov/steel/countries/pdfs/exports-china.pdf.)} Besides giving rise to widespread hostility, and imposing large costs on the US and on American firms, it is doubtful whether the case for such a trade restriction could be sustained before a WTO panel. (In the 55 years since the law enabling such actions to be undertaken, only two cases have resulted in import restrictions. The last time was 35 years ago.\footnote{Jacqueline Varas, “Steel Imports and National Security,” July 12, 2017, https://www.americanactionforum.org/insight/steel-imports-national-security/. She notes that every living former

3. The flawed underlying hypotheses

Trump’s trade policies are predicated on a number of elementary misunderstandings of international trade, some of which economists have been inveighing against for two centuries.

The first is his neo-mercantilism, the argument that the US should be running a surplus, and that it is only because of others’ unfair trade practices that it is not. There are several fallacies underlying these presumptions. The most obvious is that because the US is “better” than other countries, it should outcompete them, and in a world in which others played fairly, would do so. Economist David Ricardo addressed this fallacy long ago: trade is based on comparative advantage, not absolute advantage. Whether a country has an overall trade surplus is a matter of macroeconomics, whether capital is flowing into the country, to offset a gap between domestic investment and domestic savings. These capital flows affect exchange rates, and exchange rates in turn determine the trade balance. In this analysis, with limited exceptions, there is no scope for fairness or unfairness.

The one exception is exchange rate manipulation. Here, the difficulty is that the exchange rate is the result of the whole gamut of policies that a country undertakes, and it is typically difficult to ascribe “manipulation” to one instrument in isolation. Changes in the interest rate in the US in 2008/9 mainly had effects through the exchange rate; the intent was to revive macroeconomic growth, but the mechanism by which this was accomplished was largely through the exchange

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chair of the Council of Economic Advisers (including me) signed a letter to Trump arguing against taking action. Ironically, conservative think tanks have also been critical. For instance, a posting on the Heritage Foundation website notes that such actions would not increase national security but would increase costs, including for the military. Toiri Whiting and Rachel Zissimos, “Steel Imports Do not Threaten National Security,” Issue Brief 4719, June 16, 2017, http://www.heritage.org/sites/default/files/2017-06/IB4719.pdf
rate. Yet few American officials would call that exchange rate manipulation. If China removed its restrictions on its citizens investing abroad, its exchange rate would fall. China might well adjust those restrictions as well as intervene directly in the exchange rate in order to stabilize the economy as well as the exchange rate. Trump accused China of manipulating its exchange rate, during a period in which it had indeed been intervening—but to strengthen the yuan, not to weaken it, as Trump alleged. Thus, its interventions had the effect of reducing the trade deficit from what it otherwise would have been, not increasing it.

Trump is also obsessed with bilateral trade deficits, and (as we already noted in the case of Korea) he differentiates between deficits in goods and that in services, somehow thinking that jobs created or lost in manufacturing are fundamentally different from those in services. This enables him to simultaneously complain about our overall trade deficit with Mexico and our goods trade deficit with Canada, with whom we had an overall trade surplus. From a macro-economic view—and from the perspective of long-term growth—jobs created through exporting manufactured goods are no better than those created through exporting “services,” like education and tourism. But, of course, politically they are different: the manufacturing jobs are in the Midwest and the South, and service sector jobs are disproportionately on the two coasts. America’s politics are now driving our trade policy.

Most importantly, Trump seems to have no grasp of the value of the international rule of law—of a rule-based global system of trade. There is broad consensus among economists that the rule of law is important for the functioning of an economy; and these principles apply to international as much as they do for domestic trade and commerce, even if the system of international law is far less complete. While it may be small countries that benefit the most from having an international rule of law, because trade is positive sum, all countries, even the US, benefit.

One reason that the rule of law is valuable is that it increases certainty. Even rules of the game that are not ideal may be better than having no rules.

4. Why Trump will fail in meaningful trade renegotiation

Trump has approached trade negotiations much like he might have approached a real estate negotiation, or like the seller of a Persian carpet might approach a negotiation: He sees the world through a zero sum lens. In such a world, one person’s gain is the other’s loss. Even after he has struck a deal, he holds out for a still better deal by threatening to walk away. If there is any “surplus” in the deal, he seeks to extract for himself as much of the surplus out of the transaction as he can. Since the US is larger and more powerful than other countries, his presumption is that we should have been able to use that power to extract virtually all of the surplus from trade for the US.

But trade negotiations occur in the context of globally competitive markets, which operate in ways markedly different from that of the New York City real estate market. Moreover, in most arenas, economic interactions are a repeated game, not a one-shot game. Bad behavior in one play

13 Bergsten and Gagnon (2017) have argued that there are criteria by which one can judge whether direct exchange rate interventions are “manipulation,” and that China has been engaged in such manipulation.

14 Politics always, of course, has played some role in trade policy. Concerns about the loss of steel jobs have motivated trade interventions in steel in the past. Still, in the past, there has been an attempt to keep trade policy focused on broad national economic interests, not the conflicting interests of different regions. In that sense, Trump’s policies represent an important departure from the past.
gets punished in subsequent plays—the reason why, it is widely reported, many reputable firms and banks ceased dealing with Trump in his career before the presidency.

Especially today, with the WTO, the threat of the failure of, say, a renegotiation of NAFTA is that tariff levels return to the bound WTO levels, which would result in much larger increases for Mexico than for the United States, with American agriculture being particularly adversely affected. Of course, Trump could break WTO commitments, leading to WTO sanctions, which would likely be targeted to have an even more adverse effect on the US economy. Trump could go even further, retaliating against WTO sanctions, thereby starting a full-scale trade war, with even more adverse effects on the US and global economy. No one wins from such wars, but Trump has vastly overestimated the power of the US relative to its trade partners.

Some worry that the recently announced US national security strategy, which accused China of economic aggression, together with pending actions on steel and intellectual property, is the start of such a trade war. But the US and its business interests are especially likely to suffer from such a war, for China has far more control over its economy than the US does over the American economy. The US can only take actions in limited circumstances, and the length of time that it has taken to bring the actions in steel and intellectual property is testimony to the difficulty of taking actions. US corporations have made large investments in China, investments which can be thought of as “hostages,” especially so since China can take a variety of actions which make life for these businesses and their expatriate employees more difficult. Moreover, American consumers and producers will suffer if they are denied access to China’s inexpensive products, or if the costs of those products increase. And low-income Americans are likely to suffer the most, simply because they spend a larger fraction of their incomes on low-price imports from China.15

Finally, China’s government has far more control over its imports than does the US government. Purchases of American airplanes can, for instance, be discouraged. Indeed, the US government has itself recognized this, in its claim before the WTO that China is still not a market economy. But Trump should realize that in a trade war, a non-market economy has distinct advantages, because there are many more levers which it can exercise. China has already opened up a case against the US on unfair trade in sorghum, and there is concern that a similar investigation might be conducted for US soybeans. The US shipped 4.8 million tons of sorghum to China in 2017, worth $1.1 billion, twice the value of Chinese exports of aluminum alloy sheets to the US.16

But, as has already become evident, Trump also did not fully grasp the complex politics of trade and the limitations of presidential authority. He might be able to pull us out of NAFTA, but (at least according to some trade lawyers), the implementing legislation, specifying the zero tariff levels, would remain in place, until Congress enacted tariffs. Doing so would entail an about-face from large numbers of Republicans who have long been advocates of trade opening. (Though, given Republicans’ sudden about-face in passing their regressive 2017 tax bill, which will lead to huge deficits while simultaneously opening up new distortions and loopholes into the tax code, nothing should be viewed as politically impossible). But more than that, leaving NAFTA would go against the economic interests of large swaths of the country, including those that have traditionally been powerful within the Republican Party and within many “red” states.

Every trade negotiation involves winners and losers—and this is especially so if one takes into account the endogenous determination of the exchange rate. Assume, for instance, that Trump

15 See Fajgelbaum and Khandelwal (2016).
were able to renegotiate NAFTA in ways which restored trade balance. Almost surely, that would entail discouraging imports of car parts, making American automobiles more expensive. Demand for American cars would decrease, and the loss of jobs in automobile assembly might well exceed the gain in jobs in auto parts, especially in the short run. But even if somehow the US were able to balance its trade with Mexico, since the overall trade deficit will almost surely increase (See section 4), the trade deficit will increase elsewhere as a result of an increase in the value of the dollar. Thus, exports to some other countries will decrease and imports increase. This is the “iron law” of trade, of which Trump seems totally unaware.

To really undermine the current rules-based global international trading system, Trump would have to have the US withdraw from the WTO. But this too would be difficult, for it would require passage in both houses of Congress. Again, the likelihood of mustering the required votes seems small.

It takes two to tango, and to make a trade deal. That means it has to be advantageous to both parties (or in the case of multilateral agreements, all parties). And that is true both for new trade agreements and for the renegotiation of old agreements. More than that: each country itself faces complex trade politics, and the agreement has to be sufficiently advantageous to enough of the powerful interests to offset the disadvantageous effects on other powerful interests. Ensuring that this is so is what makes trade negotiations so hard and takes so long. Opening up trade negotiations (such as NAFTA) also opens up a range of contentious issues that may have to be resettled, especially since circumstances may well have changed since the original agreements were signed. Among the most contentious issues in the TPP negotiations were several that had been seemingly settled in NAFTA—issues in which there were strong conflicts between Canada, Mexico, and the United States. These included provisions related to dairy, intellectual property, and investment. Chapter 11 provides a vivid illustration. When NAFTA was approved, this provision was not contentious, partly because no one then recognized its full implications. It entailed compensation for regulatory takings—and the Clinton administration had strongly opposed such compensation, but it took the terms of NAFTA as negotiated by the administration of George H.W. Bush as given. The Clinton administration knew how difficult it would have been to renegotiate NAFTA, so limited changes to relatively ineffective side agreements on the environment and labor. There was no discussion within the administration of Chapter 11, and no public discussion of the investment agreement. But in the twenty-some years since NAFTA was enacted, numerous cases have illustrated its power, and there is now huge opposition, including from civil society, especially environmental groups, and many academics. Senator Warren has provided a cogent critique. In Europe, there have been large marches against such provisions in European trade agreements.

17 Anti-environmentalists were pushing compensation for so-called regulatory takings, at least partly on the grounds that such a provision would greatly inhibit further environmental regulation. For a broader discussion of investment agreements, see Stiglitz (2008).


19 See Stiglitz (2017b) and the references cited there as well as other papers in the volume.

5. Why Trump’s policies will lead to an increased trade deficit and lower standards of living

The one aspect of Trump’s economic analysis that may be right is that an excess of imports over exports can depress aggregate demand, contributing to unemployment. But whether that is a problem depends on whether there is an insufficiency of aggregate demand, and especially whether the Fed perceives that to be the case. That is, if the Fed believes the economy is at or near full employment, then any increase in aggregate demand as a result of an increase in net exports will be offset by an increase in interest rates. This, according to standard theory, leads to a decrease in investment. At the current time, it appears that the Fed does believe that the economy is at or near full employment, so were Trump successful in reducing the trade deficit, it would imply a change in the composition of aggregate demand away from investment, slowing economic growth—another trade-off of which Trump’s administration has shown no awareness.

It is possible, of course, that such a policy might benefit Trump supporters. But Trump is unlikely to succeed in lowering the trade deficit, because that is an endogenous variable, as we noted earlier, determined by the disparity between domestic (national) savings and investment. While the 2017 tax bill did little to affect corporate or household savings, government savings will (by its own admission, especially in the short run) decrease, i.e. the fiscal deficit will increase. The administration further claims that private investment will increase, though those effects are ambiguous at best. Even if investment did not increase (as it claims), the gap between national savings and investment will increase, and hence so will the trade deficit. If investment does increase, the trade deficit will increase all the more.

The resulting increase in the exchange rate (from what it otherwise would have been) will, of course, make America less competitive. But so too will other provisions of the tax bill. Overall, there were large winners and losers from the bill, and among the winners was the real estate sector—tilting the balance towards a non-tradable sector. Perhaps even worse, the long-term competitiveness of the US depends on the quality of the labor force, on investments in higher education, technology, and science. Both in the stances taken on appropriations, in particular provisions of the tax bill, and on regulations, the administration and the Republican Party have undercut support for higher education, technology, and science. Examples include: In the tax bill, the endowment of our leading universities, which helps support their enormous investments in

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21 There are a number of complexities: Corporate after tax-profits will increase, and some of that will be saved, partially offsetting the increased fiscal deficit. Some of it will be spent on increased share buy backs and dividends, and some of that will be saved, again partially offsetting the increased fiscal deficit. The Trump administration claims that most of it will be spent on increased investment, and if that is so, the gap between national savings and investment will be all the larger. Ricardian equivalence would suggest that households and corporations would increase savings in response to the increased government deficit, but there is little reason to believe that is the case. Changes in the relevant marginal cost of capital relative to the marginal return to investment will vary greatly by industry, with uncertain effects. The elimination for large portions of the population of tax deductibility of mortgage interest and property taxes will increase the price of housing, discouraging investment in housing. The resulting decrease in property values and household wealth could decrease consumption of housing services going forward, and decrease savings targeted at the purchase of a home. The tax preferences given real estate trusts may lower the cost of corporate office space, encouraging more spending on real estate relative to more productivity-enhancing investments.

22 There are many determinants of the exchange rate, e.g. if investors become pessimistic about US economic policy because of the looming fiscal deficit, they may try to pull their money out of the country, and the effect of this will be to lower the exchange rate. It is important to bear this in mind, since at the end of 2017, the dollar depreciated against the euro. It will take a while for the full effects of the tax bill to get reflected in the trade deficit.

23 A 1.4% tax on earnings of endowments was retained in the final version of the bill.
basic sciences, will, for the first time perhaps in any democratic country, be taxed. And the Trump administration has gone so far in its opposition to science as to issue orders that the Center for Disease Control and Prevention (CDC) not use the phrases “evidence-based” or “science-based” in their documents.

But America’s competitiveness will be hurt for another reason: American producers have benefited from access to low-cost inputs. The world has created an efficient global supply chain. Depriving American producers of access to this global supply chain—or imposing tariffs or other trade barriers making it more costly for them to do so—will increase their costs and decrease competitiveness.

Even American workers are likely to be worse off, for two reasons. First, job loss from the decreased demand for American goods because of the loss of competitiveness may occur faster than job creation from the costly import substitution that Trump is trying to encourage. There may have been job losses as these global supply chains were created, but there will be further job losses as they are destroyed. Economic adjustment is costly, and especially in America, with its weak system of social protection and virtual absence of active labor market policies, workers are likely to bear the brunt of those costs. And secondly, as we noted earlier, as consumers, Americans, including workers, will no longer benefit from the lower prices that access to, say, China’s goods affords.

What Trump and many of his supporters fail to grasp is that while globalization may have been vastly oversold, with aggregate benefits less than its advocates claimed and with distributive effects far greater than its advocates admitted, undoing globalization has also been oversold.

6. Global response

As we noted in the beginning of this paper, the US played a central role in creating our global rules-based system. We were remarkably successful in persuading others of the benefits of such a system, and even as Trump walks away from it, and asserts an “America First” nationalism, other countries remain committed. While his critique of globalization—including how America has been hurt—may have struck a chord for those who have been left behind in the US, it has left most of the rest of the world totally unconvinced. He claims that globalization has been unfair to the US, that NAFTA, along with virtually every other international agreement, are the worst agreements ever, and that US trade negotiators got snookered. To the rest of the world, these claims are laughable: the US always dominated trade negotiations, only the EU was of anywhere equal bargaining power, and the US got most of what it wanted in the trade negotiations. To be sure, as the TPP illustrated, the US may have wanted the wrong things, at least from the perspective of American workers; and even more importantly, the US provided far too little in assistance for those workers who lost their jobs, whether from globalization or technology. (In the US, ironically, the political party most strongly advocating globalization was also the one most consistent in its opposition to trade assistance.) It was a corporate-driven trade agenda, one which was not averse to the lower wages at which it could obtain labor abroad, or the lower wages resulting from workers’ weakened bargaining power and the lower demand for especially unskilled labor in the US.

25 See Stiglitz and Charlton (2005) for the many ways in which trade agreements have been unfair to developing countries and emerging markets.
26 See Rodrik (2017).
Beginning with the January 2017 speech by Chinese president Xi Jingping to the World Economic Forum in Davos, just before President Trump’s inauguration (Xi, 2017), foreign leaders made it clear that they would not let Trump destroy the global rules-based system. At Davos, American business leaders expressed concern that it would not be the same kind of rules-based system. There would be less attention to intellectual property rights (but in that, they may be mistaken, as China itself relies increasingly on the intellectual property regime) and to investment protections. So too, activists in the West expressed concern that there would be less concern about labor rights, human rights, and the environment. But, except from the US (and within the US, from Trump and his clique), there has been no dissent from the broad WTO framework, and its ability to resolve disputes through what has been established over the last two decades as a fair and efficient system of adjudication. There is, accordingly, every reason to believe that the rest of the world will proceed with current arrangements, shoring up the rules-based global trading system, where necessary, to mitigate US disengagement, and extending it, in many cases, in part because of the opportunities afforded by disengagement. The world will move towards more plurilateral agreements, among “coalitions of the willing,” among those countries who see the benefit of such agreements. Almost surely, as such agreements lead to some trade creation, there will be some trade diversion away from the US: its role in the global economy will diminish.

That the current global rules-based system will need shoring up is clear: as noted earlier, the US has refused to approve three vacancies in the WTO appellate body, and with additional vacancies in 2018 (one in October), there will not be the necessary quorum. This will necessitate the WTO facing a hard decision. It has always proceeded by consensus. A “WTO minus one” could presumably proceed by a new consensus—it could appoint new perhaps temporary appellate judges that would hear all cases not involving the US. In effect, because the US had destroyed the key WTO institution, the judicial body with which disputes were adjudicated, the US would have de facto withdrawn from the WTO. One would have gone back to a system of resolving disputes not seen for a long time, by cajoling, threats, and tit-for-tat trade wars.

The US would almost certainly win (in some sense) in disputes with smaller countries, but that, in turn, would make trading with the US far less attractive. But there are particular firms and their workers that benefit from trade even from small countries, and almost surely their voices (through their elected representatives) would be heard, and especially so in a closely divided Congress. But there is no presumption, as we noted earlier, that the US would win in the disputes that it cares most about, those with say Mexico, China, and the EU. Quite the contrary: strong-arm tactics are likely to generate political resolve not to give in. In Mexico, Trump’s virulently bigoted and prejudiced anti-Mexican stance may well result in the election of the strongly anti-American Andrés Manuel López Obrador. Lab experiments in the ultimatum game verify what has long been apparent: individuals are willing to sacrifice their own well-being when they believe they are being unfairly treated. Mexicans have good cause to believe that they are being unfairly treated, while, apart from Trump and his followers, most Americans realize

27 There are other views. In particular, there are some who suggest that the discord between China’s system of state capitalism and more market-based systems is too large and is itself putting too much stress on the global trading system. See, e.g. Financial Times, 2017. Still others suggest that the tension between globalization, national sovereignty, and democracy is too great, and to preserve democracy, there will have to be a retreat from democracy. See Rodrik (2017).
28 There is some legal controversy over whether, in these matters, it is compelled to do so. The WTO has always acted by consensus. But, by the same token, there has never been a country so willing to undermine the rules-based international system as the US seems to be now.
that NAFTA was broadly fair, with a November Pew Research Center survey showing that 56% of Americans thinking NAFTA has been good for the American economy (Pew, 2017a). Indeed, in the aftermath of the signing of NAFTA, the giant sucking sound that Ross Perot had predicted never happened; rather, because of good overall macroeconomic management, the unemployment rate fell to a low of 4.0 percent in 2000. Meanwhile, the poorest Mexicans, their corn farmers, had to compete with vastly subsidized American corn; US corn acreage expanded as Mexican corn acreage contracted.30

In Latin America, the fact that the US is no longer a reliable trading partner has generated support for strengthening the Pacific Alliance. US refusal to curb its agricultural subsidies has been an impediment to the creation of a Free Trade Area of the Americas. Freed from this constraint, some are talking about seizing this opportunity to create a trade agreement embracing all the countries of the Americas other than the US.

In Asia, Trump’s protectionism could not have come at a better time for China and a worse time for the US. China under Xi was finally stepping onto the world stage in a big way. Previously, it had wanted to keep a more modest profile. It spoke about being a moderately prosperous country by 2030. It argued with statistical authorities when they claimed that China was the largest country in the world in purchasing power parity. It seemingly did not want the onus that might be associated with that position. Obama had bristled at Xi’s early efforts at creating the Asian Infrastructure Investment Bank, urging others not to join, though having nothing to offer them as a substitute. When the UK joined, it was as if a dam broke, and membership quickly soared to more than 52 founding members; by October 2017 a total of 80 prospective members had been approved. Obama had constructed the TPP to contain China’s influence (not unlike the futile containment policy of the early years of the Clinton administration). It is unlikely that it would have done so, but we shall never find out.

US withdrawal from the TPP has met with two responses from others. First, as I noted earlier, the other 11 members of TPP have decided to go forward on their own, without the US, and without the objectionable provisions of the TPP that the US had insisted on including.

Secondly, it has provided greater scope for the China-led initiative called the “new silk road initiative” or “One Belt, One Road”—a massive trade and infrastructure initiative that will change the geo-economic and geo-political landscape, putting China squarely in the center of much of Asia.

With China’s share in global output, global trade, and global savings increasing, there would in any case have been a shift in the balance of economic and political power; and the world would have in any case moved towards a more multipolar system. It was inevitable that the period of US dominance, between the fall of the Berlin Wall and the collapse of Lehman Brothers, would have been short lived. Trump has accelerated these changes. For the US, as Obama illustrated, trade has been an instrument of foreign policy—and foreign policy has been used to advance trade and economic interests. America’s standing in the world has depended, of course, partly on its military power. But the inability of the US to resolve with arms the conflicts in Afghanistan and Iraq—wars with a multi-trillion dollar price tag—has made the limits of military power increasingly evident.31 It is clear that it is soft power that matters (Nye, 1990). And there is little doubt that Trump, with his antics and his seeming affinity for authoritarian leaders, has greatly eroded US soft power, especially in democratic societies (Pew, 2017b). There is a growing body of literature suggesting

30 From 1994 to 2013, Mexican corn production was reduced from 8 million hectares to 6.8 million hectares while in the US it increased from 29.3 million to 35.5 million. See Stiglitz (2017c).
31 See Stiglitz and Bilmes (2008, 2010) and Bilmes (2016) and the references cited there.
that trust is important for economic relations and economic performance; under Trump, there has been an erosion of trust in government, in institutions, and in the US.\textsuperscript{32}

It is uncertain how long lasting these effects will be. Almost surely, there will be hysteresis effects: even if the next American president reaffirms America’s traditional commitments to the rules-based international trade system, Trump has created new uncertainties. For three quarters of a century, the US tried to convince others that borders did not matter, or should not matter, at least as far as the movement of goods and services was concerned. Trump has shown otherwise; and America’s trading partners will know that it could once again elect a protectionist and someone who does not believe in international institutions. Global businesses will know that there is risk in creating global supply chains on the presumption that borders do not matter. All of this is a major setback to globalization, especially as it had been proceeding.

Thus, while the country is fortunate, more than a year since his inauguration, that Trump has left many of his campaign promises behind, there has already been long-lasting damage—and there will be even more if he and his team continue on the course that they have struck.

While Trump was wrong in claiming that the trade agreements were unfair to the US, there is little doubt that globalization contributed to the weakening of wages of America’s unskilled workers. Both parties, as a whole, paid insufficient attention to the distributive consequences of globalization—or other aspects of economic policy. The belief that policies that lead to higher growth would “trickle down” enough to offset such adverse effects was based on little more than blind faith.\textsuperscript{33} Learning this lesson—if in fact we do—may be the only silver lining in this dark cloud hanging over the global horizon.\textsuperscript{34}

References


\textsuperscript{32} See CNN Poll from August 2017, available at: http://edition.cnn.com/2017/08/07/politics/poll-trump-approval-down-amid-distrust/index.html which noted that only 24% of Americans say they trust all or most of what they hear from the president’s office, while 30% say they trust “nothing at all.”

\textsuperscript{33} See Rodrik (2017) for a particular trenchant criticism of the economics profession.

\textsuperscript{34} See Stiglitz (2018) for a set of proposals for how to ensure that globalization is inclusive.


