

## **Globalization and All That**

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Globalization is one of those strange things that everyone is for or against but no one feels the need to define. It is, of course, all those things that are in the news these days---call centers in Accra, French farmers lying down on the highway, bee-bop nights in Bangladesh---but what do they all add up to?

It seems natural and tempting to try to define a globalized world as one where there is unrestricted flow of commodities and ideas across national boundaries, and globalization as the process of approaching that ideal. This would mean, however, that Canada would have to move toward U.S. gun laws and Dutch drug laws, which seems unfair: Perhaps countries could have the right to have their own laws about who can consume what (but not where it was made). The bigger problem, of course, is what to do with all the Indians who want to move across the U.S. boundary: Clearly, not even the most enthusiastic globalizer is talking about the unregulated movement of people.

Unrestricted migration is not an option, we are told, because of its potential for enormous displacement and damage to the social fabric. But is not there damage to the social fabric when cotton farmers in India end their lives because, with imports so much cheaper, no one wants their cotton anymore? In the first half of 2004, there were over 300 reported farmer suicides in the state of Andhra Pradesh alone, many of them by drinking the very pesticides that they had bought to protect their cotton crop.<sup>1</sup> The sad truth is that we have been taught to privilege the costs of migration by the sheer virulence of the racist reaction that it has sometimes engendered. The victims of freer trade are handicapped by their inability to effectively invoke the irresistible rhetoric of blood and honor.

There are, of course, many others who have reason to be grateful for what globalization has done for them. And this includes not only the millionaires in Bangalore and Beijing, but also their chauffeurs and cleaning ladies. The starvation of the cotton farmer ought to be weighed against the potential starvation of his sister, who, after being abandoned by her husband, found a bearable living cleaning dishes in the homes of the software rich.

Indeed, as David Ricardo explained almost exactly two hundred years ago, since trade allows the country to specialize in what it does best, total income ought to go up when a country opens itself to trade, implying that the income gains to the winners should be larger than the income losses suffered by the losers. After all, we all understand the advantage of specializing in what we do best: This is the reason why most of us choose to rely on the baker for baking our bread and the potter for our pottery.

The past couple of centuries have given us a chance to appreciate the many ways in which this simple and powerful argument is not entirely complete, but it is a rare economist who fails to be compelled by its essential logic. He will concede that there are cases where trade might reduce total income, and accept that there are situations where that might justify protection, but for the most part, when an economist worries about globalization, he is worrying about the losers. He knows that the losers, especially if they happen to be poor to start with, cannot be especially comforted by the fact that there are winners and that these winners are winning big (indeed it might grate all the more for that).

Economists have always had useful things to say about the distributional consequences of international trade. Indeed, some of the most important insights of that most creative era of modern economics, the thirty years starting around 1930, come from attempts to say something about who gains (and who loses) from trade. The theory that builds on these insights, what one might call high trade theory, is as elegant as anything economists have produced. Nevertheless, I will argue, in order to have a useful conversation about globalization today, we need to go beyond this way of looking at the world, not because the theory was wrong to start with, but because the world for which it was conceived is no longer the world in which we live. This is the point of departure of this essay: My hope is that it conveys a sense of why today's world is different from the world of high trade theory, and helps the reader in thinking about who are likely to be the winners and losers in today's world, and how one might try to help the losers.

## **2. The world of high trade theory**

One of the most insightful results in modern economics is the Samuelson-Stolper Theorem: It tells us that if a labor abundant country is opened to trade with a labor scarce country, laborers in the first country and the employers of labor in the second will profit at the expense of the workers in the second country and the employers in the first. The logic is simple: Trade gives each

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<sup>1</sup> <http://www.indiatogether.org/2004/jun/psa-farmdie.htm>

country a bigger market for the goods it is best suited to produce, i.e., goods where it has comparative advantage. We would expect countries to have comparative advantage in goods that make greatest use of its abundant resource: Thus a labor abundant country should see an expansion of its production of labor-intensive goods, with corresponding increases in the demand for labor and its price. Since nowadays labor abundant countries also tend to be poor, and laborers are usually poorer than their employers, this implies that freeing up trade helps the poor in the poorer country. Their employers, of course, suffer for much the same reason---higher wages mean higher costs for them---and as a result, inequality in the poorer country ought to fall. And laborers in the rich country are hurt by the fact that their countrymen can go elsewhere for their labor-intensive goods, with the result that wages in the two countries are drawn closer---illustrating the famous link from free trade to what used to be called *factor price convergence*.<sup>2</sup>

According to the data we have, these heartening predictions seem to have held up rather well throughout the nineteenth century and until well into the twentieth. In the first half of the nineteenth century, international trade was, as it had always been, largely a matter of exchanging goods that had more value than weight, and as such, a marginal (albeit highly profitable) part of economic life. On the Atlantic rim this was a period of divergence. Wages were growing fastest in the richest countries---England and the U.S.---and some of the less favored countries, like the Spain and the Netherlands, were in a slump.<sup>3</sup> But in each case the driver was at home---U.S. wage growth was propelled by the growing realization of its many natural advantages (the period ends with the California Gold Rush) and in England, workers were finally getting the benefits of decades of industrialization. Globalization was still a bit player.

Then, suddenly, the floodgates are opened. In 1846, England repeals the Corn Laws, which allowed the government to restrict the import of corn to protect domestic farmers, setting off a spate of unilateral and bilateral lowering of barriers to trade, all across Western and Central Europe.<sup>4</sup> Transatlantic steam shipping was introduced in 1838, and by 1870 a series of innovations---the screw propeller, the compound engine, steel hulls, etc.---had made bulk freight by steamships practical. Railways, introduced in the 1830s, come of age after 1850---mileage all over the world grew by more than five times between 1850 and 1870---completing the integration of the interior with the ports that begun with the canal revolution of the first half of the century.

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<sup>2</sup> Because labor, land and capital used to be called factors of production, and it is their prices that converge.

<sup>3</sup> O'Rourke, Kevin and Jeffrey Williamson, Globalization and History, MIT Press, 2000.

<sup>4</sup> O'Rourke and Williamson, *ibid*.

And mechanical refrigeration started being used for transporting meat across the Atlantic after 1870.

The combination of these forces led to rapid expansion of trade over the period 1870-1913, with the share of merchandise exports in 1913 across a set of 16 OECD countries going up to levels that they will typically not exceed till well after 1950, and in some cases (such as the U.K.), not until the 1980s.<sup>5</sup> It meant that the price of grains and meat in the labor abundant, land scarce countries of Western and Central Europe fell to levels comparable to those in the labor scarce land abundant countries in the new world---Argentina, Australia, Canada and the United States. Wheat prices in Liverpool were 57.6% higher than wheat prices in Chicago in 1870 but only 17.8% higher in 1895, while the U.S.-British meat price gap shrunk from nearly a 100% in 1885 to less than 20% in 1913.<sup>6</sup>

If nothing else had changed, the fall in the price of food should, by itself, have shrunk the gap in the real (consumption) value of wages between Europe and the new world. And there is indeed some evidence of faster wage growth in Europe over this period. While there is almost no wage growth in Australia between 1870 and 1913, and U.S. wages grow by about 1% per year, wage growth was around 2.5% per year in Scandinavia and around 1.75% per year in Ireland and Italy. But there are also a number of anomalies: Wage growth in the richest European countries was no higher than in the U.S.---Belgium, France, Germany, the Netherlands and the U.K.---and the less developed countries in the new world, like Argentina and Canada, actually grew considerably faster.

The same theory that tells us that there should be convergence in wages also tells us that there should be convergence in the price of land, though the gains from trade here go to the landowners in the land abundant countries. We do find that prices for agricultural land rose by almost 400% in land abundant Australia between 1870 and 1913, and nearly trebled in the U.S. over the same period, and declined in Britain, France and Sweden. But in Denmark, Germany and Spain, also land scarce countries, land prices went up.

Of course we are asking for a lot here: Quite so much fealty to a specific theory may be unreasonable to expect, given that there are many other reasons why wages and prices go up---

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<sup>5</sup> Based on O'Rourke and Williamson, *ibid*, table 3.1.

<sup>6</sup> O'Rourke and Williamson, *ibid*.

capital accumulation and technological upgrading being the most obvious among them. A more modest goal would be to ask whether there is convergence in the ratio of wages to land prices: If there was something (say political change) that made both wages and land prices go up in one country and down in another, neither wages nor land prices will converge, but their ratio might yet. And indeed, this is exactly what we find: Every Western and Central European country with the exception of Spain shows sharp growth in the ratio of wages to land prices, and every new world country for which we have data, shows a decline.<sup>7</sup>

For labor abundant Europe, the period of expanded trade that led up to First World War, was a period of growing equality within. The nervous years between the wars saw the reversal of all that. In these years of growing xenophobia and economic nationalism, tariff barriers were raised and borders were closed to immigrants. And, at least for Western Europe, inequality started to grow once again. Between 1870 and 1913, equality, measured by the ratio of the wages of unskilled workers to the output produced by an average worker, went up in the countries where wages were low and went down where wages were the highest. Between 1921 and 1938, we see exactly the opposite pattern---no one really did well, this being the era of the Depression, but the poor did the worst in Italy and France and the best in Canada, Australia and the U.S.<sup>8</sup>

After the brutal interlude of the Second World War, trade resumed, now under the supervision of the newly created guardians of the world trading system, the World Bank, the IMF and the GATT. Decolonization followed, and suddenly the poorest countries in the world had a chance to make their own trade policies. Over the last fifty years, trade barriers have been raised and brought down many times over in every corner of the world (though perhaps today we live in a world that is more open to trade than at any time since 1930). Do we still believe that being open to trade is good for the world's poor?

There have been a number of in-depth studies of what happened when specific countries liberalized: Adrian Wood studied the East Asian "tigers" and found that low skilled workers did relatively well in Korea, Singapore and Taiwan (but not in Hong Kong), in the decade that followed the lowering of trade barriers. This is as one might have expected, given everything we have been told about how they grew rich by exporting labor-intensive goods.

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<sup>7</sup> O'Rourke and Williamson, *ibid*, table 2.2.

<sup>8</sup> O'Rourke and Williamson, *ibid*.

### 3. Problems

Problems start with the Mexican liberalization of 1985-87. Over this two-year period, Mexico massively reduced both the coverage of its import quota regime and the average duty on imports. Over the rest of the decade, blue-collar workers lost almost 15% of their wages while their white-collar counterparts gained in the same proportion, reversing the trend towards greater equality of the years leading up to the trade liberalization. Argentina shows a similar pattern: Trade barriers were massively lowered at the beginning of the 1990s, and between 1990 and 1998 the college premium, which is the ratio of wages for those who have a college degree to that of the average unskilled worker, almost doubled for men and almost trebled for women, in both cases reversing an equalizing trend that started in 1980.<sup>9</sup> This meant that the lowest wage earners were effectively excluded from the wage growth that took place in this period. In Colombia, trade barriers were massively lowered between 1985 and 1992, leaving the economy more open than it had ever been. Between 1990 and 1998, the college premium went up by over 20%, which is small by Argentine standards, but not negligible. Similar patterns also have been found in Chile in the 70s, Costa Rica in the late 80s and Uruguay in the 90s.

Lest one think that this is some Latin American perversion, the same correlation between liberalization and increasing inequality shows up in the two Asian giants, China and India. Between 1980 and 1998, while China became increasingly open to the world economy, the income share of the poorest quintile went down from 8% to 7%, while the share of the richest quintile went up from about 30% to about 45%. And in India, all evidence points to an explosion of inequality in the urban areas over the post-liberalization years (1991-2000), after many decades when inequality neither went up nor down.

To check on what we are finding here, we could compare what happened over the last few decades in countries that were open to trade, with what happened in countries that were closed (or we could compare countries that *became open* with countries that did not). This is really what we were doing with the historical data, and now that we have data from a hundred countries and more, it is actually possible to be more precise, and try and eliminate other sources of possible difference between these countries. A number of people have now tried this exercise: Most have found, sometimes to their surprise, that being open to trade either increases inequality or has no effect at all. And the one study that directly focuses on the well-being of the poor (defined as the

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<sup>9</sup> Galliani, Sebastian and Pablo Sanguinetti, "The Impact of Trade Liberalization on Wage Inequality: Evidence from Argentina", mimeo, Universidad di Tella, Buenos Aires, 2002.

bottom 40%) finds that their income grows more slowly when the economy is more open to trade, not just in comparison to the rich, but in absolute terms.

Correlation, as social scientists never tire of reminding each other, is not causation, and none of this evidence is quite strong enough to entirely transcend that old divide. What some of the case studies do prove is that something happened when countries opened themselves to trade, that was strong enough to make the countries change course, towards greater equality in the nineteenth and early twentieth century, and towards greater inequality in the last decades of the twentieth.

But perhaps other things changed when the countries liberalized. The studies do offer some clues that we have been deliberately ignoring so far: The O'Rourke and Williamson study, which is the source of most of our information about the nineteenth and early twentieth century, emphasizes that the pro-trade decades were also pro-immigration decades. Enormous numbers of people emigrated from all over Europe to the Americas, creating the melting pot that we know it to be today: The U.S. labor force would have been smaller by about a quarter in 1910, were it not for the flow of immigrants over the previous four decades. This drove wages up where they left from and down where they went to. Indeed O'Rourke and Williamson do a calculation that shows that immigration alone can explain all the changes in the income distribution in this period and more, though they are at pains to convince us that this cannot be right. Moreover, their data precisely leaves out those countries, like India, that were drawn into the world trade network but did not see large-scale out-migration, making it harder to tell what would have happened to Europe had the labor scarce countries of that time been as averse to the great unwashed, as today's rich countries seem to be.

If this says that the past was never quite what it was supposed to be, there are also enough people saying that the same goes for the present. According to Feenstra and Hanson, the increase in inequality in Mexico was substantially driven not by trade, but by the foreign investment that came in with the liberalization. This presumes that foreign investors would want to work with skilled laborers, which is by no means obvious. Feenstra and Hanson suggest the following line of argument: When an American firm builds a factory in Mexico to make something it used to make at home, the demand for skilled labor should go up, simply because anything that used to be produced in the U.S. ought to be much more skill intensive than most things Mexico used to produce. This is correct, but only if we accept the assumption that once production moves to Mexico, they would not switch to a different (and less skill intensive) way to do things.

Moreover, outsourcing is not the only reason to invest abroad: When Nike goes to Vietnam, our presumption is that they were attracted by the cheap labor and not the ease of hiring MBAs. Nevertheless, *prima facie* it does seem that, at least in Mexico and probably elsewhere, direct foreign investment has been associated with a rise in the skill premium. Feenstra and Hanson estimate that almost half of the rise in the wages of non-production workers (a proxy for white-collar workers) can be explained by this factor alone.

The other, more straightforward, explanation of what happened to wages attributes the (relative) fall in the wages of the low-skilled workers to the fact that in Argentina, Colombia and Mexico, it was the industries with a high concentration of low-skilled workers that had the highest tariffs to start with, and where the cuts were the biggest. But tariffs only matter if you are in an industry that is a net importer, and indeed most of these studies do find that prices fell more in industries where the tariff cut was deeper---confirming that the barriers to trade in these industries were actually binding. It follows that these countries must have been importing all these labor-intensive goods, despite the fact that nearly 90% of Latin America's external trade is with rich labor scarce countries.

The puzzle deepens when we push this argument a step further. When these studies directly look at changes in employment across sectors, the striking thing is the lack of correlation between changes in tariffs (or the resulting change in imports) and changes in employment. After all, our faith in the therapeutic qualities of trade comes from the belief that trade helps the country specialize in what it is good at, and we might have expected that removing the barriers to trade would set off the process of reallocation of labor in that salubrious direction.

One might wonder, especially if one comes from a certain political persuasion, whether the absence of labor reallocation is a result of draconian labor regulations that make it impossible to fire anyone. As it turns out, manufacturing employment fell dramatically in Argentina, considerably in Colombia and more modestly but still significantly, in Mexico. It also does not seem to be true that people in what would have been shrinking sectors protected their jobs by taking huge pay cuts (say out of a love of their jobs). Wages did fall, but the correlation between the fall in wages and the changes in protection is never very large.

Trade in LDCs these days, it seems, is much more effective at destroying jobs than at creating them, at least over the short horizon. I realize that this is controversial, but I see no obvious other

way to read the evidence. You may still feel that I am leaning too heavily on these Latin American examples, so let me try and explain the logic that brought me to this point.

#### **4. Rethinking Trade Theory**

The first step is to note that brand names and reputations are hugely important in today's trade. This makes perfect sense, given that the average buyer in the North (who has all the money), is rich enough today to afford to indulge his sense of quality: Clothes must not shrink or bleed; machines must not fall apart in a week; and software must be ready when promised. Consumers would rather pay something extra for a brand name because they feel assured of the quality. Retailers are willing to pay more to reputed suppliers because they do not want to offend their buyers by selling duds. And manufacturers want suppliers who are known to be reliable, because what they make and sell is only as good as its weakest link.

The obverse of quality being important is that the price is not quite as important as it used to be. In 1997, when the Indian software industry was just beginning to become a household name, I happened to be in the offices of one of the leading exporters of customized software. We were talking about the industry, and the CEO said, almost casually, "We just raised the price per line of code by 50% and our clients did not seem to mind. I think we will raise it by another 50% in a few months." I happen to know that he was not bragging. Indian software in those days (we are now in the time scale of the software world) was so cheap that it did not make sense for the average overseas buyer to give up someone they know and trust for someone new, even at half the price. After all, the new supplier could be incompetent or worse and chances are that the buyer only find out after the software is ready, many months hence. For the typical buyer of customized software, a Fortune 500 company, the cost of the lost time was probably worth as much as they were paying for the software, or more.

The logic here applies as much to T-shirts as it does to software. The famous New York department store, Macy's, orders its t-shirts from its overseas suppliers in the fall of each year, but the T-shirts only go on sale the next spring. If, when the T-shirts arrive in early spring, Macy's discovers that they were not what it had asked for, it would be too late to do much about it for that year. The loss of face *vis a vis* its clientele could be enormous. It has to be worth paying extra to suppliers that it can trust.

Several consequences follow from recognizing the centrality of reputation. First, reputation is a bit like a fixed cost---the advantage it gives you is independent of how much you sell, though if you expand beyond the point where you are able to maintain quality, your reputation will eventually collapse. Over some range, however, it clearly pays for firms that have reputation to keep expanding: It is no accident that Gucci now markets everything from perfumes to polo-necks, and Amazon.com is no longer just the book-seller to the world.

Second, the urge to capitalize on their brand name is what drives multinationals into LDCs that are willing to have them. And since services are where brand names count the most (would you trust your money to a bank that you have never heard of; or get advice from a consultant on his first day on the job?) a lot of multinationals are headed for the service sector. Since service industries tend to employ a lot of white collar workers, this can explain at least a part of why the skill premium goes up when the multinationals come in.

Third, we would expect a great deal of inertia in the choice of whom to buy from. Combined with the fact that those who have a reputation will tend to want to grow, this implies that it could take a long time before cost advantages show up in the pattern of trade. This may explain why the Argentines and the Colombians import labor-intensive goods from the labor-scarce North. It also explains why so many domestic firms shrink or shut down when opened to trade---they cannot compete with the reputation of the best-established multinational suppliers. The firms that survive and expand, apart from the few that already have an established international reputation, will be the ones that are in sectors where reputation does not matter so much---manufactures aimed at the lower end of the local market, exports to other third world countries, etc. This may be one way to interpret the fact that in all the Latin American examples, the informal sector expanded following trade liberalization.

Fourth, all this suggests that it may be some time before those who lose their livelihoods with the liberalization find comparable jobs in the industries that start to grow after the liberalization. In the long run, we would expect the country to broadly specialize in industries where its factor endowments give it a natural advantage, but success in building a reputation will clearly be crucial in determining exactly what it ends up exporting to the world. This process is likely to be slow because building a reputation takes time: Esther Duflo and I found that in the Indian software industry it took about five years to be really trusted by foreign buyers, and in software

everything happens quickly.<sup>10</sup> It is likely to be doubly slow because capital markets in developing countries work very poorly, and even visibly successful firms have trouble getting enough capital to expand as fast as they want. In another joint project with Esther Duflo, we found that even in India, where the return on the extra dollar is 100% or more, firms cannot get enough capital.

This problem is made worse now by the fact that the two biggest countries in the world, China and India, are in the process of expanding their exports to the level that their enormous reserves of skilled man power would justify. They have cheap wages, a large and wealthy émigré population that provides them with the necessary contacts, and a growing reputation. Most other countries would have to build their own reputations in competition with these two established players, just when they are gathering steam. It cannot be easy.

## **5. What then?**

If I am right in looking at the world in this way, where does it leave us? Relative to the benign vision of globalization offered by the Samuelson-Stolper Theorem, at least for the poor in poor countries, all this is obviously bad news, though recognizing the problem does help us control the damage. It tells us, for one, that countries need to think hard about reputation.

There are a number of steps that a country can take to make reputation acquisition less of an issue: More effective court systems, for one, by making it easier to sue for damages if a supplier misbehaves, which encourages buyers to consider sellers who are yet to make a name for themselves. Developing trade relations with other developing countries has a similar effect, because poorer buyers may be more willing to trade off quality for low prices. It is perhaps no accident that Guido Porto found that Mercosur, which integrated the economies of Argentina, Brazil, Paraguay and Uruguay into a single (almost) free trade zone, benefited the poor in Argentina.

A public scoring system for buyers and sellers, where buyers simply report their experiences with specific suppliers and vice versa (as for example, on CNET.com or Dealtime.com), may be one way to speed the process of building up a reputation, simply by making it easier to identify

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<sup>10</sup> Banerjee, Abhijit and Esther Duflo, “Reputation Effects and the Limits of Contracting”, *The Quarterly Journal of Economics*, 1999.

malefactors. We do however have to be careful about the possibility of abuse here: Sellers may try to blackmail buyers by threatening to give them a harsh report.

Creating an environment that is friendly towards multinational investors also helps, though most countries seem to trust domestic capitalists more than their foreign counterparts. My sense is that this is largely unwarranted (though perhaps politically necessary). The *prima facie* evidence seems to be that within any sector multinationals pay higher wages, to people with the same observable qualities, compared to domestic firms. Indeed, the simple fact of being in the public eye probably makes them behave better.

Multinationals are useful because their reputation can intermediate between domestic sellers and foreign buyers and also because they are better at negotiating with regulators in the North, who are often all too willing to protect domestic producers from cheaper imports, in the name of protecting the health of domestic consumers. Much of what China now exports is produced by nameless firms in China, but marketed under some global brand name. In the typical case, the Chinese firm sells to some other established firm, often based in Hong Kong, and it is this firm that sells to the eventual marketer. This double intermediation is useful because the firm in Hong Kong has a reputation in the world of other firms not among the eventual buyers, while the firm that does the final sale, does not need to learn all the nuances of Chinese supply chains. Indian customized software firms have a similar system: The firm will often have a U.S. front office that the buyers know and deal with, who in turn will pass on the actual work to their Indian partners, who the buyers only vaguely know about.

Finally, improving capital markets is yet another way to make building a reputation easier. Firms that have been doing well need to go to scale quickly, and inefficient capital markets slow down their growth.

All this, of course, does not answer the really basic question: Is trade worth it? The conventional answer, at least among economists, is that trade is worth it as long as it makes the pie bigger: If the income gains to those who gain from trade is larger than the losses to those who lose, we should be in its favor, because we could always redistribute the gains to make everyone better off. I have never quite understood why we are supposed to find this compelling, particularly where the poor are the likely losers, unless we have reason to believe that the gains will really be distributed to them. The problem is that targeted redistribution is never easy: Identifying the losers is hard,

taxing the winners is harder and making sure that the money does not somehow get lost along the way is sometimes well nigh impossible. The best way to make sure that no one loses from liberalization is almost surely to not do it.

On the other hand, I know of no example of a labor abundant developing country that has had sustained growth without being outwardly oriented in some broad sense of the term. The problem is that growing countries need technology and capital from abroad. To pay for these imports and to take full advantage of what they are good at doing, they need markets abroad.

It is true that none of this directly requires being totally open to imports: China, after all, is only starting to get there. But it does require a credible commitment to remain open for the foreseeable future, to convince foreign investors that the country will earn enough foreign currency to repay what its borrowing now. And it requires being sufficiently open to imports from the North to keep the WTO happy, if for no other reason than keeping the markets in the North open to its exports. In the end, the choice is between cutting oneself more or less completely off and giving up on fast growth, and accepting a very substantial degree of openness.

Having thought about it, I think I came out on the side of openness. We live in a world where people have come to see the good life as something that they can legitimately aspire to. There is no way to put that genie back in the bottle (even if we could, I do not know that I would want to). The explosion of ethno-religious conflict around the world in the last two decades, I believe, is a product of an era where hopes were created and then denied. To go back and convince people that growth is not worth it, is to invite a blood bath.

Given that, our job as economists should be to think of ways to make the whole process as painless for the many losers as it can be made to be. There seem to be broad agreement these days that openness should go with a strong commitment to an acceptable guaranteed minimum living for all. While I am certainly in favor, two remarks are in order: First, the popular view seems to be that the guarantee should primarily take the form of a right to education and health. This is in many ways very appealing, but my sense is that we know very little about how to deliver these services effectively to the poor in poor countries. An income support program, targeted towards the elderly and women with young children, combined with a negative income tax program targeted towards those who working for low wages (modeled on the Earned Income Tax Credit in the U.S.), has the obvious advantage that we know that it helps the poor. Second, many of the

biggest losers will be the owners of very small firms and farms and workers in the organized sector, rather than the very poor. The minimum guarantees that are being discussed are clearly not going to compensate them for what they will have lost. While in some ways this is fair---after all, they do have more to start with---we should recognize that at the very least, they think that they have a right to be compensated. There is very little work that I know of that thinks hard about how to target the non-destitute.

Finally, there is the issue of how to share the benefits of trade fairly across countries. The economics of how the gains from trade get distributed across the trading partners is always subtle and I have no way to say who gains more. The distribution of costs, on the other hand, seems clear enough. Every rich country has a well-established system of welfare that will automatically compensate its losers. Every poor country will have to set up new mechanisms to do so, and pay for them now. In addition, migration today is explicitly a system by which rich countries raid the poor countries for talent. With every engineer or doctor that settles in the North, a poor country loses a potential entrepreneur and a public servant, and it is hard for me to believe that the money they send back is compensation enough. Globalization, by the simple fact of increasing contact, can only make it easier for the North to pick off the people it wants. It is true that globalization has encouraged some of these people to take a second look at the opportunities in their own countries, but on balance I suspect it is still a cost (China and India may be exceptions here, though I would not be sanguine).

I therefore see no reason why the poor countries should not demand an explicit price from the rich for agreeing to remain open. There are many ways the price could be paid, but let me end by mentioning one that appeals very much to the economist in me: Given that rich countries are aging fast and need labor, why not a system of quotas for immigration to rich countries, that are open to everyone (i.e., not just the doctors and engineers) in poor countries that agree to remain open.<sup>11</sup> The quota will be allocated by a lottery, and will allow one person between the ages of twenty and thirty-five to have a work permit in a rich country for a fixed period, say five years. His/her travel expenses and some resettlement costs would be paid for, and precautions will be

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<sup>11</sup> I am certainly not the first person to think along these lines: See, for example, Jagdish Bhagwati, "Borders Beyond Control," *Foreign Affairs*, January-February 2003; and Rodrick, Dani. "How to Make the Trade Regime Work for Development", mimeo, Harvard University, February, 2004.

taken to make sure that in most cases, he/she does go back, so that the home country benefits from his/her savings and the skills he or she has acquired.

This will not be easy: Le Pen and his like will have their day. But, in the end, if we cannot ask the rich democracies to do what is both just and economically rational, what is left for us to hope for?