

Does Globalization Hurt?



SK

Michel Henry BOUCHET
September-December 2013

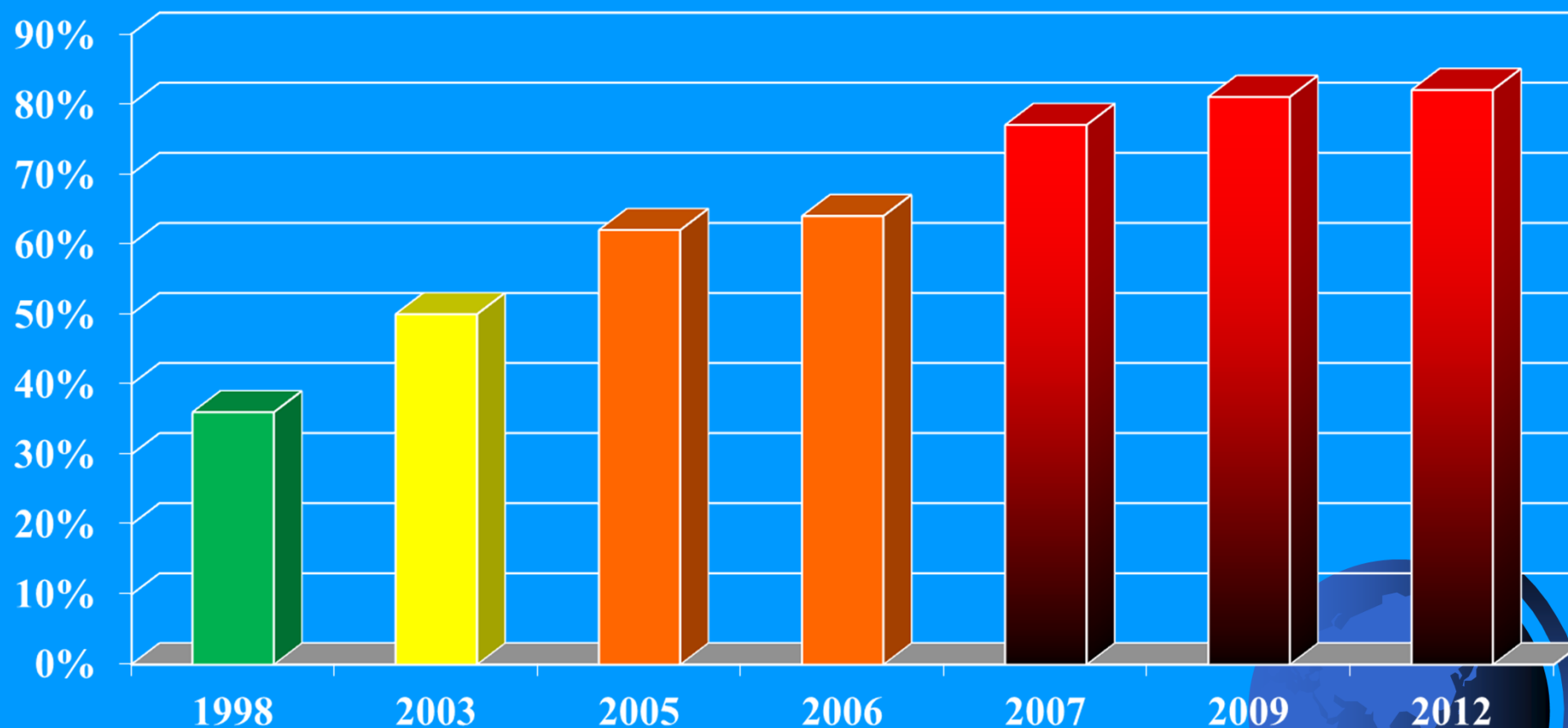
www.developingfinance.org

skema
BUSINESS SCHOOL

EFMD
EQUIS
ACCREDITED

MH Bouchet/SKEMA (c) 2013

« Globalization is a *threat* for France, for job creation and for well-being»



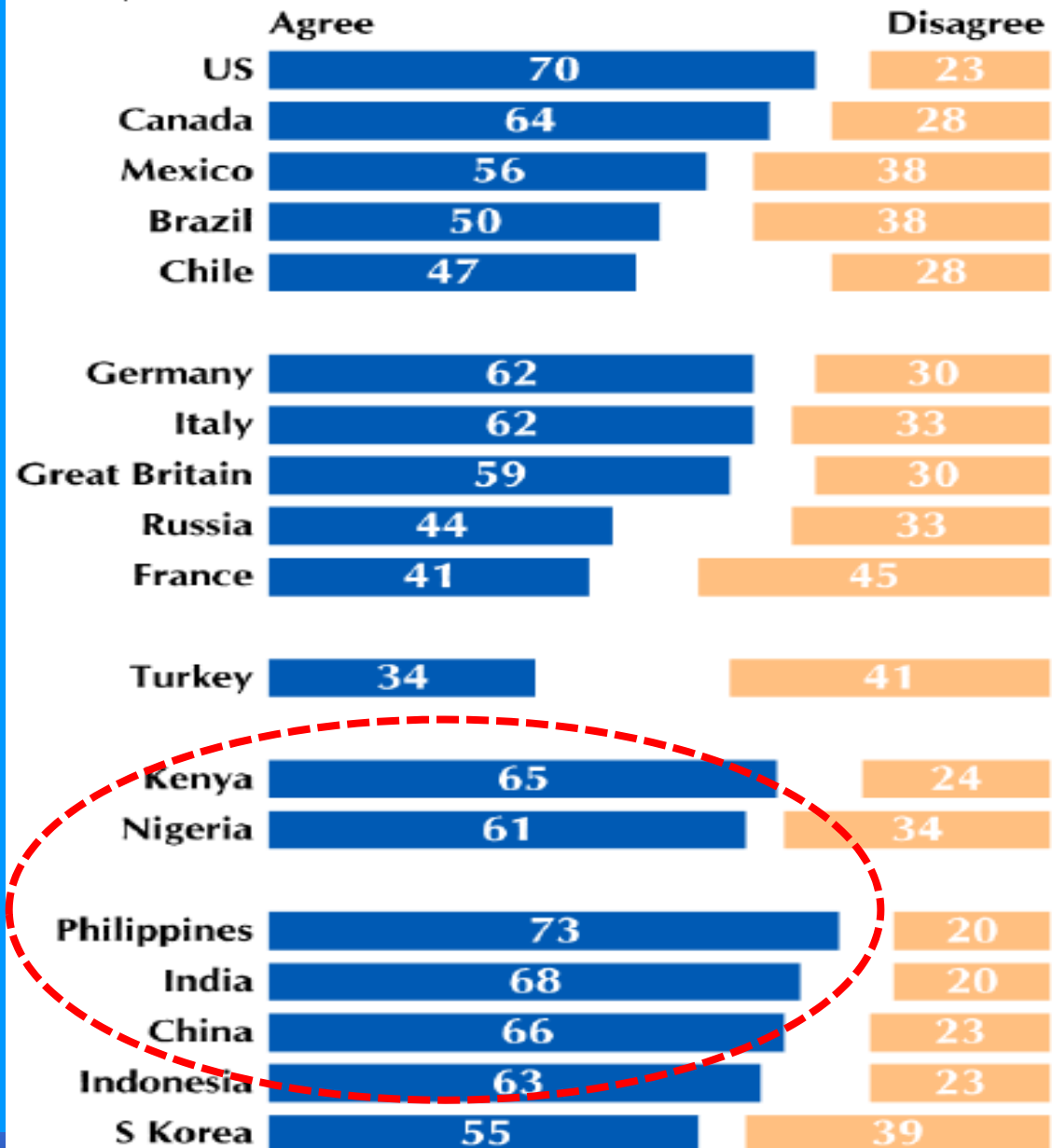
Sondages CSA-Challenges 12/2005, Eurobaromètre 2006-2009, IPSOS 2012

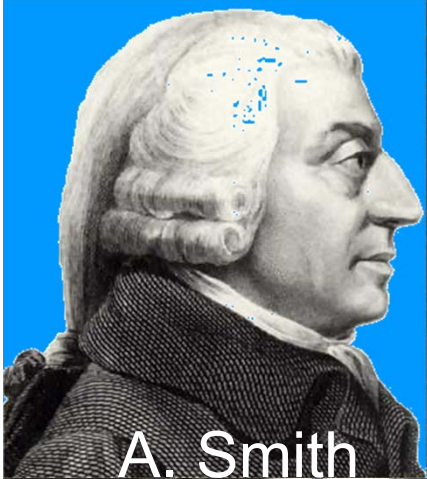
MH Bouchet/SKEMA (c) 2013

Should the free market system be the future of the world?

Free Market System

The free enterprise system and free market economy is the best system on which to base the future of the world.

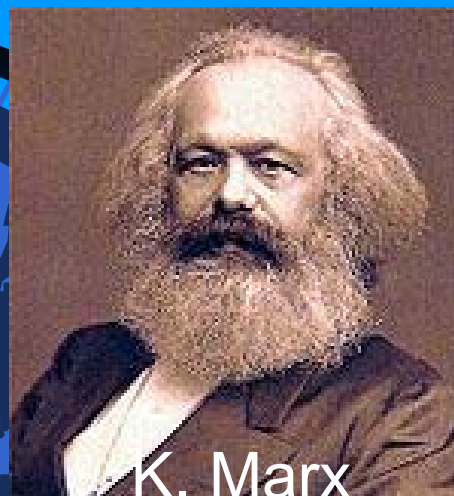




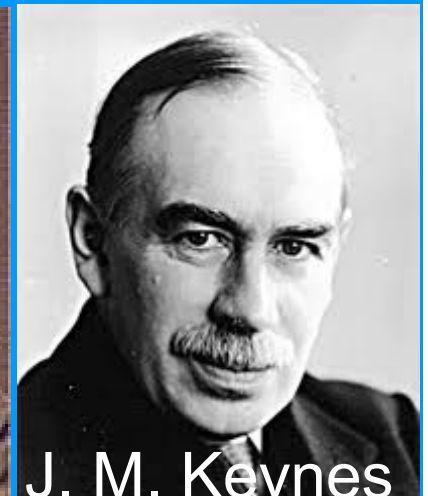
A. Smith



D. Ricardo



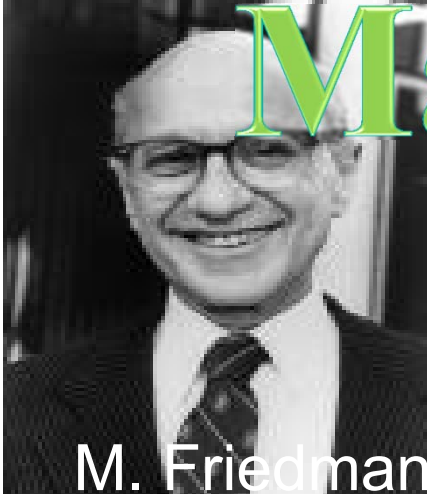
K. Marx



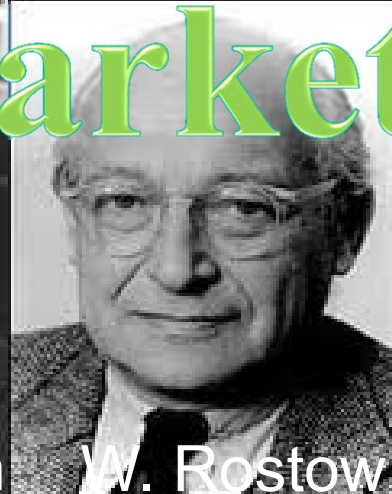
J. M. Keynes

Market

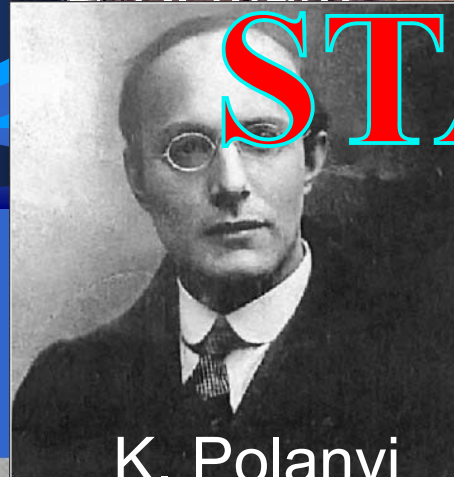
STATE



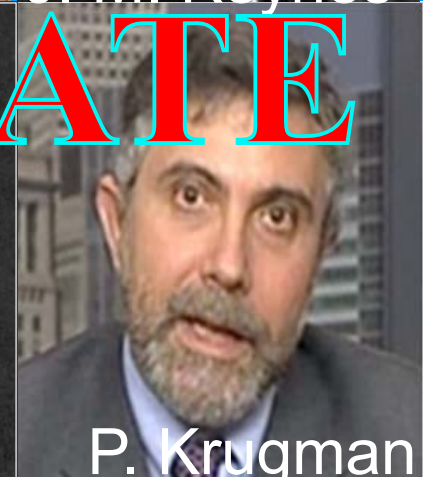
M. Friedman



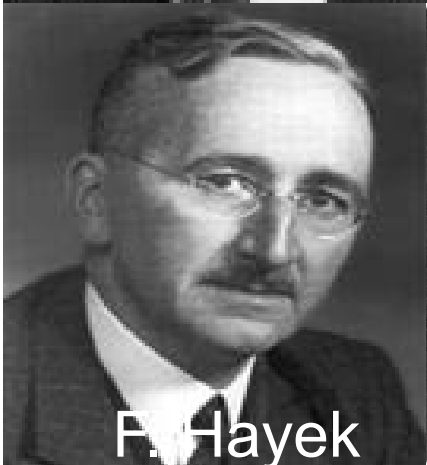
W. Rostow



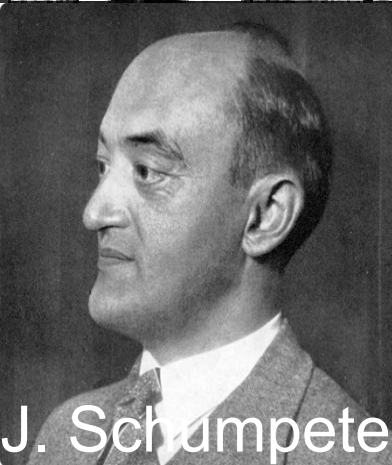
K. Polanyi



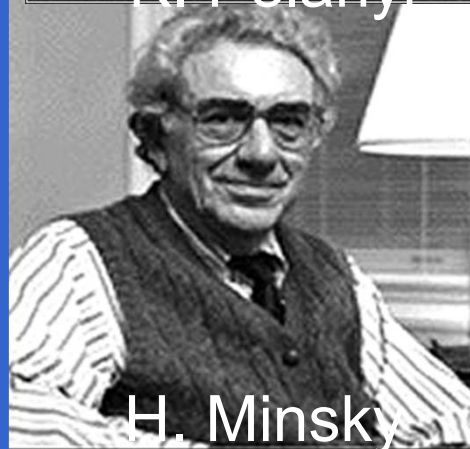
P. Krugman



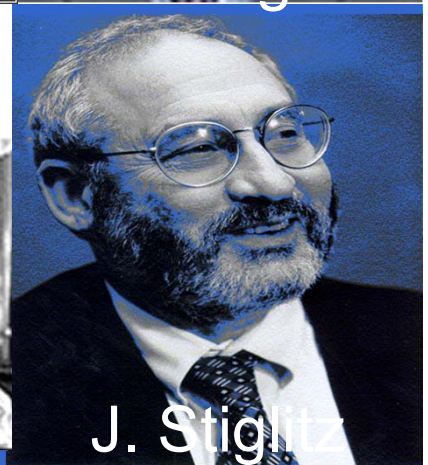
F. Hayek



J. Schumpeter



H. Minsky



J. Stiglitz



State versus market forces = at the heart of the socio-political debate



Globalization has subordinated politics to economics and economics to finance

Decoupling = Two-fold emancipation:

Phase I: 1970s-80s: Economic system from Political system (MNCs, trade openness, economic liberalization, privatization, deregulation, IFIs, rating agencies, Maastricht...)

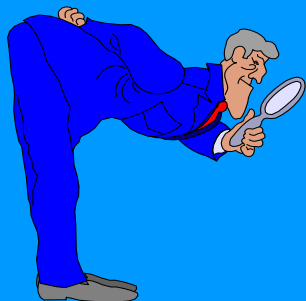
Phase II. 1990s: Financial system from Economic system (global investment funds, derivatives, offshore and shadow banking system...)



Phase I- Gradual emancipation of economics from politics

1. Flexible exchange rates 1970s
2. Economic and trade liberalization (IMF/GATT/WTO)
3. Privatization (1970-80s)
4. Economic automatic pilot (Maastricht: 12 EU-1992)
5. Washington consensus (late 80s)
6. Rating agencies





Governments are bypassed by market forces and under the scrutiny of IFIs and rating agencies

Rating Distribution of Sovereign Issuers on Selected Dates

Rating	1983	1990	1995	2000	2005	2010	2011	2012
Aaa	79%	33%	16%	12%	19%	15%	14%	13%
Aa	21%	28%	25%	15%	7%	15%	11%	12%
A	0%	17%	18%	10%	22%	13%	14%	8%
Baa	0%	8%	18%	21%	14%	18%	21%	26%
Ba	0%	8%	16%	19%	15%	16%	15%	16%
B	0%	6%	5%	18%	17%	23%	23%	22%
Caa-C	0%	0%	0%	5%	5%	1%	2%	3%
Investment-grade	100%	86%	78%	59%	63%	61%	59%	59%
Speculative-grade	0%	14%	22%	41%	37%	39%	41%	41%

Washington Consensus: One-size fits all!

“Ten rule” of sustainable market-economic policy

John Williamson (IIE 1990)

1. Fiscal discipline
2. Redirection of public expenditure priorities toward fields offering both high economic returns and the potential to improve income distribution (health care, primary education, infrastructure)
3. Tax reform (to lower marginal rates and broaden the tax base)
4. Interest rate liberalization
5. Competitive exchange rate
6. Trade liberalization
7. Liberalization of FDI inflows
8. Privatization
9. Deregulation
10. Secure property rights



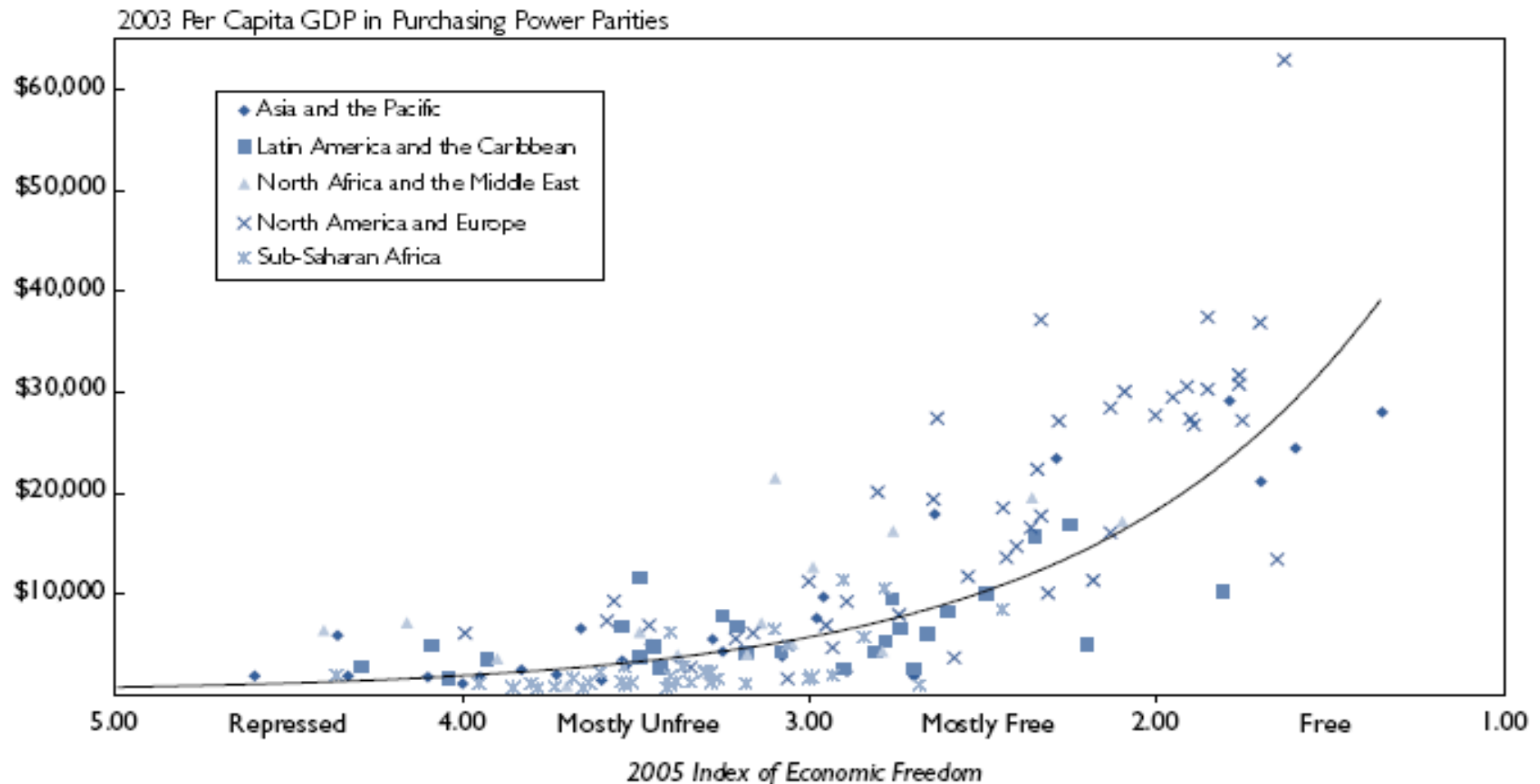
Globalization might stimulate (volatile) Economic Growth

➡ **Globalization + international openness**
= Efficiency + competitiveness =
= High-growth strategy

➡ High correlation between globalization,
competitiveness (economic performance, institutions quality,
business efficiency, infrastructure), and dynamic growth rates



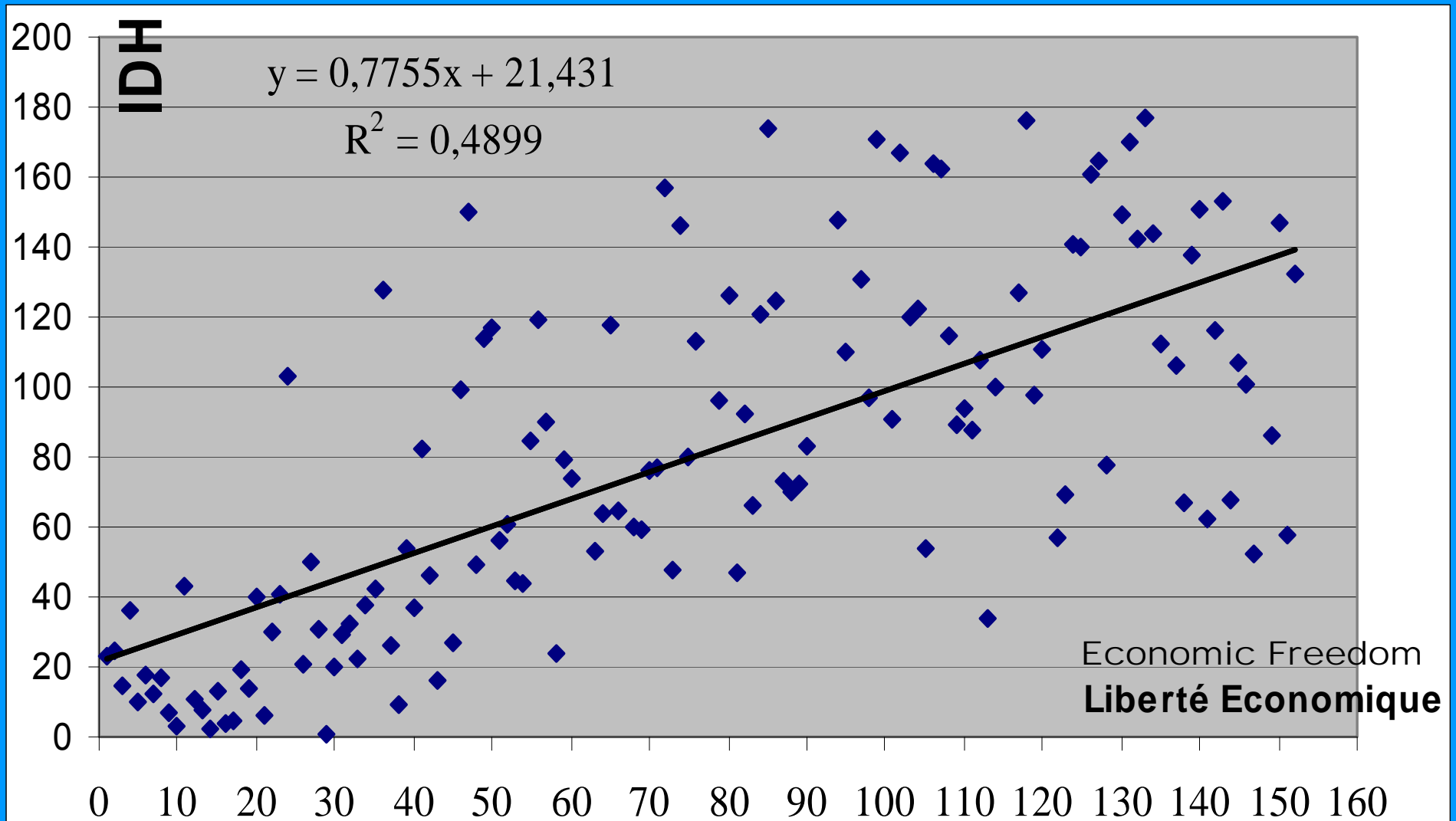
Correlation economic liberalization/GDP growth



Source: World Bank, *World Development Indicators Online*, available by subscription at www.worldbank.org/data; Central Intelligence Agency, *The World Factbook 2004*, available at <http://www.cia.gov/cia/publications/factbook/index.html>, for the following countries: Bahamas, Burma, Cuba, Cyprus, Equatorial Guinea, North Korea, Libya, Qatar, Suriname, Taiwan, Zimbabwe; Marc A. Miles, Edwin J. Feulner, and Mary Anastasia O'Grady, *2005 Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc., 2005), at www.heritage.org/index.

Correlation

Economic freedom – Human development



Phase II- 1980s-90s

The toothpaste got out of the tube



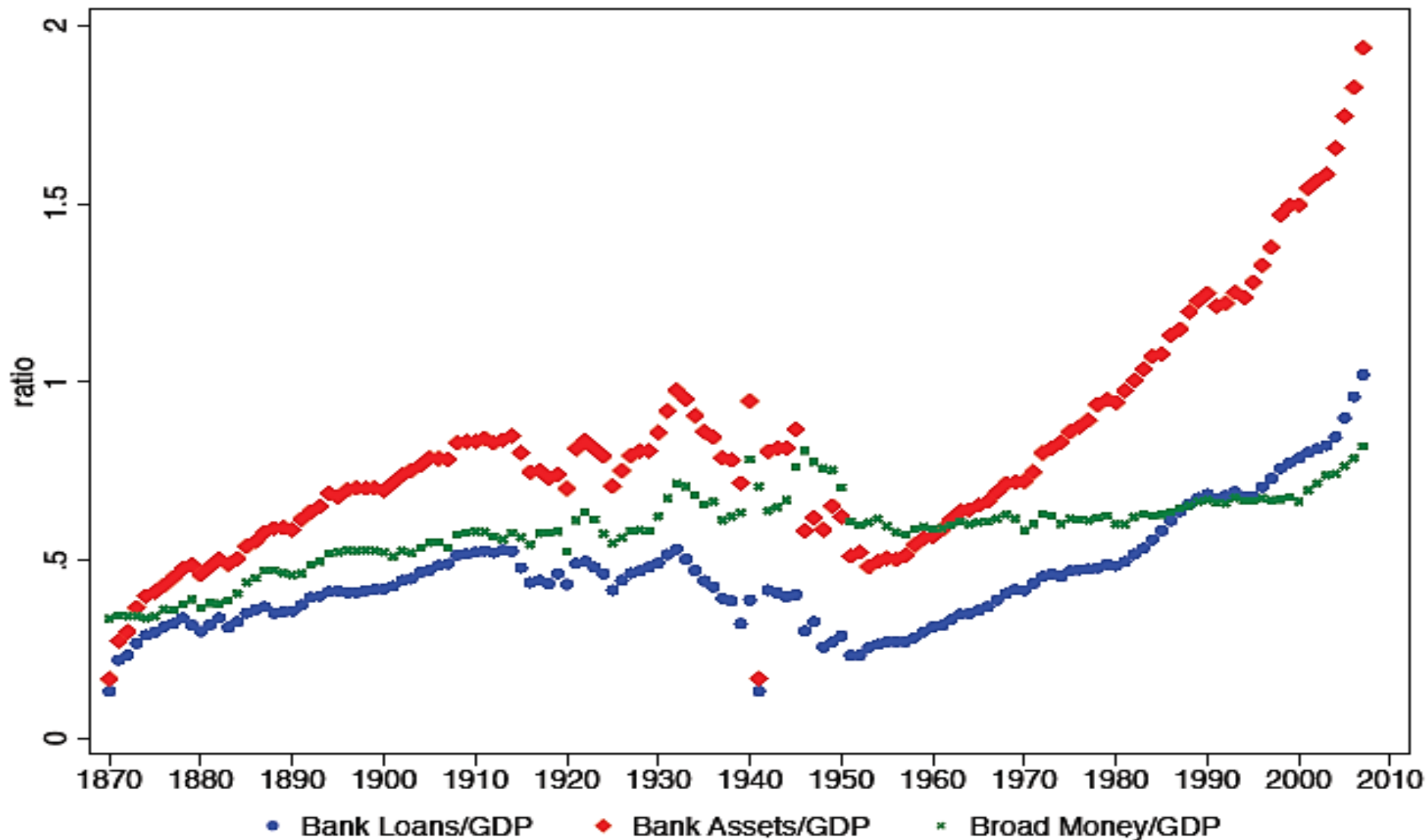
The emergence of Hyperfinance?

1. Financial Market Globalization (1980s)
2. Capital market deregulation (1990s)
3. Financial innovations and dematerialization
(securitization, options, derivatives...)
4. NTIC (Internet!)
5. TBTF global banks

Free-wheel global finance?



Swelling banking sector in post WWII era (ratio of loans + assets + M2/GDP in developed countries)

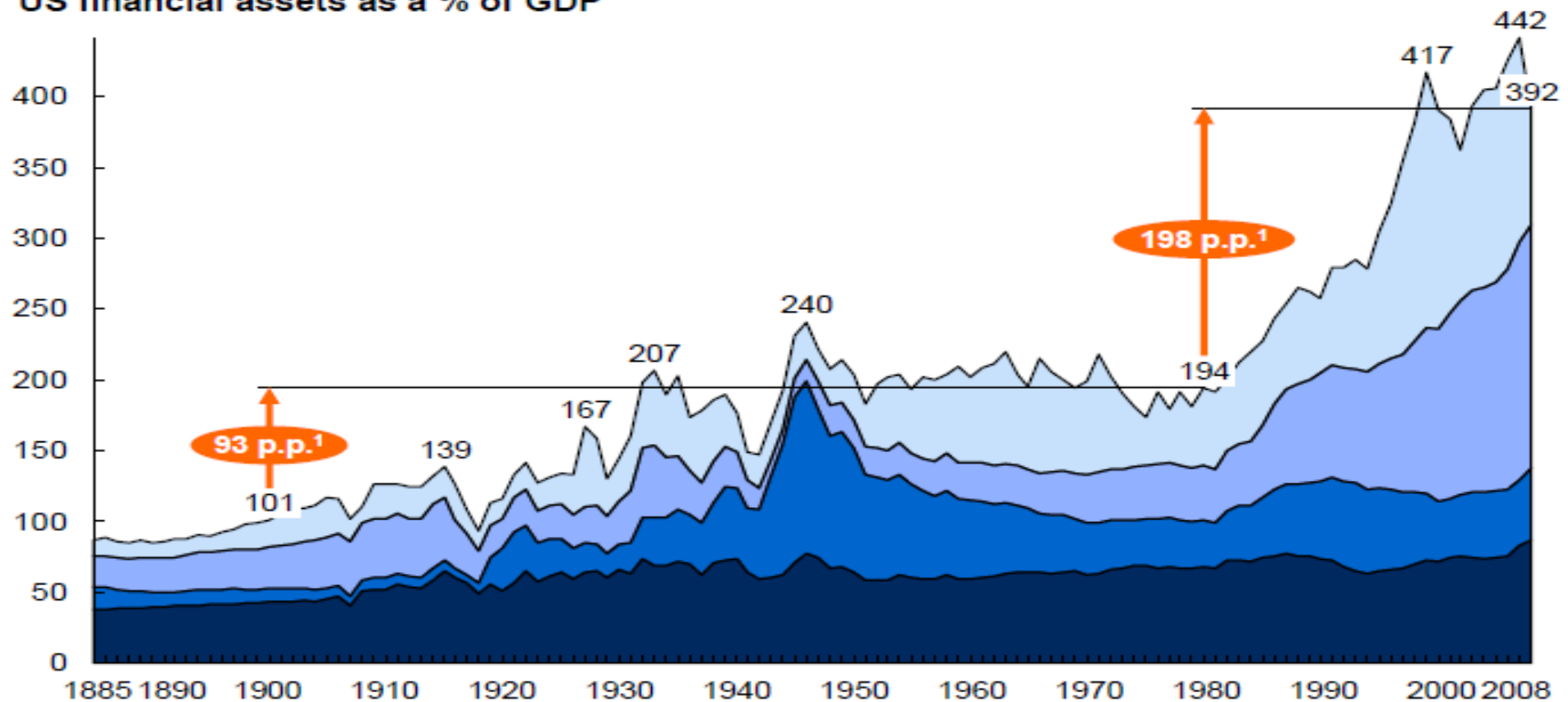


The rise in financial assets over GDP since the 1980s

After 1980, financial asset growth accelerated

- Equity
- Private debt securities
- Government debt securities
- Deposits

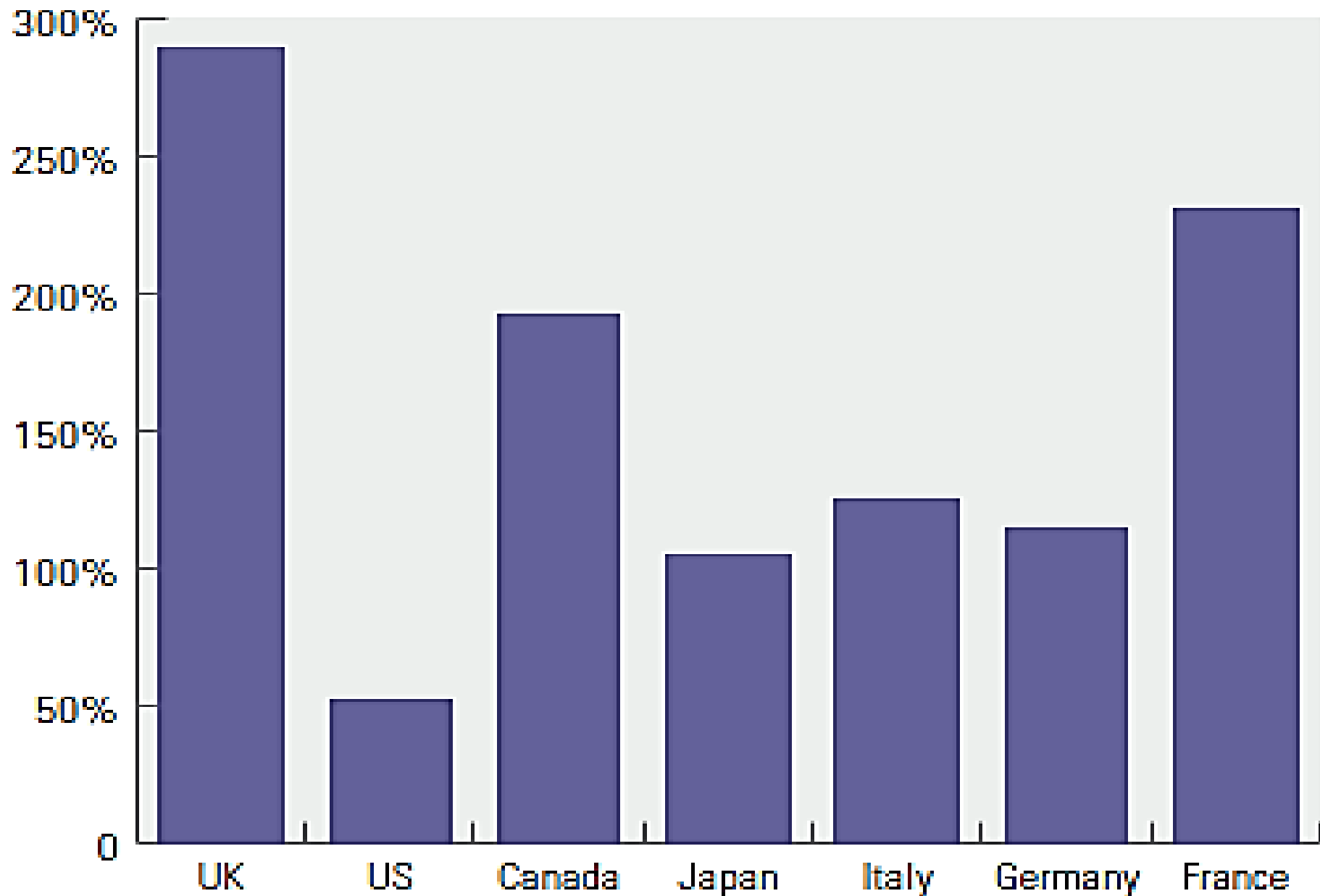
US financial assets as a % of GDP



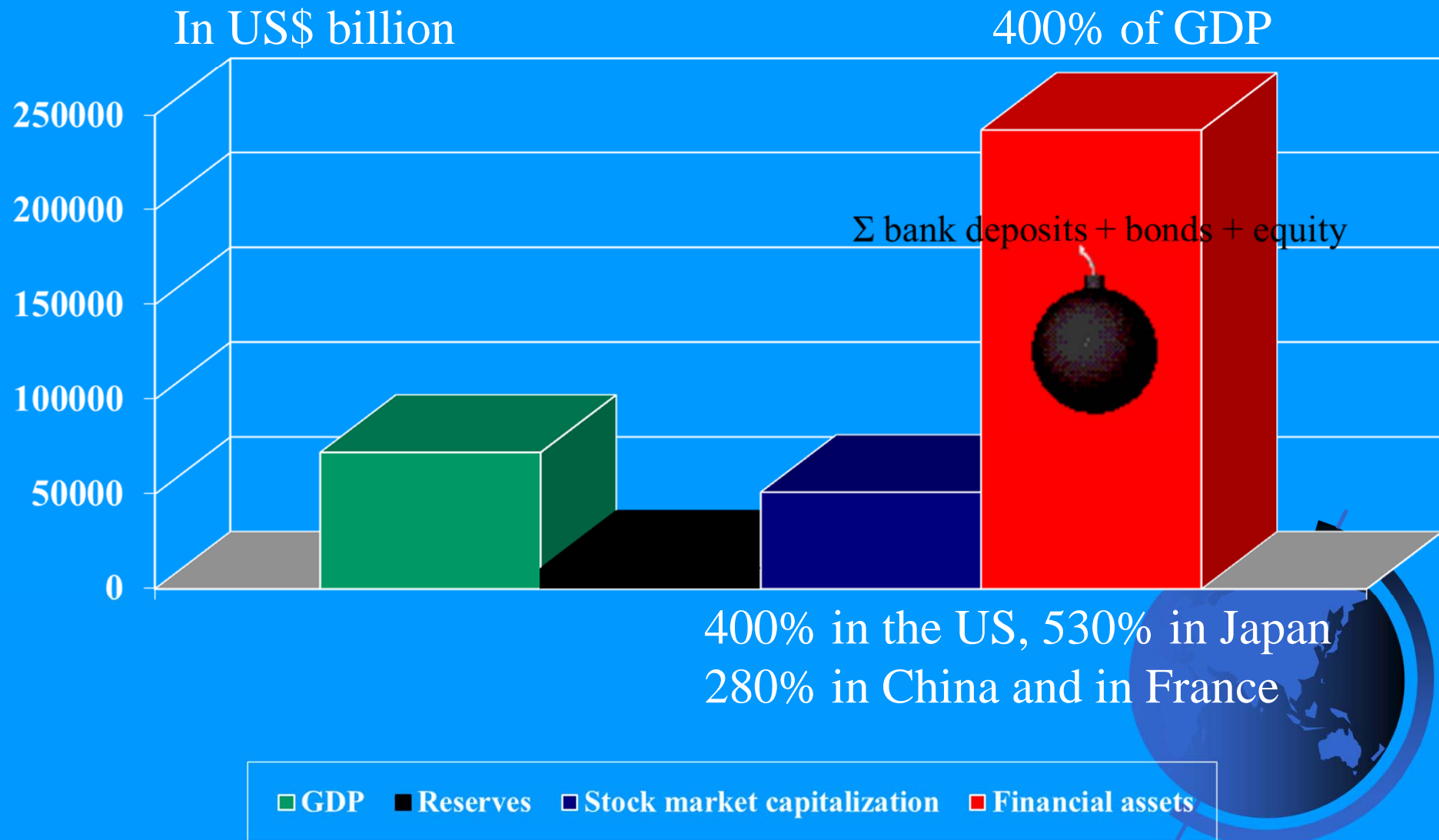
¹ Percentage points of GDP.

SOURCE: Federal Reserve; National Bureau of Economic Research; Robert Shiller; McKinsey Global Institute analysis

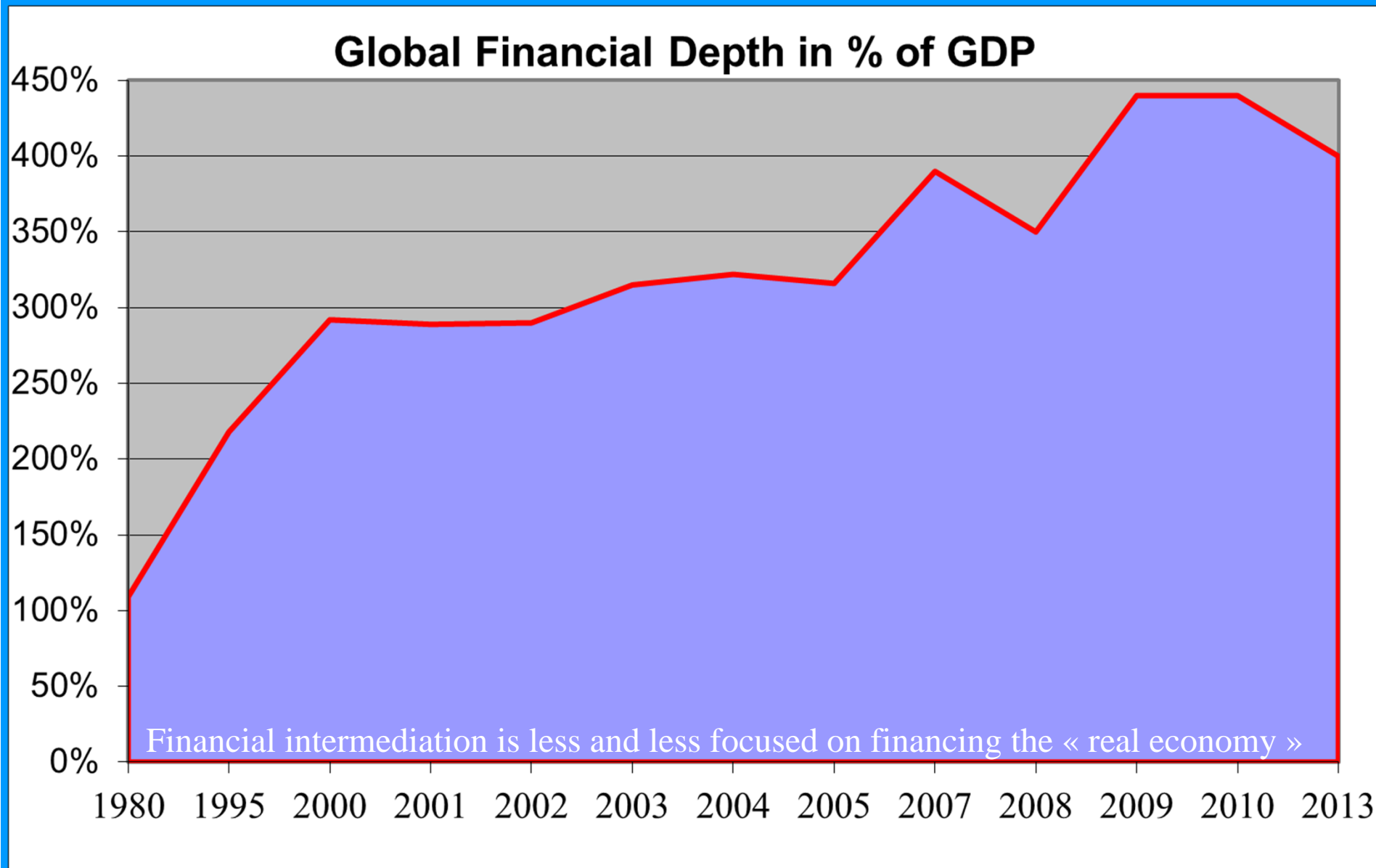
International Banks Assets/Country GDP



Financial depth: Overwhelming supremacy of Finance (of 'virtual' over 'real')

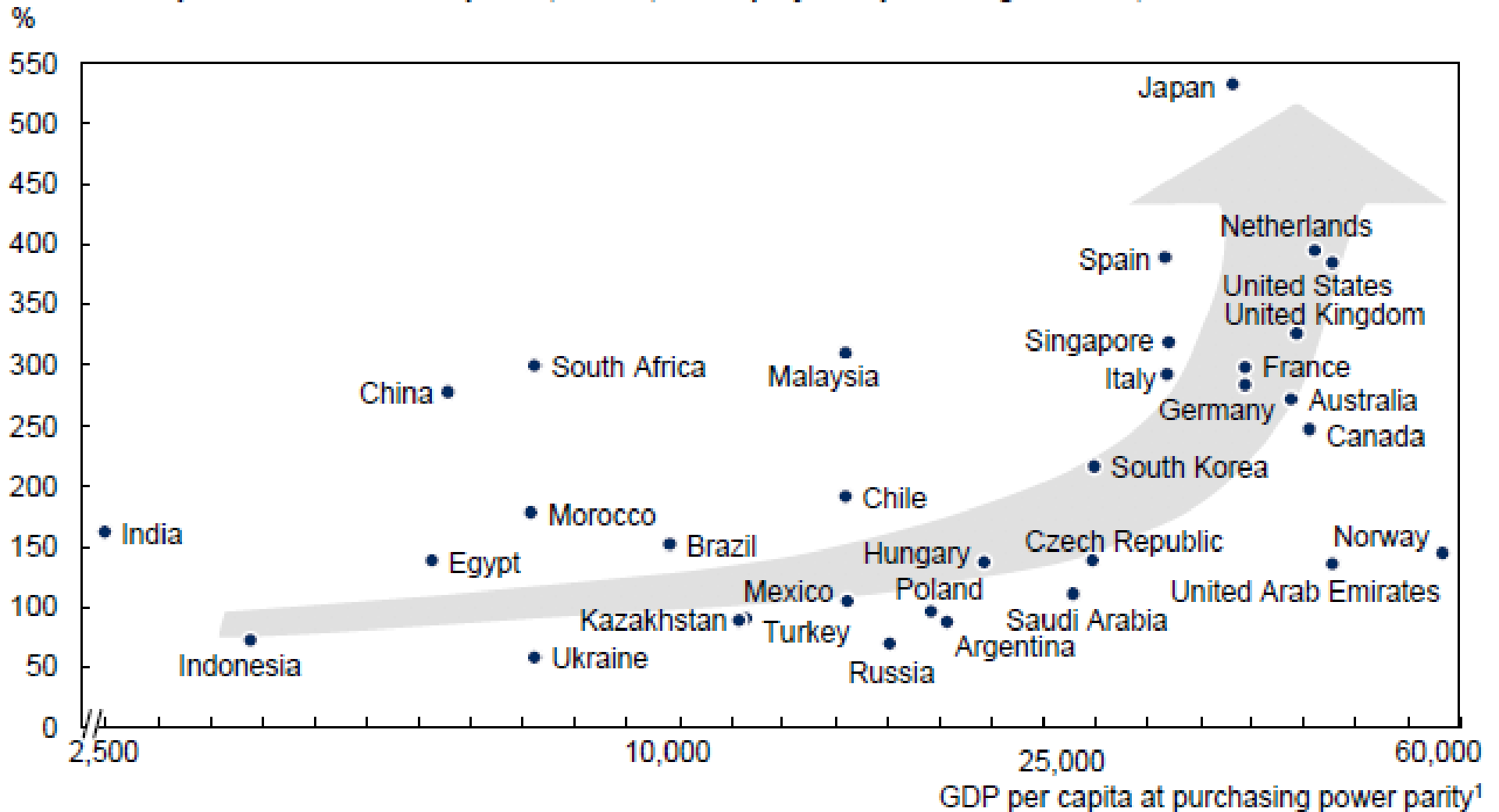


1990s: The financial genie has escaped from the bottle!



Financial globalization

Financial depth: Value of bank deposits, bonds, and equity as a percentage of GDP, 2008



Emerging markets

Mature markets

Is globalization bad?

Four myths and misconceptions regarding
the **pitfalls** of Globalization



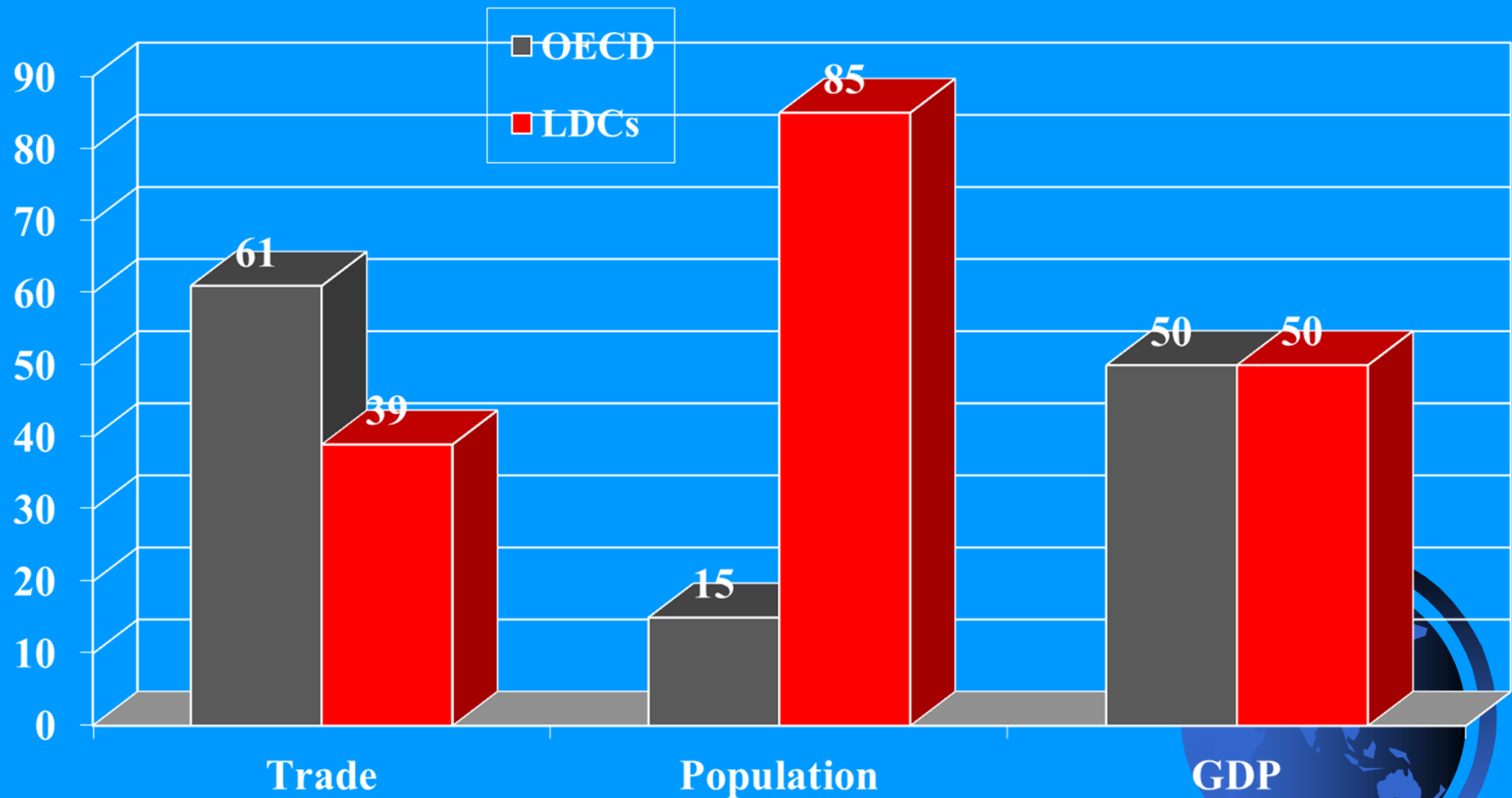
Myth 1.

Globalization generates growing wealth and well-being for all...

- Economic growth boils down to rising GDP
- GDP says nothing regarding **wealth distribution** nor regarding inclusiveness and sustainability
- Development = growth coupled with those conditions that make it ... **sustainable!**



Share in GDP, trade and population %



Challenge of Globalization?

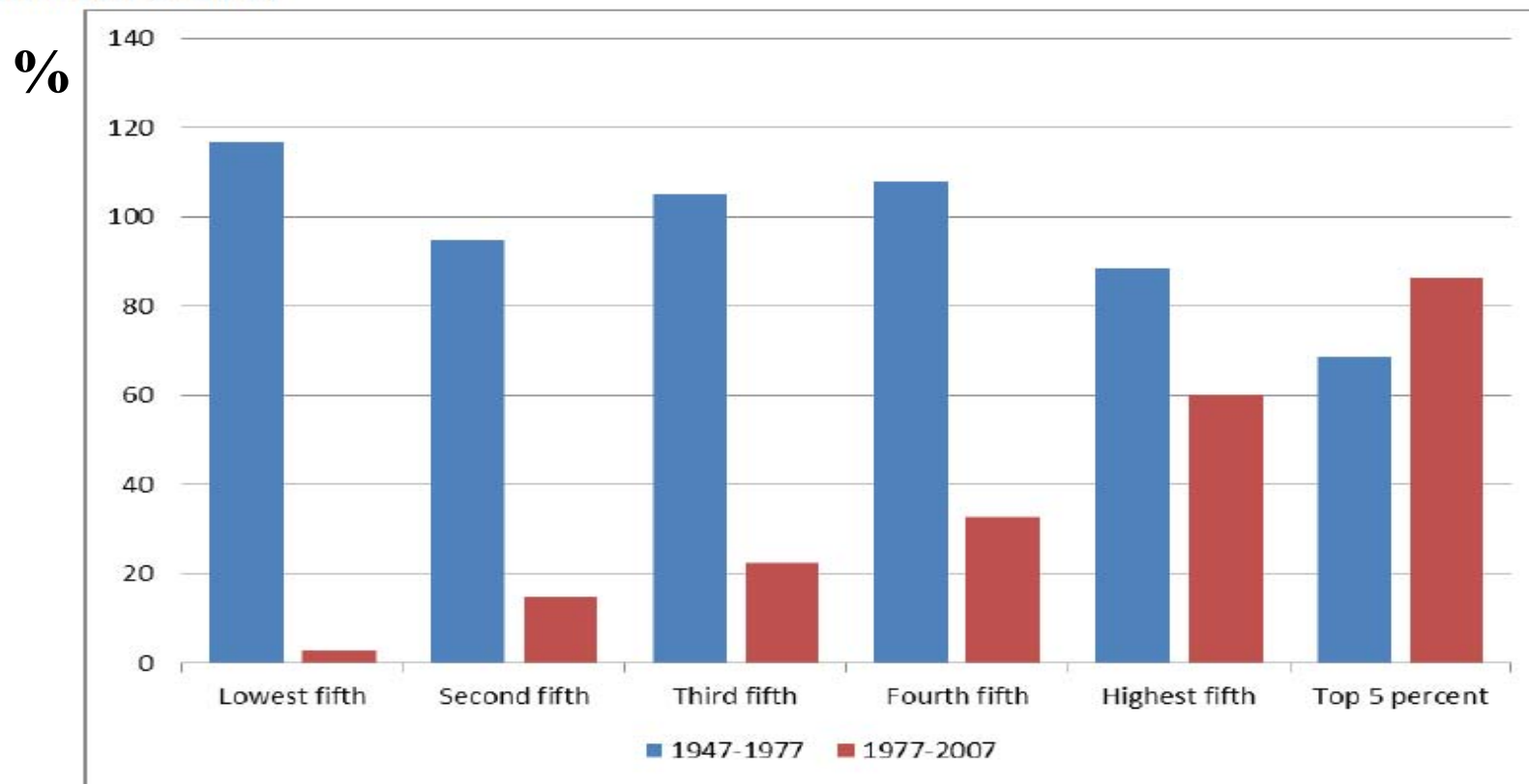
☞ « Globalization reveals the *liberating potential* of the market for generating unlimited wealth, and its *blindness* as a mechanism for distributing the wealth benefits »



Ashraf Ghani, Washington Quarterly, Autumn 2006

Rising growth + rising income inequality?

Figure 5: Growth of real pre-tax family income, excluding capital gains, United States, 1947-1977 and 1977-2007



Source: http://www.stateofworkingamerica.org/files//family_income_growth.xlsx based on U.S. Census Bureau, Historical Income Tables, tables F.2, F.3, F.5 (CPS)

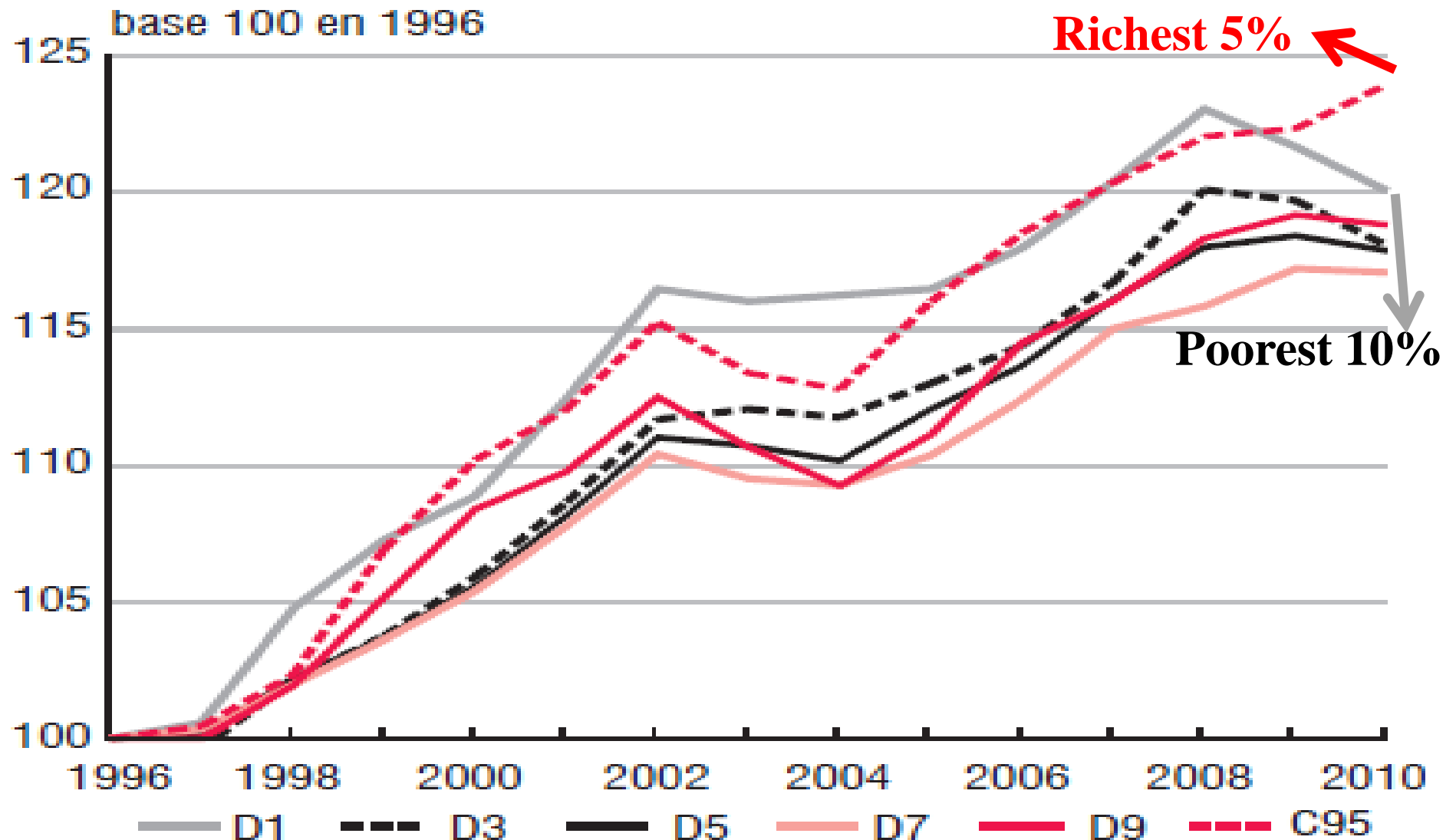
The winner takes all: Share of the richest 10% Americans in total national income 1917-2010



Emmanuel Saez, <http://elsa.berkeley.edu/~saez/saez-UStopincomes-2006prel.pdf>

MH Bouchet/SKEMA (c) 2013

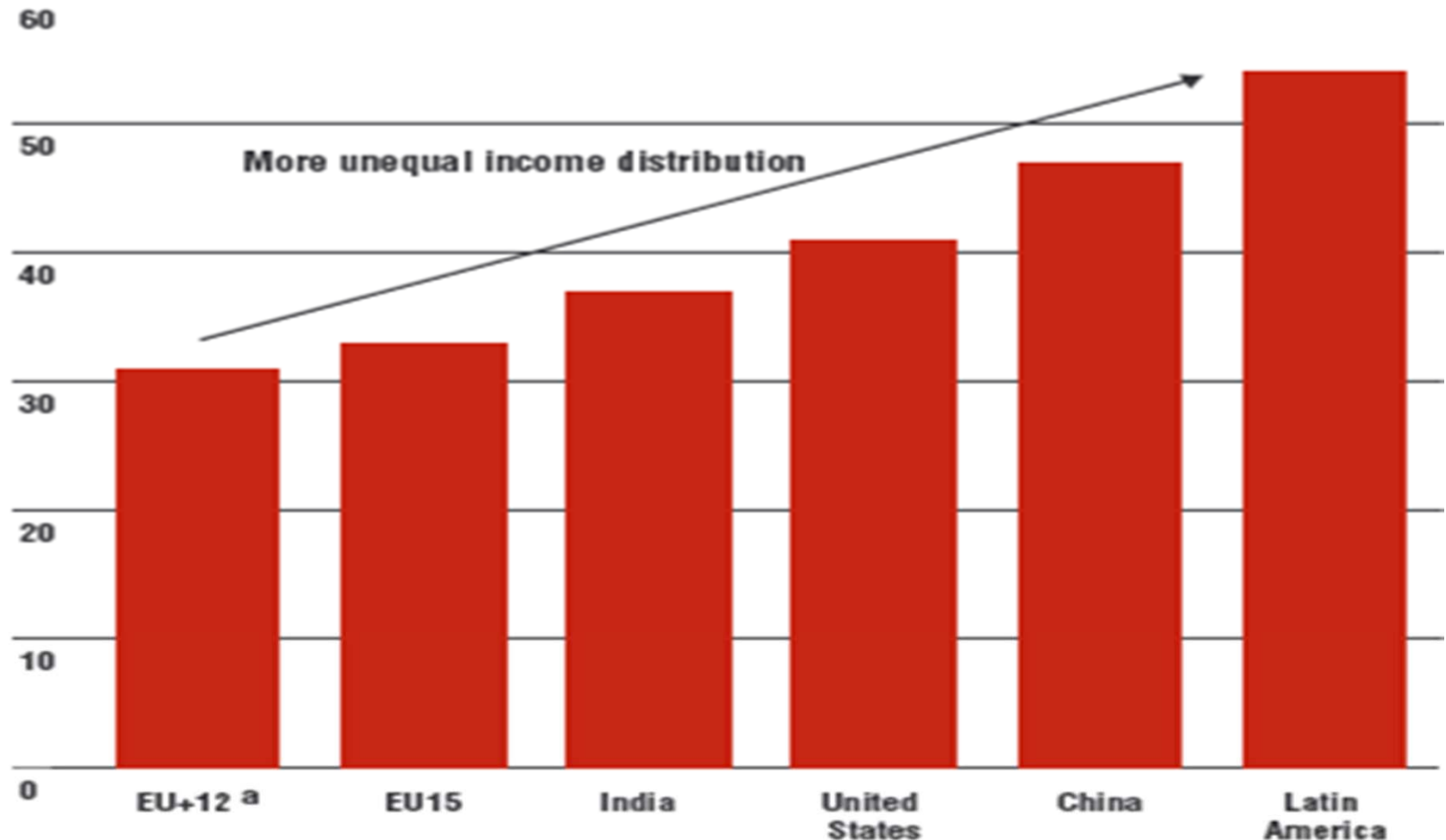
France: Evolution in per capita income between 10% poorest and 5% richest 1996-2010



Growing, but more unequal!

Index of regional income inequality

Gini Index, most recent survey (0-100)



^aEuropean Union Nations that acceded in 2004 or later.

Source: UNDP, Human Development Report 2007/2008; World Bank.

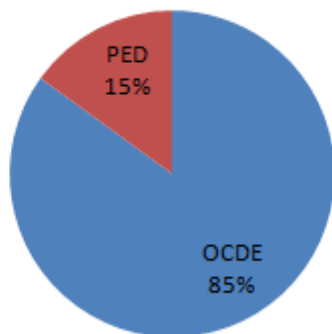
Myth 2. Globalization leads to catching up between nations?

- **1820-1960: The Colonial era: diverging North & South**
- **1960-1990: the Development Aid decades**
- **1990-2013: the « catching up » myth: rising income gaps within and between nations**

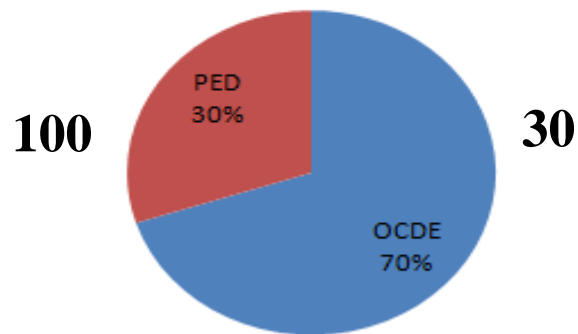


The Global Economy: Yesterday, Today and Tomorrow

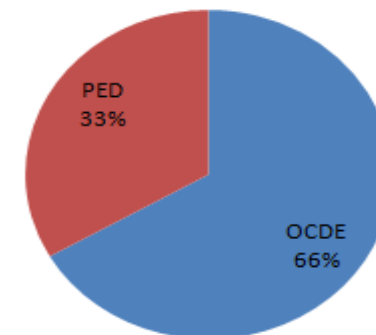
1945



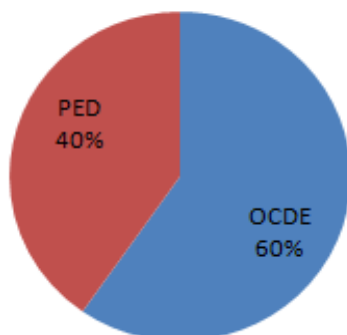
1960



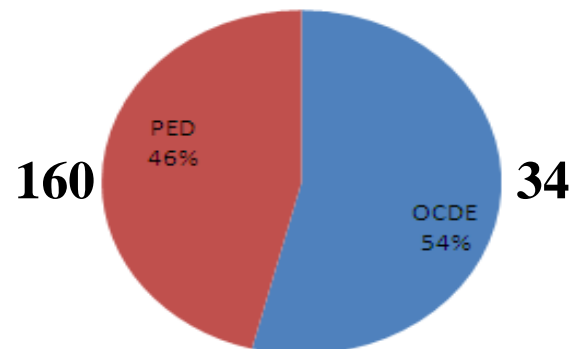
1980



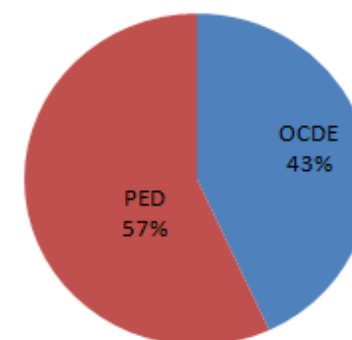
2000



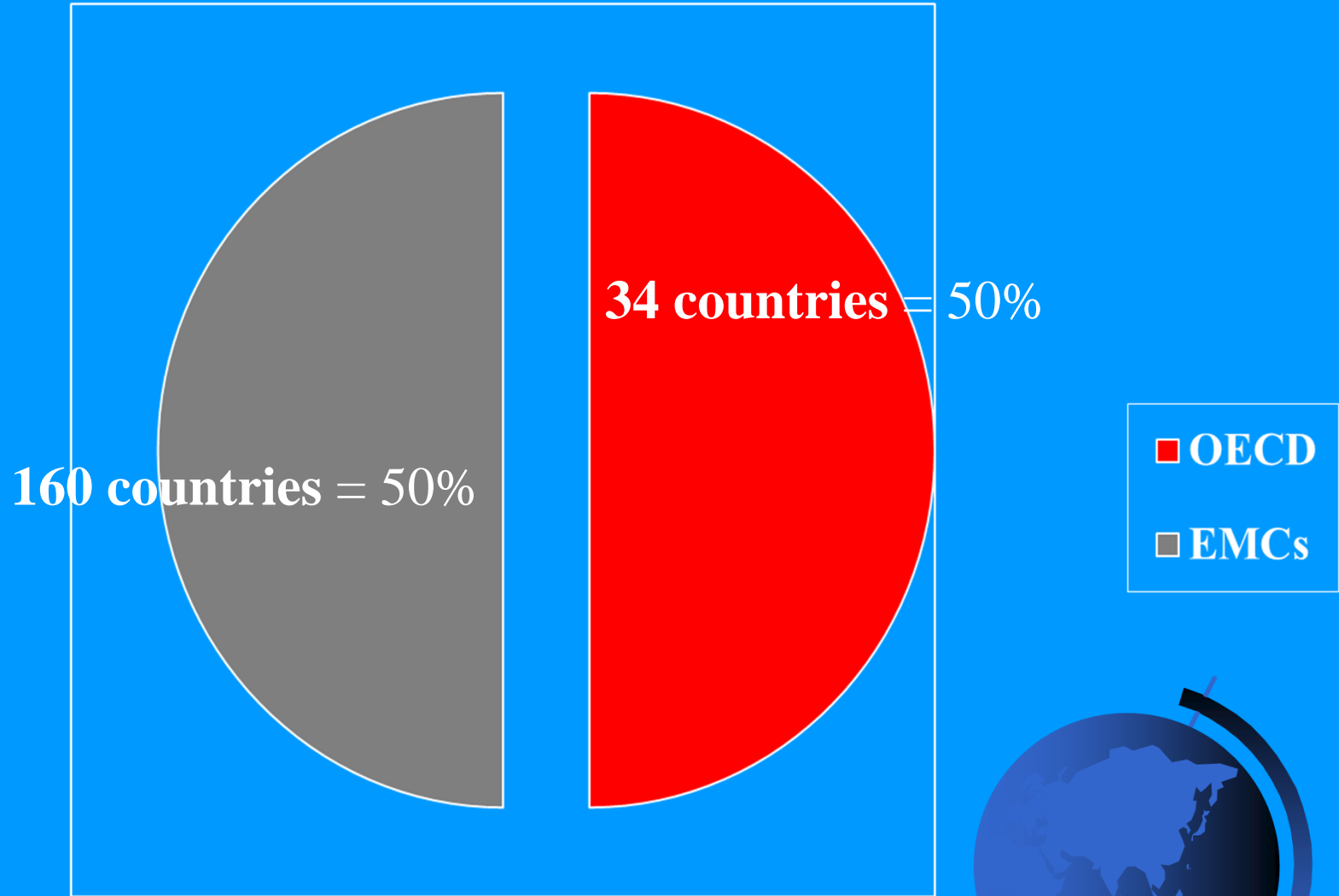
2010



2030



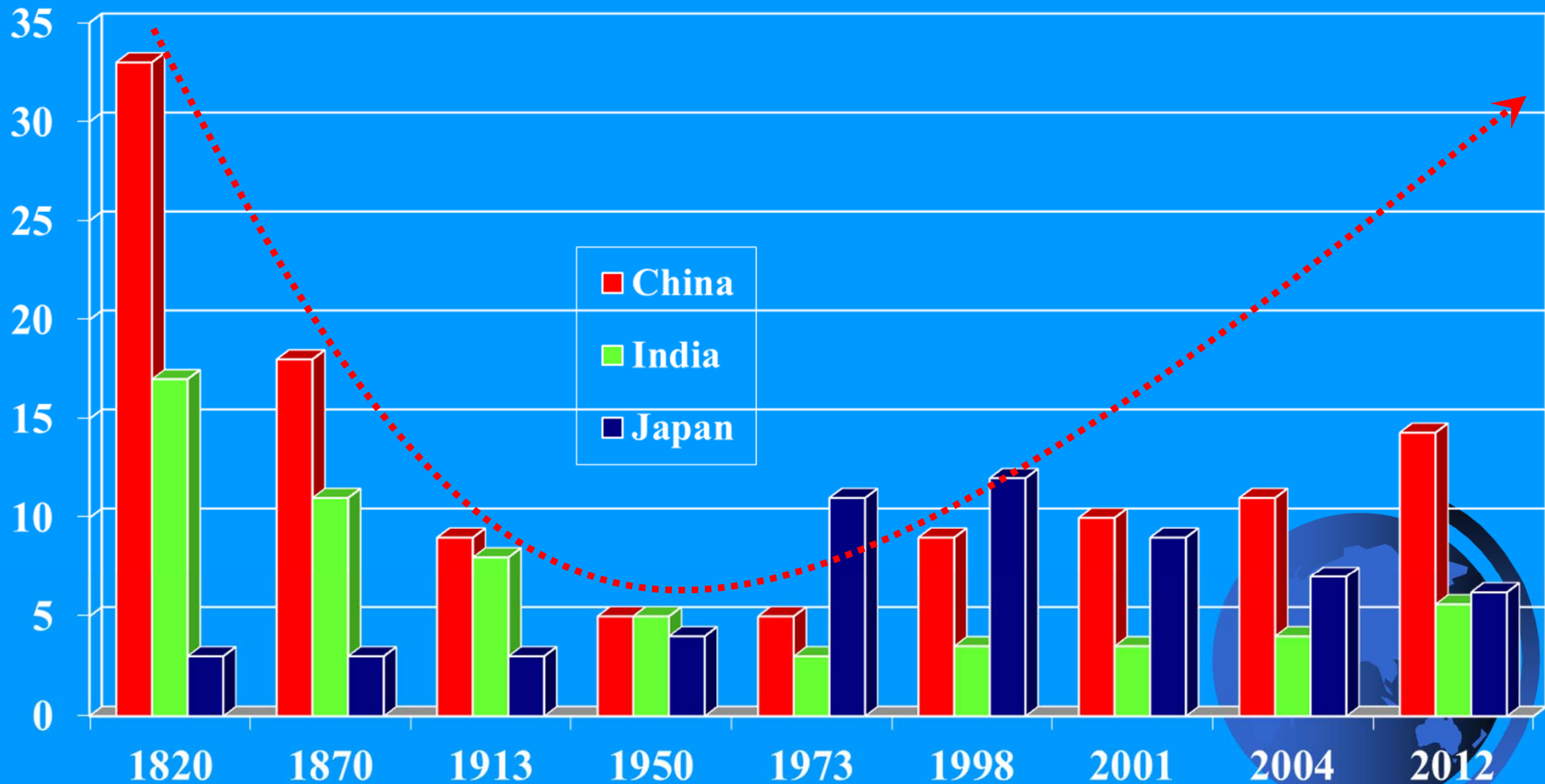
2013 Global economic divide : GDP %



China is back!

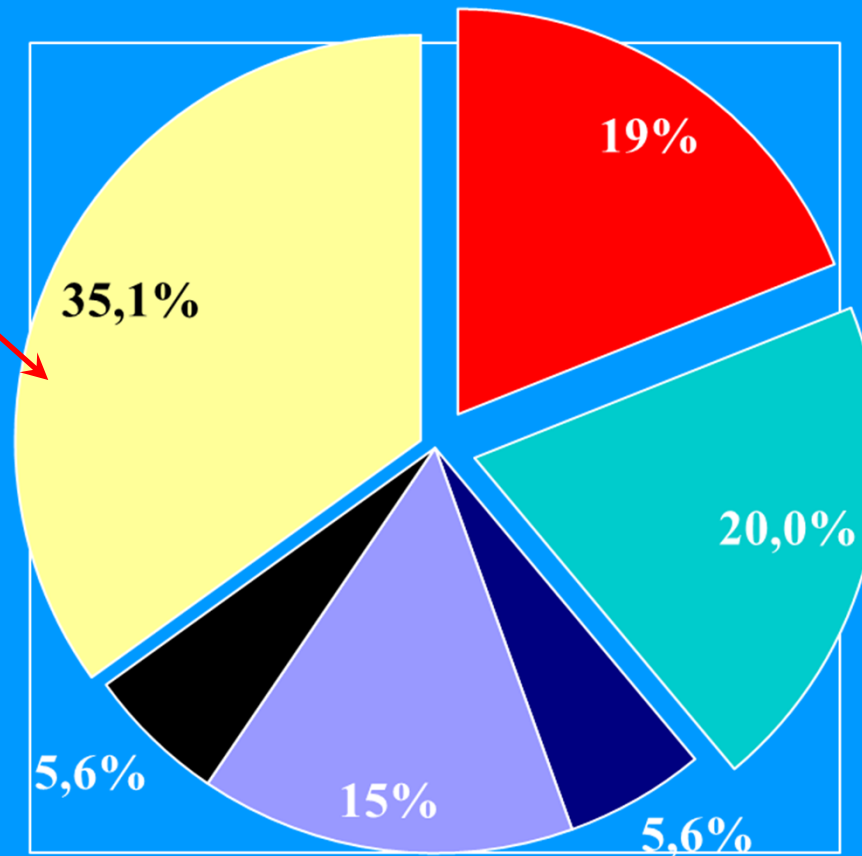
Share of Global GDP % : 1820-2012

China= 15%
Japan= 5,6%
India= 5,6%



Regional shares of global GDP in ppp

160 countries



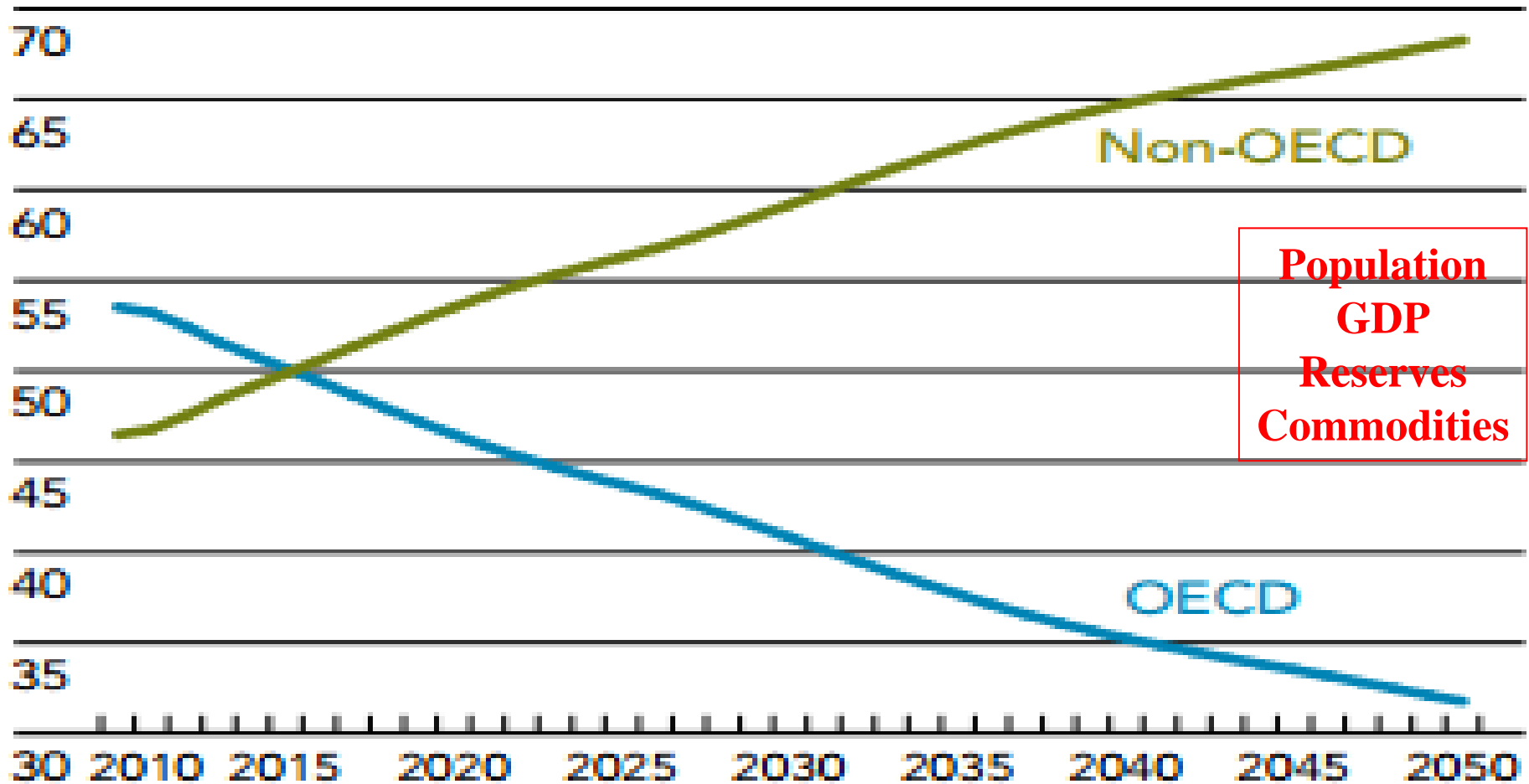
■ USA ■ EU ■ Japan ■ China ■ India ■ Others



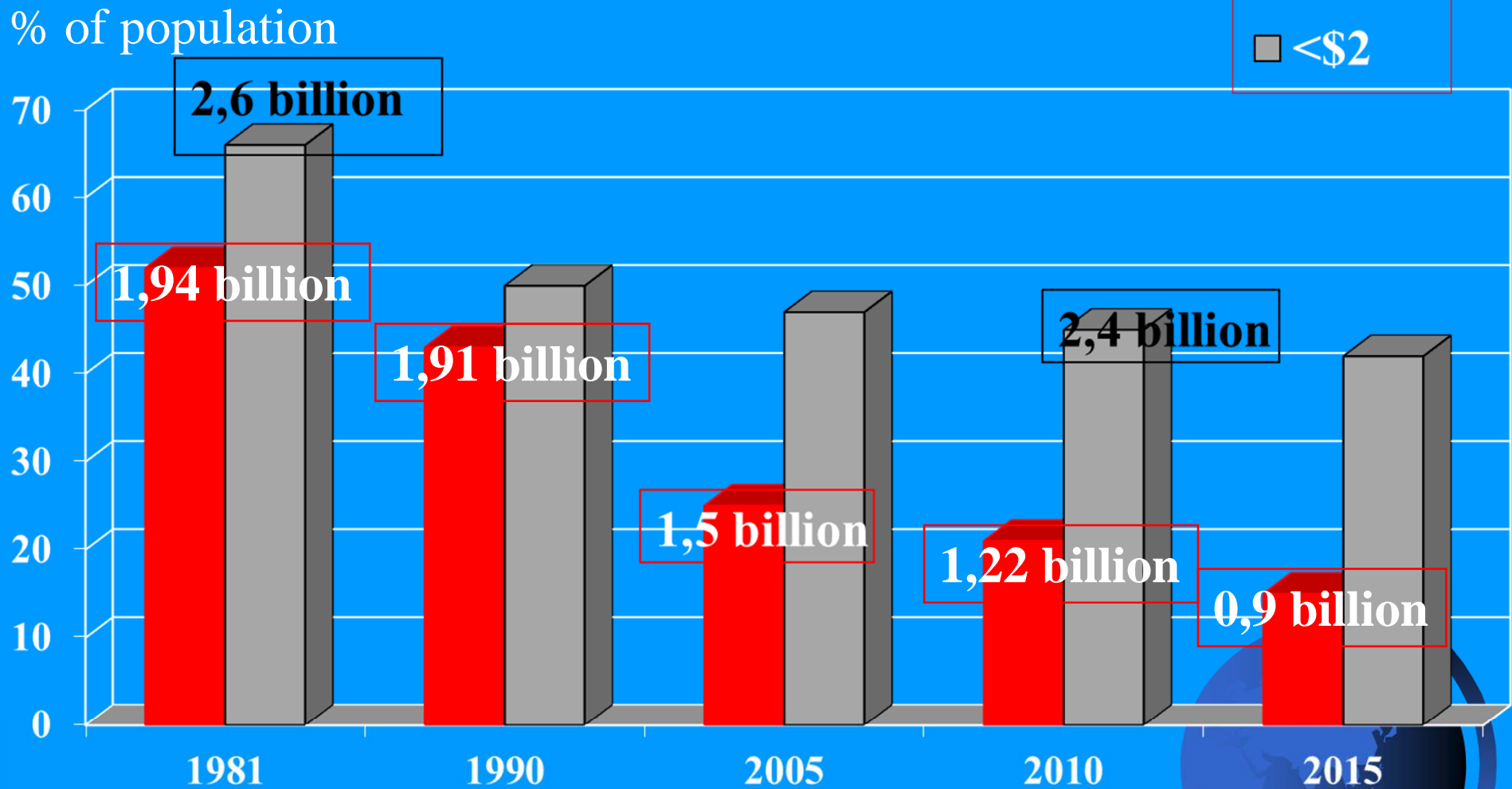
Though 2015 might see a global economic power shift, the non-OECD include **160 countries**, including many stubbornly poor!

Traditional, Four-Component Power Forecast

Index



Stubborn world poverty



Myth 3

☞ Globalization = End of cyclical boom and bust

Facts:

- Sustained, meteoric growth in emerging economies may no longer be possible (growth slowdown in Brics + social unrest)
- The great “**age of industrialization**” may be behind us
- Something special about the 20th-century? mix of widespread, well-paying manufacturing jobs, higher education, rise of a middle class that acts as voters and taxpayers
- End of high growth success stories?
- Global crisis = spill-over effect
- In search of new growth engines?



Long-term decline in economic growth?

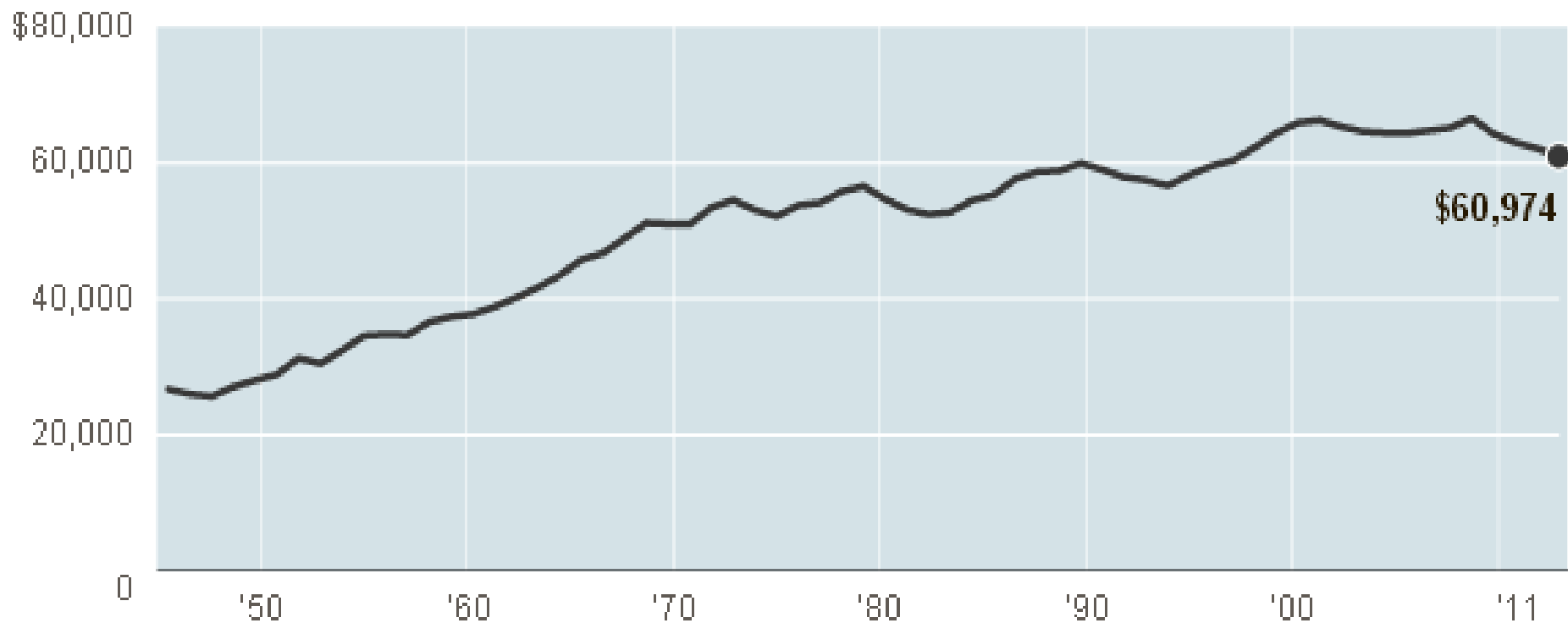


1. **RISE OF AUTOMATION** in manufacturing and sometimes even in services (harder for EMCs to compete with low wages): bad news for China?
2. **GLOBAL SUPPLY SOURCES** scattered across many countries : bad news for South Korea, that built a nearly complete domestic industrial supply chain?
3. **WIDER ECONOMIC GAPS** within and between nations
4. **AGING POPULATIONS and falling fertility rates:** many lower-income countries will be old before they are rich
Emergence of **DEVELOPMENT ENCLAVES** : parts of countries will stand out as advanced or wealthy (Richard Baldwin)

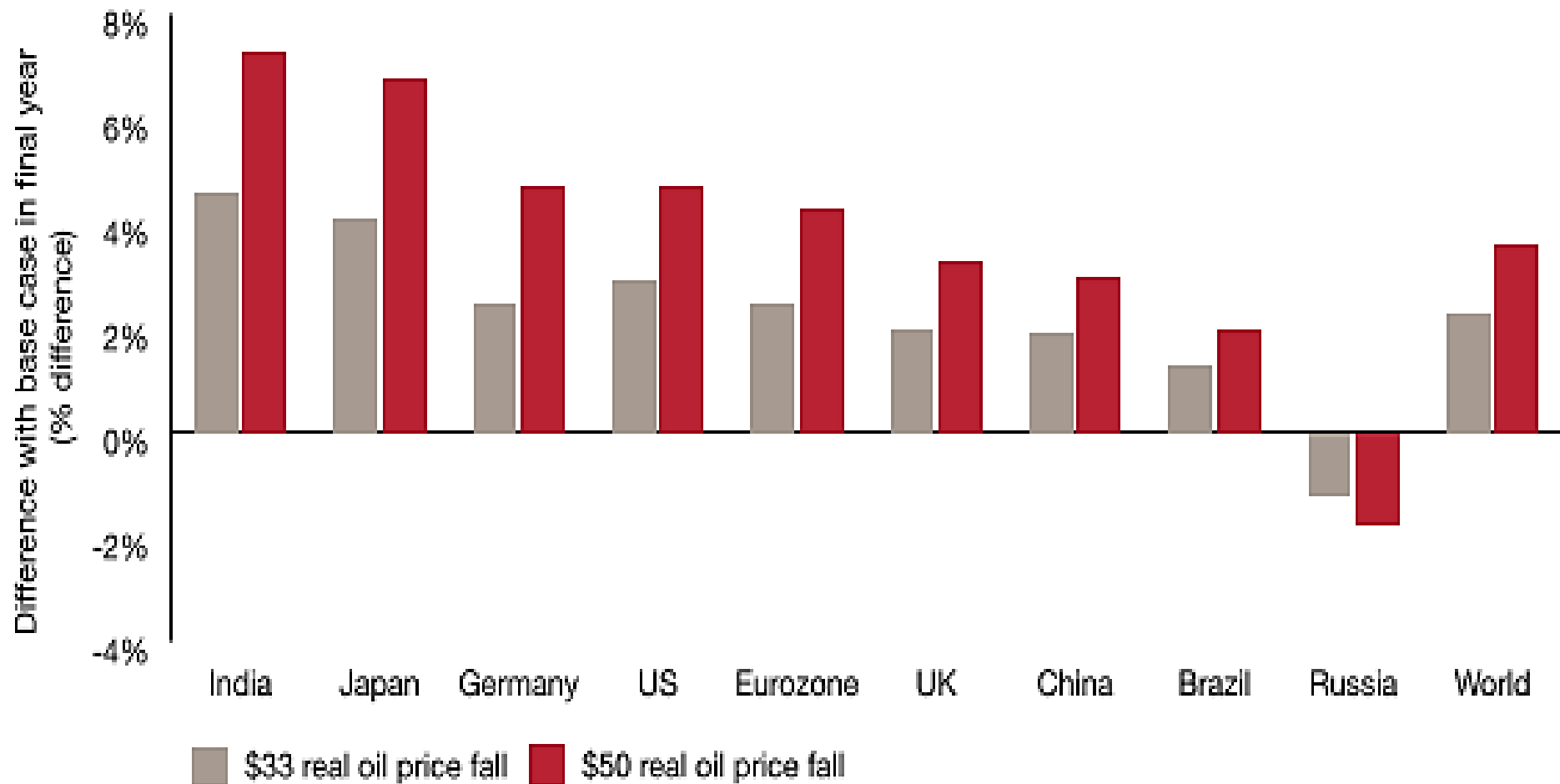
For the first time since the Great Depression, US median family income has fallen: the notion of « American dream », mass upward mobility, is eroding. Economic stagnation brings pessimism, political turmoil and a lack of social progress.

Median Family Income

Adjusted for inflation in 2011 dollars



Shale gas revolution: Global winners and losers of lower global oil prices (% change in GDP)

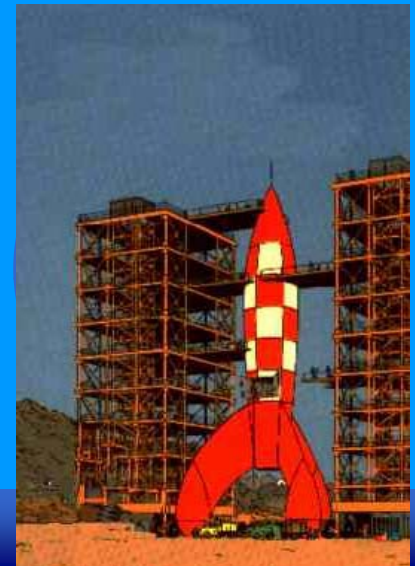


Source: PwC analysis using NIGEM

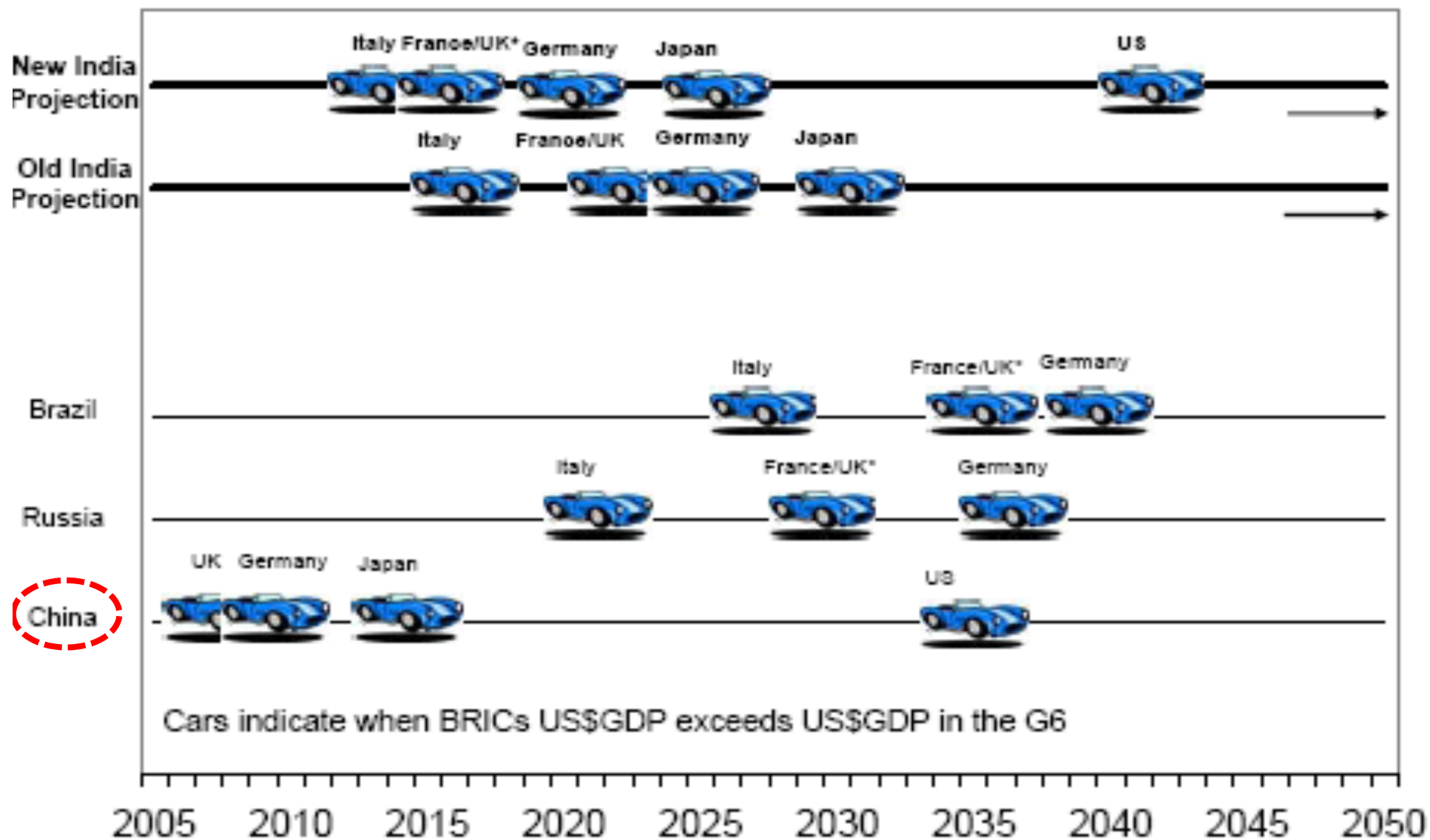
Myth 4

Globalization = Growth take-off for all

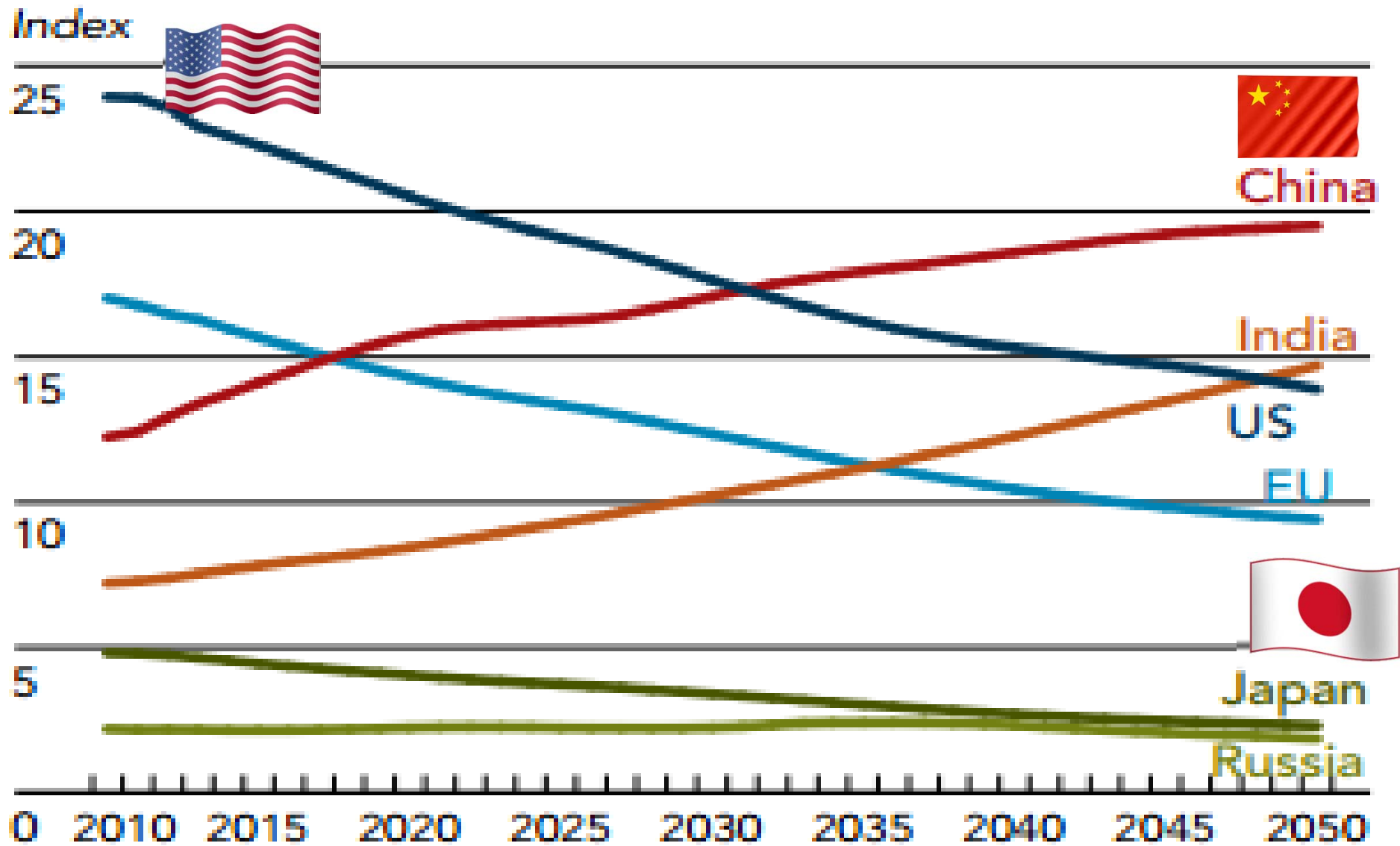
- Globalization is a dynamic growth engine whose momentum helps countries take off ?
- Facts: Taking off is still a remote dream for many developing countries even though GDP per capita rises



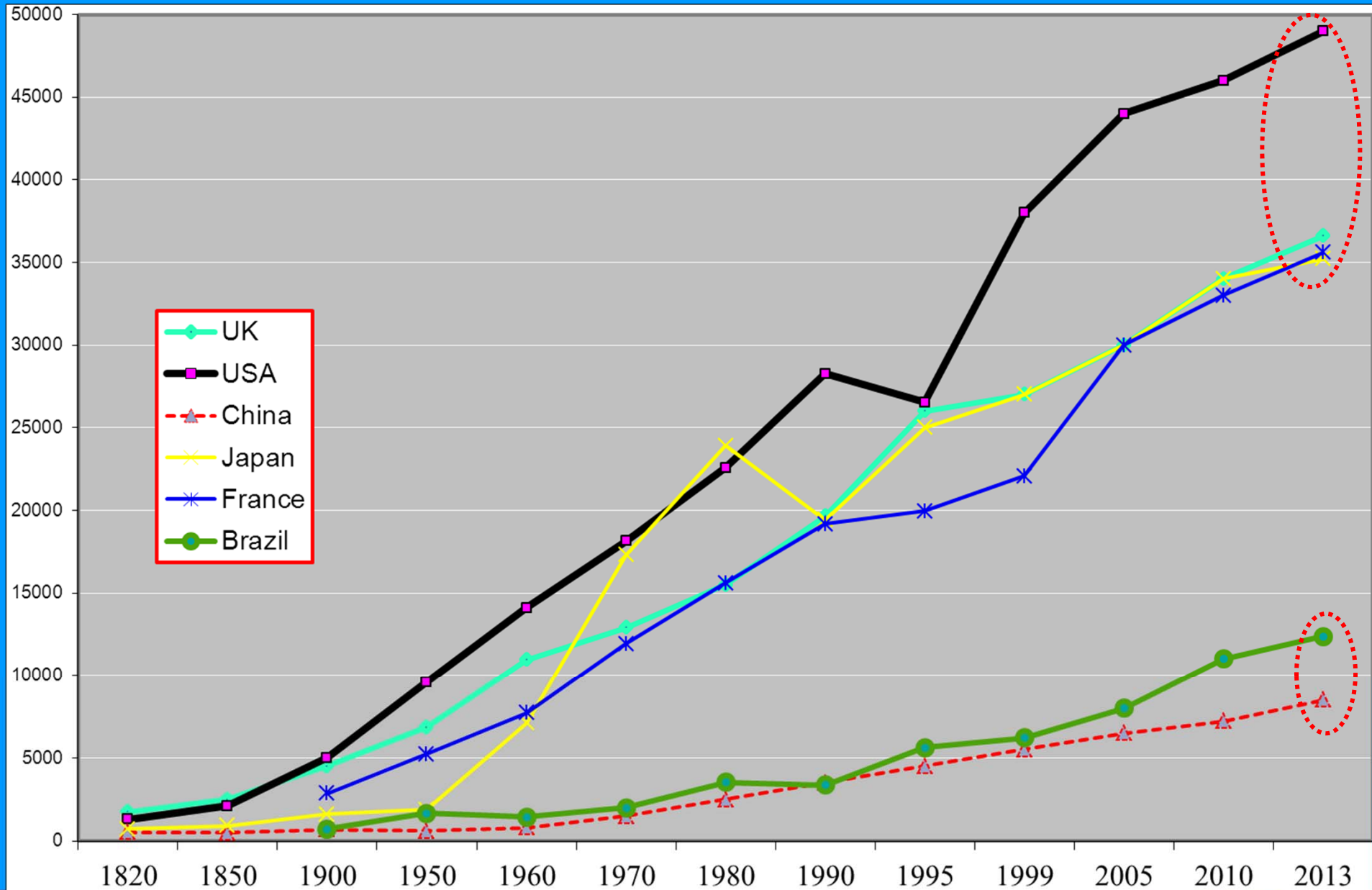
The BRIC's catch up process



When do the curves cross?



Taking off? US\$-GDP per capita (on ppp basis)



Myth 5 - Financial Globalization stimulates Economic Growth:
it would equalize marginal returns to capital around the world, transfer savings from rich to poor, and enhance risk sharing, growth and convergence.

1- Fischer, Summers, Kose...

☞ Openness to global capital flows = higher capital efficiency North-South + technology spillover + FDI
➡ Δ GDP

2 - Stiglitz, Krugman, Rodrik, Lane...

☞ Financial and capital account liberalization = capital flow volatility + financial crises
capital controls + Tobin tax ➡



See: Prasad-Rogoff IMF-Harvard 2006 and P. Lane, BIS Dec. 2012

Empirical evidence?

1. No clear evidence that financial globalization improves institutional quality and macroeconomic discipline
2. Strong evidence that financial integration promotes overall financial sector development and corporate governance
3. Strong evidence that financial sector development increases FDI and portfolio equity flows, domestic investment and growth
4. **Premature financial liberalization leads to capital flow volatility and financial crisis**



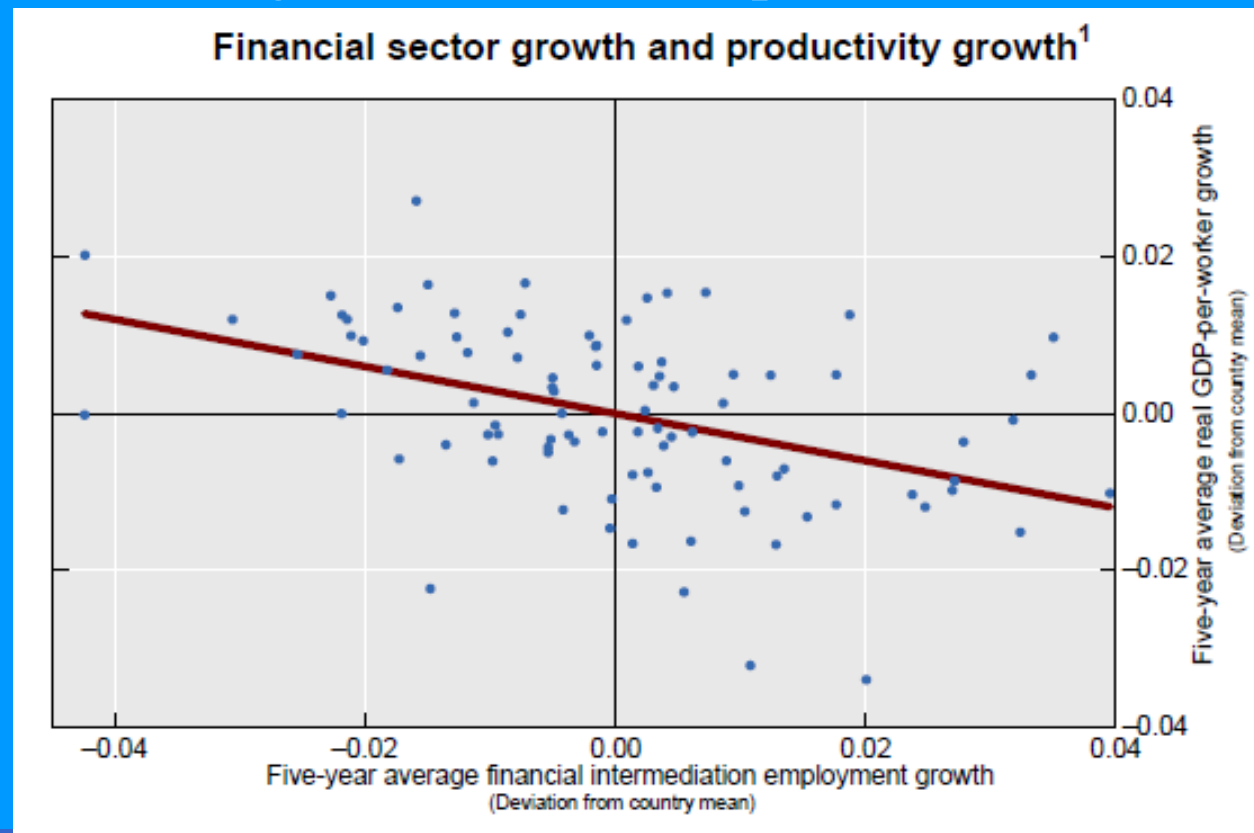
Financial development can become a drag on productivity and real economic growth

The **inverted U-shaped** effect of financial development:

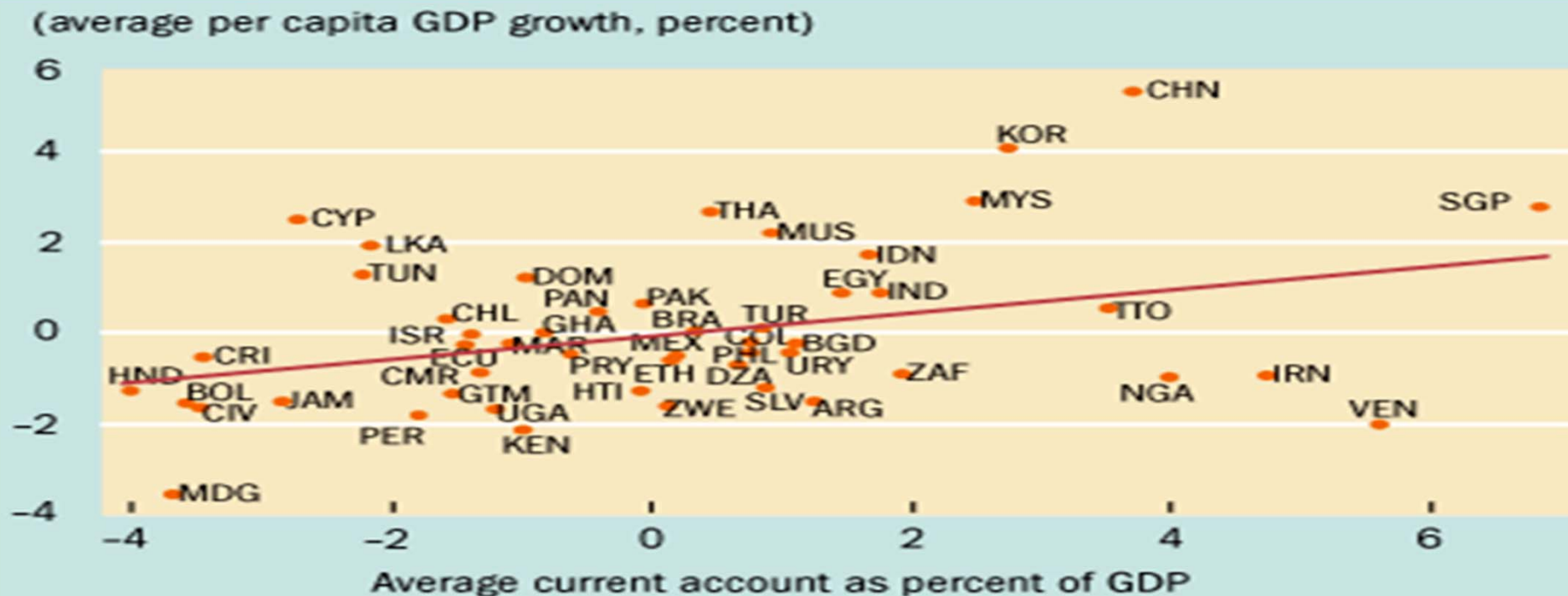
A fast growing financial sector is detrimental to productivity growth

Too high a ratio of private credit/GDP and fast growing financial sector mean that essential resources will get drawn at the expense of the real economy:

**More finance
is not better**



Developing countries that have relied less on foreign capital have grown faster! (IMF/03-2007)



Source: Authors' calculations.

Note: Sample excludes Nicaragua.

ARG=Argentina, BGD=Bangladesh, BOL=Bolivia, BRA=Brazil, CHL=Chile, CHN=China, CIV=Côte d'Ivoire, CMR=Cameroon, COL=Colombia, CRI=Costa Rica, CYP=Cyprus, DOM=Dominican Republic, DZA=Algeria, ECU=Ecuador, EGY=Egypt, ETH=Ethiopia, GHA=Ghana, GTM=Guatemala, HND=Honduras, HTI=Haiti, IDN=Indonesia, IND=India, IRN=Iran, Islamic Republic of, ISR=Israel, JAM=Jamaica, KEN=Kenya, KOR=Korea, Republic of, LKA=Sri Lanka, MAR=Morocco, MDG=Madagascar, MEX=Mexico, MUS=Mauritius, MYS=Malaysia, NGA=Nigeria, PAK=Pakistan, PAN=Panama, PER=Peru, PHL=Philippines, PRY=Paraguay, SGP=Singapore, SLV=El Salvador, THA=Thailand, TTO=Trinidad and Tobago, TUN=Tunisia, TUR=Turkey, UGA=Uganda, URY=Uruguay, VEN=República Bolivariana de Venezuela, ZAF=South Africa, ZWE=Zimbabwe

VIDEO : Joseph Stiglitz on the pitfalls of Globalization



CONCLUSION

Globalization contributes to boosting Economic Growth coupled with volatility, financial crises, and wealth gap both within and between countries

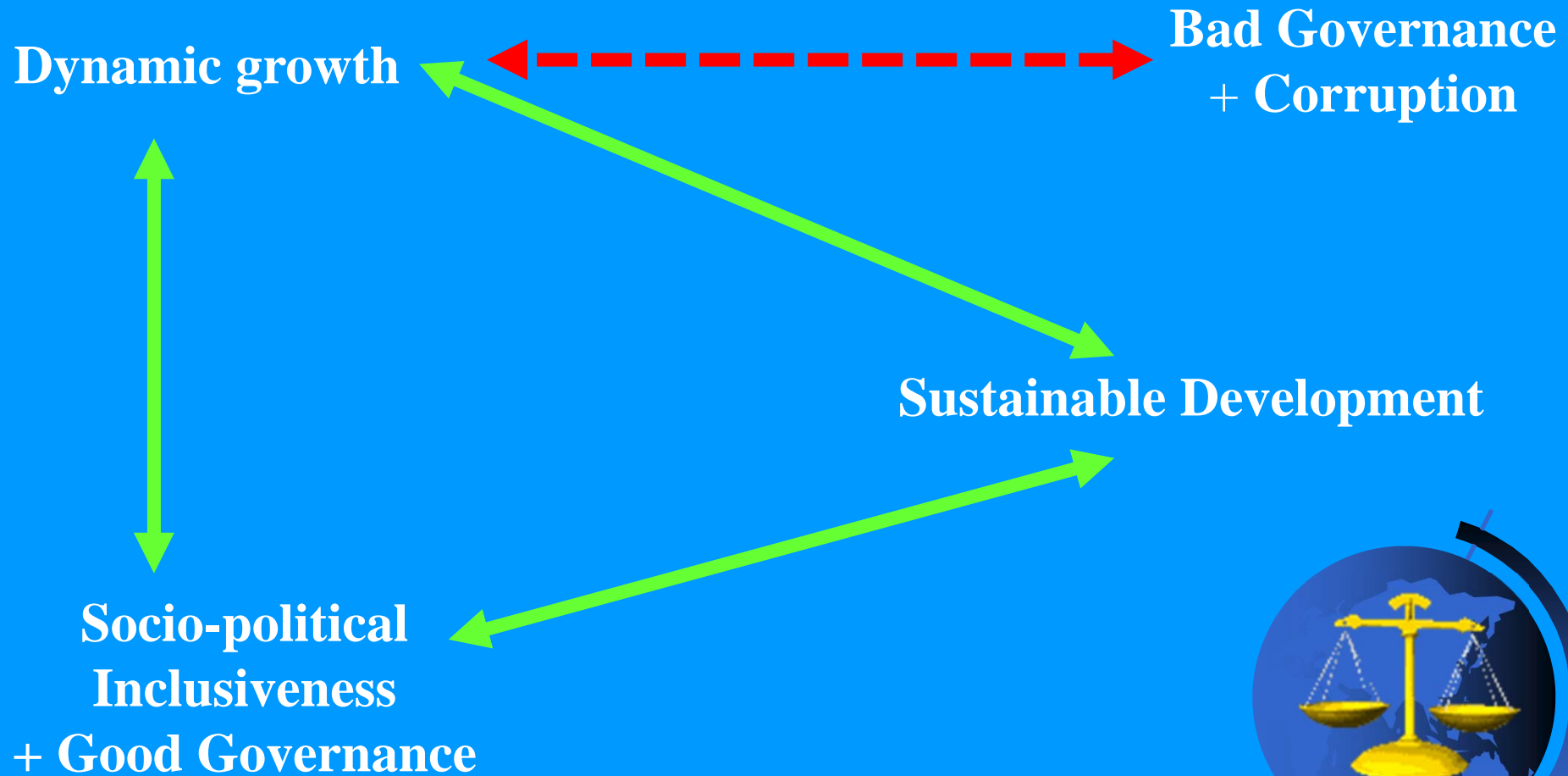


Sustainable growth requires social mobilization
and political stability
within a « nation » rather than in a « country »

☞ Development = social inclusiveness
 Σ (policy choice + political choice)



Trilemma of growth and development?



Globalization is not be be blamed for low HDI

1	Norway
2	Australia
3	United States
4	Netherlands
5	Germany
6	New Zealand
7	Ireland
8	Sweden
9	Switzerland
10	Japan
11	Canada
12	Korea
13	Iceland
13	Hong Kong
15	Denmark

HDI-UNDP 2013

170	Malawi
171	Sudan
172	Zimbabwe
173	Ethiopia
174	Liberia
175	Afghanistan
176	Guinea-Bissau
177	Sierra Leone
178	Guinea
178	Burundi
180	Central African
181	Eritrea
182	Mali
183	Burkina Faso
184	Chad
185	Mozambique
186	Niger
186	Congo (DR)