

## **The Hyperglobalization of Trade and Its Future - Summary**

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The period of hyperglobalization that began in the late 1990s has been associated with the most dramatic turnaround ever in the economic fortunes of developing countries. It is characterized by seven major features:

- hyperglobalization, reflected in trade integration rising rapidly, faster than the growth in world output: merchandise trade now represents 26 percent of GDP, from about 15 percent in the 1970s
- the dematerialization of globalization, reflected in the growing importance of services trade
- democratic globalization, whereby openness has been embraced widely
- criss-crossing globalization (the similarity of North-to-South trade and investment flows with flows in the other direction)
- the rise of a mega-trader (China), which is large relative to the world and relative to its own economy, features unseen since Imperial Britain
- the proliferation of regional trade agreements and the imminence of mega-regional ones
- the decline of barriers to trade in goods but the continued existence of high barriers to trade in services

Regardless of the view one takes of the relationship between hyperglobalization and growth, it is safe to say that a broadly open system [has been good for the world, good for individual countries, and good for average citizens in these countries. Going forward, even if the pace of hyperglobalization slows, the aim of policy at the national and collective level must be to sustain steady and rising globalization and avoid sharp reversals.

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Three issues that illustrate the proximate challenges for the open trading system illustrative are “currency wars,” or the tendency to use exchange rates as a mercantilist tool; the harnessing of trade policies to facilitate climate change; and trade restrictions, which can exacerbate food and natural resource scarcity, with especially adverse impacts on the poorest people around the world.

But these proximate challenges can be addressed cooperatively only if the trading system can contend with deeper or more fundamental challenges. These challenges are threefold. The challenge for rich countries is to sustain the social consensus in favor of open markets and globalization at a time of considerable economic uncertainty and weakness: weak growth, high levels of debt, looming entitlement burdens, stagnating median incomes, and rising inequality. Especially in the United States, public support for and intellectual consensus in favor of free trade are wobbly.

The second is what might be called the China challenge. As China becomes the world’s largest economy and trader, its markets become more important for other countries, especially low-income ones. Its openness, and that of other middle-income countries, will therefore be critical for the development progress of the poorest countries. Relatedly, as a rising power, China will be called upon to shoulder more of the responsibilities of maintaining an open system.

If China continues to be open, trade tensions will remain contained. If China’s future opening slows, trading partners may be increasingly tempted to play the unfairness card, based on the disparate levels of policy openness: why should our markets be more open than those of a rival and equal? In this scenario, especially if economic conditions are weak in advanced economies, the scope for trade conflict and tension could increase considerably, jeopardizing the openness of the global system.

The third challenge will be to prevent the rise of mega-regionalism from leading to discrimination and a source of trade conflicts.

Much of how these challenges will be resolved will be determined at the national level. For the United States and Europe, actions are needed to revive growth and address fiscal challenges, especially the challenges stemming from growing entitlements. For the United States, there is the additional challenge of addressing the problems of stagnating wages, rising inequality, and declining mobility. Success on these fronts will provide a surer guarantee that globalization will proceed apace.

For its part, China should have a stake in preserving the open system for the simple reason that its rapid economic transformation over the last three decades was predicated crucially on openness. That transformation is still far from complete: China's standard of living is still only 20–25 percent that of industrial countries. Completing that transformation is critical for the political legitimacy of China's policy makers. In these circumstances, disrupting the open system would amount to biting the hand that has fed China and its rulers. Indeed, going forward, the Chinese agenda for reforms should be entirely consistent with an open system: China's domestic needs are broadly outsiders' wants. They include increasing the transparency of state enterprises, reducing financial repression, opening up the capital account, creating an innovation-based economy, and reducing pollution and moving toward a more carbon-efficient economy, which would allow it to play a constructive role in global climate change efforts. In all these cases, tensions will undoubtedly arise from differing senses of urgency about specific actions. But across the board, there is no fundamental conflict between what China needs to do domestically and what it needs to do to sustain an open system.

International/collective responses are needed to address the mobility of capital and its ability to escape taxation. Two new developments have exacerbated this problem: capital has become more mobile (reflected in growing financial globalization and increased FDI flows), and the distribution of income in most OECD countries has moved substantially in favor of capital (and also in favor of high skilled people), increasing the size of the tax base that can elude taxation. If countries and companies exploit the mobility of capital, the global ability to provide social insurance will decline, creating problems for globalization. Hence, there needs to be much greater cooperation between rich and emerging market countries (and, of course, tax havens) on how to tax capital and how to share the taxes from capital. This cooperation can take the form of

greater harmonization (which would be difficult and entail a degree of regulatory convergence that countries will find difficult). Or it can take the form of countries doing their best to allow other countries to better enforce their own tax rules.

At the risk of overgeneralizing, the challenge in the trade arena can be summarized as follows: China is happy with the status quo and the United States is not. China—and the other larger emerging markets, such as Brazil, India, and Russia—is reasonably content to have Bretton Woods rules apply to it and hyperglobalization rules apply to its large partners. China will liberalize and open up its markets in line with domestic rather than external imperatives.

The larger partners of the United States and China need to deploy a strategy that takes account of the possibility that China might occasionally be tempted into a less than-benign economic hegemony while reinforcing its incentives to act to preserve an open economic system. The “hyperregionalization” of trade can be read in this context: the Trans-Pacific Partnership and the Transatlantic Trade and Investment Partnership both could have exclusionary effects on nonparticipants, especially China. But regionalism undermines the rule-based system.

History suggests that the best defense against hegemony is multilateralism. Keeping China tethered to the multilateral system, in which the United States and other major countries can exercise some countervailing influence, offers the best insurance against its unrestrained exercise of hegemony.

Multilateralism could work as a defense against China in several ways: in shaping rules, in promoting adherence to them, and more broadly in defining legitimate behavior. With China’s growing size, the balance of negotiating power will be with China rather than its partners. Multilateralism also ensures that China’s trading partners will have enough heft to negotiate in a more balanced manner. For example, China might be willing to open its markets in return for the United States, European Union, India, and Brazil opening theirs. Its willingness to open up in a similar manner in negotiations with just the United States or European Union or with some less powerful combination is far from clear.

The open, rules-based trading system has delivered immense benefits for all, especially today's emerging market economies. Preserving it will ensure that low-income countries can also make successful growth transitions. It is often overlooked that the international trading system has witnessed more successful cooperation, especially between the systemically important countries, than the international financial and monetary system. So cooperation to preserve globalization, even if not in its most hyper current incarnation, is of critical importance. It may also prove less difficult.