



ECONOMIC VIEWPOINT

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Trade is Slowing Down: What Does This Imply for Globalization?

As is widely reported by the IMF and others, global trade is growing at a far slower pace since 2012 than at any time in the previous 30 years. This is all the more worrying since economic growth itself has been anemic since the Great Recession and current forecasts are not terribly ebullient. Do these factors spell doom for globalization as we have come to experience it? Is this further validation of the political economic reality of more vigorous pursuit of national economic interest as noted by Prof. Dani Rodrik in his *Globalization Paradox* (2011)? Let's first take a look at the slowdown in world trade.

According to IMF's *World Economic Outlook* (October 2016), the fall-off in trade values can potentially be traced back to cyclical factors such as the slowdown in global investment as well as the re-balancing in China, if one looks at the demand side. The *WEO* claims that three-fourths of the trade slowdown can be attributed to weaker economic activity and a subdued investment picture. This may also include the indirect effects of a leveling off in logistics improvements. More interesting, however, is the claim that there has been a marked shift in Global Value Chains, namely, that the process of off-shoring may have reached its limits.

If we dig further than the recent global under-performance of economic growth as a result of near-recession in Europe, slower growth in China and other BRICS, and a reluctance of consumers to spend, businesses to invest and governments to pursue fiscal expansions, we need to look at the composition of trade itself. An important 2015 IMF working paper by Constantinescu, Mattoo, and Ruta (WP/15/6) seeks to find the roots of the trade slowdown in structural forces, concluding that at least half the recent slowdown stems from a now lower elasticity of trade to GNP than observed in the 2000s. Moreover, this follows a declining pattern seen in the first decade of the 2000s as compared with the 1990s, where in the U.S. and even in China, the trade to income relationship has declined. The same researchers then attribute much of this decline not to a change in trade composition per se, but rather to a fall in the tradable component of manufactures.

If indeed, China's rebalancing involves a re-retrenchment in its own import basket, and new and potentially disruptive

technologies offset the cost advantages normally associated with global value chains (GVCs), then the process of de-globalization has already begun. This can only be further accelerated by populist rhetoric that blames trade for the majority of job losses in the U.S., still the most vibrant and open market, as well as the anti-centrifugal forces inside the EU that seem to be in play post Brexit.

What can be the logical consequences of these phenomena that seem to be moving in a singular direction? First, again drawing on Constantinescu *et al*, there is a sense that we have passed the peak in terms of trade driven by GVCs and that a retrenchment of production is already well underway. These authors present data showing a marked decline in the rate of growth of foreign value added to domestic value added in global exports, indicating that the expansion of global supply chains is faltering. This process implies that domestic sources of growth will become more important in future, which could provide some relief to industries that are struggling to compete; however, the great risk is that this will produce disguised protectionism. The only antidote to this phenomenon is vibrant competition and markets that are truly contestable and exhibit low barriers to entry.

We are already seeing signs of protectionism in various guises in the EU, whether actions against Uber or others; and market concentration in many sectors has arguably increased due to scale economies. The only way to counteract these forces is to allow for vigorous competition, such as that provided by new technologies. This disruption will cause greater stress in labor markets, however, and trade will not be the culprit. Public policy will need to come to grips with the problem through more effective taxation, more redistributive social policies and greater opportunities to the bulk of income distribution. Contrary to the view of Rodrik's tri-lemma, where countries choose among national goals, hyper-globalization and democracy, de-globalization will not solve this dilemma. Rather it will depend on more enlightened and more effective national economic policies. Without them we will witness a retreat from globalization that far exceeds the economic dimension.