

The 2005 Angelo Costa Lecture (Rome)

**In Defense of Globalization:
It Has a Human Face**

By

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Jagdish Bhagwati, a University Professor at Columbia University and Senior Fellow at the Council on Foreign Relations, New York, has just published In Defense of Globalization (Oxford). This Lecture reflects the views developed in that book. The book has been translated into Italian by Laterza..

The Rector, Mr. Costa, Mr. Montezemelo, Professors Piga and Garonna, and Friends:

I am delighted by the invitation to give this year's Costa Lecture. This prestigious Lecture commemorates one of modern Italy's great entrepreneurs. I am delighted to be here, honouring his memory in the only way a Professor can: by talking! Indeed, India is also known, like Italy, as the fluent society, a witty variation on Professor Galbraith's affluent society, so I am an even more appropriate choice to be lecturing today than the organizers of this event thought.

I should add that Italy holds a special place in my life. I had the privilege, when I was teaching at MIT, to have known extremely well Italy's great economist, the Nobel Laureate Franco Modigliani. Indeed we treasure a photograph of Franco holding our daughter, then just a few months old, in his hands with his wonderful smile. Then again, I have had several distinguished Italian students during the twelve years I have taught at MIT and the 35 years I have taught at Columbia University: and I am happy to see many of them today at this Lecture.

But I must also add that Italy has played no small part in my own life. I note that Mr. Montezemelo is now the CEO of Fiat, having moved from Ferrari: he has the distinction of leading two of Italy's world-class companies. Fiat, I must inform Mr. Montezemelo, happened to launch me on an important part of my career, as an economist in the public and policy spheres, strange as it may appear. I was an underpaid Professor in the Delhi School of Economics in 1964, not quite the clerk in Gogol's story on the Overcoat but still constrained to travel in an overcrowded bus for over an hour each way

to the campus. So I wanted to buy a Fiat: the best of three cars in India. The queue for it was enormous; so I arranged to be an Adviser to the government so I could jump with priority ahead of the others. So, my interest in economic policy was strongly reinforced by Fiat! But when I got the Fiat allotted to me, I had no money to buy it: it cost the equivalent of a thousand British pounds and there was no way a Professor could afford it. But, as luck would have it, George Weidenfeld of Weidenfeld & Nicolson in London had just launched, along with Mondadori and others, a series of small non-technical books with wonderful illustrations for the general public. Professor Jan Tinbergen, the first Nobel laureate in Economics, was asked to write one on Central Planning; I was asked to write a companion one on The Economics of Underdeveloped Countries. And, believe it or not, they offered me an advance royalty of a thousand pounds, the exact price of a Fiat. It was a contract I could not refuse. So I started my public writing career as well, thanks to Fiat, Mr. Montezemelo. Indeed, without Fiat, I would have remained only a theorist: not bad at all but hardly sufficient in a social science.

But, of course, our two countries India and Italy have now grown bonded by marriage, in the old-fashioned way! India owes gratitude to Italy for the gift of Sonia Gandhi: a major figure in India's politics today. I must tell you, however, how my mischievous temperament got me into trouble once. Some time ago, I was asked by Indian journalists what I thought of the prospect of foreign-born Sonia Gandhi becoming India's Prime Minister. I replied with a witticism, saying: "What Alexander could not accomplish for the Greek empire, Sonia may achieve for the Roman one". But then I added: "by using the Greek strategy of the Trojan Horse". Alas, the double witticism was reported in some of the Indian papers with the headline: "Professor Bhagwati compares

Sonia Gandhi to a Horse”! So, when on US television I was asked the same question recently, I changed my witticism and said: “ The UN demographic projections show that in three decades, Italian population will have declined substantially and almost a quarter of Italy’s labour force will be foreign-born. With skilled Indians inevitably constituting a large fraction of these immigrants, and given the high rate of turnover of Italian Prime Ministers, there is a good prospect that Italy will have an Indian-born Prime Minister down the road. And then we Indians will have exacted our revenge!”

Let me then turn to the topic of this Lecture: Globalization and the controversies that surround it. Now, the challenge to globalization comes conventionally from protectionists reflecting special producer interests. Ever since Adam Smith wrote about the advantages of free trade, and economists such as David Ricardo and John Stuart Mill elaborated on this demonstration of the gains from specialization and hence from trade, the free traders have had to fight the special interests that seek protection against the general interest of overall economic prosperity. Today, one sees a return of such conventional protectionism in the United States over outsourcing: the phenomenon of the new trade in services at arm’s length where the provider and the user do not have to be in geographical proximity and can transact through snail-mail or the Internet. One also sees it in the resistance in the European Union to the liberalization of agriculture under the ongoing Doha Round of multilateral trade negotiations, the first under the World Trade Organization (WTO) which replaced in 1995 the GATT which had been signed just after the Second World War had ended.

But it would be wrong not to recognize that, in every generation, there has also been some dissent from within the economics profession itself to the proposition that

freer trade will produce greater economic prosperity. This dissent, I have observed elsewhere¹, comes principally from the fact that the case for free trade is based on an extension to the international arena the case for allowing market prices, or Adam Smith's invisible hand, to guide the allocation of resources. But if market prices do not reflect true social costs, the invisible hand may well point in the wrong direction. Such "market failures" need to be corrected for the case for free trade to be restored to full cogency. The correct policy response to this important insight from the postwar theory of commercial policy is, however, to insist that where such market failures exist--- e.g. when environmental pollution exists without a "pollution pay tax" in place --- the optimal policy is not to shift to protectionism but to fix the market failure and then to use free trade to reap the gains from trade.² So, there is no real reason for economists today not to be supportive of freer trade.³

But today, aside from such conventional protectionism, whether from special producer interests or a handful of economists, we also face massive protectionism, indeed more general anti-globalism, by vast numbers of anti-globalizers worldwide. These critics always say they wish to be stakeholders in the process of globalization. But they divide into two groups: those who wish to drive a stake through the global system, like in Dracula films, because they reject the global system altogether; and those who wish to exercise their stake in the system. The former group take to the streets; and if you extend a hand to them, they will bite, not shake, it. The latter group, on the other hand, is willing

¹ I have reviewed these dissents from the earliest times since Adam Smith, and the important clarification of the common intellectual basis for these dissents, in my Stockholm Lectures, Free Trade Today, also being translated into Italian by Laterza.

² For a fuller, more nuanced statement of this argument, consult my Free Trade Today, *ibid.*, Chapter 1.

³ Nonetheless, there are a couple of economists who play the protectionist role, wittingly or unwittingly, with arguments that are not intellectually compelling. Several of these arguments have been noted and rejected in the Report on The Future of the WTO by an expert group, of which I was a member, appointed by the Director General of the WTO and released on January 17th 2005.

to sit down with us, prepare policy briefs, and to reshape the system. I call the former the stake-wielding, the latter the stake-asserting, anti-globalization critics.

The stake-wielding groups cannot be talked with; they can only be understood intellectually. But the stake-asserting groups can indeed be engaged. The principal task before the proponents of globalization then is to understand what bothers these groups and then to examine their fears and phobias with an open mind, separating the wheat from the chaff. So, I ask: what ails these groups?

Their principal focus is not on the effect of globalization on economic prosperity. They are concerned instead with what I call the “social” effects of “economic” globalization. They fear, indeed claim, that economic globalization is harmful to social agendas such as the reduction of child labour, removal of poverty, the maintenance of rich-country labour and environmental standards, the exercise of national sovereignty and democratic rights, the maintenance of local mainstream and indigenous culture, and women’s rights and welfare. With the substantial agitation in that vein worldwide by vast numbers of the stake-asserting anti-globalizers, most politicians can be forgiven for thinking that (economic) globalization is a phenomenon that imperils the social agendas that we value.

Thus, Prime Minister Tony Blair, former President Bill Clinton and Chancellor Gerhard Schroeder, the social-democratic proponents of the “Third Way”, lament economic globalization, even as they pursue it, as a phenomenon that “needs a human face”. Of course, if it needs one, it lacks one. And the former Prime Minister of Ireland, Mrs. Mary Robinson, having finished her term as UN Commissioner for Human Rights, seeks an “ethical globalization”, implying that it is not so.

Indeed, in the anti-globalization circles, there is a general tendency to blame globalization for all shortfalls in social agendas. Typically, many reports in international agencies observe that globalization has increased, that social ills such as poverty exist or have increased, and therefore the former is the cause of the latter. But, like Tina Turner's famous song "What's love got to do with it?", we must ask: what has globalization to do with it?

The contrary view, which I develop and defend in my just-published book, In Defense of Globalization (Oxford), is that economic globalization has a human face. It advances, instead of inhibiting, the achievement of social agendas as wide-ranging as the promotion of gender equality worldwide, reduction of poverty in the poor countries and the shifting of children from work to schools.

The choice between these two assessments of economic globalization --- broadly defined as increasing integration of nation states into the international economy via trade, direct foreign investment by chiefly multinational firms, short-term capital flows, cross-border flows of humanity and diffusion and sale of technology --- is a matter of the utmost importance. It has immediate implications also for the issue of what I call "appropriate governance".

For, if you believe that globalization lacks a human face, then appropriate governance will encourage policy interventions to restrain globalization. Witness the recent Presidential campaign in the United States where the fears over the alleged adverse effects on American workers (which is clearly a "social" issue, one can say) from outsourcing of services led the Democratic Presidential aspirants to embrace protectionist policies to tax or prohibit the outsourcing (i.e. import on line) of services by firms whom

Senator Kerry of Massachusetts characterized as traitors, never mind that he doubtless joined the company of these traitors when, a man of excellent Yale education and considerable wealth, he probably supped that night on imported French red wine and brie instead of Kraft cheese and Milwaukee beer and watched a BBC Masterpiece Theater play instead of watching an American sitcom.

But if you believe, as I now do, that globalization has a human face, then you will want very different policy interventions --- ones that preserve and celebrate the good effects that globalization generally brings but supplement the good outcomes and address the phenomenon's occasional downsides.

This contrast is best seen in relation to child labour in the poor countries. If globalization brings increased incomes to parents, will parents then send more children to work now that their incomes have improved or less because they do not need children to work and can send them to school instead? If the former, then clearly globalization creates a tradeoff between increased prosperity and the reduction of child labour; and policies that inhibit globalization become sensible. But if the latter, then we are likely to ask: what can we do to accelerate the pace at which child labour will be reduced by globalization? But more of this later when I discuss the nature of Appropriate Governance in greater depth.

The Human Face of Globalization

For the present, let me illustrate with a few examples --- you will have to read my book In Defense of Globalization for much fuller analysis --- how economic globalization has beneficial, not malignant, effects on social agendas.

Child Labour: The anti-globalization critics argue that increased access to foreign markets and resulting increase in poor-family incomes will lead to more child labour: this is the “wicked parents” hypothesis. By contrast, one can hypothesise that increased family incomes among the poor will lead “normal” parents, who do care about their children, to use the opportunity provided by increased incomes to take, say, the fourth child off work and put the child into a primary school instead.

As it happens, economists who have studied child labour empirically have also argued that economic analysis explains why parents act virtuously rather than wickedly. It turns out that the rates of return to primary education are very high in the poor countries. But credit markets are imperfect so that parents are unable to borrow against future income from educated children. These credit constraints are what hold back the education of children and their assignment to work instead. Once incomes improve, that automatically eases the credit constraint through infusion of cash; so education expands and child labour diminishes. Economists have produced a lot of evidence in support of this benign conclusion. Thus, for instance, an econometric study of Vietnam by a husband-wife team of econometricians at Dartmouth College in USA shows that significantly expanded incomes for peasants following liberalization of rice trade led to a significant shift of children from employment into schooling: and a double dividend followed from the fact that the beneficiary children included a number of girls.⁴

So, when globalization leads to increased prosperity, it also leads to less child labour. Indeed, there are many studies, for countries worldwide, that are supportive of this benign-impact outcome.

⁴ These studies are reviewed in Chapter 6 of In Defense of Globalization, *ibid.* Yet more evidence has accumulated in support of the benign hypothesis since the publication of my book.

Poverty in the Poor Countries: Critics also argue that globalization increases, not reduces, poverty in the poor countries. This is a comforting conclusion for those who oppose reducing trade barriers in the rich countries: if you can argue that your protectionism, which is good for yourself, does not harm the victimized abroad but in fact helps them instead, that is fantastic: you can even have a warm good feeling even as you open up with an AK47 on the poor souls! I have heard such self-serving rubbish from the opponents of NAFTA in the United States.

The evidence, however, certainly does not support this bit of sophistry. Globalization helps reduce poverty. Why? We have a two-step argument here. Globalization increases income. Income expansion in turn reduces poverty.

The former relationship is pretty robust, though exceptions can always be found. The economist Arvind Panagariya has shown that, over three decades in the postwar period, no country that has been an “economic miracle” in the sense of having a sustained growth rate of 3% per annum per capita and over, has not had trade also grow rapidly; whereas “economic debacles” with low or declining per capita incomes have also been characterized by similarly declining trade. Can the decline in incomes have come about because of “exogenously” declining incomes? Yes, sometimes for sure. Thus, civil strife may decimate a country’s economic prosperity and growth and, in consequence, her trade also: Angola and Sri Lanka could well be examples of this reverse relationship. But, outside of such singular circumstances, the relationship (when sustained over long periods) hardly goes from income to trade, rather than trade to income, in most cases.

But then, has opening up trade further failed to increase income sometimes? Yes, but no one denies this. For instance, you may have infrastructure bottlenecks or civil

strife or investment controls that prevent a utilization of the improved trade opportunity. But straw men such as these are constructed by serious people to pretend that the case for free trade is flawed. It is as if the fact that on 9/11 the two flights from Boston to New York crashed into the Twin Towers is used to argue that therefore the introduction of such flights need not lead to an improvement in the ability to get from Boston to New York and back!

The latter relationship, between growth and poverty reduction, is also empirically robust. In the two countries, China and India, where poverty has been immense, this relationship has worked dramatically since the 1980s when both countries retreated from autarkic policies and opened to trade and direct foreign investment, more dramatically in China and with more dramatic effects on growth rates and associated poverty reduction. The ability of a rapidly growing economy to suck people up into gainful employment, and thus to make a sustained dent on poverty, has rarely been demonstrated so well. It puts to rest the absurd contention that growth is a conservative, feeble “trickle down” strategy for reducing poverty; I have long argued that it is instead a radical, effective “pull up” strategy for poverty reduction.⁵

Women’s Equality: One more example of the benign influence of economic globalization on social agendas comes from the question of women’s equality and rights. Two examples suffice to show this.

Consider the effect of globalization on gender pay inequality. That women are paid less than men who are no more qualified is a widespread scandal. This prejudice is however expensive for the employer who indulges in this practice because he then pays

⁵ In my book In Defense of Globalization, I do consider several institutional and policy measures to strengthen the impact of growth on poverty. I also consider ways in which a specific growth process might harm the poor, or any specific groups, and how to handle such possible downsides, if and when they arise.

more than he should if he hires more expensive men than equally productive women. One can then argue that, in internationally competitive industries, the reduction of such pay inequality will follow because those who fritter away money on indulging such prejudice will yield in competition to those who do not. It turns out that an empirical examination of two decades of experience in US industries shows precisely that the gender pay inequality shrank faster in the traded, than in the non-traded, industries.⁶

A different kind of example comes from the way in which Japanese direct foreign investment in the West in the 1980s and early 1990s led to the acceleration of the assertion of women's rights in Japan. When Japanese firms went abroad, their executives were of course men since women were simply not for recruitment into executive ranks. But the women went to New York, Rome, London and Paris with their husbands and they saw how women were treated a lot better there. That gave them ideas and they became a force for change, as women often do everywhere. Globalization, in shape of multinational investments, had turned out to be a source of beneficial influence for Japan's progress towards women's rights.

Appropriate Governance

Indeed, as one goes down the litany of complaints and fears of the anti-globalizers, the conclusion is inescapable that the effects economic globalization on several social dimensions are benign, on balance, rather than malign. But then we must ask: what institutional and policy framework is necessary to improve on the benign outcomes that globalization fetches?

⁶ This study by the two women economists Elizabeth Brainerd and Sandra Black is discussed in Chapter 7 of *In Defense of Globalization*, *ibid.* Needless to say, this benign outcome need not hold in every country, particularly if the supply of female labour is perfectly elastic at a given wage and men's wages are at a legislated minimum: conditions that may obtain in some developing countries. The conditions under which the wage differential would go in the perverse direction can be imagined but are improbable in practice.

Evidently, three types of issues matter. First, even if the effect is benign, it is not always so. Therefore, we must devise institutions to deal with downsides, as and when they arise. I have long argued that the developing countries often lack adjustment assistance programs of the kind that the developed countries, which have liberalized trade far more (contrary to Oxfam's ill-informed talk about "double standards" in trade), have evolved over time. But how can the poor countries finance such programs? Evidently, aid agencies such as the World Bank can be mobilized to provide such funds to support trade liberalization. I am happy to note that, after years of exhortation, Mr. James Wolfensohn, the outgoing President of the World Bank, did announce such a scheme to support developing country trade liberalization last year.

Second, we need to ensure that we do not repeat the mistake made by the reformers in Russia, where shock therapy was tried and failed. Maximal speed is not the optimal speed; both economic s and politics require cautious adjustment. When the economist Jeffrey Sachs insisted on shock therapy in Russia, he used the analogy: "You cannot cross a chasm in two leaps". The Soviet expert Padma Desai --- transparency requires that I reveal that she is my wife --- replied: "You cannot cross it in one leap either unless you are Indiana Jones; it is better to drop a bridge." Events proved her right.

Finally, we need to use supplementary policies to accelerate the pace at which the social agendas are advanced. True, child labour will be reduced by the prosperity enhanced by globalization. But then what more can we do to reduce it faster? Here, the unions in the rich countries have taken the view that only trade sanctions have "teeth". This is a myopic and counterproductive view. It is far better, as many intellectuals from the developing countries argue, to use moral suasion today. After all, God gave us a

tongue as well; and in today's age, with democratic regimes worldwide, with CNN and with NGOs, a good tongue-lashing is far more powerful than sanctions imposed by governments whose own credentials often are not unblemished.

And so, while globalization has a human face, that face can be made to glow yet better with appropriate governance along these lines. Globalization works; but we can make it work better. That is the chief task before all of us today.