General Discussion:
Factors Driving Global Economic Integration

Chair: Gordon Thiessen

Mr. Thiessen: Well, I must say that when you look at the recent economic experience in the U.S., if ever there was a time when global integration would be an easier sell, it should be now. Shouldn't it? I mean a run of really good economic times—unemployment rates down lower than you've had for the longest time. I must say that those of us who are outside can't imagine why freer trade would not be an easier sell in the U.S. these days.

All right. Let's begin. Questions? Yes, Alan.

Mr. Greenspan: I think you and I probably responded in much the same way with respect to this extraordinary benevolent sense that everything is going to come out just right—that trade barriers are going to continue to fall, that the barriers against the continuous inexorable move toward free and open markets will continue—yet I think our experience has been precisely as you indicated. Namely, despite the extraordinary prosperity, the ability to move forward on various trade initiatives has clearly come to a remarkable stall. I would like very much to believe what I've heard this morning, and it cheered me up somewhat, but I'm not sure it's going to last very much longer.

I remember that in the 1960s, for example, the free-trade thrust coming out of the Kennedy round. The issue of the Cold War was not irrelevant to what was going on: The extraordinary surge and free trade initiatives did, to a substantial extent, reflect the Cold War and the need for the West to maintain unity. But with the end of the Cold War, certain things started to grind to a fairly slow pace, and I don't see the momentum picking up readily. Mike looks at history, and I would merely suggest to him that my recollection of the annals of 1913 was that there was, in retrospect, an utterly unimaginable view of what was about to happen in the subsequent decades. And our ability to forecast glacial work or tectonic changes in the views of the world has historically been exceptionally limited. We all need to press very hard on the political process to maintain what we all perceive is a major advance in civilization as a consequence of opening up international markets. But I think the presumption that it's a simple game is misleading.

Having said all of that, may I ask Mike a technical question?

Mr. Thiessen: Absolutely.

Mr. Greenspan: Mike, I think we're all aware that declining transportation costs are an obvious crucial issue with respect to globalization. But they, in turn, are a function of transportation processes themselves and the size of transported products. The data that we have in the post World War II period—which, for the United States show pounds per constant dollar of exports and imports—describe a very dramatic downsizing in what it is we import and export. And I'm, frankly, curious whether or not you've seen any evidence in the earlier periods that suggest the balance of forces of bringing down the transportation cost. I mean, to what extent it would changing transportation capabilities in the 19th century be crucial then and downsizing be crucial today. To what extent is that verifiable or otherwise available in the data systems that you've looked at?

Mr. Thiessen: Well, why don't we accumulate some questions and then Mike can respond to them. Question right there.

Mr. Brinner: My question is whether there has been enough exploration of the important contribution equity investment, as opposed to debt investment, has made the transmission of technology across borders? My contention would be that it's enormous. Once countries allowed equity investment, then the owners of technology were willing to share it because they could share in the benefits.

Mr. Johnston: Where are the cheerleaders now?

Mr. Thiessen: Okay. Allen.

Mr. Sinai: I have three questions. One is for Chairman Greenspan who mentioned the possible continuing acceleration of productivity growth even after stripping out cyclical forces. The question is a technical one, which has to do with the methodology of the calculation in the current situation of taking that cyclical component out of productivity growth and getting at the structural growth in productivity.

My second question is for Doug. It may be a little bit of nitpicking, but you use as a policy example NAFTA and the exports presumably of Mexico and United States in the calculation of the table. But how do you know that that's NAFTA and not private sector forces in maquiladora before NAFTA and the incentives to locate and produce in Mexico? How do you separate out and use, as an example, NAFTA as the source of that which was in the Mussa remarks?

And then I have a more general question for everyone on immigration and the data, which are very striking in terms of the absolute numbers of immigration flows in Mike's chart. As a force in globalization, both into the United States and to Europe and to other parts of the world where anecdotally large immigration seems so clear now, are the numbers, the ones in the U.S., accurate? Or are they understating what is going on? And what is the opinion of the panelists and anyone else on immigration as a force in globalization and the importance and significance of it?

Mr. Thiessen: Okay, Alice Rivlin.

Ms. Rivlin: In dealing with this question of why has the movement toward freer trade stalled, it does seem to me that the proglobalization elite gathered in this room and elsewhere haven't addressed questions that really need to be addressed in the context of answering the protesters. It's all very well to say, "Can't they understand that everybody benefits in the end?" But many of them have not benefited. Over the last few years, over the last several decades, the bottom of the income distribution has not benefited from much of anything. Relative wages—absolute wages at the bottom of the income distribution—went down in the United States in the 70s and the 80s. Relative wages have not increased in the 90s, although things aren't getting better. There has to be some addressing of the question regarding how are we going to deal with the relative wage disadvantage at the bottom. Now, it may not all be due to trade. It mostly isn't. I mean, mostly we think it's due to the increase in demand for highly skilled people. But that's a hard thing to sort out.

And, more briefly, what about the environment? There is a plausible, serious sounding argument that we raise our environmental standards here. And that just means that you buy from people who don't have as high standards. That has to be answered. And the other question is about labor standards. We need to have better answers to these questions, even for the kids gathered in the streets.

Mr. Thiessen: Thank you. There's a question back there?

Mr. Breimyer: I wanted to sound a bit of a different note. We have seen inside State Street Bank—a basically fairly standard bank providing, perhaps, unusual services—a significant change in culture. It reflects on Michael Mussa's point about the movement to globalization, in this case involving a financial service firm. What we have essentially done at State Street is to move from a supporting role in providing global custody at a very high level of activity, to a more active direct involvement in financial markets. In doing this, we have used global custody as a springboard. It provides a platform that gives us information on a daily basis regarding portfolio flows, which then can be related to imbalances in global financial markets. It then becomes our choice whether we take positions using this information. At times, we have acted aggressively—as have our clients—and, perhaps, increased financial market instability. This has been an interesting evolution for us, and now reading and responding to portfolio flows is an important part of our foreign exchange operation. But, at times, we have essentially contributed to imbalances such as in the Brazilian crisis, for example. I was wondering Michael, how you see this particular aspect in terms of the overall change in the global financial market environment?

Mr. Thiessen: Okay. One more question and then we'll let Mike and Doug respond. Henry Kaufman.

Mr. Kaufman: I think Mike Mussa is understating the importance of migration or immigration in the last decade or so, more than from the historical perspective. I'm all in favor of migration and immigration. It's a wonderful thing, particularly in the United States. But it is gradually changing the social fabric, and it will have political consequences. Look at what's happening in some states like California. We are bringing into the United States more than a million new immigrants a year. The statistics can't really keep track of it, particularly illegal immigrants. Any of you who have had any housework done, gardening done, you probably don't speak the language of the individual who's doing the work and the individuals doing the work don't speak your language. In Europe, I think this is even a more difficult problem socially and potentially politically. Suppose we go into another recession sometime? Who knows when? Those immigrants, those people who are even technology trained whom we're bringing in here on visas temporarily are going to stay and they will drive down labor costs very hard in a period of a recession. And all of that is going to bring about some social and political conflict, which we probably tend to underestimate because we don't want to take up this particular complex issue. The information is incomplete. These historical relationships are sparse. Migration is an important part of globalization. Economists have a difficult time not only in spotting structural changes but also in interpreting their consequences.

Mr. Thiessen: Okay, Mike. Why don't you respond?

Mr. Mussa: Well, I mainly agree with what Henry said in his last comment. I don't think I really underplay the importance of human migration as a factor in economic integration; however, it often tends to be neglected, where as I, in fact, devote substantial attention to it.

Regarding the question about the role of global financial markets and the operation of globalized financial institutions in terms of the stability of the financial system, that is not the main subject of this paper by any means. I refer to it really only very briefly. I think that in terms of public policy, as well as private business activity, that this is a very important area in which to focus attention. The financial crises of recent years that has affected emerging market countries, in some cases very severely, suggests that all is not well with how the global international financial mechanism operates. But that is too broad of a subject for me to attempt to address, in this paper or in these remarks.

Regarding what Alice Rivlin said, I take a somewhat different view. I think it has always been true that the process of economic integration has had its losers, as well as its winners, and we ought to be more up front about recognizing that. One of the things that trade liberalization is supposed to do is to change domestic relative prices and align them better with international relative prices. Well, almost always when you change relative prices, there are some people whose factor incomes go up and there are other factor incomes that go down.

I didn't tell the story in this paper, but I do in another paper, regarding how globalization destroyed my grandfather's trade and reduced his income very substantially and then induced his movement to America, which was part of the solution to the problem created by globalization. But I think that we need to recognize that there are, indeed, losers in the process of economic integration, as well as winners. And the Luddites and the saboteurs and the rest of them are testimony to that phenomenon of long historical duration.

On Roger Brinner—there have been a number of studies of factors that influence the spread of technology. And it does appear that foreign direct investment provides an important impetus to transfers of technology in a way that is not true of either debt flows or portfolio equity flows. Some of the more recent analyses in this regard say that it's not all foreign direct investment that has this beneficial effect. It's foreign direct investment, in particular, that tends to utilize at least a reasonable degree of human capital in the country into which the investment is going that provides this additional benefit. If you're building some vast mine out in the wilderness and importing huge Japanese trucks and American bulldozers to do the work, you don't get much technology transfer that has an additional benefit to the economy.

Allen Sinai—well, the official immigration numbers undoubtedly understate the total immigration. I think immigration remains an important economic force affecting the U.S. economy, both the legal means, which has gone up considerably as the rules have been liberalized over the course of the past twenty-five years, and also the less than legal component of it.

Don Johnston—where are the cheerleaders? And I also want to take Alan's comment a bit into this. The question of, what about all the problems we are encountering with trade liberalization? I think there is a little bit of a distorted view on this issue. Trade liberalization continues to be a very important and vital force in the development of the global economy, but not trade liberalization by the industrial countries. We basically finished with the main agenda for that with the Uruguay round. And, indeed, before that, tariff barriers, particularly from manufacturer's products among the industrial countries, were reduced to very low levels and we are stuck with in terms of trade and goods, barriers and a few hard nut areas like agricultural and textiles.

But what has been happening the last twenty years is that developing countries have been moving, many, many of them, massively to reduce the magnitude of their trade barriers. Now, we talk about NAFTA. NAFTA was a minor step of trade liberalization for the United States. It was a very important step of trade liberalization for Mexico, and it was proceeded by an even more important decision on a unilateral basis for the Mexican government to liberalize its trade regime. And that is happening in China; it's happening even in India. What we saw a decade ago with the end of the Soviet Empire is changing the structure of world trade for all of the economies that used to participate in the CMEA and integrating them into the modern global economy. That's where the dynamism of trade liberalization has been for the last two decades and I think is likely to continue to be.

The other important area where I think progress is being made, driven largely by technology improvement, is in the services area. That is an area where U.S. exports have been growing and technological advances in transportation and communication are an important driving force behind the growth in global trade in the services. Now, the failure to reach political agreements to liberalize in that area I think is an important problem. I remain hopeful that progress will be made on that front. Partly, I remain hopeful because I believe that the impetus for it will come largely driven by those improvements in technology. That is, I think, to an important extent what we have seen domestically that the functional barriers between different components of the financial services industry have been driven down largely by the improvements of technology which has changed the way in which that business is done in terms of its production technology. And public policy has really responded to those developments, rather than being the principal force driving them forward.

Finally, regarding Alan's technical question, I really don't know. What we do know is that intra-industry trade—trade in the same products or more or less the same products of the same industries across international boundaries—which dominates manufactured trade for the industrial countries today. That ain't the way it was a century ago. The cross-cost of transporting back and forth were such that you shipped one good in one direction and another good in the other direction predominantly. And that is not particularly true today where we have a lot more cross-trade in products of the same or similar industries.

Mr. Irwin: Just one quick point on this issue you raised, Gordon, about if times are so good, why is trade liberalization so difficult? Sometimes, unfortunately, you need a crisis to jump-start trade liberalization. When did Congress open hearings on the Smoot-Hawley tariff? Not in the depths of the Depression but at the peak of the business cycle of the summer of 1929. When did the U.S. move toward trade liberalization? Not when times were good—in 1934 when the Congress passed the Reciprocal Trade Agreements Act. What did we do in the 1940s when there was tremendous economic uncertainty after the war? We founded the GATT. What did we do in the 1950s when the economy was cruising along and unemployment rate was very low? "Zip," in terms of reducing trade barriers. When did New Zealand decide to embark on unilateral reforms? When times were good? No, when times were bad and they faced a crisis. So, unfortunately, the correlation between good times and opening up markets to international trade is not necessarily very strong.

Mr. Thiessen: Well, thank you very much. I must say I think the issue of cheerleading is very important. Mike, the agriculture and textile areas do matter a lot in those developing countries. And if we are going to make trade something that is seen to be attractive to them, we are going to have to deal with those and I think that does, indeed, take a lot of cheerleading and a lot of political courage in the industrial countries. But I think that, nonetheless, it has to be done and I must say by the economics community generally. You know a country like Canada, which is very open to trade, selling first the Free Trade Agreement with the United States and then the NAFTA agreement with the U.S. and Mexico was not an easy sell, despite the fact that we basically live off of trade. We've got one of the most open economies in the world, and it was still a hard sell. It's one of those things that you simply cannot stop selling because it isn't easy.