FROM GLOBAL TO LOCAL

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THE MAKING OF THINGS AND THE END OF GLOBALISATION

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GO EAST, YOUNG MAN?

FOR THE PAST THIRTY YEARS or more, the global economy has been run based on three big assumptions: that globalisation will continue to increase, that trade is the route to growth and development, and that economic power is moving from the West to the East. More recently, it has been taken as a given that our levels of interconnectedness – both physical and digital – will rise without limit. But what if some or all of these assumptions are wrong? What if everything is about to change? Indeed, what if the global economy has already started to change its rules, but we just haven't noticed?

This is a story that is hard to tell. When there have been thousands if not millions of books, articles and academic papers claiming that globalisation is the only game in town, saying that it isn't so may lead to me being put to the back of the class. If you are to believe much that is written on the evolution of the global economy, we have arrived at the equivalent of Fukuyama's (in)famous *End of History*, but this time for companies.[1] The caricature version of Fukuyama's thesis was that liberal democracy had won out over all other forms of political organisation. Communism had fallen, socialism was nowhere to be seen, there were no more challengers left on the field. Twenty-five years later what was an irresistible thesis had fallen from grace. 'Today, it's hard to imagine Fukuyama being more wrong.'[2]

Globalisation has become something analogous, portrayed as the end of economic history in many articles. In the common currently accepted version of the story of our world economy, offshoring of production to

Asia by the developed economies came, made and won. The spectre of China in particular looms large, with millions of cheap workers, huge industrial cities created instantly where there was nothing and a scale of ambition that seems to dwarf that of the West. For many commentators, politicians and economists this is a game that is already over. In their eyes we've seen a permanent deindustrialisation of the West and economic power has shifted significantly and permanently eastward.

But sometimes the stories that seem the most secure are actually fading away from the inside out. Our faith in the shining city on a hill, the project of American democracy, appears to have been significantly tarnished through the presidential election campaign of 2016. The long running Syrian conflict and the refugee crisis that it has spawned have challenged our ideas of progress and the march of peace through democratisation. And there are new voices questioning whether we've really settled on this new global economic order, questioning whether we are telling the right story about the world economy as we move further into the new century. These are the voices that will be heard in this telling of the global economy.

THE CORE ARGUMENT of this book is that the accepted interpretation of the future of globalisation is misleading and flawed. We are running the global economy on a model that went out of date without anyone noticing at some point in the past decade. But working as if continuing globalisation (or hyper-globalisation for some) is the only show in town opens us all up to huge risk, potentially as dangerous as the financial crash of 2008 that brought the world economy to its knees.

The *Titanic* provides an unexpected metaphor for this phenomenon. Apparently, the most senior officer to survive its sinking, Second Officer Charles Lightoller, said on his deathbed that there had been an order to steer away from the iceberg but that it had been misinterpreted. If true, how could such a thing have happened? Left is left or in this case, port is port – surely? Maybe not. At the time of the *Titanic*'s maiden voyage the shipping industry was going through major changes as sail was giving way to steam. With that came a change in how ships were steered, from tiller to wheel. Why is that important? Well, with a tiller you steer *away* from the direction in which you want to go, whereas with a wheel you steer towards it. So the order the captain would have given to turn to port on a steam ship such as the *Titanic* was the exact opposite of that used on a sailing ship. And the helmsman may have misunderstood his command. The order and the execution were carried out in two different languages.

This may be just another great tall story to add to the *Titanic* archive but, whether it is true or not, it highlights the importance of having a narrative that reflects how the world works today, rather than how it worked yesterday. For if the story or shorthand we carry in our heads is out of date and wrong it can lead to catastrophic consequences, whether it is the loss of a ship, the greatest recession in a hundred years, or, as this book will suggest, many countries entering an economic wilderness in the coming decades.

Out-of-date stories and understandings are everywhere once you start to look, from our private lives up to narratives about the world itself. On a personal level, for how long after a relationship has effectively ended does one of the soon-to-be ex-partners cling to the belief that all is well? And how long do we hold on to a mental picture of ourselves in our twenties when we've long ago passed into our forties or fifties? On a macro level, the world has a long history of out-of-date stories causing more than a little trouble – the long and bloody history of proving that the earth revolves around the sun, the Cuban missile crisis and, of course, every financial crash from the South Sea Bubble to that of 2008, in which many individuals, investors and governments believed wrongly that risk had been designed out of the financial system when the exact opposite was true. It is hard to shake a story once it has become established. But without challenging our world view on a regular basis we run the risk of steering the global economy into another iceberg.

'GLOBALISATION IS AN IRREVERSIBLE PROCESS, not an option.'[3] Writing in 1999, the secretary general of the United Nations Kofi Annan didn't leave much room for doubt. Here at the cusp of the new millennium there were large questions being asked about the role of the United Nations and other multilateral organisations in promoting development in the context of globalisation. The 1990s had seen the consequences of the fall of the Berlin Wall, the opening up or the fall of communist countries and the emerging powers of China and India beginning to take a greater role in international trade. It is not hard to put yourself in Annan's shoes, looking at what appears to be an inevitable and unstoppable process playing out in front of you. Following decades of international negotiation on trade agreements the path forward was clear. Globalisation was the engine of the global economy and there was no need, no reason to turn it off.

Similar statements on globalisation were made by the leaders of various states and international organisations throughout this period. The then prime minister of the UK, Tony Blair, speaking to the 1998 World Trade Organization (WTO) Ministerial Conference, argued that 'the global economy is a fact' and that the question was 'not so much whether there should be free trade, but how best to manage what I believe is an irreversible and irresistible trend'.[4]

Statement after statement, newspaper article after newspaper article pointed in the same direction. The world had globalised and would continue to globalise, resulting in greater prosperity for all. For the liberal elite the question of the day became how this new prosperity could be shared to raise the standard of living for the millions living on less than a dollar a day. Globalisation was never in question.

In some ways this statement of intent to raise all boats on the tides of globalisation was a response from those in power in the multilateral organisations and Western governments to the many critics of globalisation. Joe Stiglitz, Nobel Prize winner and former chief economist at the World Bank, wrote a scathing critique of how multilateral organisations, in particular the International Monetary Fund (IMF), were working. Commenting on the decision-making process at the IMF he said, 'Decisions were made on the basis of what seemed a curious blend of ideology and bad economics, dogma that sometimes seemed to be thinly veiling special interests.'[5] The street protests at the Seattle meeting of the WTO in 1999 were a clear signal of the level of public discontent with the process of globalisation. But again these were not a denial of the process. Even those opposed to the negatives of globalisation were not denying its existence. They thought it should stop because of the damage it was causing.

As the financial crisis of 2008 was bringing the global economy to a very sudden and painful halt, the IMF was no less certain of the long-term outcomes for the world economy. 'Globalisation is irreversible. In the long run, globalisation is likely to be an unrelenting phenomenon.'[6] It did, however, caveat this with a warning that for periods of time the momentum could be lost, as occurred following the outbreak of the First World War. This, in the IMF's eyes, would be a pause in the long-run trajectory of development, with greater and greater economic integration expected as the world turned. The more things change, the more they stay the same.

Eight years after the start of the financial crisis, there are many voices again speaking out against globalisation, in particular arguing that it has not delivered on its promises. There are fears of a rise in protectionism in many countries, most clearly seen in the political rhetoric of the race for the White House that has played out in tabloid form through 2016. Throughout the campaign Donald Trump returned again and again to plans to increase tariffs on foreign goods, pledging to remove the United States from all its large-scale trade deals, including the North American Free Trade Agreement (NAFTA), and to kill off the multilateral deals being negotiated such as the Trans-Pacific Partnership (TPP).[7] Now in office, President Trump has signed an executive order pulling the US out of the Trans-Pacific Partnership (TPP), has talked up but not yet carried out plans to renegotiate NAFTA and has danced around the idea of a border adjustment tax.

The United Kingdom's vote to leave the European Union is another flashpoint, highlighting that the economic and social ties some take for granted are not as durable as they may believe. Attempts to unravel why the vote went in favour of exit are many, with commentators unable to agree on a clear story of what led to the result.[8] For some it is the long-term neglect of those negatively affected by globalisation in the poorer regions of the UK that led to the Leave campaign's success. For others it is simply about perceived levels of migration, having seen David Cameron pledge to reduce net migration to the tens of thousands only to see the flow of people into the UK increase significantly. Whatever the reason, the UK entered a period of great uncertainty in 2016, clinging to the reflexive statement that 'Brexit means Brexit' from the new prime minister Theresa May to try to stay afloat and see where it was going.[9]

According to Global Trade Alert, an independent initiative coordinated by the Centre for Economic Policy Research in London, there have been close to 6,000 protectionist measures introduced worldwide since 2008, leading to what it calls 'global trade disorder'.[10] These interventions can be anything from an increase in local content control (more of what is in a product has to be made in the home country) to the introduction of tariffs on products as they come across the border. It seems that as global economic conditions deteriorate countries cannot resist trying to protect their domestic industries at the expense of trade.

In a curt response to those hinting at protectionism and the end of globalisation the current director general of the WTO, Roberto Azevêdo, wrote in a comment piece for the *Financial Times*: 'Complementing the antitrade rhetoric is the notion that we have reached "peak trade" or that globalisation has ground to a halt. One argument is populist, one is intellectual – both are wrong.'[11] While his language was forceful and backed up by the status of his office, his argument or lack of one was shored up by faith alone.

What if those who run our multilateral organisations and many political leaders are wrong about the inevitable continuation of globalisation? Whether the process of globalisation has been managed well, whether it has fulfilled its promise to lift the poorest out of their precarious situations, is not the main argument of this book. What I want to explore is whether the process of globalisation is as inevitable as is being asserted, and, if not, the effect that will have on trade and international relations. We need to be clear both about whether countries are actually coming closer together or not and about the limits to globalisation.

THE STORIES WE TELL help us to make sense of the world. Each of us has a set of stories, some generated from personal or professional experience, some from our time as students, some handed down as tradition or history.[12] Thinking of what economists, historians, scientists and other thinkers do as a form of storytelling is uncomfortable for some, but the hope is that as the stories get better over time, we all gain a clearer sense of the world as it is rather than as it might be.

It is difficult to change a story that has existed for a long time, in particular one that has support from many people. This phenomenon, well recognised in science, was most clearly captured by Thomas Kuhn in his classic 1962 book *The Structure of Scientific Revolutions*, in which he speaks of paradigms, that is a shared understanding in a discipline of the methods that can be used and the problems that are worth studying. Once established, paradigms remain until there is a crisis that forces a move away from 'normal science'. But these 'paradigm shifts' are hard, for 'Novelty emerges only with difficulty, manifested by resistance, against a background provided by expectation.'[13] There usually has to be a significant build-up of contrary evidence, specifically a large number of anomalies which challenge the dominant view, to force a change of paradigm. So is there evidence which contradicts the continued expansion of globalisation? Can we see the anomalies in the globalisation story?

When Allied forces invaded Iraq in 2003 there was a large question hanging over the operation: would any weapons of mass destruction (WMD) be found? In the run-up to the invasion two dossiers were produced by the UK government which detailed claims about Saddam Hussein's possession of weapons of mass destruction and whether he could launch those weapons within forty-five minutes. The first, referred to as the 'September Dossier', had a foreword by Tony Blair in which he claimed that Hussein's 'military planning allows for some of the WMD to be ready within forty-five minutes of an order to use them'.[14] The US Secretary of State at the time, Colin Powell, made a presentation to the United Nations Security Council in February 2003 to convince them and other sceptics not only that Hussein had weapons of mass destruction but also that he was working hard to conceal them from inspectors in violation of UN resolutions. In that presentation he depended on the second British dossier, the 'February Dossier', calling it a 'fine paper [that] describes in exquisite detail Iraqi deception activities'.[15]

The problem was that the dossier was not all it claimed to be. As *The Economist* politely put it, 'This [dossier] mixed genuine intelligence with bits of an old academic thesis, lifted without attribution.'[16] There has been much written on the motivations of those producing the documents that supported the invasion of Iraq, but one probably generous view is that the signals they were receiving were simply misinterpreted. The intelligence they were trying to interpret didn't stand up to the weight that was placed on it. As we try to make sense of the global economy we are in an analogous situation as our data, our intelligence, is also weak, even if we don't realise it.

The second reason we do not see what is in front of us is subtler and harder to correct. This is when something accurately describes a situation but over time the context changes and what was initially a correct interpretation becomes misaligned. This is the slow-boiling frog problem applied to our understanding of the world. As the temperature changes slowly the frog doesn't realise it is being cooked. For us, no individual change is large enough to grab our attention and so it isn't until very late in the process that we suddenly see that there has been a very significant if gradual shift in the world.

The way in which a population changes over time, absent a large shock such as a war or a great pandemic, is an example of this kind of change. Successive generations will have varying numbers of people in every category (class, race, religious affiliation) and as the changes are driven by births and deaths in the main, they happen at a pace which is too slow to observe on a day-to-day basis. In May 2015 Ireland voted to amend the constitution of the country to allow same-sex marriage. This in a country that had been referred to by Pope Paul VI as the most Catholic country in the world and which in 2011 still had 84 per cent of the population indicating their religion as Catholic.[17] But the cultural make-up of the country had changed over generations, becoming more socially liberal, and so Ireland became the first country in the world to use a popular vote to legalise gay marriage.

The changes in the structure of the global economy are happening one company at a time. There is no one seismic moment that leads to every company siting all their production facilities in their home markets. Instead, older companies adapt or die and new ones with different ideas come into the market, again a rate of change too slow to see on a day-to-day basis.

Sometimes we try to mistakenly apply a story from one part of life to another that doesn't connect to what we are trying to understand. For instance among tech commentators and writers a common mistake is to apply digital models to the physical domain. The breathless way in which we talk about digitisation, disintermediation and the weightless economy distracts us from the actual rules of the physical world rather than those of the digital.

The perception of the past thirty years is that the world has become more and more connected, that it costs less and less to get anywhere or to contact anyone. And that there is a direct correlation in the decline of the costs between the movement of people, the shipping of things and the sending of bits of data around the world leading to one story – globalisation. Most of us have spent all our lives in this period of correlated change and so it is very hard for us to imagine an existence in which things are otherwise.

However, there are many popular examples of correlation not being causation, a field so rich it has led to a book and a popular website by Tyler Vigen, who was a law student at Harvard when he started the whole thing.[18] He created a blog, collecting data and looking for spurious correlations pretty much from anywhere. So you get Nic Cage and drowning put together, or the divorce rate in Maine with the per capita consumption of margarine, things which clearly have nothing to do with one another but which have an incredibly high level of correlation.

We have done the same thing with our understanding of the global economy. We've tangled up many things which are different – like falls in transportation costs, the deployment of dense communication networks and changes in production technologies – and put them all in a box labelled 'globalisation' without putting a health warning on the outside.

Over the past thirty years or so the signals on globalisation have all been moving in the same direction. The costs of communicating have been falling quickly, as have global transportation costs. But just because these two things happened at the same time does not mean that they are linked.

We'll talk more about the actual costs of these two phenomena in Chapter 5 and about their differing dynamics. For now, the most important thing to realise is that globalisation is not a single entity, a simple concept that is becoming either more or less prevalent. There are many things that can be moved between countries and they all have different dynamics. There are separate elements of globalisation and they can all move in different directions, complicating still further our picture of how the global economy is developing.

So what is globalisation? And what is the evidence for globalisation happening over the past ten, twenty or thirty years?

Most of us are aware that there has been increasing economic integration around the world since the end of the Second World War. A key measure of how integrated the world economy has become is the ratio of world trade to world gross domestic product (GDP). Looking at what is referred to as 'merchandise trade' (essentially physical products as opposed to services or financial flows), there have been significant changes since the 1960s. As flower power was taking over, global merchandise trade was about 20 per cent of world GDP. Then, following the energy crisis in the 1970s, the ratio varied but was roughly 30 per cent until the early 1990s. From that point on the ratio takes off, climbing to 40 per cent by 2000 and on to a high of just under 52 per cent in 2008. The story here is one of increasing economic integration through trade as more countries are becoming connected through the goods that move between them. Global trade grew at 3 per cent per year from 2000 to 2006, and for the year before the financial crash climbed 6.5 per cent.[19]

On any measure of trade the world has reached out more and more beyond national borders over the past half century. And this is another reason the concept of deglobalisation is so foreign to many economists and commentators – increasing integration has been with us over a generational cycle. It is hard to imagine the global economy working in any other way.

Following the financial crash of 2008 there was a severe contraction of growth and trade, with a ten percentage-point drop in the ratio of global merchandise trade to GDP. After such a spectacular crash, trade has recovered some of its intensity, but the ratio of trade to growth has flatlined. Having had trade growing at about twice the growth rate of global GDP, to have them now increasing at the same pace has got some people worrying whether we've reached 'peak trade'.[20] In relative terms we probably have, even if with an increasing global population we may have an absolute rise.

These are special circumstances and we have only four or five years of post-crash data to work with, but there could be a new trade dynamic emerging. It appears that, at a gross level, for the first time since 2008 growth in world trade no longer outpaces global economic growth. This may become the new normal. The question is whether this relative decline in trade in goods should be a concern, or whether it signals a new mode for the global economy. Does it signal a slowing or a shift of the pattern of growth? If so, is it going to last and what are the causes of the change?

HOWEVER, WE HAVE TO BE CLEAR – the making and trading of physical goods is only one part of globalisation. There is also the money side of the world. The old phrase should probably be flipped on its head – it is the world which makes money go around. As well as the movement of things across the globe, we have a long history in moving money or capital from country to country. The pace of financial globalisation was relatively slow up to the 1990s, and most companies were funding their developments using domestic sources of finance. Now, though, a company director can 'choose between issuing stocks and bonds in domestic or foreign financial markets. He or she can reduce his or her cost of capital if foreign currency loans are available at more attractive terms than the domestic loans. These loans can be hedged by using a variety of financial products. He or she can also consider selling equity at foreign bourses.'[21] There are many ways to find the money to build the factories that are needed to keep pace with global demand for new products.

Investors will always look at risk and return, and if that means investing across borders, so be it. One measure of the globalisation of finance (of which there are many) is the ratio of foreign assets (financial claims held by companies in another country) to world GDP. This ratio was 17 per cent in 1914 but by the end of 1945 it was only 4.9 per cent following the disintegration of the international system in the inter-war period. The peak of the ratio of foreign assets to GDP in 1914 was not reached again until 1980, and it then continued on to much higher levels, reaching 56 per cent in 1995.[22]

The financial crisis saw many of the indicators of international finance collapse, leaving many commentators concerned that there would be a lacklustre recovery in international capital. A 2011 issue of the magazine *The International Economy* had a special section which asked the question 'Is financial globalisation beginning a process of reversal?'[23] The fourteen experts consulted included a former president of the Federal Reserve Bank of New York, a member of the executive board of the European Central Bank and the chairman emeritus of the Chicago Mercantile Exchange. Even in this relatively conservative group, three responded that there was a process of reversal, five said definitely not, while the other six hedged their bets, indicating that there would be a change or pause in financial globalisation. This is the one aspect of globalisation where there is a widespread conversation on whether things will continue to integrate or whether there will be a retrenchment.